Attachment 22

DBNGP tariff history from 1995

See attached.

Epic Energy
Dampier to Bunbury Natural Gas Pipeline

DBNGP tariffs 1995 - 2000

This note sets out the tariffs for third party access to the Dampier to Bunbury Natural Gas Pipeline (**DBNGP**) which have applied since 1995, and briefly summarises the way in which they were determined. Prior to 1995, there was no third party access regime to the DBNGP, although a small number of shippers had succeeded in negotiating transportation service agreements with the then owner, the State of Western Australia under the guise of the State Energy Commission of Western Australia ("Corporation").

It is important to understand that the tariffs for third party access on the DBNGP have reduced significantly over time since third party access was first prescribed under legislation in 1995. However, the biggest reductions in tariff occurred from 1 January 1998 through the time that Epic Energy has owned the DBNGP. The reductions over time go some way to demonstrating that the tariffs and tariff path proposed by Epic Energy in its access arrangement were reasonable. At the high point of 31 December 1997, the tariff for T1 full haul service was \$1.27/GJ. From 1 January 2000, the prescribed tariff was \$1.00/GJ for T1 full haul.

It is also important that this paper be provided to the Regulator at this stage because of the following comment by the Court in the Epic Energy case at paragraph 219:

> "Epic submits that the draft decision should be quashed and the Regulator should commence afresh his assessment of the proposed Access Arrangement. This would afford Epic the maximum opportunity to reinforce its case to the Regulator and the full measure of the procedural stages provided by the Code. This process would, however, extend the time necessary for the Regulator's assessment and ultimate decision in respect of the proposed Access Arrangement and thereby extend the period during which Epic would enjoy the continued advantage of the tariffs established under the former regime."[1]

The tariffs (reservation plus commodity charge, at 100% load factor) for full haul firm (Tranche 1) service applying since 1995 were as follows:

FROM	RESERVATION CHARGE	COMMODITY CHARGE	TOTAL TARIFF[1]
1 January 1995	\$1.030000/GJ	\$0.220000/GJ	\$1.250000/GJ
1 January 1996	\$1.030000/GJ	\$0.227374/GJ	\$1.257374/GJ
1 January 1997	\$1.030000/GJ	\$0.233633/GJ	\$1.263633/GJ
1 January 1998	\$0.917457/GJ	\$0.271971/GJ	\$1.189428/GJ

[1] Re Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231 at page 90

FROM	RESERVATION CHARGE	COMMODITY CHARGE	TOTAL TARIFF[1]
1 January 1999	$0.822743/GJ	$0.271971/GJ	$1.094714/GJ
1 January 2000	$0.728029/GJ	$0.271971/GJ	$1.000000/GJ

[1] Tariffs are in dollars of the day

Each tariff is dealt with individually in subsequent sections of this note.

1995 tariff

Section 91 of the *Gas Corporation Act 1994* provided that Schedule 5 of the Act was to govern pricing to transmission capacity. Importantly, section 95 stipulated that regulations could be developed to further provide for access to, or pricing of, transmission services. Schedule 5 was concise, and provided, relevantly, for:

- the creation of an obligation upon the Corporation to offer access to spare and developable capacity on a "non-discriminatory basis and on a first come, first served basis" (schedule 5(2)(1));
- terms and conditions to apply to access were to be specified in the regulations (schedule 5(2)(2)); and
- regulations to be made which may make specific provision for ("without limitation") price, and the components of price to apply to third party access seekers.

The regulations referred to in Schedule 5 were subsequently created. These were the *Gas Transmission Regulations 1994.*

Regulation 138 created a "transitional" tariff arrangement by stating:

> "*The Corporation must adopt and apply the prices announced by the Minister for Energy in a Ministerial Statement to the Legislative Assembly on 29 November 1994, until the first redetermination under regulation 151.*"

The Ministerial Statement set out the tariffs that were to apply from 1 January 1995. For full haul firm (Tranche 1) service, the tariff comprised:

- a capacity reservation charge of $1.03/GJ; and
- a commodity charge of $0.22/GJ;

The total charge (at 100% load factor) was therefore to be $1.25/GJ.

The tariffs set out in the Ministerial Statement were consistent with those developed and published by the Energy Implementation Group which had been set up by the Government in 1993.[2]

The Energy Implementation Group tariffs were developed using a cost of service model.

A capacity reservation charge was to recover the capital costs of the Pipeline comprising depreciation and a return on a historical cost asset base.

The tariffs were approved by the Government as being appropriate tariffs.

The operating and maintenance costs of the DBNGP were to be recovered through the commodity charge.

Regulation 151 of the *Gas Transmission Regulations provided* that the tariff be redetermined at the service provider's option, but only after a major enhancement but then only after at least three years had elapsed since the last redetermination. Furthermore, Regulation 152 allowed the Corporation to make annual adjustments to the commodity charge for:

- changes in fuel costs;
- increases in labour, materials and services cost (an increase of 75% of the increase in the Consumer Price Index was permitted); and
- any new or increased tax.

We note that, taking into account CPI and fuel cost adjustments, the tariff applying at the time the DBNGP sale *Information Memorandum* was published in mid 1997 was approximately \$1.26/GJ.[3]

1998 tariff

The *Information Memorandum* foreshadowed that the tariff from 1 January 1998 would be \$1.24/GJ, made up of a capacity reservation charge of \$0.97/GJ and a commodity charge of \$0.27/GJ. This was qualified by the statement that the proposed tariff was still uncertain and subject to approval by the AlintaGas Board. In any event, the tariff was to be set at a level which would be consistent with a tariff redetermination conducted under Regulation 151 of the *Gas Transmission Regulations*.

AlintaGas redetermined the DBNGP tariffs because of the stage 2 expansion being completed in 1997 and the 3 year cap expired as at 31 December 1997. In October 1997, it published the

[2] Energy Implementation Group, "*Dampier to Bunbury Natural Gas Pipeline Initial Charges for Gas Transportation*", November 1994.

[3] DBNGP Information Memorandum, August 1997, page 99.

tariffs which were to apply from 1 January 1998. The redetermined full haul firm service (Tranche 1) tariff comprised:

- a capacity reservation charge of $0.917457/GJ; and
- a commodity charge of $0.271971/GJ.

The total full haul firm (Tranche 1) service tariff, at 100% load factor, was $1.189428/GJ.

The AlintaGas redetermination drew upon the initial tariff setting by the Energy Implementation Group in 1994. It used the same cost of service method with an asset base comprising the Energy Implementation Group's depreciated historic cost asset base, plus capital expenditure between 1 January 1995 and 31 December 1997, less depreciation over the same period. The weighted average cost of capital used in determining the return on the asset base was updated for changes in the nominal risk free rate of interest, the cost of debt, and the corporate tax rate.

Late in 1997, the Government enacted the *Dampier to Bunbury Natural Gas Pipeline Act 1997* to facilitate the sale of the Pipeline.

Section 51 of the *Dampier to Bunbury Pipeline Act 1997* allowed the State to make regulations to give effect to the purposes of the Act. Specifically, section 51(2)(b) allowed the State to impose pricing requirements for the DBNGP.

Regulation 35 prescribed the tariff for full haul T1 service as at 1 January 1998 as being comprised of:

- a capacity reservation charge of $0.917457/GJ; and
- a commodity charge of $0.271971/GJ.

The total full haul firm (Tranche 1) service tariff, at 100% load factor, was $1.189428/GJ.

The 1998 charges set out in Regulation 35 were identical to the charges redetermined under the *Gas Transmission Regulations to apply from 1 January 1998.*

Schedule 39 of the asset sale agreement, a copy of which is **attached** as **Attachment 1** reflected the prescribed tariffs for 1998.

1999 tariff

Regulation 35(3) of the *Dampier to Bunbury Natural Gas Pipeline Regulations 1998* set out the tariff to apply to full haul firm (Tranche 1) service on the DBNGP from 1 January 1999. This comprised:

- a capacity reservation charge of $0.822743/GJ; and
- a commodity charge of $0.271971/GJ.

The total full haul firm (Tranche 1) service tariff, at 100% load factor, was \$1.094714/GJ.

Again, Schedule 39 of the asset sale agreement, a copy of which is **attached** as **Attachment 1** reflected the prescribed tariffs for 1999.

It is noted that the 1999 (total) tariff was effectively the "mid-point" between the 1998 tariff of \$1.19/GJ and the tariff to apply from 1 January 2000 which, according to the stated intention of the Government of the day, was to be \$1.00/GJ. This was consistent with the concept indicated in the Information Memorandum, although the figures were different for 1998 and 1999.

2000 tariff

Schedule 39 of the DBNGP Asset Sale Agreement, provided the tariffs Epic Energy expected to apply from 1 January 2000. This assumed that an effective access arrangement would be in place as from 1 January 2000. The tariffs were for \$1.00/GJ in zone 9 and \$1.08/GJ in zone 10 in dollars of 2000.

Notwithstanding the provisions in schedule 39 of the asset sale agreement, different tariffs for the DBNGP reference services from 1 January 2000 were legislated for. They were prescribed under the *Gas Pipelines (Privatised DBNGP System)(Transitional) Regulations 1999* made pursuant to the *"repealed access scheme"* as prescribed under s.51 of the *Dampier to Bunbury Pipeline Act 1997. These were to remain* until the approval of the proposed Access Arrangement for the DBNGP.

In accordance with the Regulations, the Governor, on the advice of the Minister for Energy, prescribed a tariff of \$1.00/GJ for zones 9 & 10 in 2000 in the *Gas Pipelines (Privatised DBNGP System)(Transitional) Regulations 1999* promulgated at 3.45pm on 31 December 1999 (those tariffs also did not adopt the zonal approach but continued the distance based charging approach of the GTRs). He subsequently amended those regulations to both enable Epic Energy to pick up the GST component and to provide only for the escalation of the Commodity Charge and only by the formula provided in Schedule 1 to the Access Manual (the same formula as applies in the GTRs). This has produced a tariff in 2002 of:

- Zones 9 & 10: \$1.019021/GJ

The above information seeks to demonstrate that:

1. not only has there been a significant actual reduction in tariffs over time, particularly since the DBNGP was sold to Epic Energy but even more in real terms; but
2. Epic Energy's legitimate business interests have been adversely affected as a result of the delayed implementation of the access arrangement which reflects Schedule 39 in the Asset Sale Agreement.

The comments by the Court at paragraph 219 of the Court Decision, referred to above, are correct if they assume that the tariffs proposed by the Regulator in the draft decision are to remain. However, this can not be the case given that the Court has determined that the Regulator's draft decision is affected by fundamental errors of law.

In reality, it is not Epic Energy who is enjoying the continued advantage of the tariffs established under the former regime – the continued advantage is being enjoyed by all Users of the DBNGP, particularly having regard to the tariffs proposed in Schedule 39 of the Asset Sale Agreement and as proposed by Epic Energy in the Access Arrangement. This advantage is at the expense of Epic Energy who has foregone revenue as a result, directly or indirectly, of the delayed implementation of the Access Arrangement. Further the continued delay in finalising the access arrangement is leading to continued uncertainty in relation to the future expansion of the DBNGP, which in turn has a direct impact on the expansion of industry dependent on that additional capacity.

The Court's comment therefore needs to be put in its proper perspective.

Epic Energy has written to the Minister for Energy on a number of occasions seeking a review of the tariffs to match those provided in Schedule 39 of the Asset Sale Agreement for the DBNGP. As proposed in the access arrangement, those tariffs were for $1.00/GJ in zone 9 and $1.08/GJ in zone 10 both in dollars of 2000 and escalated at 67% of CPI. If those changes had been made the tariffs in 2002 would be:

- Zone 9: $1.052491/GJ
- Zone 10: $1.136690/GJ

It is also interesting to note that while Epic Energy's business interests have been adversely affected, those of at least one of the major users has benefited, even if one were to ignore any benefits that may be accruing as a result of the delayed implementation of the access arrangement. In this respect, Epic Energy has noted with some surprise that despite the Government securing a reduction in transmission tariffs of more than 27% since 1997 (through a combination of the asset sale agreement and legislation), it has approved tariff increases for retail tariffs for AlintaGas, one of the major Users of the DBNGP, of 3.5% in 2001 and 3.00% in 2002. If these increases were applied to the tariff for the DBNGP prescribed in the Regulations, the tariffs for zones 9 & 10 in 2002 would be:

- Zones 9 & 10: $1.066050/GJ

Epic Energy also notes the recent announcement of the Minister of Energy of 11 September 2002 of an agreement with AlintaGas under which household and small business tariffs (other than residential customers in the South-West Coastal Area which will remain at CPI plus 2%) "will be escalated annually from July 1, 2003 at CPI", again not reflecting the savings that have already been passed onto AlintaGas from the reductions in gas transmission tariffs. Nor is it consistent with Epic Energy's proposed escalation of 67% of CPI. AlintaGas has already been the beneficiary of an actual reduction in the tariffs on the DBNGP from 1997 of 27%, but at no stage has that been passed on to AlintaGas' retail customers.

It is also important to note that Epic Energy's return on the DBNGP for 2001 was approximately 2.0%, yet AlintaGas announced on 1 August 2002 that for the **6 month period** ending 30 June 2002 it had a 33.4% increase in profit with a profit of $21.4million on revenue of S177.5million, giving a return (calculated on a similar basis) of 12.1%.

The fact that the government to date has chosen to allow significant increases in AlintaGas' tariffs (now coupled with ongoing full CPI increases) compared to the limited increase it has allowed for Epic Energy (1.9% - which is well below CPI increases for the period - compared with 6.6% for AlintaGas) when AlintaGas is making significant and increasing profits, is incongruous.

Section 94 of the standard contract appended to the *DBNGP Access Manual* provided that, for new contracts entered into in that form, from 1 January 2000, the full haul firm (Tranche 1) service tariff was to comprise:

- a capacity reservation charge of $0.728029/GJ; and
- a commodity charge of $0.271971/GJ.

These charges sum to $1.000000/GJ.

This is consistent with the intentions of the State, intimated at the time of the sale and expressed in the *Information Memorandum* as:

> *"The IGRT [Indicative Global Reference Tariff] analysis has considered a number of possible price paths that would support a tariff on a price capping basis of $1.00/GJ, nominal at 1 January 2000. It is the Government's expectation that the tariff will be of that order at that time."*[4]

As a final point, it is important to note that the Regulator appears to have relied upon the transitional regime tariffs in an inconsistent or asymmetric manner. This is evident in certain amendments contained in the draft decision. In his amendment #63 in the draft decision, he requires the "tariff structure proposed by Epic Energy to be amended to ensure that there is no increase in the total gas transmission charges under the reference tariff relative to the total charge that Users or Prospective Users would have paid under a contract for the T1 Service entered into under the Gas Transmission Regulations 1994 or the Dampier to Bunbury Pipeline Regulations 1998."[5] *In this respect, it is apparent that he has sought to rely on the transitional arrangements as acting as a cap on the level of tariffs.*

However, in the setting of the overall level or quantum of the reference tariffs for the full haul service, the Regulator has not sought to have regard to the transitional tariffs acting as either a "cap" or a benchmark tariff. This is an inconsistent approach.

[4] DBNGP Information Memorandum, page 107.

[5] Draft Decision Amendment 63, page B251

Attachment 1

Schedule 39 of Asset Sale Agreement

SCHEDULE 39
Buyer's Proposed Tariff Rates and Path
(Schedule 5 Paragraph 9)

[Buyer Insertion required - to set out details as required by Paragraph 9 of Schedule 5]

This information is provided by Epic in relation to:

SCHEDULE 39
Buyer's Proposed Tariff Rates and Path
(Schedule 5 Paragraph 9)

INTRODUCTION

Epic's proposed tariff rates and path have been structured to be in compliance with the State of Western Australia's draft Transitional and Long Term Access Regimes and the National Access Code ("NAC"). The proposed tariff rates and path in conjunction with the access principles to be defined by Epic in the Access Arrangement for the DBNGP are expected to form the basis for the certification of the DBNGP by the National Competition Council ("NCC") as an effective access regime.

OBJECTIVES

In setting its tariff principles Epic has focussed on satisfying four tariff objectives:

- Promote greater gas throughput and development of the gas industry in Western Australia.
- Consistent with the regulatory review process, share the benefit of load growth with all customers through tariff reductions.
- Incorporate a zonal distance based element to the tariffs to more accurately reflect costs.
- Simplify the existing tariff structure and standardise tariffs for transportation services.

GENERAL PRINCIPLES AND GUIDELINES

The following general principles and guidelines are incorporated in Epic's Final Bid:

- Existing GTR contracts will continue to have full contractual effect for the duration of each contract. The tariff basis for the existing GTR contracts will be as prescribed by the draft Transitional and Long Term Access Regimes.
- The Alcoa contract is considered an exempted contract for purposes of the GTR.
- Epic has the right to negotiate with potential and existing shippers the terms and conditions of service, subject to a fallback mechanism to be incorporated in the DBNGP Access Arrangement.

- The capacity of the DBNGP can be expanded to meet the requirements of new loads, provided that the capacity enhancements are commercially viable.
- The DBNGP Access Arrangement will incorporate provisions which will allow Epic to enhance the operating efficiency and utilisation of the asset.
- The proposed tariffs provide for the recovery of prudently incurred costs, including a reasonable rate of return on the investment over the full term of the asset economic life.
- The proposed tariffs reflect the costs of providing service to the shippers.
- From 1 January 2000 onward, Epic will submit to scheduled regulatory reviews where access principles and reference tariff paths will be approved by the regulator under an effective access regime that complies with the NAC.

TARIFF PRINCIPLES

In addition to the general guidelines and principles described above, the proposed tariff path incorporates the following principles:

- From 1 January 2000, the tariff path is based on escalation at a percent of CPI.
- From 1 January 2000, the tranche methodology is not used to define the capacity of the pipeline.
- From 1 January 2000 prudent discounts (as defined by the National Access Code) which benefit all shippers by improving the utilisation of the asset, may be recovered from the other users of the asset.
- New shippers and existing shippers which switch to the reference service, will provide for their fuel in-kind.
- Certain reference tariff setting principles, to be included in the DBNGP Access Arrangement, will be fixed for a period which exceeds the scheduled regulatory review periods including capital recovery mechanism, risk premium on WACC and asset life.
- The capital recovery mechanism will be structured such that it is consistent with the efficient growth of the markets over the economic life of the asset.
- The tariff structure includes zonal tariffs reflecting the cost of providing service.

Signatures

SCHEDULE 39
Buyer's Proposed Tariff Rates and Path
(Schedule 5 Paragraph 9)

PROPOSED TRANSPORTATION SERVICES

Epic will continue to offer the existing T1, T2 and T3 reference services during the transition period up to 31 December 1999 to meet the Transitional Access Regime.

Epic's proposed tariff path from 1 January 2000 onwards is based on the underlying principles embodied in the National Access Code.

Epic will offer two classes of transportation service:

- Forward Haul Firm Transportation Service (T1 equivalent reference service); and
- Forward Haul Interruptible Transportation Service(T3 equivalent reference service)

An Authorised Overrun Service and a Shipper Facility Service would also apply although incentives would be put in place to encourage uniform customer conduct on the system (e.g. unauthorised overruns/gas imbalances).

Epic will also offer a backhaul transportation service.

FORWARD HAUL FIRM TRANSPORTATION SERVICE

Epic proposes a standard tariff for Forward Haul Firm Transportation Service for all existing contracts and new contracts (excluding Negotiated Contracts such as Alcoa). The proposed Standard Forward Haul Firm Tariff is $1.00/gj on a combined basis (at 100% load factor) based on a receipt point upstream of the inlet side of CS1 and delivery point at Kwinana Junction ("BP-KJ") from on 1 January 2000. Yearly tariff increases are proposed to be limited to 2/3 (67%) of annual inflation (CPI).

The Forward Haul Firm Tariff would represent a substantial discount to the current T1 tariffs of $1.189/GJ for 1998 and $1.095/GJ for 1999. The reduction in transportation tariffs would increase the demand for gas by contributing to significant real reductions in the delivered gas price.

The Forward Haul Firm Tariff would be levied as three separate charges all of which will be zone-distance based:

- Pipeline Capacity Charge (MDQ based)
- Compression Charge (MDQ based)
- Pipeline Commodity Charge (throughput charge only)

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SCHEDULE 39
Buyer's Proposed Tariff Rates and Path
(Schedule 5 Paragraph 9)

The Pipeline Capacity Charge will be zone-distance based. The distance between each compressor station will represent one zone with Kwinana Junction also treated as a "compressor station" for this purpose.

In total there will be 10 "Pipeline" zones which will be of equal size (approximately 150km each). A summary of the Pipeline Zones and the Pipeline Capacity Charge per zone is set out in the following table:

Zone	Pipeline Zone	1 January 2000 Pipeline Capacity Charge $/gj (MDQ based)
1	KP0 to CS2	$0.0629
2	CS2 to CS3	$0.0629
3	CS3 to CS4	$0.0629
4	CS4 to CS5	$0.0629
5	CS5 to CS6	$0.0629
6	CS6 to CS7	$0.0629
7	CS7 to CS8	$0.0629
8	CS8 to CS9	$0.0629
9	CS9 to KJ	$0.0629
10	BP-KJ to MLV 157	$0.0629
Full Haul Cap	KP0 to BP-KJ	$0.572

The Compression Charge will be zone-distance based. Excluding CS1 which is part of the gas header, there will be eight compression zones based on the location of existing compressors CS2 to CS9. Shippers will be able to use their own compression and avoid compression charges. The compression charge per zone will be $0.0392/gj (MDQ based) and will be capped at $0.285/gj for a full haul through all eight compression stages (KP0 to BP-KJ)

SCHEDULE 39
Buyer's Proposed Tariff Rates and Path
(Schedule 5 Paragraph 9)

The Pipeline ~~Commodity~~ Charge will be throughput based at $0.148/gj.

Recognising the need for flexibility and commercially acceptable outcomes, Epic and a shipper can agree to vary the Standard Forward Haul Firm Tariff and escalation rate to meet a shippers particular circumstances.

Epic believes that a tariff structure that is zone-distance based best meets the needs of the current and future Western Australian gas market participants as it promotes gas-on-gas competition while it reflects underlying distance based cost drivers. In particular shippers can decide if they wish to introduce gas above or below a compressor station and would therefore potentially avoid one compression charge if gas producers can more efficiently compress gas into the pipeline system.

FORWARD HAUL (INTERRUPTIBLE SERVICE)

Epic proposes a standard tariff for Forward Haul Interruptible Transportation Service for existing and new customers for incremental or new loads based on the Firm Service tariff. Epic expects a market to develop for Interruptible services and that the rate paid will be negotiated.

AUTHORISED OVERRUN CHARGES

Authorised Overruns will have priority to the Interruptible Service and therefore Authorised Overruns would be charged at a premium (10-20%) to the published Standard Forward Haul Interruptible Tariff to reflect the priority to be given to Authorised Overruns.

SHIPPER FACILITIES

Epic proposes nominal operating and maintenance charges which will be cost reflective in respect of Shipper Facilities including laterals and metering stations. Epic will also contribute to capital if required and shippers will be charged for capital recovery for the installed Shipper Facilities.

Signatures

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Buyer's Proposed Tariff Rates and Path
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SUMMARY

Reference Tariff Assumptions

Firm Transportation

Transition Period	1998 total (Full-haul combined tariff)	$1.189/GJ
	1999 total (Full-haul combined tariff)	$1.095/GJ
Post Transition (NAC)	2000 (nominal $)	$1.000/GJ (Perth customers @ 100% load factor)

Compression Charge (MDQ based)	$0.285/GJ
Pipeline Capacity Charge (MDQ based)	$0.572/GJ
Pipeline Commodity Charge (Throughput)	$0.148/GJ
Total (combined tariff)	$1.000/GJ (Customers with delivery points after Kwinana Junction pay a tariff higher than $1.000/GJ

Escalation	Tariffs escalation	67% CPI

Interruptible Transportation

Transition Period	1998 & 1999	Binding as per Regulations
Post Transition (NAC)	2000 (nominal $)	Firm Transportation Rate (see above)

Part Haul

Transition Period	Both capacity & commodity charges distance based by kilometre in 1998 and 1999
Post Transition (NAC)	Both capacity & commodity charges distance based by zone post-2000

Discounts

Contracted Discounts	Wesfarmers LPG	50% discount on total tariff
Special Discounts	Nil	

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