TUBRIDGI PIPELINE SYSTEM
Public Forum

Dr Ken Michael AM

Independent Gas Pipelines Access Regulator

Rydges Hotel

Wednesday 6 September 2000

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Welcome / Introduction

- Purpose to consider Draft Decision.
- Provide clarification.
- Comments to assist Final Decision.
- Transcript of meeting will be available.

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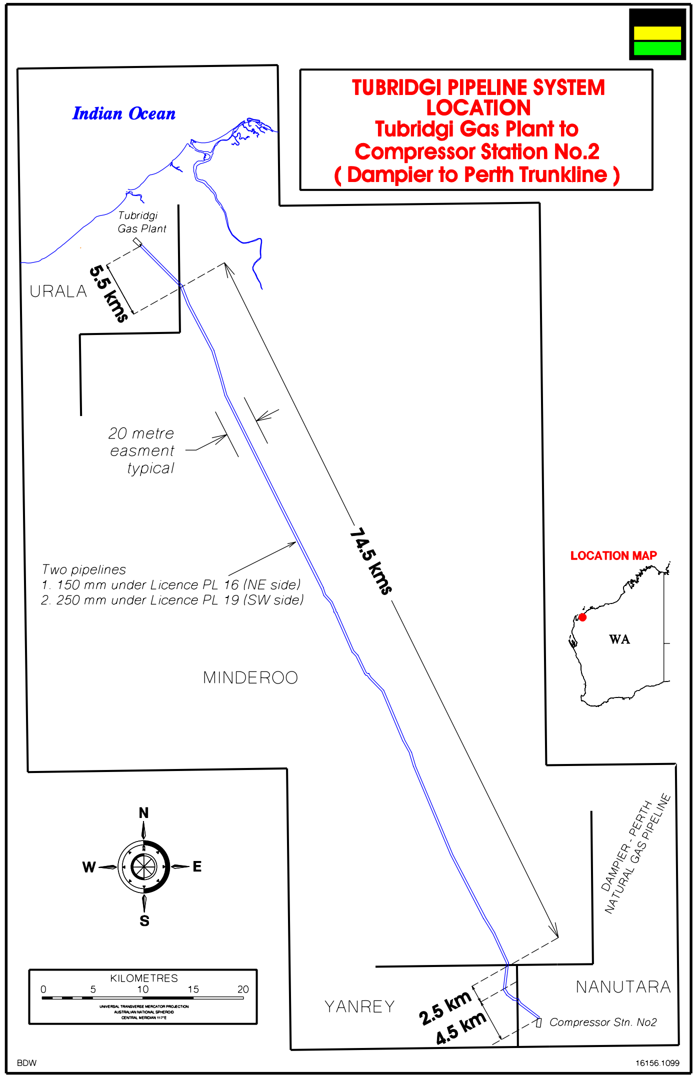
Program

2:00 pm	Welcome – Dr Ken Michael
2:05 pm	Overview – Dr Ken Michael
2:15 pm	Key Issues – Dr Ray Challen
2:45 pm	Afternoon Tea
3:00 pm	Open Forum
5:00 pm	Close



Tubridgi Pipeline System

Overview

- Tubridgi AA raised particular issues:
  - Throughput uncertainty
  - Valuation of ICB
  - Depreciation policy
  - Capital redundancy
- Other areas also attracted attention.

Throughput Uncertainty

- Throughput Uncertainty is the basis for:
  - accelerated depreciation; and
  - has a significant impact on reference tariffs.
- The Draft Decision calls for clarification of the throughput forecast.

Initial Capital Base

- The Pipeline System is relatively recent.
- ICB based on 120 TJ/d.
- Current throughput about 30 TJ/d.
- Capital redundancy may be relevant.
- ICB set at $16.9 million.

Rate of Return

- Rate of Return has been set using CAPM.
- Risk allowed is at the higher end of the spectrum.
- Return on Equity 14.2% (nominal post-tax)
- WACC 8.2% (real pre-tax)

Reference Tariff

- The estimated Reference Tariff is 22.9 cents/GJ
- This compares with 42.7 cents/GJ sought.
- Difference mainly attributable to a different throughput assumption.

Other Matters

- The Draft Decision also seeks amendments in respect of other matters including:
  - the provision of a backhaul service;
  - changes to proposed terms and conditions; and
  - changes to the trigger mechanism for a review of the Access Arrangement.
- Dr Challen to provide a more detailed presentation on particular issues.

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Reference Services and Reference Tariffs

Dr Ray Challen
Environmental Resources Management Australia

Reference Services

The Tubridgi Parties have proposed a single reference service comprising a continuous forward haulage service.

Reference Tariffs

Provide the service provider with the opportunity to earn a stream of revenue that recovers the efficient costs of delivering the corresponding reference services:

- operating costs;
- capital costs;
- depreciation costs; and
- a return on capital.

Procedure for Tariff Determination

- Initial capital base
- Capital expenditure
- Non-capital costs
- Rate of return on capital
- Depreciation schedule
- Total revenue
- Revenue allocation across services
- Reference tariff structure
- Incentive mechanisms

Initial Capital Base

- Code provides for the value ascribed to the initial capital base to normally be in the range of the depreciated actual cost (DAC) of assets and the depreciated optimised replacement cost (DORC) of assets.
- General approach of regulators in Australia has been to consider a balance of interests between the service provider and users in selecting a value of the initial capital base within this range.

Initial Capital Base (cont.)

Tubridgi Parties' methodology:

- determination of an optimised replacement cost of $26.092 million based on replacement of the existing two pipelines of the Tubridgi Pipeline System with a single pipeline of the same nominal capacity;
- straight line depreciation over technical asset lives to derive a DORC value of $23.755 million.

Initial Capital Base (cont.)

Regulator's revision:

- determination of an optimised replacement cost of $22.500 million assuming different unit rates of pipeline construction than used by the Tubridgi Parties;
- depreciation of this value using an accelerated depreciation schedule consistent with the "forward looking" depreciation proposed by the Tubridgi Parties for the Access Arrangement Period, giving a capital base valuation of $16.943 million.

Initial Capital Base (cont.)

Redundant capital policy:

- The Access Arrangement should be amended to include a redundant capital policy that provides for the capital base to be reduced at the end of the access arrangement period in accordance with pipeline throughput and the use of pipeline assets at that time.

Capital Expenditure

- None proposed by the Tubridgi parties for the access arrangement period.

Non-Capital Costs

- Proposed non-capital costs of $495,000 per annum.
- Accepted by the Regulator subject to further substantiation of some cost line items prior to issue of a final decision.

Depreciation

- Proposed accelerated depreciation.
- Straight line depreciation over a 20 year remaining life of the pipelines and meter stations assets and 15 year remaining life of SCADA and communications assets.
- Accepted by the Regulator given uncertainty over future use of the pipeline system.

Rate of Return

Code requirements:

- Provide for a return on capital investment that is commensurate with prevailing conditions in the market for funds and the risk involved in delivering the reference service.
- Weighted average cost of capital (WACC) should be calculated by reference to a financing structure that reflects standard industry structures for a going concern and best practice.

Rate of Return (cont.)

- Tubridgi Parties utilised the capital asset pricing model to derive a real pre-tax WACC of 8.75 percent.
- The Regulator has adopted a real pre-tax WACC of 8.2 percent for the purposes of assessing the Tubridgi Parties' proposed reference tariff.
- Difference arises primarily from reductions to the corporate taxation rate.

Total Revenue

Total Revenue ($million)

	99/00	00/01	01/02	02/03	03/04
Proposed revenue	3.821	3.799	3.775	3.746	3.713
Revised revenue	2.739	2.669	2.599	2.529	2.459

Reference Tariff

- Tariff structure should be generally at the commercial discretion of the service provider subject to consistency with broad criteria of efficiency and equity.
- Regulator accepted the cost allocation methodology and tariff structure proposed by the Tubridgi Parties.
- Regulator revised the reference tariff to reflect a different forecast of gas throughput over the access arrangement period.

Reference Tariff (cont.)

Throughput Forecast (Petajoules)

	99/00	00/01	01/02	02/03	03/04
Proposed	11.7	10.4	6.2	2.8	1.1
Revised	12.3	12.1	7.9	6.6	6.2

Reference Tariffs (cont.)

	Capacity ($/GJ MDQ/day)	Throughput ($/GJ)	Indicative Total ($/GJ)
Proposed	0.322	0.105	0.427
Revised ex GST	0.173	0.056	0.229
Revised incl. GST	0.190	0.062	0.252

Tariff Variation and Incentive Mechanisms

- Regulator accepts escalation of tariffs in accordance with changes in the CPI.
- Mechanisms for triggering a review of the access arrangement and rebatable revenue provisions should be made consistent with objectives for incentive mechanisms as set out in the Code.