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DAMPIER TO BUNBURY NATURAL GAS PIPELINE - PROPOSED REVISIONS TO THE ACCESS ARRANGEMENT

Alinta Pty Ltd (Alinta) appreciates the opportunity to comment on the proposed revisions to the Access Arrangement for the Dampier to Bunbury Natural Gas Pipeline (DBNGP), which were submitted by Dampier Bunbury Pipeline (DBP) on 1 April 2010.

At this time, Alinta has commented only on certain issues arising from DBP's proposed revised Access Arrangement, proposed revised Access Arrangement Information (AAI) and submissions. The absence of a comment on any specific issue should not be taken to indicate that Alinta supports, or does not support, that particular aspect of DBP's proposed revised Access Arrangement.

Summary of Alinta's views

A summary overview of Alinta's submission is provided below, with Attachment A discussing each of the issues below in more detail. Further, Attachment B provides comments on the terms and conditions on which DBP proposes to offer to provide the R1 Reference Service.

2004 Contractual Arrangements

As the Authority would be aware, in 2004 DBP and DBNGP Shippers entered into critical arrangements of a contractual nature (2004 Contractual Arrangements) outside the National Gas Code but clearly linked to the Code and any successor regime, including the National Gas Law (NGL) and National Gas Regulations (NGRs) (Applicable Regime).

These arrangements were critical in re-commercialising and debottlenecking the DBNGP, but resulted in existing shippers paying more for existing capacity than they would under the Applicable Regime. The essential elements of the arrangements are publicly available on DBP's website as part of DBP's T1 Standard Shipper Contract, which DBP must offer to any existing or potential shipper that requires access to expanded capacity on the DBNGP.

The 2004 Contractual Arrangements have been instrumental in ensuring that pipeline services provided by the DBNGP and the tariffs paid for those pipeline services have supported investment in the DBNGP in a manner that is entirely consistent with the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas. That is, the effect of the special circumstances of the DBNGP, which are outlined in more detail below, are entirely consistent with the national gas objective set out in clause 23 of the NGL.

The links with the Applicable Regime are an essential part of the 2004 Contractual Arrangements because the arrangements provide for the T1 Service provided to shippers to return to pricing under the Applicable Regime in 2016. The links with the Applicable Regime are necessary to ensure that the transition of the T1 Service to pricing under the Applicable Regime is meaningful and is based on the elements that were agreed by the parties in 2004. There is no basis on which those elements should and can be excluded under the Applicable Regime.

DBP has contracted with Alinta, and most 2004 shippers under the T1 Standard Shipper Contract, to have a T1 Service as part of its access arrangements for 2005 and 2016. Consequently, the absence of the T1 Reference Service in the proposed revised Access Arrangement between 2011 and 2015 is not consistent with the contractual obligations entered into by DBP under the T1 Standard Shipper Contracts.

To the extent that the 2004 Contractual Arrangements have supported outcomes that are entirely consistent with the objective of the NGL, Alinta considers that the fact that DBP is now proposing to substantially alter these arrangements must be carefully examined by the Authority in assessing DBP's access arrangement proposal.

Reference services

Irrespective of DBP's contractual obligations under the 2004 Contractual Arrangements, Alinta's fundamental concern is that under its proposed revised Access Arrangement, DBP intends offering only a single reference service, the full haul R1 Reference Service. Alinta considers that no evidence has been provided by DBP to support a conclusion that the proposed R1 Reference Service is a service that is likely to be sought by a significant part of the market.

There is however abundant evidence that the T1 Service (or an equivalent service) is the pipeline service that is, and will be, sought by an overwhelming majority of users and/or prospective users of the DBNGP. Consequently, Alinta considers that in order to comply with the National Gas Rules (NGRs), the T1 Service (or an equivalent) must be offered by DBP as a reference service in a revised Access Arrangement proposal for the period 2011-2015.

Further, to the extent that the P1 Service and the B1 Service have previously been considered by the Authority under the National Gas Code as being services that are likely to be sought by a significant part of the market, Alinta considers that there is no basis for concluding this cannot reasonably be expected to remain the case for the period 2011-2015. Consequently, Alinta considers that the P1 Service and the B1 Service (or equivalents) must also be offered by DBP as reference services in a revised Access Arrangement proposal for the period 2011-2015 in order to comply with the NGRs.

Finally, as a result of the Gas Supply and Emergency Management Committee's recommendations, Alinta considers that a service where gas is delivered from the Mondarra storage facility into the DBNGP and transported to Outlet Points downstream of CS9 is likely to be sought by a significant part of the market in the period 2011-2015, and therefore should be included as a new reference service in a revised Access Arrangement proposal for the period 2011-15.

Alinta does not agree with DBP's claim that the proposed R1 Reference Service will be more attractive to shippers, and will encourage shippers to access capacity on the DBNGP. Specifically, Alinta considers that for at least the following reasons, the proposed R1 Reference Service is significantly less attractive than the T1 Service and/or the T1 Reference Service.

- Omission of outer imbalance band and outer hourly peaking band.
- Significant increase in penalties for overrun, imbalance, hourly peaking excursions.
- Requirement that shippers agree to an Inlet Sales Agreement to nominate on behalf of another shipper.
- Monthly cashing out of imbalances.
- Significant expansion of the circumstances in which DBP can refuse to accept or deliver gas, or to curtail, without liability.
- Different methodology for determining capacity quantities.
- Absence of a concept equivalent to the Aggregated T1 Service.

Given existing T1 Service shippers can gain access to further T1 Service by having DBP expand the capacity of the DBNGP under clause 16 of their shipper contracts, and that new shippers must be offered similar rights - obligations that were insisted on by the ACCC and the State in 2004 - Alinta considers it highly improbable that DBP's proposed R1 Reference Service could reasonably be expected to be sought by a significant part of the market for DBNGP pipeline services in the period 2011-2015.

Capital expenditure

DBP's claim that its actual and forecast capital expenditure meets the requirements of NGR 79 does not appear to be supported: in any detail in the information contained in its proposed revised AAI or submissions (public versions); or by independent analysis or review of its actual and/or forecast capital expenditure; or by benchmark comparison to other natural gas transmission businesses.

- Actual capital expenditure has not been shown to satisfactorily meet the tests in NGR 79(1), and the difference between actual and forecast capital expenditure for the period 2005-2010, of around $616 million (or 53 per cent) is not sufficiently explained.
- Actual capital expenditure has not been shown to satisfactorily meet the tests in NGR 79(2).
  - Alinta considers that the 2004 Undertaking cannot be relied on to justify actual expansion related capital expenditure under NGR 79(2)(c)(iii).

- No direct and specific evidence appears to have been provided as to the basis on which actual capital expenditure might satisfy NGR 79(2)(a).

- It is unclear whether DBP's forecast of capital expenditure for the period 2011-2015 complies with NGR 74(2).

Capital contributions

It appears to Alinta that the practical manner in which DBP has calculated the return on its capital base and return of capital does not align with the detail of the description contained in either the access arrangement proposed or the proposed revised AAI. Alinta suggests that the Authority may choose not to approve DBP's proposal to roll capital contributions into the capital base as this would be consistent with the approach to accounting for capital contributions in DBP's Proposed Tariff Model.

Alinta is also concerned at the lack of detail around the manner in which capital contributions may be calculated, and the very broad discretion afforded to DBP under the terms and conditions of the proposed R1 Reference Service. As a specific example, Alinta considers that the rate of return on these assets and the manner in which an amortised payment is calculated should require the pipeline operator to apply the rate of return that has been determined as part of an approved Access Arrangement.

Rate of return

DBP is proposing that a real pre-tax rate of return of 10.76 per cent be used in determining a return on its projected capital base for the period. This compares with a real pre-tax rate of return that applied for the 2005 Access Arrangement of 7.24 per cent, and represents an increase of almost 49 per cent.

Alinta notes that the Authority recently determined that the real pre-tax rate of return for the Goldfields Gas Pipeline (GGP) should be 7.78 per cent. That DBP's proposed rate of return of 10.76 per cent should be almost 300 basis points (or 38 per cent) higher than that for the GGP is concerning given the prevailing conditions in the market for funds and the risks involved in providing reference services on the GGP and the DBNGP could reasonably be expected to be similar, if not the same.

- Alinta considers that the proposed rate of return on capital does not meet the requirement of NGR 87(2)(b) because it appears that DBP has adopted a methodology for determining a cost of equity that does not use a well accepted financial model.

  The use of alternative financial models was the cause of significant recent debate in relation to the Jemena gas distribution network in New South Wales, where the Australian Energy Regulator did not accept Jemena's use of the Fama-French model, and instead required the rate of return to be calculated using a cost of equity based on the Capital Asset Pricing Model.

- Much of the detail about the manner in which DBP has calculated the cost of debt has been deleted from Submission 9, or if it is contained in attachments to the submission these have not been made publicly available. As a result, it is not possible to comment on whether DBP's cost of debt complies with NGR 74(2).

Operating expenditure

Alinta considers that DBP's claim that its forecast operating expenditure complies with NGR 91(1): does not appear to be supported by information contained in its proposed revised AAI or it submissions does not appear to be supported by: independent analysis or review of its actual or forecast operating expenditure; or any benchmarking comparison to other natural gas transmission businesses.

- There appears to be no discussion of DBP's decision in early 2009 to bring back in-house a significant proportion of the operating and maintenance services that were then contracted out to Westnet Energy Services Pty Ltd. This decision appears to be very relevant to both DBP's actual operating expenditure for the period 2005-2010 and its forecast operating expenditure for the period 2011-2015.
- DBP has not adequately explained why operating costs (excluding fuel gas) in 2009 and 2010 increased by more than 20 per cent from 2008 levels, and in the absence of information on actual level of operating expenditure by category, Alinta is concerned that DBP's decision to bring back in-house operating and maintenance services may have contributed to this increase.
- DBP has not adequately explained why forecast operating expenditure (excluding fuel gas) for 2011 should be almost $16.9 million, or around 26.1 per cent, higher than (estimated) actual operating expenditure (excluding fuel gas) in 2010.
- DBP has not provided any information as to either the forecast volume of fuel gas it expects the DBNGP to require each year in the period 2011-2015, nor the price at which it has assumed it will be able to obtain this volume of fuel gas, and the absence or suppression of this information means that users and prospective users cannot reasonably be expected to form a view on whether the forecast complies with NGR 91(1) and NGR 74(2).

Tariffs

Alinta estimates that DBP's access arrangement proposal would result in an increase of almost 45 per cent in tariff for the prevailing full haul reference service. However, as the proposed R1 Reference Service is a far inferior service to the existing T1 Reference Service, this does not adequately reflect the full transfer of value from shippers to DBP as the operator of the DBNGP.

Further, increasing the proportion of the reference tariff recovered from the capacity component from 80 per cent for the T1 Reference Tariff to 95.4 per cent for the proposed R1 Reference Tariff would result in a reduction of around 75 per cent in DBP's exposure to pipeline volume risk (i.e. from 20 per cent to less than 5 per cent). The effect is to provide far greater revenue certainty to DBP, and significantly weakens the incentive DBP currently has to efficiently optimise pipeline throughput. The financial impact on users of the DBNGP who operate at less than a 100 per cent load factor is even more significant

It is unclear to Alinta why in setting the reference tariff for the proposed R1 Reference Service, DBP has elected to allocate **all** costs to the proposed R1 Reference Service, instead of, as it is required to do by NGR93(1), first allocating costs (and revenue) on the basis that they are directly attributable to providing the proposed R1 Reference Service and existing services, and then to allocating any remaining costs between the proposed R1 Reference Service and existing services on the basis of a methodology determined or approved by the Authority.

At this stage, and based on the information provided by DBP, it would appear to Alinta that DBP's approach in allocating costs to the proposed R1 Reference Service is fundamentally flawed and clearly inconsistent with the requirements of NGR 93.

DBP is also proposing to include as a Fixed Principle that, during the period commencing on 1 July 2005 and ending on 31 December 2015, revenue earned by it from the sale of full haul services that is in excess of that which would have been earned had those services been priced at the prevailing reference tariff (and revenue from other non-full haul services) not be taken into account when setting the R1 Reference Tariff.

Alinta considers that this Fixed Principle has no application to the setting of the reference tariff for the proposed R1 Reference Service, and that it is critical that the Fixed Principle **only** be retained if **at least** a T1 Reference Service, which is substantially the same as the T1 Reference Services in the 2005 Access Arrangement, is offered in the revised Access Arrangement for the period 2011-2015, and that the Fixed Principle must only apply to the relationship between the T1 Reference Tariff (as properly priced under the NGR) and the tariff under the 2004 Contractual Arrangements.

Tariff Variation Mechanism

Alinta considers that in the absence of evidence to the contrary, regulatory precedent suggests that the objectives of the NGR and internal consistency in an access arrangement proposal will be best achieved by applying as the consumer price index (CPI), the Consumer Price Index (All Groups, Eight Capital Cities) for the period 2011–2015.

If this is the case, the CPI Formula Variation in DBP's Tariff Variation Mechanism (and the financial estimates underpinning DBP's proposed revised Access Arrangement, proposed revised AAI and Proposed Tariff Model for the period 2011–2015) should be amended to be based on the Consumer Price Index (All Groups, Eight Capital Cities).

Alinta notes that there is now also significant uncertainty as to whether the Carbon Pollution Reduction Scheme (CPRS) (or a similar scheme) will be introduced, and that the Tax Changes Variation Mechanism proposed by DBP may not be consistent with the requirements of NGR 97(1). As a result, Alinta considers that the Authority should require that:

- no allowance for costs that may be associated with a future CPRS should be made in DBP's forecast operating expenditure for the period 2011–2015; and

- the Tax Changes Variation Mechanism component of the tariff variation mechanism be amended so as to provide a mechanism through which DBP is allowed to pass through the costs that might be incurred under a CPRS (or similar scheme); and
- the definition of Tax Change be amended accordingly.

Alinta considers that the New Cost Pass Through Variation mechanism is unreasonably broad, and in any event does not meet the requirements set out in NGR 97(1) for a tariff variation mechanism. As a result, Alinta considers that the Authority must reject the proposed New Costs Pass Through Variation mechanism in DBP's proposed tariff variation mechanism.

Proposed R1 Terms and Conditions

As noted earlier, Alinta considers that there is abundant evidence available that the T1 Service (or an equivalent service) is the full haul pipeline service that is, and will be, sought by an overwhelming majority of users and/or prospective users of the DBNGP. Consequently, Alinta considers that the T1 Service (or an equivalent) must be offered by DBP as a reference service under the access arrangement proposal for the period 2011-2015.

To the extent that the revised Access Arrangement for the period 2011-2015 includes a T1 Reference Service that was substantially the same as the existing T1 Reference Service (and therefore the T1 Service), Alinta considers that the matters raised in respect of capital contributions must still be addressed. Further comments on the terms and conditions on which the proposed R1 Reference Service would be offered by DBP to the market are provided in Attachment B.

Capacity transfers

Alinta considers that the requirement at Clause 6.3(a) that the Operator's consent to a transfer of Contracted Capacity to a Third Party will be conditional upon the Third Party complying with the Queuing Requirements in clause 5.4 is must be rejected.

Should the Authority require further information on any of the above issues, or those discussed in the attachment, I can be contacted on 9486 3749.

Yours sincerely

Corey Dykstra
Manager Regulatory Affairs
Alinta Pty Ltd

Att.

ATTACHMENT A

DAMPIER BUNBURY PIPELINE - PROPOSED REVISIONS TO THE ACCESS ARRANGEMENT

Introduction

Alinta Pty Ltd (Alinta) appreciates the opportunity to comment on the proposed revisions to the Access Arrangement for the Dampier to Bunbury Natural Gas Pipeline (DBNGP), which were submitted by Dampier Bunbury Pipeline (DBP) on 1 April 2010.

At this time, Alinta has commented only on certain issues arising from DBP's proposed revised Access Arrangement, proposed revised Access Arrangement Information (AAI) and submissions. The absence of a comment on any specific issue should not be taken to indicate that Alinta supports, or does not support, that particular aspect of DBP's proposed revised Access Arrangement.

Information requirements for Access Arrangement Information

Section 2 of DBP's Submission 1 argues that the specific content requirement for Access Arrangement Information (AAI) is governed by NGR 42(2), and that NGR 42(1) relates only to the quality of the information provided. If DBP's interpretation of NGR 42(1) and (2) were accepted, Alinta believes that the effect would be to unreasonably limit the scope of the information that would otherwise reasonably be required to be provided as part of the AAI under NGR 42(1) and NGR 43(1).

Alinta considers that the interpretation ascribed to NGR 42(1) and (2) by DBP cannot be supported. The plain meaning and intent of NGR 42(1) and NGR 43(1) is clearly to require the provision of all information in the AAI that is reasonably necessary to understand, in particular, the basis and derivation of the various elements of the access arrangement or proposal. NGR 42(2) merely provides that, as part of that general obligation, particular information expressly required by the National Gas Law and Rules must be provided in the AAI.

The potentially perverse outcome of DBP's interpretation of NGR 42(1) and (2) is demonstrated by its proposed revised AAI, which at paragraph 1.3 purports to contain all information that is necessary for users and prospective users of the DBNGP to understand the background to the access arrangement proposal, and the basis and derivation of the various elements of the access arrangement proposal.

It is however patently clear that DBP's proposed revised AAI does not contain all information that is necessary for users and prospective users of the DBNGP to understand the background to the access arrangement proposal, and the basis and derivation of the various elements of the access arrangement proposal. As a simple example, Alinta considers that DBP's AAI does not adequately explain the basis or derivation of forecast operating expenditure for the period 2011-20015. Detailed reasons for why Alinta considers this to be the case are provided later in this document. Importantly, no evidence is provided in the proposed revised AAI itself to demonstrate that DBP's forecast of operating expenditure satisfies the test in NGR91(1).

At paragraph 1.4 of Submission 1, DBP states that it has filed additional submissions (presumably Submissions 1 to 12) to assist the Authority in assessing the access arrangement proposal and to address the categories of information requested in the Regulatory Information Notice (RIN). This statement appears to imply that DBP considers that Submissions 1 to 12 do not form part of its proposed revised AAI. If these submissions were not provided by DBP as part of its proposed revised AAI, then it reasonably follows that these submissions would therefore not be bound by the requirements of the NGRs.

If Alinta's presumption noted above is correct, Alinta considers that such an approach of including significant information (or what would presumably constitute significant information had the information not been deleted) in submissions where the submitter may consider such submissions not to form part of its proposed revised AAI (or that it does not intend to form part of its AAI), is likely to be inconsistent with the obligation imposed by NGR 42(1).

Alinta considers that the interpretation ascribed to NGR 42(1) and (2) by DBP results in a perverse outcome that is clearly inconsistent with the national gas objective set out in section 23 of the NGL. Alinta is concerned that if DBP's narrow interpretation of NGR 42(1) and (2) is not challenged, it risks establishing a precedent that has the potential to significantly undermine the objective of the NGL, being to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.

Alinta considers that the Authority must enforce the plain meaning of NGR 42(1) and (2), and require DBP to submit an AAI that endeavours to satisfy the requirements of NGR 42(1), such that the AAI contain all information that is reasonably necessary for users and prospective users of the DBNGP to understand the background to the access arrangement proposal, including the basis and derivation of the various elements of the access arrangement proposal. Alinta considers this would require that, at least, the information included in DBP's Submissions 1 to 12 be included in an amended proposed revised AAI.

Suppression of information

As discussed above, Alinta considers that DBP's proposed revised AAI does not contain the information that is reasonably necessary for users and prospective users to understand either:

- the background to the access arrangement proposal; or
- the basis and derivation of the various elements of the access arrangement proposal

as required by NGR 42(1).

As outlined in more detail below, Alinta also considers that DBP's proposed revised AAI may not include all of the information specifically required to be included in the AAI by the NGRs, as provided for by NGR 42(2).

Alinta notes that DBP's proposed revised AAI indicates it is a public version, and that the document itself does not indicate that any information has been suppressed or deleted. Consequently, to the extent that DBP's proposed revised AAI does not contain information that is reasonably necessary to satisfy NGR 42(1) and/or (2), it would appear that this information has not been provided by DBP to the Authority.

While it appears to Alinta that DBP may intend that its Submissions 1 to 12 not form part of the proposed revised AAI and that these submissions are therefore not bound by the requirements of the NGRs, Alinta considers that even if these submission were to form part of DBP's proposed revised AAI, Submissions 1 to 12 do not contain all of the information required to be provided in the AAI by NGR 42(1) and/or (2).

In any event, a very substantial amount of the information provided by DBP in Submissions 1 to 12 appears to have been suppressed. Alinta presumes that all of the sections that are shown as DELETED in the public versions of the submissions have been disclosed to the Authority in non-public versions of these documents.

To the extent that DBP's Submissions 1 to 12 were to form part of DBP's proposed revised AAI, the amount and nature of the information that has been suppressed means that users and prospective users of the DBNGP cannot reasonably be expected to:

- understand the background to the access arrangement proposal; nor
- the basis and derivation of the various elements of the access arrangement proposal; nor
- whether the access arrangement proposal and proposed revised AAI comply with the requirements of the National Gas Law and the National Gas Rules.

While NGR 43(2) allows for information provided in the AAI to be suppressed, information may only be suppressed where it is:

1. confidential; and
2. its public disclosure could cause undue harm to the legitimate business interests of the service provider, a user or prospective user; and
3. it is not possible for the information to be aggregated or generalised so as to avoid disclosure of the elements that make it sensitive.

That is, it is not sufficient for the information to be confidential for it to be suppressed (or deleted). Rather NGR 43(2) imposes three necessary tests that must each be satisfied before information can be suppressed.

The AER's Access Arrangement Guideline also notes that in considering whether information may be suppressed, the regulator will consider any hindrance in the ability of the regulator to perform its functions in assessing the veracity of the information provided to it.

Alinta has compiled below a non-exhaustive list illustrating where it considers important information has not been provided by DBP in the public versions of the proposed revised AAI and/or its submissions or where such information has been suppressed, and where the non-provision or suppression of such information significantly affects the degree to which users and/or prospective users can reasonably be expected to understand the background to the access arrangement proposal, and the basis and derivation of the various elements of the access arrangement proposal.

Subject to the interpretation that is determined should be ascribed to NGR 42(1) and (2) (as discussed above), and any revisions that the Authority may subsequently require DBP make to its proposed revised AAI, Alinta considers it is also necessary that the Authority review the information that has been suppressed in DBP's submissions (or may be suppressed in an amended proposed revised AAI) by applying the tests set out in NGR 43(2), in order to confirm whether the information that has been suppressed satisfies each of the three tests.

By way of comparison, Alinta notes that the most recent submissions of Western Power and gas distribution businesses in Victoria proposing revisions to access arrangements were substantially more detailed, and suppressed significantly fewer details of their respective AAI.

Alinta would draw to the Authority's attention that this submission can only be based on the information DBP has made available so far. If DBP were to provide further information in an updated and amended (or replacement) proposed revised AAI, whether as a result of a request by the Authority or otherwise, Alinta considers, and requests the Authority to confirm, that it and other interested parties will be provided with an opportunity to make further submissions on the amended (replaced) revised proposed AAI.

Examples of potential information deficiencies

The following is a non-exhaustive list of information that appears not to have been provided by DBP in its proposed revised AAI, or has been suppressed, in relation to the access arrangement proposal but which Alinta considers should be provided by virtue of NGR 42(1) and/or (2):[1]

- DBP appears not to have provided a Submission 2 and the information that may be contained in Submission 2 is not apparent (unless Submission 2 is the Proposed Tariff Model).
- Submission 3 "Pipeline Services" seeks to justify the removal of the T1, P1 and B1 Services as Reference Services, but suppresses information in paragraphs 5.3 and 5.10 to 5.14, which appear to go to the heart of DBP's reasons for removing, in particular, the T1 Service. Sections 6 and 7 of Submission 3 are withheld in their entirety, which has the result that scant information is available to users and prospective users in relation to a fundamental element of DBP's proposal, namely removal of the existing three reference services and replacement with a single, and materially different, full haul reference service, the R1 Service.

[1] References to submissions are to the submissions lodged by DBP with the Authority during April and May 2010 and published on the Authority's website.

- Submission 7 "Capacity and Throughput Forecast" does not provide any throughput forecasts for the R1 Service itself. The lack of such forecast information for the R1 Service makes it impossible to assess DBP's claim that the R1 Service will be sought by a significant part of the market (including whether it will be sought at all), and the reasonableness of the R1 Tariff.
- Submission 9 "Justification of Expansion Related Capital Expenditure" does not provide sufficient qualitative information to assess the reasons for significant deviations between actual and forecast capital expenditure. This is a fundamental issue given DBP is seeking to have around $1.8 billion added to the Capital Base, and that a proper assessment as to whether the expenditure is conforming under the National Gas Rules is one of the most important exercises to be undertaken by the Authority.
- Section 12 of Submission 9 relating to a breakdown of actual expenditure on Stage 5A contains a cross referencing error (presumably to a suppressed Attachment) and nothing more.
- Submission 9 also refers (in paragraph 1.6) to lodgement of a separate submission by DBP relating to justification of capital works that were not expansion works. It is not clear whether this is a reference to the "stay-in-business capital expenditure" detailed in Submission 10 or something else, although on the basis that Submission 9 was lodged after Submission 10 it would seem likely that it is referring to a separate submission that has so far not been made available to the public on the Authority's website at least.
- In addition to the overall information deficiencies for Submission 9 and DBP's justification of its capital expenditure during 2005 to 2010, 21 out of 25 Attachments for Submission 9 are suppressed, which seems an extraordinary approach. Alinta submits that there must be a way that at least some, if not all, of the Attachments could be presented that does not disclose confidential information (or presents it in an aggregate or other benign form) but increases the meaningful information on which users and prospective users can assess the Revised Access Arrangement.
- Submission 11 purports to justify DBP's forecast of capital expenditure for the period 2011-2015, but all information that could provide such justification (as contained in section 5 and the accompanying tables) are suppressed, meaning there is no description at all as to the planned expenditure.
- Submission 12 "Justification of Operating Expenditure" essentially suppresses the entire discussion of the forecast fuel gas costs (paragraphs 5.18 to 5.28).

Background

Issue 1 Special Circumstances

Submissions are invited from interested parties on whether, and in what manner, the special circumstances of the DBNGP should have a bearing on the Authority's assessment of the proposed revised access arrangement, having regard to the NGL including the national gas objective.

Alinta considers that the special circumstances of the DBNGP, and the manner in which they emerged, are relevant to the Authority in determining both the reference services that should be available as part of any revised access arrangement and in setting the reference tariffs for such reference services.

This is because these special circumstances have been instrumental in ensuring that pipeline services provided by the DBNGP and the tariffs paid for those pipeline services have supported investment in the DBNGP in a manner that is entirely consistent with the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas. That is, the effect of the special circumstances of the DBNGP, which are outlined in more detail below, are entirely consistent with the objective of the National Gas Law (NGL).

To the extent that the special circumstances of the DBNGP have supported outcomes that are entirely consistent with the objective of the NGL, the fact that DBP is now proposing to substantially alter these arrangements must be carefully examined by the Authority. The following sections summarise Alinta's understanding of the special circumstances applying to the DBNGP.

Gas Transmission Regulations

Alinta understands that a thorough consultation process undertaken during 1993 and 1994 resulted in the Gas Transmission Regulations 1994 prescribing a T1 Service, a T2 Service and a T3 Service that were available on the DBNGP from 1 January 1995.[2]

It is understood that initial shippers and new shippers embraced the T1 Service, while the T2 and T3 Services were utilised less and less, and eventually became largely irrelevant. The probability of supply, the priority of curtailments, the balancing and peaking regimes and nominations and allocations logistics were all important elements of why the T1 Service was the service that the majority of shippers demanded, and upon which these shippers subsequently made significant upstream and/or downstream commercial decisions.

Sale of DBNGP and first access arrangement under the National Access Code

When the DBNGP was sold by the Gas Corporation on behalf of the Western Australian Government to Epic Energy (now DBP) in 1997/98, the Government secured a covenant from Epic Energy that in the move to the National Access Code (Code) in 2000, it would propose a T1 - Equivalent Reference Service as a reference service. Shippers with transmission contracts governed by the Gas Transmission Regulations 1994 in existence at the time the Access Arrangement came into effect were able to stay on the terms and conditions of their existing contracts, but could elect to move from the T1 Service tariff set by the Gas Transmission Regulations (the statutory T1 tariff) to the reference tariff for the T1 - Equivalent Reference Service. The reference tariff for the T1 - Equivalent Reference Service was expected to reduce in time against the statutory T1 tariff, and shippers, especially initial shippers, were intended to be able to capture the benefits of that reducing tariff path.

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[2] Alinta understands that the major difference between the T1 Service and the T2 Service was a lower interruptibility threshold (two per cent versus eight per cent), whereas the T3 Service was fully interruptible.

Consistent with this covenant, the first Access Arrangement for the DBNGP contained as a T1 - Equivalent Reference Service, the Firm Service.

However, due to the level of the initial capital base approved by the regulator for that Access Arrangement against the purchase price paid by Epic Energy, Epic Energy contended that it could not expand the capacity of the DBNGP unless the shippers for whom the expansion was built paid the full capital costs of that expansion, which produced a very expensive tariff for new shippers which did not have the benefit of the statutory T1 tariff or the T1- Equivalent Reference Service Reference Tariff. This meant that there was no capacity expansion of the DBNGP between 2001 and 2004.

2004 Contractual Arrangements

In 2004, DBP and DBNGP Shippers entered into critical arrangements of a contractual nature (2004 Contractual Arrangements) outside the Code but clearly linked to the Code and any successor regime, including the NGL and NGR (Applicable Regime). These arrangements were critical in re-commercialising and debottlenecking the DBNGP, but resulted in existing shippers paying more for existing capacity than they would under the Applicable Regime. The essential elements of the arrangements are publicly available on DBP's website as part of DBP's T1 Standard Shipper Contract, which DBP must offer to any existing or potential shipper that requires access to expanded capacity on the DBNGP.

The links with the Applicable Regime are an essential part of the 2004 Contractual Arrangements because the arrangements provide for the T1 Service provided to Shippers to return to pricing under the Applicable Regime in 2016. The links with the Applicable Regime are necessary to ensure that the transition of the T1 Service to pricing under the Applicable Regime is meaningful and is based on the elements that were agreed by the parties in 2004. There is no basis on which those elements should and can be excluded under the Applicable Regime.

The most important links between the 2004 Contractual Arrangements and the Applicable Regime are as follows.

1. DBP is required to offer the T1 Service as a reference service from 2005 (T1 Reference Service).
2. The split between the capacity reservation charge and the commodity charge of the T1 Reference Service is to be 80%/20%.
3. The cost of equity as an input into the calculation of the reference tariff for the T1 Reference Service is to be determined by applying the Capital Asset Pricing Model (CAPM).
4. Capital expenditure incurred in meeting DBP's obligations under the 2004 Contractual Arrangements between 2004 and 2016 is required to meet pre-agreed budgeted levels (or approved variations to those budgeted levels) or is to be approved by the relevant regulator under the Applicable Regime applying the usual tests of prudent operator and efficient investment/expenditure (not an abridged version, or part, of those tests).

5. The T1 Reference Service is to have a reference tariff calculated in accordance with the requirements of the Applicable Regime, so that in 2016 the T1 Service held by the Shippers under the 2004 Contractual Arrangements will be accurately priced under the Applicable Regime. This includes an accurate allocation of the correct proportion of the total revenue to the efficient costs of providing the T1 Reference Service to the T1 Reference Tariff, and not an erroneous allocation to the costs of providing hypothetical or assumed services, such as the proposed R1 Reference Service.

   For this purpose, the throughput of, and the efficient costs of providing, the T1 Service to the Shippers under the 2004 Contractual Arrangements is identical to the throughput of, and the efficient costs of providing, the T1 Reference Service (but not the R1 Reference Service) as the services, the throughput and the costs are one and the same.

Importantly, the Australian Competition and Consumer Commission (ACCC) and the Western Australian Government supported the re-commercialisation of the DBNGP outside the Code on the basis that all shippers, existing and new, had the same opportunity to access expanded capacity on the DBNGP on a contractual tariff that was based on a methodology set in concrete in the shipper contracts, and that would be paid by all shippers regardless of whether they utilised the expanded capacity. These arrangements are set out in an undertaking made by the owners and operators of the DBNGP to the ACCC in 2004 (the 2004 Undertaking) and in an agreement between the owners and operators of the DBNGP (including DBP) and the State entered into in or around October 2004.

Apparent effect of DBP's Access Arrangement proposal

It appears that the revisions now being proposed by DBP to the Access Arrangement are likely to have the effect of severing the critical links between the 2004 Contractual Arrangements and the Applicable Regime and jeopardising the intended outcomes of the 2004 Contractual Arrangements at the critical juncture in 2016.

It is arguable that the effect of the revisions to the Access Arrangement proposed by DBP involves the following steps and potential outcomes.

- The proposed R1 Reference Service is priced at the highest allowable price in 2010 under the Applicable Regime (and the boundaries of allowable total revenue to determine that highest allowable price are pushed beyond breaking point in that exercise).
- The proposed R1 Reference Service is priced in 2010 as if it were the T1 Reference Service.
- The T1 Reference Service would then be required to be re-offered in 2016. Given, it is a significantly more valuable service than the proposed R1 Reference Service, it appears reasonable to presume that it will be argued that the price for the T1 Reference Service in 2016 should be significantly higher than the proposed R1 Reference Service.

- What the 2004 Contractual Arrangements shippers potentially revert to in 2016 is not a reference tariff for the T1 Reference Service which has been determined consistently with the Applicable Regime from 2005, but a tariff that has been determined with reference to pricing very highly in 2010 a service which no Shipper wants or will want in the period 2011-2015, and establishing that as the benchmark base reference tariff for a full-haul service on the DBNGP.

Bearing on the Authority's assessment of DBP's Access Arrangement proposal

A critical aspect of the 2004 re-commercialisation was that the tariff for the T1 Service would return to the reference tariff for the equivalent reference service in 2016. DBP has contracted with Alinta, and most 2004 shippers under the T1 Standard Shipper Contract, to have a T1 Service as part of its access arrangements for 2005 and 2016. Consequently, the absence of the T1 Reference Service in the proposed revised Access Arrangement between 2011 and 2015 is not consistent with the contractual obligations entered into by DBP under the T1 Standard Shipper Contracts.

Irrespective of the extent to which the special circumstances themselves have a bearing on the Authority's assessment of DBP's access arrangement proposal, Alinta considers that DBP is bound by the terms of the 2004 Contractual Arrangements to do the following.

- Offer the T1 Service as a reference service in 2011 so that it is consistent and meaningful to offer it in 2016.
- Determine the capital base for inclusion in the calculation of the total revenue allowable on which the T1 Reference Tariff is based by applying the standard tests as to prudent operator efficient expenditure/investment required by the NGR.
- Base the reference tariff for the T1 Reference Service on the requirements of the NGL and NGR as properly applied by the Authority, including the correct determination of the total revenue allowable and the correct allocation of the revenue to the efficient costs of providing the services, including the T1 Reference Service.
- Base the T1 Reference Tariff on the application of the CAPM methodology and the 80/20 split between capacity and commodity charges.

As noted earlier, Alinta considers that the obligations imposed on the parties to the 2004 Contractual Obligations are entirely consistent with the objective of the NGL and the requirements of the NGRs.

For this reason, Alinta considers it appropriate that the 2004 Contractual Arrangements have a bearing on the Authority's assessment of DBP's access arrangement proposal given these arrangements have been instrumental in ensuring that pipeline services provided by the DBNGP and the tariffs paid for those pipeline services have supported investment in the DBNGP in a manner that is entirely consistent with the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas. That is, the effect of the 2004 Contractual Arrangements are entirely consistent with the objective of the NGL.

Consequently, to the extent that the 2004 Contractual Arrangements of the DBNGP have supported outcomes that are entirely consistent with the objective of the NGL, the fact that DBP is now proposing to substantially alter these arrangements must be carefully examined by the Authority in assessing DBP's access arrangement proposal.

Pipeline Service

Issue 2 Reference Services

Submissions are invited from interested parties on:

- *whether the proposed reference service (R1 Service) is likely to be sought by a significant part of the market;*
- *whether there are any pipeline services not currently proposed as reference services that are likely to be sought by a significant share of the market;*
- *whether the proposed reference service imposes any constraints on users that are inconsistent with the regulatory requirements;*
- *whether information about reference services is easily understood by the market; and*
- *any other matters in relation to the pipeline services proposed to be provided under the proposed revised access arrangement.*

Definition of Market

Alinta disagrees with DBP's assertion that the relevant "market" assessment under NGR 101 should be a consideration of the market excluding existing T1 Shippers. Together with DBP's claim that the term "likely to be sought" in NGR 101 refers to services likely to be applied for by prospective shippers and which can become the subject of an executed access contract during the Access Arrangement period, Alinta considers DBP is importing an unjustified gloss on the plain meaning of these words, unnecessarily and unreasonably limiting the intent and actual wording of NGR 101.

Clause 23 of the NGL, which sets out the National Gas Objective, states that the objective of the Law is to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas. Alinta submits that the focus generally on consumers of natural gas in the objective, invalidates DBP's interpretation of NGR 101.

Further, NGR 42(1) clearly states that the purpose of AAI is to enable users and prospective users to understand the background to the access arrangement or the access arrangement proposal, and to understand the basis and derivation of the various elements of the access arrangement or the access arrangement proposal. Alinta considers that it is therefore patently clear that the NGL and the NGRs intend that an access arrangement and an access arrangement proposal should have regard to the interests of existing and prospective users of pipeline services. The significance of the interests of existing users given in this aspect of the NGRs means that the market contemplated by the NGL and the NGRs include existing users in that market.

Would the proposed R1 Reference Service be sought by a significant part of the market?

DBP provides no support or evidence for its proposition that the R1 Reference Service is likely to be sought at all, and certainly not that it is likely to be sought by a significant part of the market, even if existing T1 Service shippers were to be excluded from the definition of market.

As noted earlier, in Submission 3 DBP seeks to justify the removal of the T1, P1 and B1 Services as Reference Services, but suppresses information in paragraphs 5.3 and 5.10 to 5.14, which appear to go to the heart of its reasons for claiming that these services are not pipeline services that are likely to be sought by a significant part of the market. Sections 6 and 7 of Submission 3 are withheld in their entirety, which has the result that scant information is provided to users and prospective users in relation to a fundamental element of DBP's Access Arrangement proposal, namely removal of the existing three reference services and replacement with a single reference service, the R1 Reference Service.

While Alinta cannot speak for other users or prospective users of the DBNGP, Alinta does not agree with DBP's claim at paragraph 4.8 of Submission 3 that the proposed R1 Reference Service will be more attractive to shippers, and will encourage shippers to access capacity on the DBNGP. Specifically, Alinta considers that for at least the following reasons, the proposed R1 Reference Service is significantly less attractive than the T1 Service and/or the T1 Reference Service.

- Omission of outer imbalance band and outer hourly peaking band.
- Significant increase in penalties for overrun, imbalance, hourly peaking excursions.
- Requirement that shippers agree to an Inlet Sales Agreement to nominate on behalf of another shipper.
- Monthly cashing out of imbalances.
- Significant expansion of the circumstances in which DBP can refuse to accept or deliver gas, or to curtail, without liability.
- Different methodology for determining capacity quantities.
- There is no equivalent to the concept of the Aggregated T1 Service.

The proposed R1 Reference Tariff comprises of a 95.4 per cent capacity reservation and 4.6 per cent commodity charges split (at a 100 per cent load factor), compared with the approved T1 Reference Tariff, which has an 80/20 split between capacity reservation and commodity charges.

The higher proportionate capacity reservation charge of the proposed R1 Reference Tariff would provide much greater revenue certainty to DBP, almost certainly increasing costs to shippers, and potentially resulting in a significant increase in revenue to DBP without any actual change in throughput. If Alinta's charges were calculated on a 95.4/4.6 reservation/commodity charge split the nature of its load (including significant seasonal swings) would result in much higher costs, even if it stayed within the much tighter operating parameters of the R1 Service.

A 95.4/4.6 split is also be inconsistent with the 2004 Contractual Arrangements, and is expressly contrary to DBP's obligations under its T1 Standard Shipper Contracts, including with Alinta.

Further comments on the terms and conditions on which the proposed R1 Reference Service would be offered by DBP to the market are provided in Attachment B.

As the comments above, and those in Attachment B illustrate, the proposed R1 Reference Service is fundamentally inferior to the current T1 Service and/or the T1 Reference Service. Given existing T1 Service shippers can gain access to further T1 Service by having DBP expand the capacity of the DBNGP under clause 16 of their Standard Shipper Contracts, and that new shippers must be offered similar rights - obligations that were insisted on by the ACCC and the State in 2004 - Alinta considers it highly improbable that DBP's proposed R1 Reference Service could reasonably be expected to be sought by a significant part of the market for DBNGP pipeline services.

Services that would be sought by a significant part of the market

Alinta submits that the following services are services that are likely to be sought be a significant part of the market for DBNGP pipeline services:

- T1 Service;
- P1 Service;
- B1 Service; and
- services for the transport of gas from the Mondarra gas storage facility to the DBNGP and to Outlet Points downstream of CS9.

The current contracted T1 Service and the (largely) equivalent Full Haul T1 Reference Service offered under the existing Access Arrangement have been an integral part of the history of third party access to the DBNGP.

Initially, a thorough consultation process undertaken during 1993 and 1994 resulted in the Gas Transmission Regulations 1994 prescribing a T1 Service, a T2 Service and a T3 Service that were available from 1 January 1995. Initial shippers and new shippers embraced the T1 Service, while the T2 and T3 Services were utilitised less and less, and eventually became largely irrelevant.[3] The probability of supply, the priority of curtailments, the balancing and peaking regimes and nominations and allocations logistics were all important elements of why the T1 Service was the service that the majority of shippers demanded, and upon which these shippers subsequently made significant upstream and/or downstream commercial decisions.

The importance of the T1 Service was highlighted in 1997/98, when the DBNGP was sold by the Gas Corporation on behalf of the Western Australian Government to Epic Energy (now DBP) and the Government secured a covenant from Epic Energy that in the move to the National Access Code in 2000, it would propose a T1 - Equivalent Reference Service as a reference service. When the first Access Arrangement for the DBNGP subsequently became operative in 2003, it contained as a T1 - Equivalent Reference Service, the Firm Service.

Due to the level of the initial capital base approved by the regulator for that Access Arrangement against the purchase price paid by Epic Energy, Epic Energy contended that it could not expand the capacity of the DBNGP unless the shippers for whom the expansion was built paid the full capital costs of that expansion, which produced a very expensive tariff for new shippers which did not have the benefit of the statutory T1 tariff or the T1- Equivalent Reference Service Reference Tariff. This meant that there was no new capacity built in the DBNGP between 2001 and 2004.

At the time of the acquisition and re-commercialisation of the DBNGP in 2004, the T1 Service was accepted (and over-subscribed) by full-haul shippers as the preferred full-haul service, and which they were prepared to commercially underwrite to allow the bottled up demand for further capacity on the DBNGP to be met. Shippers at that time agreed to pay well above the Reference Tariff for the Firm Service to obtain the T1 Service on the existing capacity and the expanded capacity of the DBNGP, even those existing shippers that did not require expanded capacity.

DBP's Submission 7 indicates that full haul pipeline services, which Alinta presumes must effectively be a reference to the T1 Service (other full-haul services, such as Tp Service, do not account for much of the DBNGP's capacity), account for between around 572 and 894 terajoules per day (TJ/d), with throughput averaging around 625 TJ/d. Given DBP is forecasting throughput of between around 700-730 TJ/d in the period 2011-2015, it is clear that the T1 Service will continue to be a pipeline service sought by a significant part of the market.

[3] Alinta understands that the major difference between the T1 Service and the T2 Service was a lower interruptibility threshold (two per cent versus eight per cent), whereas the T3 Service was fully interruptible.

Alinta considers that DBP's claim that because the T1 Service is "fully contracted" it should be ignored in the proposed revisions to the Access Arrangement is without merit for the following reasons.

- The T1 Service is not fully contracted - existing T1 Service shippers can gain access to further T1 Service by having DBP expand the capacity of the DBNGP under clause 16 of their shipper contracts. New shippers must be offered similar rights. This obligation was insisted on by the ACCC and the State in 2004.
- The fact that a service is likely to be sought in exercise of existing contractual rights or those available to new shippers under a Standard Shipper Contract does not detract from it being sought by a substantial part of the market. The fact is that shippers on the DBNGP will continue to seek that a T1 Service be provided by existing capacity on the DBNGP and by seeking expanded capacity on the DBNGP, both of which meets the NGR 101 test.

When Alinta's view of "market" under NGR 101 is taken, and the existing and new T1 Service shippers are included, the T1 Service is demonstrably a service sought by a "significant part of the market". Any proposal to have the R1 Reference Service as the only reference service must therefore be rejected by the Authority.

Therefore, and even putting aside DBP's obligations under the 2004 Contractual Arrangements (discussed further below), which Alinta considers compels it to offer a T1 Service as a reference service from 2005, Alinta considers that there is abundant evidence available to the Authority that the T1 Service (or an equivalent service) is the pipeline service that is, and will be, sought by an overwhelming majority of users and/or prospective users of the DBNGP. Consequently, Alinta considers that the T1 Service (or an equivalent) must be offered by DBP as a reference service under the access arrangement proposal for the period 2011-2015.

Alinta notes that critical parts of the public version of DBP's Submission 3 on Pipeline Services, which seeks to provide justification of the reason for removal of the T1, P1 and B1 services as reference services are shown as "DELETED", presumably due to confidentiality issues. Withholding this information (e.g. sections 5.10-5.14 of Submission 3) significantly reduces the usefulness of the submission, and results in only scant justification being provided to existing and prospective users of the DBNGP in relation to potentially fundamental changes to the Access Arrangement.

The importance of retaining the T1 Service as the reference full haul service under the NGL is magnified by the 2004 Contractual Arrangements relating to the T1 tariff from 1 January 2016. This departure from the contractual arrangements with T1 Shippers in particular is, in Alinta's view, contrary to the objective set out in section 23 of the NGL. This is because shippers, and the gas market in Western Australia generally, have clearly evidenced their considered commercial assessment that the T1 Service, priced in accordance with the 2004 Contractual Arrangements up until 2016, and then priced under the NGL, was and remains the best way to promote efficient investment, operation and use of natural gas resources in the long term interests of consumers with respect to price, quality, safety, reliability and security of supply. Alinta submits that departing from that carefully formulated and structured regime now is likely to have direct negative consequences for consumers of gas in relation to at least price and reliability of supply.

Further, part haul and back haul services have been offered to shippers on the DBNGP since 1995, and a number of shippers have existing contracts for the P1 and B1 services. Shippers who will continue to have a demand for such services, existing or new, may not be a majority but will be material enough in the overall market for services from the DBNGP to be significant. DBP has not produced any evidence or support for the proposition that the P1 or B1 will not be required by a significant part of the market during the Access Arrangement period.

Rather, DBP's Submission 7 appears to indicate that forecast average daily throughput for the part haul pipeline service (presumed to be the P1 Service) and the back haul pipeline service (presumed to be the B1 Service) for the period 2011-2015 are likely to remain at least at current levels.

To the extent that the P1 Service and the B1 Service has previously been considered by the Authority under the Code as likely to be sought by a significant part of the market, Alinta considers that there is no basis for concluding this cannot reasonably be expected to continue to be the case for the period 2011-2015. Consequently, Alinta considers that the P1 Service and the B1 Service (or equivalents) must also be offered by DBP as reference services under any revised Access Arrangement.

Utilisation of storage services is an affordable and well-accepted method of improving security of supply, and the Gas Supply and Emergency Management Committee, in its report to the Western Australian Government (September 2009), identified the Mondarra storage reservoir as a potential provider of a cost effective gas contingency service. It proposed that a storage facility should be capable of withdrawal rates of between 35 TJ/d and 100 TJ/d, with interconnection to the DBNGP and the Parmelia Pipeline to allow gas to flow into these pipelines and WA Gas Network's gas distribution system. The Committee also considered that gas retailers should have adequate back-up supply arrangements to ensure continuity of supply for residential and small business customers.

As a result of the Committee's recommendations, Alinta considers that a service where Gas is delivered from the Mondarra storage facility into the DBNGP and transported to Outlet Points downstream of CS9 are likely to be sought by a significant part of the market in the period 2011-2015, and therefore should be included as a new reference services in a revised Access Arrangement proposal.

The inclusion of a reference service and a reference tariff for a service from Mondarra to outlet points downstream of that storage facility would require a departure from the "postage stamp" pricing policy for a full haul service which has existed since 1995. Alinta suggests that the reference tariff should be based on an equitable allocation of the costs required to provide that service and would likely be on a distance related proportional part of the full haul tariff. This is justifiable on any commercial analysis as shippers will have paid the distance related P1 Service tariff to get gas to the Mondarra storage facility in the first place.

Capital Expenditure

Issue 3 Capital Expenditure

Submissions are invited from interested parties on whether:

- *the capital expenditure in the 2005 to 2010 access arrangement period conforms to Rule 79(1)(a) as expenditure that would be incurred by a prudent service provider acting efficiently, in accordance with good industry practice, to achieve the lowest sustainable cost of providing services;*
- *DBP has adequately demonstrated that capital expenditure in the 2005 to 2010 access arrangement period is justifiable under the terms of rule 79(2);*
- *the forecast of conforming capital expenditure for the 2011 to 2015 access arrangement period has been arrived at on a reasonable basis and represents the best possible forecast or estimate possible in the circumstances; and*
- *the forecast of conforming capital expenditure for the 2011 to 2015 access arrangement period has been adequately demonstrated to meet the requirements for conforming capital expenditure under rule 79.*

Overview

DBP is seeking to have $1,790 million added to the capital base of the DBNGP as conforming capital expenditure for the period 2005 – 2010 (Table 9, AAI p.11). It appears this figure corresponds to a nominal capital expenditure of $1,804 million (Table 2, AAI p.6), which would be approximately:

- $670 million, or almost 60 per cent, higher than the $1,137 million that was approved by the Authority (Table 3, Issues Paper p.15); and
- $280 million, or almost 19 per cent, higher than the forecast of $1,521 million presented by DBP to the Authority in 2006 as part of an application under section 8.21 of the Code to approve a 310TJ/d expansion project (not withstanding that this application was ultimately withdrawn by DBP).

DBP's Submission 9 indicates that for the period 2005 – 2010, actual "expansion related capital expenditure" totalled around $1,698 billion (p.4), leaving a residual of around $106 million (i.e. $1.804 billion less $1.698 billion).

- The nature of the capital expenditure to which this residual amount can be attributed is unclear given it differs markedly from the actual amount of "stay in business" (SIB) capital expenditure of $78.89 million incurred by DBP, which is reported in Submission 10 (Table 1, Submission 10, p.11).
- There also appears to be some inconsistencies between the data reported in Table 2 of the AAI (p.6) and that reported at 1.13 of Submission 9 (p.4).

As shown in Table A.1 below, based on information in the Authority's Issues Paper and DBP's Proposed Tariff Model, Alinta estimates that the real level of capital expenditure approved for the period 2005-2010 was around $1,174.1 million, meaning that DBP's actual capital expenditure for the period was around $616 million, or around 53 per cent, higher.

Table A.1 DBP – Access Arrangement, Actual and forecast capital expenditure (excluding shipper capital contributions ($M, December 2009)

	1	2	3	4	5	6	Total
Forecast 2005-2010	15.59	90.84	428.16	363.13	103.33	173.00	1,174.06
Actual 2005-2010	0.78	61.54	409.42	628.23	17.93	672.19	1,790.10
Forecast 2011-2015	70.11	17.97	15.39	14.64	14.93	na	133.06

Source: Economic Regulation Authority 2010, Dampier to Bunbury natural gas Pipeline: Proposed Revisions to the Access Arrangement, Table 3, p.15
DBP 2010, Proposed Tariff Model

In contrast, DBP is forecasting capital expenditure of just $133.06 million for the period 2011 to 2015, of which more than 50 per cent is expected to be incurred in 2011 (Table 12, AAI p.13).

For the reasons set out below, Alinta submits that the information provided by DBP does not support the actual and forecast capital expenditure being characterised as conforming capital expenditure under the NGRs.

- The difference between actual and forecast capital expenditure for the period 2005-2010, irrespective of whether it is $670 million or $280 million (or $616 million), is not sufficiently explained by DBP.
- Actual capital expenditure has not been separately shown to satisfactorily meet the NGR 79(1) prudence and operator efficient investment/expenditure test;
- The 2004 Undertaking cannot be used to automatically justify all expansion capital expenditure as if it were required to comply with a regulatory obligation or requirement.
- It is unclear whether DBP's forecast of conforming capital expenditure for the period 2011-2015 has been arrived at on a reasonable basis and represents the best forecast or estimate possible in the circumstances.
- DBP has not provided any direct and specific evidence as to why the capital expenditure satisfies the positive economic value test.

Is DBP's actual and forecast capital expenditure 'conforming?

In order for DBP's actual and forecast capital expenditure to be added to its capital base, the capital expenditure must be 'conforming', meeting the tests set out in both NGR79(1) and (2).

Essentially, NGR 79(1) requires that capital expenditure be 'efficient' - the capital expenditure is such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of providing services.

In addition to satisfying NGR 79(1), the capital expenditure must also satisfy at least one of the tests in NGR 79(2) for the capital expenditure to be added to the capital base. This rule requires:

1. that the overall economic value of the expenditure is positive; or
2. that the present value of the expected incremental revenue to be generated as a result of the expenditure exceeds the present value of the capital expenditure; or
3. that the capital expenditure is necessary (for certain defined reasons); or
4. a combination of the above.

Evidence provided in DBP's Access Arrangement Information and Submissions

DBP's AAI and submissions indicate that all actual capital expenditure for the period 2005–2010 and forecast capital expenditure for the period 2011 - 2015 is conforming capital expenditure, and is to be added to the opening capital base at the commencement of the respective Access Arrangement period. DBP's Submissions 9, 10 and 11 appear directed at supporting this conclusion.

It appears to Alinta that much of the information provided by DBP in Submission 9 is directed at addressing the question of whether the options selected for each of the DBNGP expansions, and the manner in which the projects were implemented, were 'prudent'. The information provided in Submission 10 appears to suggest that, in the main, a Safety Case that has been approved by the State safety and technical regulator drove the need for SIB capital expenditure for the period 2005 – 2010.

Submission 11 provides some details of DBP's forecast capital expenditure for the period 2011 – 2015. Although the submission indicates that DBP expects that there will not be further expansions of DBNGP capacity over the period 2011 – 15 beyond the completion of Stage 5B in 2011, which is forecast to account for around 38 per cent of forecast capital expenditure in the period, it provides no information about SIB expenditure expected to be incurred.

In Alinta's view, the information provided by DBP in Submissions 9, 10 and 11 do not provide sufficient evidence for concluding that the requirements of NGR 79(1) have been satisfied in respect of the capital expenditure incurred by DBP in the period 2005–2010, or forecast to be incurred for the period 2011-2015. Specifically, the information in these submissions does not address the fundamental question of whether the capital expenditure achieved, or will achieve, the lowest sustainable cost of providing the services on the DBNGP.

There also appears to be an inconsistency in information provided about the capacity created by the Stage 5B expansion, which needs to be clarified as the capacity created will be important in determining the reasonableness of the expenditure on a per GJ/d basis (as shown in Table A.2).

- Paragraph 1.11 of Submission 9 states that 261 TJ/d of firm full haul capacity was created by Stage 5B.
- Other sources, including a DBP media release in January 2010 that is available on DBP's website, indicate that Stage 5B created approximately 110TJ/d of additional capacity.

Table A.2 Dampier Bunbury Natural Gas Pipelines, capacity expansion projects

	Cost ($M, nominal)	Capacity (TJ/d)	Average cost ($/GJ)
Stage 4	$446.71	124.9	$3,576
Stage 5A	$625.96	93	$6,731
Stage 5B	$670.90	261.2 / 110	$2,569 / $6,099

Source: DBP 2010, Submission 9, p.2 and http://www.dbp.net.au/press.html

Further, Submission 9 does not appear to provide information relating to the application of the tests in NGR 79(2) to "expansion related" capital expenditure, which means that users and prospective users cannot reasonably be expected to be able to understand the basis for DBP's claim that all actual "expansion related" capital expenditure is conforming capital expenditure.

In Submission 10, DBP outlines the reasons that actual SIB capital expenditure for the period 2005 – 2010 meets the requirements of NGR 79(2). As an example, DBP claims that routine replacement of white goods at compressor stations (p.19) satisfies NGR 79(2) because the capital expenditure was necessary to maintain and improve the safety and integrity of (pipeline) services. Similarly, DBP argues that capital expenditure on printers and servers (p.20) was necessary to maintain the integrity of (pipeline) services because it was required to meet DBP's obligations to meet contracted capacity.

However, it is not apparent to Alinta that had these whitegoods, printers and services not been replaced, it could reasonably have been expected that DBP's ability to provide pipeline services would have been affected, or that the expenditure was necessary for the safe provision of pipeline services. While these examples may be selective, Alinta considers they serve to highlight the tenuous nature of the reasons provided by DBP for why the capital expenditure undertaken by it during the period 2005 – 2010 meets the criteria set out in NGR 79(2)(c). Alinta considers that the Authority must carefully examine the basis on which DBP claims all of the actual SIB capital expenditure satisfies NGR 79(2).

In any event, given the significant increases in the capital base and the associated increase in the total revenue requirement for 2011-2015, Alinta considers that a detailed investigation of DBP's actual capital expenditure during the period 2005-2010 should be undertaken. The following sections provide further reasons.

History indicates strongly that not all actual and proposed capital expenditure will be conforming

There is substantial evidence from regulatory decisions in respect of recent proposed revised Access Arrangements in similarly regulated industries and other jurisdictions that compellingly supports the view that it is likely that not all of DBP's actual and forecast capital expenditure will be conforming. This evidence is as follows.

- The Authority did not allow Western Power to add $249.40 million (equivalent to 11.1 per cent of actual capital expenditure during the first Access Arrangement period) to the opening capital base for the second Access Arrangement period.

- The Authority reduced by almost $106.4 million (or 7.4 per cent) the capital expenditure that was allowed to be added by Western Power to the capital base during the second Access Arrangement period.

  (The capital expenditure allowance of $1,327.1 million approved by the Authority was almost $400 million lower than the $1,723.4 million originally proposed by Western Power, although this amount was later reduced to $1,433.5 million after taking account of the economic slowdown following the Global Financial Crisis).

- In its Final Decision following the Gas Access Arrangement Review 2008-2012 for Victorian gas distribution businesses, the Essential Services Commission (ESC) in Victoria approved combined capital expenditure for the four distribution businesses that was almost 29 per cent lower than that originally sought.

  The reduction in approved capital expenditure for each of the individual businesses ranged from around eight per cent up to 46 per cent.

Lack of independent review or benchmarking of actual and proposed capital expenditure

A detailed investigation of DBP's actual capital expenditure during the period 2005 - 2010 and its forecast capital expenditure for the period 2011 - 2015 is warranted given DBP appears not to have provided any independent evidence to corroborate its claims that its actual and forecast capital expenditure meets the requirements of National Gas Rules.

The apparent lack of independent external review of DBP's actual and forecast capital expenditure is in contrast with the regulated businesses referred to above (i.e. Western Power, and the four Victorian gas distribution businesses) and to Jemena's New South Wales gas distribution system, which each engaged independent consultants to review and advise on whether actual and forecast capital expenditure met the requirements of, respectively, the Western Australian Electricity Networks Access Code 2004, the (then) National Gas Code and the NGRs.

- Western Power engaged Sinclair Knight Merz (SKM) to assess its capital-works processes (design standards, planning policies, plant specifications and procurement processes), to benchmark the project-cost performance of Western Power against major capital projects in other industries, and to assess in detail ten capital projects.

- Envestra, the largest Victorian gas distribution business, engaged WorleyParsons to review current and forecast capital expenditure. WorleyParsons conducted a benchmarking study that examined Envestra's expenditure relative to other natural gas distribution businesses, and also undertook an audit of a random sample of projects, in order to confirm whether the justifications, economic analysis and approval processes provided a sound basis for concluding that expenditure was prudent.

  WorleyParsons also examined Envestra's forecast capital expenditure, including analysing various categories of expenditure and underlying assumptions and parameters, and concluded that Envestra's capital expenditure was within a range of values that it considered was efficient for Envestra's Victorian network.

- Jemena engaged Parsons Brinckerhoff Australia (PB) to assess its historical and forecast capital expenditure and conducted benchmarking exercises for compliance with NGR 79. PB (and Jemena) provided detailed description of actual and forecast expenditure, including line by line explanations of differences between actual and forecast expenditure.

It is important to note that for both Western Power and the Victorian gas distribution businesses, despite the consultants' reports being used to support the businesses' claims that actual and forecast capital expenditure met regulatory requirements, in each case the respective regulator found this not to be so (making the adjustments referred to earlier). Significantly, although WorleyParsons concluded that Envestra's forecast capital expenditure was efficient, the ESC reduced Envestra's forecast capital expenditure by more than $323 million, or around 46 per cent.

Changes in composition of actual and forecast capital expenditure

As noted earlier, DBP's actual capital expenditure during the period 2005-2010 was around 52 per cent higher than that original forecast, while there were also significant movements in capital expenditure between asset classes, as shown in Table A.3 below.

Table A.3 DBP –2005 - 2010 Access Arrangement, forecast and actual capital expenditure ($M, December 2009)

	Forecast	Actual	Variance
Pipeline	875.33	1,191.05	+36.1%
Compression	265.07	513.65	+93.8%
Metering	2.92	0.18	-93.8%
Other	30.74	85.22	+177.3%
Subtotal	1,174.06	1,790.10	+52.5%

Source: Alinta estimates based on Economic Regulation Authority 2010, Dampier to Bunbury Natural Gas Pipeline: Proposed Revisions to the Access Arrangement, Issues Paper, 7 May, Tables 3 and 4, p.15. and DBP 2010, Proposed Tariff Model
DBP 2010, Proposed Tariff Model

Given the significant variation between the composition of capital expenditure forecast for the period 2005-2010, and that actually incurred by DBP, Alinta considers it necessary that the Authority investigate in detail whether actual capital expenditure satisfies the requirements of NGR 79(1) and (2).

For example, in Submission 9 (section 4.3, p.18), DBP argues that the reasons that actual "expansion related" capital expenditure is significantly different from that forecast are attributable to the following causes.

- Differences in the volumes to underpin the expansion [of the DBNGP]
- Differences in the assumed configuration for the expansion profile
- Differences in the unit rates applied for key cost inputs (such as looping construction rates and the cost of compressor units)

However, Submission 9 does not appear to provide information to detail the extent to which each of these issues is responsible for the variation between forecast and actual "expansion related" capital expenditure in the period 2005 – 2010. Instead, much of the information in Submission 9, particularly that on the expenditure for expansion Stages 5A and 5B, is an unhelpful collection of design assumptions, contracting options and various specifications without providing any direct comparison or explanation as to the divergence between forecast and actual capital expenditure.

DBP also point to differences between ledgers in recording actual capital expenditure compared to line items in forecasts as a reason why forecast and actual expenditure cannot be properly reconciled. If true, this would be a significant shortcoming in the information provided to the Authority for its assessment of whether capital expenditure is conforming for the purposes of the NGRs. Further, in Submission 10, DBP attributes the fact that actual SIB capital expenditure is 25 per cent higher than forecast to " the circumstances acquisition process (sic) and the ability to provide an accurate forecast at the time and the major expansions that have occurred over the period which have contributed the need for further expenditure" (p.11).

Without an appropriate reconciliation of actual expenditure against that forecast, it will be extremely challenging for the Authority, users and prospective users of the DBNGP to make an informed assessment of whether actual capital expenditure for the period 2005 – 2010 satisfies the test in NGR 79(1).

Table A.4 DBP –Access Arrangement, Actual and forecast SIB capital expenditure ($M, December 2009)

	1	2	3	4	5	6	Total
Forecast 2005-2010	13.17	14.00	7.33	9.05	10.13	9.37	63.05
Actual 2005-2010	0.69	4.07	3.79	5.80	12.78	51.76	78.89
Forecast 2011-2015	20.0	20.63	16.84	14.64	14.93	na	87.04

Source: DBP 2010, DBNGP Revised Access Arrangement Information, Table 12, p.13, DBP 2010, Submission 10, Table 1, DBP 2010, Submission 11 Forecast Capital Expenditure, Table 1, and DBP 2010 Proposed Tariff Model

Finally, as shown in Table A.4 above, DBP's actual SIB capital expenditure was materially below that forecast from 2005 through to 2008, but since that time has increased exponentially. Specifically, actual SIB capital expenditure in 2010 alone is forecast to be more than 80 per cent of that forecast for the entire period from 2005 – 2010. The reason for the material increases in DBP's SIB capital expenditure in 2009 and 2010 is not apparent, and should be investigated by the Authority.

Alinta notes that there appears to be no discussion of DBP's decision in early 2009 to bring back in-house a significant proportion of the operating and maintenance services that were then contracted out to Westnet Energy Services Pty Ltd. This decision may be relevant to both DBP's actual SIB capital expenditure for the period 2005-2010 and its forecast SIB capital expenditure for the period 2011-2015 (and may also be relevant in the context of the marked increase in actual and forecast expenditure, which is discussed later).

While Alinta is not aware of the precise details, it would appear reasonable to presume that DBP's decision was intended, and should be expected, to result in lower unit rates for SIB capital expenditure.

However, as shown in Table A.3, it appears that DBP's SIB capital expenditure in 2009 and 2010 increased by more than 120 per cent. In the absence of detailed information on drivers of actual SIB capital expenditure and better information on how such expenditure meets the requirements of NGR 79(1), it is not possible to ascertain the reasons for this increase, but it is nevertheless concerning that DBP's decision to bring back in-house operating and maintenance services may have contributed to this increase.

For this reason, Alinta considers that the Authority should review the basis for DBP's decision to bring back in-house a significant proportion of the operating and maintenance services that had been contracted out to Westnet Energy Services Pty Ltd in order to ensure that this approach will result in capital expenditure that is consistent with the requirements of NGR 79(1), being that it is such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services.

Reliance on 2004 Undertaking to satisfy NGR 79(2)

As noted earlier, in addition to satisfying NGR 79(1), for capital expenditure to be conforming it must also satisfy at least one of the tests in NGR 79(2). This rule requires:

1. that the overall economic value of the expenditure is positive; or
2. that the present value of the expected incremental revenue to be generated as a result of the expenditure exceeds the present value of the capital expenditure; or
3. that the capital expenditure is necessary (for certain defined reasons); or
4. a combination of the above.

In its Submission 9, DBP appears to contend that all capital expenditure for the period 2005 - 2010 is conforming capital expenditure for the purposes of NGR 79(2) as either:

- the overall economic value of the expenditure was positive; or
- the expenditure was to comply with a regulatory obligation or requirement, namely the 2004 Undertaking.

While Submission 9 discusses the nature of the positive economic value test in NGR 79(2)(a), and provides views on possible interpretation of the wording, DBP does not provide any evidence or justification, even in general terms, that capital expenditure for the period 2005–2010 actually satisfies the positive economic value test, other than inclusion of some very broad media releases by the then Western Australian Minister for Energy. Alinta considers it unlikely that the test implied by NGR 79(2) is able to be satisfied simply by reference to a media statement.

In respect of the second basis used to claim that the capital expenditure satisfies NGR 79(2), Alinta notes that by clause 5.7(a) of the 2004 Undertaking, DBP voluntarily undertook to spend up to $400 million to expand the capacity of the DBNGP by not less than 100TJ/d in aggregate. DBP notes that this obligation was satisfied through the Stage 4 expansion, which provided around 127TJ/d additional capacity by 1 January 2007.

Alinta considers that there are several other issues that the Authority should consider in connection with DBP's assertion that all expansion related capital expenditure during the period 2005-2010 was necessary to comply with a regulatory obligation or requirement, being the 2004 Undertaking.

Firstly, as noted above, clause 5.7(a) of the 2004 Undertaking requires DBP to expand the DBNGP by not less than 100 TJ/d in aggregate to meet the known capacity requirements of Contracted Shippers or Prospective Shippers who enter into Standard Shipper Contracts. Under clause 5.7(c), DBP undertook to spend up to $400 million in connection with the expansion under clause 5.7(a), which is a clear obligation in relation to capital expenditure.

However, Alinta submits that it is not a regulatory obligation for the purposes of NGR 79(2). It may be an "undertaking" but it is an undertaking extraneous to the regulatory regime in which the obligation is relevant. This obligation should be distinguished from an obligation incurred, for example, in a competitive tender process to construct a pipeline system or expansion.

Secondly, Alinta notes that clause 5.6(a) of the 2004 Undertaking merely requires DBP to offer "Prospective Shippers" a Standard Shipper Contract with expansion rights not materially less favourable than the expansion rights contained in "any other Shipper Contract for a T1 Service". As such, clause 5.6(a) is an obligation to offer a particular form Standard Shipper Contract, it is not a regulatory obligation to undertake capital expenditure that would satisfy NGR 79(2)(c)(iii). The actual obligation on DBP to expand the DBNGP is a contractual one only, and there are many conditions that must be satisfied before the expenditure obligation actually arises. For these reasons, Alinta considers that DBP's argument that expenditure that may (ultimately and indirectly) result from the inclusion of clause 5.6(a) satisfies NGR 79(2)(c)(iii) is not correct and should be rejected by the Authority.

Submission 9 indicates that DBP's actual capital expenditure on Stage 4 to satisfy the clause 5.7(a) obligation was $446.7 million (p.20). However, as noted earlier DBP is seeking to have $1,790 million added to the capital base of the DBNGP as conforming capital expenditure for the period 2005–2010, which appears to correspond to a nominal capital expenditure of $1,804 million. This amount is $1,4004 million higher than the amount of capital expenditure that DBP voluntarily committed to in the 2004 Undertaking.

Alinta considers that NGR 79(1)(a) remains a threshold test to be satisfied before the expenditure can be approved as conforming by the Authority, but that even if the clause 5.7(a) obligation were a regulatory obligation, it could reasonably only have application only to the maximum extent of the $400 million.

DBP notes that it has contracted to provide a shipper with additional capacity within 30 months of receiving a notice of additional capacity requirement. To the extent that much of the remaining $1,4004 million may relate to "expansion related" capital expenditure undertaken to meet this contract ual obligation (i.e. expansions 4, 5A and 5B at a cost of around $446.7 million, $626.0 million and $620.9 million respectively), Alinta's view is that this:

- does not detract from the requirement that the capital expenditure must satisfy NGR 79(1); and
- does not constitute a regulatory obligation to undertake a capacity expansion (i.e. is not a basis for satisfying the tests set out in NGR 79(2)).

The Authority may also consider it relevant as to whether or not the undertakings voluntarily given by DBP in the 2004 Undertaking constitute a regulatory obligation or requirement with which, for the purposes of NGR 79(2) it was required to comply, the fact that clause 4 of the 2004 Undertaking expressly states that the undertakings made do not limit any of the obligations of the parties to the 2004 Undertaking in respect of the application of the Gas Access Law.

DBP's Submission 11 does not detail the basis on which its forecast capital expenditure satisfies both NGR 79(1) and NGR 79(2) and is therefore conforming capital expenditure that may be added to the capital base.

In fact, Submission 11 suppresses all of the information relating to the application of the tests in NGR 79(2), which means that users and prospective users cannot reasonably be expected to be able to understand the basis for DBP's claim that all its forecast capital expenditure is conforming capital expenditure. It is unclear to Alinta that this information would satisfy the requirements in NGR 43(2) for the information to be suppressed.

Basis for forecast 2011-2015 capital expenditure

DBP indicates that its forecast of capital expenditure for the period 2011 – 2015 is based on an expectation that no further expansion related capital expenditure is expected to occur in the period 2011-2015. DBP provides virtually no information in the public version of its Submission 11 as to how it has arrived at this conclusion, nor how it has estimated its SIB capital expenditure for the period 2011-2015.

As a result, it is difficult to comment on whether DBP's forecast of conforming capital expenditure for the period 2011-2015 has been arrived at on a reasonable basis, and represents the best forecast or estimate possible in the circumstances as required by NGR 74(2).

Table A.5 DBP –Access Arrangement, Forecast capital expenditure ($M, December 2009)

	2011	2012	2013	2014	2015	Total
Pipelines	15.40	8.39	3.88	4.62	7.81	40.11
Compression	8.27	0.49	2.66	2.66	0.16	14.22
Metering	5.57	4.35	4.71	0.62	0.82	16.06
Other depreciable assets	40.86	4.74	4.15	6.75	6.15	62.67
Sub Total	70.11	17.97	15.39	14.64	14.93	133.06

Source: DBP 2010, DBNGP Revised Access Arrangement Information, Table 12, p.13, DBP 2010, Submission 10, Table 1, DBP 2010, Submission 11 Forecast Capital Expenditure, Table 1, DBP 2010, Proposed Tariff Model

Even leaving aside DBP's assumption that there won't be an expansion of the DBNGP in the period 2011-2015, it is unclear that the proposed level of capital expenditure is sufficient to maintain the integrity of the DBNGP and reliability of supply. Specifically, forecast annual SIB capital expenditure equates to less than 0.5 per cent of the proposed capital asset base each year. Alinta considers that DBP should be requested to confirm that its forecast capital expenditure is sufficient to maintain the integrity of the DBNGP and reliability of supply, including that it contains sufficient allowance for capital refurbishment and maintenance of the compressor turbines, which now number in excess of 20.

Turning to DBP's assumption that there won't be an expansion of the DBNGP in the period 2011-2015, Alinta questions whether this is reasonable, and therefore whether DBP's forecast of capital expenditure represents the best forecast or estimate possible in the circumstances as required by NGR 74(2). This is because DBP itself comments that the DBNGP is fully contracted, and therefore any incremental increase in gas demand for major industrial projects, including for example gas-fired generation, would likely require an expansion of the capacity of the DBNGP.

Importantly, the *Western Australia Natural Gas Demand and Supply – A Forecast*, a recent report prepared for the Domgas Alliance by Economic Consulting Service, indicates that demand for gas is likely to increase by around 490 TJ/d by 2015. It appears likely that a significant proportion of this gas would be required to be transported by the DBNGP, which would in turn be likely to create demand for additional capacity on the DBNGP and require further expansion projects.

This information appears to provide compelling evidence that DBP's expectation that there will not be any expansion related capital expenditure during the period 2011–2015 has not been arrived at on a reasonable basis and does not represent the best possible forecast or estimate possible in the circumstances.

Finally, Alinta is also concerned that DBP has not explained the significant variation in forecast SIB capital expenditure for the period 2011 – 2015 when compared with actual SIB capital expenditure for the period 2005 – 2010 (refer Table A.3). While it is clear that the technical and operational characteristics of the DBNGP have changed materially since 2005, DBP has not provided any explanation for the level of forecast SIB capital expenditure for the period 2011 – 2015. Specifically, the reason for the high level of SIB capital expenditure in both 2009 and 2010 is not clear.

In the absence of detailed information on drivers of actual SIB capital expenditure and better information on how such expenditure meets the requirements of NGR 79(1), it is not possible to ascertain the reasons for this increase, but it is nevertheless concerning that DBP's decision to bring back in-house operating and maintenance services may have contributed to this increase.

For this reason, Alinta considers that the Authority should review the basis for DBP's decision to bring back in-house a significant proportion of the operating and maintenance services that had been contracted out to Westnet Energy Services Pty Ltd in order to ensure that this approach will result in capital expenditure that is consistent with the requirements of NGR 79(1), being that it is such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services.

In summary, DBP's claim that its actual and forecast capital expenditure meets the requirements of NGR 79:

- does not appear to be supported in any detail in the information contained in its AAI or submissions (public versions);
- does not appear to be supported by independent analysis or review of its actual and/or forecast capital expenditure; and
- does not appear to be supported by benchmark comparison to other natural gas transmission businesses.

Capital Contributions

Issue 4 Capital Contributions

Submissions are invited from interested parties on:

- *aspects of the proposed revised access arrangement that deal with capital contributions;*
- *DBP's supporting information about capital contributions;*
- *information from interested parties about capital contributions actually made; and*
- *any other matters in relation to capital contributions under the proposed revisions.*

Capital contributions

Table A.6 DBP – Access Arrangement, Actual and forecast shipper capital contributions ($M, December 2009)

	1	2	3	4	5	6	Total
Forecast 2005-2010	na	na	na	na	na	na	na
Actual 2005-2010	2.21	0.00	0.08	0.00	21.27	14.30	37.86
Forecast 2011-2015	0.23	2.66	1.44	0.00	0.00	na	4.32

Source: DBP 2010, DBNGP Revised Access Arrangement Information, Table 12, p.13, Economic Regulation Authority 2010, Dampier to Bunbury natural gas Pipeline: Proposed Revisions to the Access Arrangement, Table 3, p.15, DBP 2010, Proposed Tariff Model

It appears that DBP has not provided any information on the level of actual or forecast capital contributions in its proposed revised AAI or submissions. Consequently, it is difficult for users or prospective users to understand the basis and derivation of this element of DBP's access arrangement proposal.

The absence of information on forecast capital contributions appears inconsistent with the requirement of NGR 74 (1), which requires that information in the nature of a forecast or estimate must be supported by a statement of the basis of the forecast or estimate. Without such information, it is difficult to assess whether this element of DBP's access arrangement proposal has been arrived at on a reasonable basis and whether it represents the best forecast or estimate possible in the circumstances as required by NGR 74(2).

Accounting for capital contributions

NGR 82(2) provides that capital expenditure to which a user has contributed may, with the Authority's approval, be rolled into the capital base for a pipeline but, subject to NGR 82(3), not to the extent of any such capital contribution.

NGR 82(3) goes on to provide that the Authority may approve the rolling of capital expenditure (including a capital contribution made by a user, or part of such a capital contribution) into the capital base for a pipeline on condition that the access arrangement contain a mechanism to prevent the service provider from benefiting, through increased revenue, from the user's contribution to the capital base.

In section 12 of DBP's access arrangement proposal, it indicates that:

- capital contributions made by users are to be rolled into the capital base; but
- an amount equal to the return on user capital contributions and the depreciation of user capital contributions will not be allocated to any pipeline service.

Sections 6 and 7 and Tables 10 and 12 of DBP's proposed revised AAI provide details of the manner in which the capital base for the period 2005-2010 and 2011-2015 have been calculated by DBP. In each case, DBP has added capital contributions into the capital base. Paragraph 14.3 indicates that an amount equal to the return on the capital contribution and the depreciation of capital contributions will not be allocated to any pipeline service.

However, based on its review of DBP's Proposed Tariff Model, it appears to Alinta that the practical manner in which DBP has calculated the return on its capital base and return of capital does not align with the detail of the description contained in either the access arrangement proposed or the proposed revised AAI. Specifically, in its Proposed Tariff Model the return on and of capital in the "Summary" sheet (refer cell range G10:K11) links to cells in the "CAPEX" sheet that have been calculated by expressly excluding shipper capital contributions (refer cell range R107:V108).

Although it would appear that the practical outworking of DBP's approach is consistent with the requirements of NGR 82(3), it appears to be achieved by excluding shipper funded capital contributions from the capital base (before total revenue is calculated) rather than by adjusting total revenue to remove the return on user capital contributions and the depreciation of user capital contributions.

That is, the capital base used by DBP to establish the value of total revenue reported in Table 22 of its proposed revised AAI is not equivalent to the capital base reported in Table 15 (compare line 104 in the "CAPEX" sheet to the data in Table 15).

While the practicalities of this may not be significant, it would appear nonetheless that DBP's approach may not be consistent with the obligation imposed by NGR 73(3), which is that all financial information be provided, and all calculations made consistently on the same basis. Alinta suggests that the Authority may choose not to approve DBP's proposal to roll capital contributions into the capital base to ensure consistency with the approach to accounting for capital contributions in DBP's Proposed Tariff Model.

Rate of return in calculating capital contributions

Capital contributions are variously referred to as Funded Capital Expenditure (paragraph 12.2 of the access arrangement proposal), or contributions which may be levied through a Contributing Agreement or a Shipper Specific Facilities Charge, which are both defined in the proposed R1 Reference Service terms and conditions.

Alinta is concerned at the lack of detail around the manner in which these capital contributions may be calculated, and the very broad discretion afforded to DBP under the terms and conditions of the proposed R1 Reference Service.

As a specific example, in its submission to the Western Australian Government's Strategic Energy Initiative, Alinta expressed a concern regarding the arrangements applying to transmission pipeline 'gate stations' indicating that it considered these arrangements could impede efficient investment in distribution network infrastructure and potentially affect the security and reliability of supply to distribution connected gas consumers.

'Gate stations' are a specific form of outlet point on a gas transmission pipeline where the pipeline joins a gas distribution network. Gate stations are owned, operated and maintained by the owner and operator of a transmission pipeline, but are paid for by users that hold capacity rights at that gate station (i.e. predominantly gas retailers).

For example, DBP as the operator of the DBNGP has been able to impose a 'maintenance charge' on users that have capacity rights at that outlet point, where the charge is based on:

- installation costs (which is the capital cost of acquiring and installing all relevant components of an inlet station, outlet station or gate station);
- maintenance, operating and decommissioning costs; and
- a 'reasonable' premium calculated to recognise operator's management time; and
- a 'reasonable' rate of return on the cost of design, installation, maintenance, operation and decommissioning.[4]

While the general manner in which the maintenance charge is calculated is defined in the 2005 Access Arrangement, unlike 'reference services' these charges appear not to be directly regulated. For example, it appears that the 'reasonable' rate of return is not required to be the rate of return approved by the Authority, and which is applied in setting tariffs for reference services. Additionally, the rate of return could, under this formulation, be earned on maintenance and operation costs, and not just the asset capital base, making the gate station a profit centre for DBP.

Alinta has had the experience of being provided with a quote by DBP for the construction and operation of a gate station, including its conversion into an annual maintenance charge that appears to have been based on a rate of return well in excess of that determined by the Authority through the access arrangement process. Given that gate stations (and outlet points generally) form part of a regulated asset (i.e. the transmission pipeline), it is unclear to Alinta why the costs associated with gate station should not be subject to the same regulatory framework.

Alinta notes that clause 6.12 of the proposed R1 Reference Service terms and conditions, the reference to "…a reasonable rate of return on the cost of such design, installation, maintenance, operation and decommissioning" has been replaced by a reference to amortising costs over the life of the assets.

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4 Economic Regulation Authority 2010, *Revised Access Arrangement for the Dampier to Bunbury Natural Gas Pipeline*, 26 June 2008, Reprinted 22 January 2010 (Incorporates corrigenda of notice dated 22 January 2010), refer clause 6.6(i) (page 78 of 519)

The reason for the change is unclear, but notwithstanding this change, Alinta considers that its concerns remain relevant. That is, given outlet points, including gate stations, are incidental to the provision of transmission pipeline services, and that the risk of providing these services is similar to (and arguably lower than) transmission pipeline services generally, the rate of return on these assets and the manner in which an amortised payment is calculated should require the pipeline operator to apply the rate of return that has been determined by the Authority as part of the approved Access Arrangement to the asset capital base of the gate station only.

Ultimately, it is growth in the number of physical connections to the distribution network that will determine the requirement for new (or augmented) gate stations (and outlet points generally). Specifically, additional gate stations may be necessary so that the distribution network is able to physically deliver the required volume of gas to customers during periods of peak demand (i.e. to support the security and reliability of gas supplies).

Consequently, it is the owner and operator of the gas distribution network that would generally identify the requirement for investment in a new (or augmented) gate station. However, under the current industry framework the owner and operator of the affected gas distribution network must rely on users of the transmission pipeline (i.e. gas retailers) to request the owner and operator of a transmission pipeline to design and construct the new (or augmented) gate station.

In a fully contestable retail market, such as which exists in Western Australia, this potentially creates practical challenges that could affect the security and reliability of supply to distribution connected gas consumers. This is because it may not be in the commercial interests of one or any of the gas retailers to incur the cost of the new (or augmented) gate station.

Alinta considers that gate stations (and outlet points generally) should form a subset of the regulated transmission pipeline asset base, and that costs associated with gate stations should be subject to the same regulatory framework.

In addition, in order to avoid a situation where the potential arises for the security and reliability of gas supply to be affected by the commercial interests of the pipeline operator and/or one or more gas retailers, where a gate station /outlet point connects a transmission pipeline and a distribution system, it appears preferable that regulatory and contractual arrangements provide for the owner and operator of the transmission pipeline to contract for the investment in a new (or augmented) gate stations/outlet points directly with the owner and operator of the distribution system (and for these costs to be recovered through regulated distribution system tariffs).

Rate of Return

Issue 5 Rate of Return

Submissions are invited from interested parties on:

- *the proposed rate of return (WACC);*
- *the proposed cost of debt;*
- *the proposed cost of equity including the methods used for calculating the proposed cost of equity;*
- *DBP's supporting information to justify its approach and proposed rate of return; and*
- *any other matters in relation to the rate of return under the proposed revisions.*

Summary

DBP is proposing that a real pre-tax rate of return of 10.76 per cent be used in determining a return on its projected capital base for the period. This compares with a real pre-tax rate of return that applied for the 2005 Access Arrangement of 7.24 per cent, and represents an increase of almost 49 per cent.

Alinta notes that the Authority recently determined that the real pre-tax rate of return for the Goldfields Gas Pipeline (GGP) should be 7.78 per cent. That DBP's proposed rate of return of 10.76 per cent should be almost 300 basis points higher than that for the GGP is concerning given the prevailing conditions in the market for funds and the risks involved in providing reference services on the GGP and the DBNGP could reasonably be expected to be similar, if not the same.

2004 Contractual Arrangements

As noted previously, and irrespective of the extent to which the special circumstances of the DBNGP have a bearing on the Authority's assessment of DBP's access arrangement proposal, Alinta considers that DBP is bound by the terms of the 2004 Contractual Arrangements to offer the T1 Service as a reference service in 2011, and to base the T1 Reference Tariff on total revenue that is determined using the CAPM.

As noted earlier, Alinta considers that the obligations imposed on the parties to the 2004 Contractual Arrangements are entirely consistent with the objective of the NGL and the requirements of the NGRs.

For this reason, Alinta considers it appropriate that the 2004 Contractual Arrangements have a bearing on the Authority's assessment of DBP's access arrangement proposal given these arrangements have been instrumental in ensuring that pipeline services provided by the DBNGP and the tariffs paid for those pipeline services have supported investment in the DBNGP in a manner that is entirely consistent with the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas. That is, the effect of the 2004 Contractual Arrangements are entirely consistent with the objective of the NGL.

Consequently, to the extent that the 2004 Contractual Arrangements of the DBNGP have supported outcomes that are entirely consistent with the objective of the NGL, the fact the DBP is now proposing to substantially alter these arrangements, including the manner in which the rate of return is determined, must be carefully examined by the Authority in assessing DBP's access arrangement proposal.

Does DBP proposed real pre-tax rate of return meet the requirements of the NGRs?

NGR 87(1) requires that the rate of return on capital is to be commensurate with prevailing conditions in the market for funds and the risks involved in providing reference services. Further, NGR 87(2) states that, in determining a rate of return on capital:

- it will be assumed that the service provider:
  - meets benchmark levels of efficiency; and
  - uses a financing structure that meets benchmark standards as to gearing and other financial parameters for a going concern and reflects in other respects best practice; and
- a well accepted approach that incorporates the cost of equity and debt, such as the Weighted Average Cost of Capital, is to be used; and a well accepted financial model, such as the Capital Asset Pricing Model, is to be used.

Alinta considers there is compelling evidence to suggest that DBP's proposed rate of return of 10.76 per cent does not comply with at least the requirements set out in NGR 87(2).

Cost of equity

Paragraph 11.10 of DBP's proposed revised AAI indicates that the nominal cost of equity used by DBP to determine its proposed rate of return on capital of 10.76 per cent was 13.50 per cent.

At paragraph 11.5, DBP indicates that the cost of equity used to determine this rate of return was determined from the results obtained from four "well accepted" financial models and an examination of equity analysts' dividend yield forecasts for the period 2010 to 2012 for comparable Australian infrastructure businesses. Table 19 of the proposed revised AAI reports the estimated cost of equity determined by applying each of the four models, while at paragraph 11.8, DBP suggests that current market information points to a cost of equity between 13.0 per cent and 14.0 per cent. These results are shown in Table A.7 below

Table A.7 DBP – Access Arrangement, Estimated cost of equity (nominal)

Model / Basis	Estimated cost of equity
CAPM	8.79%
Black' CAPM	11.98%
Fama-French three factor model	11.57%
Zero beta Fama-French three factor model	14.36%
"Market information"	13.0% - 14.0%

Source: DBP 2010, DBNGP Revised Access Arrangement Information, Table 19, p.23 and paragraph 11.8, p.23

Alinta considers that the proposed rate of return on capital of 10.76 per cent does not meet the requirement of NGR 87(2)(b) because it appears that DBP has not used a well accepted model to determine the cost of equity.

Alinta also notes that the estimates of the cost of equity using each of the four models that is reported in Table 19 of DBP's proposed revised AAI differs marginally from those in the report from NERA included in Submission 8 as Attachment 1. The reasons for these differences, albeit small, do not appear to be addressed in the information provided by DBP.

While it is clear that the intended outcome of NGR 87(1) is that the pipeline operator be able to apply a rate of return commensurate with prevailing conditions in the market for funds and the risks involved in providing reference services, Alinta considers that NGR 87(2) limits the discretion available to the pipeline operator in determining that rate of return. The two specific requirements of NGR 87(2)(b) are that the rate of return must be determined using:

- a well accepted approach that incorporates the cost of equity and debt (e.g. the Weighted Average Cost of Capital); and
- a well accepted financial model (e.g. the Capital Asset Pricing Model).

Alinta considers that the reference to the CAPM in NGR 87(2)(b) makes it clear that the requirement to use "a well accepted financial model" applies in respect of the cost of equity capital. On the evidence available to Alinta, it would appear that DBP has not used a well accepted financial model to determine its proposed cost of equity of 13.50 per cent.

This is because the figure of 13.5 per cent differs to the cost of equity determined by each of the four models used by DBP to derive potential estimates of the cost of equity. If each of the four models used by DBP represented "a well accepted financial model", then it is apparent that NGR 87(2)(b) would allow the cost of equity that could be used in determining the rate of return to be any one of four values: 8.79 per cent; 11.98 per cent; 11.57 per cent; or 14.36 per cent. This discrete set does not include the value used by DBP for the cost of equity.

Alternatively, if it were assumed that NGR 87(2)(b) permitted the use of more than one "well accepted financial model" in deriving a cost of equity, then it is possible that the cost of equity assumed by DBP meets the requirement of NGR 87(2)(b) given it falls within the range of values established for the cost of equity by the four models (i.e. 8.79 per cent to 14.36 per cent).

Consequently, in determining whether the cost of equity used by DBP meets the requirements of NGR 87(2)(b), the Authority must determine:

- whether NGR 87(2)(b) permits the use of more than one financial model in determining the cost of equity; and
- whether, aside from the CAPM, the models used by DBP are "well accepted".

Do the National Gas Rules permit the use of more than one financial model?

Alinta considers that the only interpretation of the wording of NGR 87(2)(b) is that a single financial model is required to be used in establishing the proposed rate of return. That is, DBP's apparent approach to adopt a value for the cost of equity based on a that is informed by four financial models does not comply with the requirements of the NGRs.

If the NGRs had intended to allow the rate of return to be based on more than one financial model, this could have been easily accomplished and, arguably, would be apparent in the wording. For example, NGR 87(2) could have been drafted as follows:

> *(2) In determining a rate of return on capital:*
> *….*
> *(b) a well accepted approach that incorporates the cost of equity and debt, such as the Weighted Average Cost of Capital, is to be used; and ~~a~~ well accepted financial models, such as the Capital Asset Pricing Model, ~~is~~are to be used.*

A potential alternative interpretation is that the reference to 'Capital Asset Pricing Model' in NGR 87(2)(b) is not a reference to a single financial model, and that therefore the rule permits the use of financial models that are Capital Asset Pricing Models.

Fortunately, the question of how a generic reference to 'the Capital Asset Pricing Model' should be interpreted was considered in expert witness advice provided to the Essential Service Commission (ESC) in 2008.[5] Specifically, the advice considered the following questions.

1. What was the commonly agreed meaning of the CAPM in the period 1997 to 2002, with reference to relevant finance texts if applicable?
2. Would a reference to the 'capital asset pricing model' be referring to a generic theory, or would it be a reference to a specific Capital Asset Pricing Model, known as the CAPM (and also known as the Sharpe CAPM)?

[5] The Origins of the CAPM and its Application in Commercial Practice and Economic Regulation, Statement of Michael Lubomyr Lawriwsky, 16 May 2008, available at www.esc.vic.gov.au/public/Energy/Regulation+and+Compliance/Decisions+and+Determinations/Gas+access+arrangements+review+2008-12/Consultant+reports.htm

In response to the first question, the advice was that, for the following reasons, the commonly agreed meaning of the term 'CAPM' in the period 1997 to 2002 was the Sharpe CAPM.

- In finance textbooks spanning the period from 1993 to 2003, the term 'CAPM' is used as a generic term to refer to the Sharpe CAPM, or what was sometimes referred to as the Sharpe-Lintner CAPM. Other asset pricing models that are extensions of the Sharpe CAPM are referred to specifically (as the 'Black CAPM' or 'Merton CAPM').
- Australian surveys of business practitioners published in 1999 and 2005 indicate that a stable 72 to 73 percent of practitioners applied the Sharpe CAPM, which in these surveys is referred to as simply 'the CAPM'.
- Independent experts' reports prepared in the course of takeover bids are required to apply business valuation methods approved by [the Australian Securities and Investments Commission] in its Practice Note 43. In the period 1997 to 2002 (and at the current time), the most popular valuation method was that known as 'market multiples'. However, in a sizeable minority of reports the main valuation method was the Discounted Cash Flow method, and in almost all of these cases the Sharpe CAPM was applied to estimate the cost of equity capital.
- Financial analysts in investment banks are constantly required to update their valuations of businesses. In the period 1997 to 2002 (and at the current time) valuations in the utility and infrastructure sectors have invariably applied the Discounted Cash Flow methodology. These estimates are almost invariably based on the Sharpe CAPM, even though it is rarely referred to in those terms, and is instead called simply 'the CAPM'

In response to the second question, the advice was that, for the following reasons, a reference to the capital asset pricing model, without any other specification or qualification, would be read by an experienced practitioner to be a reference to the Sharpe CAPM, rather than to any other version or extension of the Sharpe CAPM, such as the Black (1972) or Merton (1973) models.

- Throughout the financial economics literature and among business practitioners the Sharpe CAPM is known as the 'standard CAPM' or simply 'the CAPM' and values of input parameters to the model are commercially available, making it easy to apply.
- Extensions to the Sharpe CAPM were undertaken by Black (1972) and Merton (1973), but would require different inputs such as the 'theta' coefficient to implement them. These inputs have not been made commercially available, and as a result these alternative CAPM models have not been widely applied in practice.
- Finance textbooks generally refer to the Sharpe CAPM as simply 'the CAPM', as do financial analysts at investment banks, regulators examining cost of capital issues (e.g. the United Kingdom Competition Commission), and independent experts in the course of valuations undertaken during takeover bids.
- Researchers testing the application of different methodologies for estimating the cost of equity employ the term 'CAPM' as a reference to the Sharpe CAPM without actually specifying that it is the Sharpe CAPM.

Consequently, the available evidence suggests that NGR 87(2)(b) does not permit the use of more than one financial model, and therefore DBP's approach to establishing the cost of equity used to inform its proposed rate of return does not comply with the NGRs.

Are the models used by DBP well accepted?

Even if it were assumed that NGR 87(2)(b) permitted the use of more than one financial model in determining the rate of return, each of the financial models would need to be "well accepted". Given the explicit reference to the Sharpe-Linter CAPM in NGR 87(2)(b), a decision to apply that model in establishing the rate of return would not require a party to demonstrate that it is well accepted.

In considering how a generic reference to the CAPM should be interpreted, the question of the level of acceptance of alternative specifications of financial models was also considered in the advice provided to the ESC in 2008.[6]

- It was noted that there was an absence of evidence to indicate that the Black CAPM has been broadly applied in Australia by financial analysts and business practitioners in valuation or capital budgeting.
- It commented that financial analysts and business practitioners in Australia had not applied the Merton CAPM in valuation and capital budgeting, and that a practical reason for this as that values of the 'theta factor' and resulting 'adjusted beta factor' were not commercially available.
- It noted that the Fama-French Three Factor Model has achieved a degree of support in academic circles, although there has also been scepticism due to concerns about 'data mining'. That is, the reporting of results of strong correlations between variables, without the benefit of a priori theory justifying the inclusion of those variables.

  The advice went on to state that, while the Fama-French model has been applied in portfolio asset allocation in the funds management industry, there was no evidence of widespread application of the model by financial analysts and business practitioners at the individual firm level.

The evidence contained in this advice supports a conclusion that the Black CAPM and the Fama-French Three Factor models are not applied widely by financial analysts and business practitioners, and consequently cannot be considered to be well accepted.

In contrast, and as noted earlier, the advice indicated that the Sharpe-Lintner CAPM, generally simply referred to as the Sharpe CAPM or just the CAPM, is applied widely by financial analysts and business practitioners, and therefore can be considered well accepted.

- Australian surveys of business practitioners published in 1999 and 2005 indicate that a stable 72 to 73 percent of practitioners applied the Sharpe CAPM.

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6 The Origins of the CAPM and its Application in Commercial Practice and Economic Regulation, Statement of Michael Lubomyr Lawriwsky, 16 May 2008, available at www.esc.vic.gov.au/public/Energy/Regulation+and+Compliance/Decisions+and+Determinations/Gas+access+arrangements+review+2008-12/Consultant+reports.htm

- Independent experts' reports prepared in the course of takeover bids are required to apply business valuation methods approved by [the Australian Securities and Investments Commission] in its Practice Note 43. In the period 1997 to 2002 (and at the current time), the most popular valuation method was that known as 'market multiples'. However, in a sizeable minority of reports the main valuation method was the Discounted Cash Flow method, and in almost all of these cases, the Sharpe CAPM was applied to estimate the cost of equity capital.
- Financial analysts in investment banks are constantly required to update their valuations of businesses. In the period 1997 to 2002 (and at the current time) valuations in the utility and infrastructure sectors have invariably applied the Discounted Cash Flow methodology. These estimates are almost invariably based on the Sharpe CAPM.

The available evidence suggests that three of the financial models applied by DBP in establishing a range for the cost of equity, used in informing its proposed rate of return, are not well accepted. In this case, DBP's approach to establishing the cost of equity in informing its proposed rate of return does not comply with the requirements of NGR 87(2)(b).

Recent regulatory decisions

The use of CAPM or the Fama-French model was the cause of significant recent debate in relation to the Jemena gas distribution network in New South Wales. Jemena, as operator of the network, sought to base its rate of return on a cost of equity using the Fama-French model. A very substantial amount if information was provided to the AER in support of Jemena's proposal.

The AER, in its final decision handed down on 11 June 2010, did not accept Jemena's use of the Fama-French model (referred to as "FFM" in the AER's decision), and required the rate of return to be calculated using a CAPM cost of equity (pp.170-172).

> *The AER assesses a range of information and material before it that is relevant to the assessment of the FFM against the requirements of r87 and r74 of the NGR. The AER considers that:*
>
> - *there is no strong theoretical basis to support the inclusion of the additional FFM risk factors for the rate of return on equity:*
>   - *the model is dependent on empirical justification—that is, the systematic observance of the FFM risk premiums*
>   - *since the FFM risk premiums are not systematically observed in the Australian market, there is no reasonable basis for the FFM to be applied in Australia*
> - *the modelling and statistical analysis presented in the revised access arrangement proposal do not provide support for the FFM, including but not limited to:*
>   - *the predictive testing presented in the Oxera report does not support the submission that the FFM is a better predictor than the CAPM*
>   - *grounds for rejecting the Carhart four-factor model could equally be used to reject the FFM*

- *Evaluation of the academic literature does not support the FFM as a reliable or accurate financial model. In particular:*
  - *analysis from Australia, which is the relevant market for funds, shows that observed empirical evidence is not consistent with the FFM, with conflicting, variable FFM risk premiums and inconsistent FFM factor coefficients. This means that it is unreasonable to conclude that the additional FFM risk factors are present in the market for funds and can be used to determine a rate of return on equity*
  - *in relation to evidence in other markets for funds:*

> *analysis from a global perspective (including the UK, Japan and Germany) shows that the observed empirical evidence is not consistent with the FFM*

> *analysis from the US shows conflicting evidence that does not support the FFM for each time period analysed.*

With regard to the evidence examined, the AER considers that:

- *the FFM does not produce a rate of return commensurate with prevailing conditions in the market for funds and the risks involved in providing reference services*
- *the estimates generated are not arrived at on a reasonable basis*
- *the estimates generated by the FFM do not represent the best estimates possible in the circumstances.*

Evaluation and conclusion

The AER notes that it has full discretion (as set out in r. 40(3) of the NGR) over determination of the rate of return to meet the requirements of r. 87 of the NGR.

The AER assesses the FFM after assessment of all material before it, including information provided in the revised access arrangement proposal and other relevant material.

Overall, the AER considers that:

- *the FFM does not meet the requirements of r. 87(1) of the NGR*
- *the FFM does not meet the requirements of r. 87(2)(b) of the NGR.*

Further, the AER also considers that the FFM does not produce forecasts or estimates that meet the requirements of r. 74(2) of the NGR.

Therefore, the AER does not accept the use of the FFM.

The AER instead uses the standard Sharpe–Lintner CAPM to estimate the rate of return on equity. The CAPM is provided under r. 87(2)(b) of the NGR as an example of a well accepted financial model. The use of the CAPM to determine the cost of equity complies with the applicable requirements of the NGL and the NGR and is consistent with the applicable criteria prescribed by the NGL and the NGR. The AER also considers that the use of the CAPM (instead of the FFM) for determining the rate of return is consistent with the revenue and pricing principles set out in section 24 of the

NGL and will or is likely to contribute to the achievement of the National Gas Objective (NGO) in section 23 of the NGL.

Alinta considers that the AER's endorsement of CAPM as the model to be used to determine the cost of equity in accordance with the NGL is compelling. In circumstances where the use of the Fama-French model has been rejected by the regulator for failing to comply with the NGRs (and noting even the Fama-French model results in a cost of equity almost 200 basis points below DBP's nominated cost), Alinta submits that DBP's proposal to not use a financial model at all, but rather base the cost of equity on a range of equity analysts views, is completely untenable and must be rejected by the ERA. It is worth repeating that the cost of equity proposed by DBP is more than 470 basis points higher than that which would be obtained using the financial model required by the AER, namely CAPM.

Cost of debt

Paragraph 11.1of DBP's proposed revised AAI indicates that the cost of debt used by DBP to determine its proposed rate of return on capital of 10.76 per cent was 9.73 per cent.

At paragraph 11.12, DBP notes that the cost of debt has been estimated as the bank bill swap rate (BBSW) plus lender's margin, and transaction and other costs, some of which may be specific to particular markets, but also that the cost of debt was of the cost of debt was built-up from the costs which a benchmark service provider (with credit rating in the BBB range) was likely to incur in sourcing debt finance from:

- the 5 year Australian Bank Market (28.6 per cent);
- the 7 year Australian Bank Market (9.5 per cent);
- the 7 year Australian Bond Market (9.5 per cent);
- the 10 year US Public Market (33.3 per cent); and
- the 10 year US Private Placement Market (19.0 per cent).

Paragraph 8.1 of DBP's Submission 8 summarises the standard approach that has been adopted by regulators in Australia to establish an estimate of the cost of debt, and at paragraph 8.5 to 8.21 (some of which ahs been deleted), DBP outlines the approach it has adopted in deriving an estimate for the cost of debt of 9.73 per cent.

However, much of the detail about the manner in which DBP has calculated the cost of debt has been deleted from Submission 8, or if it is contained in attachments to the submission these have not been made publicly available. As a result, it is not possible to comment on whether the cost of debt proposed by DBP has been arrived at on a reasonable basis and represents the best forecast or estimate possible in the circumstances.

It is also unclear whether DBP's approach is that it may not be consistent with finance theory underpinning the derivation of a WACC, using the CAPM. Specifically, it appears that accepting DBP's proposal may result in the rate of return being applied in such a way as to take into account the specific business risks. In this context, the Authority has previously commented that:[7]

> *…under generally accepted finance theory and commercial practice, non-systematic risks are not relevant to the calculation of a rate of return because it is assumed that they are diversifiable in a portfolio of investments. In this, it is not the diversification opportunities of the utility that are relevant, but those of investors. That is, since investors who could purchase the assets of the utility are capable of diversifying investment portfolios, the returns that these investors require and therefore the amount they are willing to pay for the regulated asset will depend only on the non-diversifiable risk of the asset.*

Operating Expenditure

Issue 7 Operating Expenditure

Submissions are invited from interested parties on:

- *whether the arrangements for fuel gas are reasonable and reflect existing arrangements in place;*
- *whether the level of operating expenditure (actual and forecast) and detail of the information provided by DBP is reasonable having regard to the legislation;*
- *DBP's supporting information to justify operating expenditure; and*
- *any other matters in relation to operating expenditure under the proposed revisions.*

Summary

As shown in Table A.8 below, DBP's proposed revised AAI indicates that its actual operating expenditure during the period 2005-2010 was $453.7 million. This is around $26.9 million, or 5.6 per cent, lower than the level of operating expenditure for the period 2005-2010 approved by the Authority, which Alinta estimates at $480.5 million based on information contained in the Authority's Issues Paper and DBP's Proposed Tariff Model.

[7] Economic Regulation Authority 2005, *Determination of the preferred methodology for calculating the weighted average cost of capital for covered electricity networks*, August 2005 paragraph 32, p.6

Table A.8 DBP –Access Arrangement, actual and forecast operating expenditure ($M, December 2009)

	1	2	3	4	5	6	Total
Approved 2005-2010	69.53	65.85	88.84	86.64	84.35	85.30	480.51
Actual 2005-2010	68.78	66.40	79.44	69.03	84.22	85.78	453.65
Forecast 2011-2015 (Nominal)	106.79	111.95	115.46	122.61	127.42	na	584.22
Forecast 2011-2015	101.64	103.96	104.60	108.37	109.87	na	528.44

Source: DBP 2010, Revised Access Arrangement Information, Public Version, 1 April 2010, Table 3 and Table 18. DBP, Proposed Tariff Model

DBP is forecasting aggregate operating expenditure for the period 2011-2015 of $528.4 million, although this relates to a period that is one year shorter than the previous period and therefore understates the actual increase in annual operating expenditure between the two periods.

Specifically, when compared with (estimated) actual operating expenditure in 2010, DBP's forecast operating expenditure for 2011 is almost $15.9 million, or around 18.5 per cent, higher in aggregate. If fuel gas operating expenditure is excluded, DBP's forecast operating expenditure is just over $16.9 million, or around 26.1 per cent higher in 2011 compared with 2010.

Completeness and sufficiency of information

Alinta considers there are a number of areas where the information provided by DBP in the AAI in respect of its actual and forecast operating expenditure may not meet the requirements of the NGR, including the requirements that:

- the AAI contain the information that is reasonably necessary for users and prospective users to understand either the background to the access arrangement or the access arrangement proposal, or the basis and derivation of the various elements of the access arrangement or the access arrangement proposal [NGR(42(1)]; and
- the AAI include operating expenditure (by category) over the earlier access arrangement period [NGR 72(1)(a)(ii)]; and
- the AAI include a forecast of operating expenditure over the access arrangement period and the basis on which the forecast has been derived [NGR72(1)(e)]; and
- all financial information must be provided, and all calculations made, consistently on the same basis [NGR 73(3)]; and
- information in the nature of a forecast or estimate must be supported by a statement of the basis of the forecast or estimate, arrived at on a reasonable basis and must represent the best forecast or estimate possible in the circumstances [NGR 74].

Specifically, Alinta requests that the Authority examine whether the AAI submitted by DBP meets the requirements of the National Gas Rules in the following areas.

- Table 3 (p.7) indicates that actual real operating expenditure for the period 2005-2010 is in December 2010 terms. It is unclear whether the reference to December 2010 is correct, or whether the reference should instead have been to December 2009 as is the case for all other actual real financial information for the period 2005-2020. For the purposes of its analysis, Alinta has assumed that the data is on December 2009 terms.

  Nevertheless, to the extent that actual real operating expenditure for the period 2005-2010 is presented in December 2010 terms, this would appear to be inconsistent with the requirement in NGR 73(3) that all financial information must be provided consistently on the same basis.

- Paragraph 4.3 claims that due to changes in the physical characteristics of the DBNGP, reference to historical operating expenditure is inappropriate. It is unclear whether DBP opted not to provide details of actual operating expenditure by category for the period 2005-2010 for this reason, given it is obliged to do by NGR 72(1)(a)(ii).

  Without information on the actual level of operating expenditure by category (with those categories being the same as those contained in Table 18. p.19) incurred by DBP for the period 2005-2010, it is not possible for users or prospective users of the DBNGP to form an opinion as to the reasonableness of forecast operating expenditure for the period 2011-2015.

  Specifically, while the configuration of the DBNGP may have changed since 2005, given the practical completion of the Stage 5B expansion and DBP's expectation that there will be no further expansions in the period 2011-2015, it appears reasonable to presume that forecast operating expenditure in 2011 should not differ materially from actual operating expenditure in 2010.

- The proposed revised AAI appears to provide forecast operating expenditure for the period 2011-2015 only in nominal terms, which makes comparison to actual operating expenditure difficult and appears to be inconsistent with the obligation imposed by NGR73(3) that all financial information must be provided consistently on the same basis.

  Alinta notes that DBP's Submission 12 and its Proposed Tariff Model do provide forecast operating expenditure for the period 2011-2015 in December 2009 terms.

Is DBP's actual and forecast operating expenditure 'efficient'?

NGR 91(1) requires that operating expenditure must be such as would be incurred by a prudent service provider:

- acting efficiently; and
- in accordance with accepted good industry practice;

to achieve the lowest sustainable cost of delivering pipeline services.

Alinta considers that a conclusion that DBP's actual operating expenditure complies with NGR 91(1) cannot be inferred simply:

- because it was below the approved forecast at the time the current Access Arrangement was approved; or
- from the existence of an incentive mechanism in the period 2005-2010 [as the Authority is permitted to do under NGR 71(1)].[8]

Specifically, given DBP is now forecasting an increase of just over 26 per cent in operating costs (excluding fuel gas) between 2010 and 2011, Alinta considers that a detailed investigation of DBP's actual operating expenditure during the period 2005-2010 and forecast operating expenditure during the period 2011-2015 is necessary. This is for two reasons, which are as follows.

- There is compelling evidence from recent Access Arrangement decisions in similarly regulated industries and other jurisdictions to conclude it likely that not all of DBP's actual and forecast operating costs will meet the requirements of NGR 91(1).
- The need for a detailed investigation of DBP's actual operating expenditure during the period 2005-2010 and forecast operating expenditure for the period 2011-2015 is highlighted by the fact that DBP has not provided any independent evidence to corroborate its claims that its actual and forecast operating expenditure meets the requirements of NGR 91(1).

Further, paragraph 9.4 of DBP's AAI claims that forecast operating expenditure for the period 2011-2015, which it derived through internal business planning and budgeting processes, represents the lowest sustainable cost of providing pipeline services by a prudent service provider acting efficiently. However, given there is no evidence that the requirements of NGR 91(1) informed DBP's process in setting forecast operating expenditure, Alinta considers a detailed investigation by the Authority is required to ensure that DBPs forecasts meet the requirements of NGR 91(1).

DBP also argues that many of its activities are required for the safe and reliable operation of the DBNGP that have been identified pursuant to a Safety Case, to which it claims the Western Australian Government has announced changes, and should therefore be accepted by the Authority. However, no information about the changes to the Safety Case has been provided to substantiate this claim.

Rather, DBP's claim that forecast operating expenditure meets the requirements of NGR 91(1) appears to be entirely based on its assertion that this is the case, rather than any persuasive evidence to that effect. Specifically, the claim made in DBP's AAI that its forecast operating expenditure represents the lowest sustainable cost of providing the Reference Services appears without evidentiary basis.

[8] This is consistent with the Authority's Draft Decision in respect of the gas distribution system operated by WA Gas Networks (WAGN) in 2005 where, while recognising that WAGN faced incentives to be efficient, the Authority did not accept that it would be appropriate to infer, simply from the existence of such incentives, that WAGN's (then) current operating and maintenance costs were efficient.

In summary, DBP's claim that its forecast operating expenditure complies with NGR 91(1) (i.e. that this is the amount of expenditure that would be incurred by a prudent service provider acting efficiently, and in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services):

- does not appear to be supported by information contained in its proposed revised AAI or submissions;
- does not appear to be supported by independent analysis or review of its actual or forecast operating expenditure; and
- does not appear to be supported by any benchmarking comparison to other natural gas transmission businesses.

Further comments on DBP's actual operating expenditure for the period 2005-2010, the inputs used by DBP to develop its forecast operating expenditure and on the quantum of proposed forecast operating expenditure by category, for the period 2011-2015, are provided in the following sections.

Operating expenditure other than Fuel Gas

As shown in Table A.9 below, DBP's AAI indicates that its actual operating expenditure (excluding fuel gas) during the period 2005-2010 was $315.3 million. This is around $10.6 million, or 3.5 per cent, higher than the level of operating expenditure (excluding fuel gas) for the period 2005-2010 approved by the Authority, which Alinta estimates at $304.7 million based on information contained in the Authority's Issues Paper and DBP's Proposed Tariff Model.

DBP is forecasting aggregate operating expenditure (excluding fuel gas) for the period 2011-2015 of $419.9 million, although this relates to a period that is one year shorter than the previous period and therefore understates the actual increase in operating expenditure.

Table A.9 DBP –Access Arrangement, actual and forecast operating expenditure (exc. fuel gas) ($M. December 2009)

	1	2	3	4	5	6	Total
Approved 2005-2010	46.94	43.61	57.02	53.72	51.28	52.15	304.71
Actual 2005-2010	41.31	43.01	47.03	53.56	65.60	64.80	315.31
Forecast 2011-2015 (Nominal)	85.87	89.29	92.34	96.49	100.15		464.14
Forecast 2011-2015	81.73	82.92	83.65	85.28	86.36		419.95

Source: DBP 2010, Revised Access Arrangement Information, Public Version, 1 April 2010, Table 3 and Table 18. DBP, Proposed Tariff Model

Paragraph 4.3 of DBP's proposed revised AAI claims that changes in the physical characteristics of the DBNGP mean that reference to historical operating expenditure is inappropriate when considering operating expenditure required to operate the pipeline as it is currently configured.

Alinta considers that given the practical completion of the Stage 5B expansion and DBP's expectation that there will be no further expansions in the period 2011-2015, it appears reasonable to presume that forecast operating expenditure in 2011 should not differ markedly from actual operating expenditure in 2010.

Therefore, it is of interest that, when compared with (estimated) actual operating expenditure (excluding fuel gas) in 2010, DBP's forecast operating expenditure (excluding fuel gas) for 2011 should be almost $16.9 million, or around 26.1 per cent, higher.

Neither the proposed revised AAI nor the various submissions provided by DBP appear to address the specific drivers that might cause forecast operating expenditure (excluding fuel gas) in 2011 to differ so markedly from estimated actual expenditure (excluding fuel gas) in 2010. The reason for this significant step increase in forecast operating costs is the more puzzling given that over the period 2011-2015, operating costs (excluding fuel gas) are forecast to increase by only between around one and two percent per annum.

The ability of users and prospective users to understand the basis and derivation of DBP's forecast operating costs (excluding fuel gas) are significantly impeded by the fact that DBP has not provided information on the actual level of operating expenditure by category (with those categories being the same as those contained in Table 18. p.19) for the period 2005-2010. In the absence of this information, it is also difficult for users and prospective users to form a view on the relevance and importance of the various drivers for movements in operating cost identified by DBP in Submission 12.

In particular, there appears to be no discussion of DBP's decision in early 2009 to bring back in-house a significant proportion of the operating and maintenance services that were then contracted out to Westnet Energy Services Pty Ltd. This decision appears to be very relevant to both DBP's actual operating expenditure for the period 2005-2010 and its forecast operating expenditure for the period 2011-2015 (and may also be relevant in the context of the marked increase in SIB capital expenditure in 2009 and 2010, which was identified earlier).

While Alinta is not aware of the precise details, it would appear reasonable to presume that DBP's decision referred to above was intended, and should be expected, to result in lower operating and maintenance expenditure. Alinta's view is consistent with the message in DBP's media release in 2009 in relation to the arrangements with Westnet Energy Services, in which DBP referred to a belief that "important efficiencies can be achieved" and efficiencies were "anticipated"[9].

However, as shown in Table A.6, it appears that DBP's operating costs (excluding fuel gas) in 2009 and 2010 increased by more than 20 per cent from 2008 levels. In the absence of information on actual level of operating expenditure by category, it is not possible to ascertain the reasons for this increase, but it is nevertheless possible that DBP's decision to bring back in-house operating and maintenance services may have contributed to this increase.

[9] DBP Media Release attached to ASX announcement by DBP's majority owner DUET Group released 9 February 2009.

For this reason, Alinta considers that the Authority should review the basis for DBP's decision to bring back in-house a significant proportion of the operating and maintenance services that has been contracted out to Westnet Energy Services Pty Ltd in order to ensure that this approach will result in operating expenditure that is consistent with the requirements of NGR 90(1), being that it is such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services.

Section 9.3(d) of DBP's proposed revised AAI and section 6.35 of its Submission 12 indicate that its forecast operating expenditure for the period 2011-2015 include costs attributable to the Carbon Pollution Reduction Scheme (CPRS). Alinta notes that there is now significant uncertainty as to whether such a scheme will be introduced by the Commonwealth Government at all, but that in any event there is no likelihood that such charges would be payable by DBP during 2011 and 2012.

Further, it would appear that the Tax Change Variation formula, which forms part of the Reference Tariff Variation Mechanism described in paragraph 15.8 of the proposed revised AAI, provides a better mechanism through which to ensure that the impost of any scheme that attaches a cost to emissions from the DBNGP can be reflected in adjustments to the reference tariffs.

Given the current level of uncertainty around the CPRS, Alinta considers that no allowance for a CPRS should be made in forecast operating expenditure for the period 2011– 2015.

Fuel gas arrangements

DBP's forecasts of fuel gas operating expenditure are shown in Table A.10 below, and will reflect the volume of fuel gas used by the DBNGP and the price assumed for that fuel gas.

Table A.10 DBP –Access Arrangement, actual and forecast fuel gas operating expenditure

	1	2	3	4	5	6	Total
Approved ($M, December 2009)	22.60	22.24	31.82	32.92	33.07	33.15	175.80
Actual ($M, December 2009)	27.47	23.39	32.40	15.47	18.62	20.99	138.34
Forecast ($M, Nominal)	20.92	22.66	23.13	26.11	27.26		120.08
Forecast ($M, December 2009)	19.91	21.04	20.95	23.08	23.51		108.49

Source: DBP 2010, Revised Access Arrangement Information, Public Version, 1 April 2010, Table 3 and Table 18.
DBP, Proposed Tariff Model

In the public version of Submission 12, DBP has not provided any information as to either the forecast volume of fuel gas it expects the DBNGP to require each year in the period 2011-2015, nor the price at which it has assumed it will be able to obtain this volume of fuel gas.

The absence or suppression of information on the forecast volume of fuel gas (e.g. fuel gas as a percentage of total gas throughput) means that users and prospective users cannot reasonably be expected to form a view on whether the forecast complies with NGR 91(1) and NGR 74(2).

It is also noted that on 10 March 2010, the ACCC accepted a variation to the 2004 Undertaking that permits DBP, as the operator of the DBNGP to reach agreements with individual shippers to pass on a proportion of the increased price it will pay for system use gas (i.e. fuel gas) under its agreement with Alinta (specifically, Alinta Sales Pty Ltd). There are two types of agreements that the DBNGP operator may reach with shippers:

- to charge a shipper a system use gas tariff; or
- to reduce the charges payable by a shipper under the standard shipper contract in consideration for that shipper supplying its own share of system use gas to the DBNGP.

The variation permits both types of agreement provided that the tariff imposed or reduction of charges is not less favourable than that agreed with Alinta Sales Pty Ltd, Alinta Energy (LPG) Pty Ltd, or a shipper that is an associate of Prime Infrastructure Holdings Limited.

It is not apparent from the information included in DBP's proposed revised AAI, nor any of its submissions, what assumptions it has made and arrangements it has in place in respect of revenue that may be gained by charging a shipper a system use gas tariff or lost where it discounts charges to shippers supplying its own share of system use gas.

In summary, Alinta considers that DBP's proposed revised AAI:

- does not meet the requirements of NGR 42(1) as it does not contain the information that is reasonably necessary for users and prospective users to understand the basis and derivation of its forecast operating expenditure, and
- hence it is also not possible for users or prospective users of the DBNGP to form an opinion as to whether DBP's forecast operating expenditure for the period 2011-2015 complies with NGR 74(2), being that it was arrived at on a reasonable basis and represents the best forecast possible in the circumstances.

Tariffs

Issue 10 Tariffs

Submissions are invited from interested parties on:

- *the proposed increase in the reference tariff;*
- *the proportion of cost of service to be recovered by each component of the reference tariff;*
- *the allocation of costs between reference and other services;*
- *DBP's supporting information to justify the tariffs; and*
- *any other matters in relation to tariffs under the proposed revisions.*

Proposed increase in the Reference Tariff

Table A.11 shows the approved Reference Tariff for the existing T1 Reference Service and Alinta's estimate of the reference tariff for DBP's proposed R1 Reference Service.

Table A.11 DBP –Access Arrangement, actual and forecast full haul reference tariffs (nominal)

	2006	2007	2008	2009	2010	2011	Percentage change
Capacity	0.936655	0.981650	1.007000	1.056431	1.069105	1.645532	53.9%
Commodity	0.107334	0.112490	0.115395	0.121059	0.122512	0.079855	-34.8%
Total	1.043989	1.094140	1.122395	1.177490	1.191617	1.725387	44.8%

Source: Economic Regulation Authority Annual Tariff variation notices, various and DBP 2010, Proposed Tariff Model

Alinta's estimate of the nominal level of the R1 Reference Tariff in 2011 shown in Table A.11 above is based on the values included in clause 3.2(c) of DBP's proposed revised access arrangement, which have then been escalated by DBP's forecast of inflation for 2010 of 2.5 per cent.

Table A.11 illustrates that DBP's access arrangement proposal would result in an increase of almost 45 per cent in the nominal tariff for the prevailing full haul reference service. However, Alinta considers that the proposed R1 Reference Service is a far inferior service to the existing T1 Reference Service, and consequently the nominal increase shown in Table A.7 does not adequately reflect the full transfer of value from shippers to DBP as the operator of the DBNGP.

Table A.7 also illustrates DBP's proposal that the proposed R1 Reference Tariff comprise of 95.4 per cent capacity reservation and 4.6 per cent commodity charge split at a 100 per cent load factor. This is a material change from the existing approved T1 Reference Tariff, which has an 80/20 split between capacity reservation and commodity charges.

Increasing the proportion of the reference tariff recovered through the capacity component from 80 per cent in the case to the T1 Reference Service to 95.4 per cent for the proposed R1 Reference Service results in a reduction of around 75 per cent in DBP's exposure to pipeline volume risk (i.e. from 20 per cent to less than 5 per cent). The effect is to provide far greater revenue certainty to DBP, and significantly weakens the incentive DBP currently has to efficiently optimise pipeline throughput. The financial impact on shippers who operate at less than a 100 percent load factor is even more significant.

Allocation of costs between reference and other services

NGR 93 (1) requires that total revenue is to be allocated between reference and other services in the ratio in which costs are allocated between reference and other services. NGR 93(2) states that costs are to be allocated between reference and other services as follows.

- Costs directly attributable to reference services are to be allocated to those services.

- Costs directly attributable to pipeline services that are not reference services are to be allocated to those services.
- Other costs are to be allocated between reference and other services on a basis (which must be consistent with the revenue and pricing principles) determined or approved by the AER.

Given these requirements, Alinta has significant concerns about the manner in which DBP has allocated costs to the proposed R1 Reference Service. Specifically, in paragraph 14.2 of the proposed revised AAI, DBP states that

> *"…costs have been allocated to the Services provided to Shippers with Access Contracts entered into prior to the commencement of the Current Access Arrangement Period, as if those Shippers had been provided with the Reference Service".*

Further, Table 21 the proposed revised AAI shows that the costs allocated for recovery by the R1 Reference Tariff match the **entire** total forecast revenue for the DBNGP shown in Table 22.

It is clear from the information contained in DBP's proposed revised AAI (e.g. Tables 4, 5 and 6) and its submissions that it provides a range of pipeline services, including at least the T1 Service under the 2004 Contractual Arrangements, and possibly to a lesser extent the T1, B1 and P1 Reference Services under the 2005 Access Arrangement or under earlier gas transmission contracts. In most cases, it is likely that the minimum term governing the provision of these services to users will mean that these existing services will continue to account for the overwhelming majority of pipeline services provided by the DBNGP in the period 2011-2015.

It is therefore unclear, why in setting the reference tariff for the proposed R1 Reference Service, DBP has elected to allocate **all** costs to the proposed R1 Reference Service, instead of, as it is required to do by NGR93(1), first allocating costs (and revenue) on the basis that they are directly attributable to providing the proposed R1 Reference Service and existing services, and then to allocating any remaining costs between the proposed R1 Reference Service and existing services on the basis of a methodology determined or approved by the Authority.

In this context, Alinta requests that the Authority advise users and prospective users of the DBNGP whether it has determined or approved a methodology by which DBP may allocate common costs (i.e. remaining costs that are costs that cannot be directly attributed to any one service) between the proposed R1 Reference Service and existing services.

At this stage, and based on the information provided by DBP, it would appear to Alinta that DBP's approach in allocating costs to the proposed R1 Reference Service is fundamentally flawed and clearly inconsistent with the requirements of NGR 93.

Although the approach adopted by DBP may at first appear to be essentially the same in concept as was used for the current 2005 Access Arrangement, its application was to an entirely different set of circumstances. Specifically, the exercise in 2005 involved allocating costs to a number of new reference services that were each ostensibly the same as a number of prevailing non-reference services. That is, each of the reference services were effectively a substitute for each of the non-reference services, with each continuing to be utilised over the Access Arrangement period by exactly the same shippers with no gap.

However, Alinta considers that such an approach has no basis or validity in relation to the proposed R1 Service, and in any event for the reasons outlined above would not comply with the NGRs. This is because the proposed R1 Reference Service is substantially different to each of the reference services under the 2005 Access Arrangement, and therefore also fundamentally different to each of the non-reference services currently received by shippers on the DBNGP.

Fully allocating all of the DBNGP costs to a new service that is significantly different to existing services on the DBNGP, and that will therefore be required to co-exist with these services, is fundamentally flawed.

In any event, DBP does not actually provide any forecast throughput volumes for the proposed R1 Reference Service in the throughput forecast contained in Submission 7. The lack of forecast throughput by service makes it difficult to assess the relative cost and revenue proportions across all services, which in turn makes it difficult to properly assess the reasonableness of the proposed R1 Reference Tariff.

Fixed Principles

DBP is proposing to include as a Fixed Principle that revenue earned by it during the period commencing on 1 July 2005 and ending on 31 December 2015 from the sale of any Services which is in excess of the amount (in net present value terms) equal to the sum of:

- the revenue that would have been earned had any of those services which were Full Haul Services been sold at the Reference Tariff; and
- the revenue actually earned from the sale of those services which were services other than Full Haul Services, must not:
  - be taken into account directly or indirectly for the purposes of setting a Reference Tariff or determining or applying any aspect of the price and revenue elements of the Access Arrangement which applies on or after 1 January 2011; or
  - otherwise be taken into account directly or indirectly by the relevant Regulator in performing any of its functions under the NGA, NGL or NGR."

It seems clear to Alinta that any relevance the Fixed Principle has or had under the 2005 Access Arrangement cannot be transposed to a revised Access Arrangement for the period 2011-2015 where the R1 Reference Service is the only reference service. This is a different issue as to whether the existing Fixed Principle has been applied, or properly applied in the 2005-2010 period and in the transition to the proposed revised Access Arrangement to apply in the period 2011-2015.

It is understood that the purpose of the Fixed Principle in 2005 was to ensure that the higher tariff that T1 Service Shippers committed to pay under the 2004 Contractual Arrangements would not be fed back into the calculation of the Reference Tariff under the Applicable Regime. That is, revenue from the contracted T1 Service was treated as if it had been priced at the Reference tariff - not the 2004 Contractual Arrangements. The reason for this was that there was a need under the 2004 Contractual Arrangements to price the T1 Reference Service entirely in accordance with the principles and requirements of the Applicable Regime. This is because when the price for the T1 Service under the 2004 Contractual Arrangements reverts to a price under the Applicable Regime it reverts to a price that has been calculated consistently and strictly in accordance with the Applicable Regime, properly applied and not a hybrid of the 2004 Contractual Arrangements and the Applicable Regime.

If DBP were not to be required to offer any or all of the T1, B1 and P1 Reference Services in the period 2011-2015 on a basis that ensures these reference services are substantially the same as the T1, B1 and P1 Reference Services in the 2005 Access Arrangement, then this Fixed Principle has no application to the setting of the reference tariff for the proposed R1 Reference Service.

Alinta considers that it is critical that the Fixed Principle only be retained if at least a T1 Reference Service, which is substantially the same as the T1 Reference Services in the 2005 Access Arrangement, is offered in the revised Access Arrangement for the period 2011-2015, and that the Fixed Principle must only apply to the relationship between the T1 Reference Tariff (as properly priced under the NGR) and the tariff under the 2004 Contractual Arrangements.

Tariff Variation Mechanism

Issue 11 Tariff Variation Mechanism

Submissions are invited from interested parties on:

- *the proposed reference tariff variation mechanism including the inflation index and the expanded scope for variation;*
- *the proposed reference tariff variation mechanism in the context of the national gas objective and the revenue and pricing principles;*
- *DBP's supporting information to justify the tariff level and methodology; and*
- *any other matters in relation to the tariff variation mechanism under the proposed revisions.*

Proposed tariff variation mechanism

DBP's proposed tariff variation mechanism is set out in section 11 of its access arrangement proposal and section 15 of its proposed revised AAI, and allows for adjustments to the reference tariff for the proposed R1 Reference Service for the following reasons.

- CPI formula variation
- Tax changes variation
- New costs pass through variation
- The mechanism contained in clause 20.5 of the terms and conditions for the proposed R1 Reference Service.

Alinta considers that, based on the information available to it, components of the reference tariff variation mechanism proposed by DBP are not likely to comply with NGR 97(1), which requires that a reference tariff variation mechanism may provide for variation of a reference tariff:

- in accordance with a schedule of fixed tariffs; or
- in accordance with a formula set out in the access arrangement; or
- as a result of a cost pass through for a defined event (such as a cost pass through for a particular tax); or
- by the combined operation of 2 or more or the above.

CPI Formula Variation

DBP's Access Arrangement Information (AAI) indicates that where necessary, the rate of inflation has been measured by the Consumer Price Index (All Groups, Perth).

Although it appears that this component of DBP's proposed tariff variation mechanism meets the requirements of NGR 97(1), prevailing regulatory practise appears to be to define the CPI as the Consumer Price Index (All Groups, Eight Capital Cities). For example, the Amended Proposed Revisions to the Access Arrangement for the South West Network (SWIN) (owned and operated by Western Power) that were approved by the Authority in December 2009 defined the CPI as the Consumer Price Index (All Groups, Eight Capital Cities).

Similarly, the Authority's approved Costing Principles (April 2009) for Westnet Rail, which provides a framework for the calculation and determination of floor and ceiling costs required under the Railways (Access) Code 2000, indicate that in determining the CPI, the Australian Bureau of Statistics Weighted Average of Eight Capital Cities All Groups CPI index is to be used.

The AER's Access Arrangement Guideline (dated March 2009) also implies that the CPI should be defined as the Consumer Price Index (All Groups, Eight Capital Cities). For example, in Section 6.1.2 discussing specified pricing formulas, the AER requires that (p.76):

> *…the CPI values are defined as the Consumer Price Index (All Groups-weighted average of eight capital cities) published by the Australian Bureau of Statistics (ABS)*

DBP also indicates it has derived its estimate of forecast inflation, used in establishing the rate of return under NGR 87(1), as the geometric mean of the Reserve Bank of Australia's (RBA) inflation forecasts (forecast changes in the CPI) for the next ten years.

Given this inflation forecast is an Australia-wide forecast, Alinta considers DBP's proposed revisions to the Access Arrangement for the period 2011 - 2015 would be internally inconsistent if it were to adopt as the CPI the Consumer Price Index (All Groups, Perth) instead of the Consumer Price Index (All Groups, Eight Capital Cities).

To the extent that the use of Consumer Price Index (All Groups, Perth) instead of the Consumer Price Index (All Groups, Eight Capital Cities) creates an inconsistency, it appears that DBP's proposed revised Access Arrangement may not comply with NGR 73(3), which requires that all financial information must be provided, and all calculations made, consistently on the same basis.

Alinta considers that in the absence of evidence to the contrary, regulatory precedent suggests that the objectives of the National Gas Rules (and internal consistency) will be best achieved by requiring DBP to apply as the CPI the Consumer Price Index (All Groups, Eight Capital Cities) for the period 2011 – 2015.

Tax Changes Variation Mechanism

As discussed earlier, section 9.3(d) of DBP's proposed revised AAI and section 6.35 of its Submission 12 indicate that its forecast operating expenditure for the period 2011-2015 include costs attributable to the CPRS. In part, the Tax Changes Variation Mechanism component of DBP's tariff variation mechanism appears directed at allowing it to pass through costs or savings that may arise should the impost of a scheme to attach a cost to carbon emissions.

However, there is now significant uncertainty as to whether such a scheme will be introduced by the Commonwealth Government at all, but that in any event there is no likelihood at all that such charges would be payable by DBP during 2011 and 2012.

Further, as DBP's proposed access arrangement, and its calculated total revenue, already includes an allowance for forecast operating expenditure associated with the introduction of legislation to tax carbon, this aspect of its Tax Changes Variation Mechanism may not be consistent with the requirements of NGR 97(1). This is because the Tax Changes Variation Mechanism would not unambiguously result in a cost pass through for a defined event, in this case the cost pass through for the CPRS. As noted earlier, the Tax Changes Variation Mechanism could also result in a pass through of savings that may arise from the tax should the cost impost be less than forecast by DBP. Such a scenario is clearly not consistent with the requirements of NGR 97(1).

For these reasons, Alinta considers that the Authority should require that:

- no allowance for costs that may be associated with a future CPRS should be made in DBP's forecast operating expenditure for the period 2011–2015; and
- the Tax Changes Variation Mechanism component of the tariff variation mechanism be amended so as to provide a mechanism through which DBP is allowed to pass through the costs that might be incurred under a CPRS (or similar scheme); and
- the definition of Tax Change be amended accordingly.

New Costs Pass Through Variation

The New Costs Pass Through Variation mechanism, set out in paragraph 11.4(a) of DBP's proposed revised access arrangement, would allow DBP to pass through "certain expenses" that:

- are beyond its control; and
- could not be predicted prior to the time at the revisions to the Access Arrangement were approved; and
- were not included in the Total Revenue for one or more years of the Access Arrangement

Paragraph 11.4(b) of the proposed revised Access Arrangement does not appear to define, or limit, the "certain expenses" that may be passed through under paragraph 11.4(a), but does indicate that without limitation examples of such "certain expenses" would include expenses resulting from:

- a Change in Law;
- unanticipated Tax Change that is not the subject of a variation to the Reference Tariff pursuant to the mechanism in paragraph 11.3(b) – including the direct and indirect costs of action by agencies of government or other statutory agencies; and
- the additional costs not included in the forecast operating expenditure and which arise from unanticipated increases in the price of System Use Gas purchased to meet the Operator's obligations under any Access Contract for the Reference Service

A "Change in Law" is defined in the proposed revised Access Arrangement as meaning "…the enactment or promulgation of any new Act of Parliament or regulation, the amendment of any existing Act or regulation, or a material change to the basis or method of calculation of any existing charge relating to:

(a) the management or protection of the environment which is specifically directed at industries which consume hydrocarbon fuels;

(b) the health and safety of workers;

(c) access to the DBNGP Corridor; or

(d) the operation and management of gas pipelines."

Alinta considers that the New Cost Pass Through Variation mechanism is unreasonably broad, and in any event does not meet the requirements in NGR 97(1) for a tariff variation mechanism. This is because the New Costs Pass Through Variation mechanism would not result in variation of the a reference tariff only:

- in accordance with a schedule of fixed tariffs; or
- in accordance with a formula set out in the access arrangement; or
- as a result of a cost pass through for a defined event (such as a cost pass through for a particular tax); or
- by the combined operation of 2 or more or the above.

For these reasons, Alinta considers that the Authority must reject the proposed New Costs Pass Through Variation mechanism in DBP's proposed tariff variation mechanism.

Mechanism in Clause 20.5 of the R1 Terms and Conditions

It appears to Alinta that clause 20.5 simply makes reference to the Reference Tariff Variation Mechanism, and it is therefore appears to be a partially circular reference.

Given that clause 20.5 itself does not include a mechanism by which the reference tariff can be varied, Alinta considers that DBP's proposed tariff variation mechanism should be amended to remove the reference to "the mechanism contained in clause 20.5 of the terms and conditions for the proposed R1 Reference Service".

Terms and Conditions

Issue 12 Terms and Conditions

Submissions are invited on:

- *whether the terms and conditions should vary from current approved terms and conditions under existing access contracts for full haul services negotiated with shippers, which go beyond amendments required to accommodate changed legislative requirements;*
- *any issues interested parties have with existing access arrangement terms and conditions (2005-2010) and the proposed revised terms and conditions;*
- *whether the proposed terms and conditions are consistent with the national gas objective and, if appropriate, the revenue and pricing principles, including comments on DBP's supporting information to justify the terms and conditions; and*
- *any other matters in relation to the terms and conditions under the proposed revisions.*

As discussed in detail under Issue 2, Alinta considers that there is abundant evidence available to the Authority that the T1 Service (or an equivalent service) is the full haul pipeline service that is, and will be, sought by an overwhelming majority of users and/or prospective users of the DBNGP. Consequently, Alinta considers that the T1 Service (or an equivalent) must be offered by DBP as a reference service under the access arrangement proposal for the period 2011-2015.

Nevertheless, to the extent that the revised Access Arrangement for the period 2011-2015 were to include a T1 Reference Service that was substantially the same as the existing T1 Reference Service (and therefore the T1 Service), Alinta considers that the matters raised under Issue 4 in respect of capital contributions must still be addressed.

As also discussed in detail earlier, a critical aspect of the 2004 re-commercialisation was that the tariff for the T1 Service would return to the reference tariff for the equivalent reference service in 2016. DBP has contracted with Alinta, and most 2004 shippers under the T1 Standard Shipper Contract, to have a T1 Service as part of its access arrangements for 2005 and 2016. Consequently, the absence of the T1 Reference Service in the proposed revised Access Arrangement between 2011 and 2015 is not consistent with the contractual obligations entered into by DBP under the T1 Standard Shipper Contracts.

Alinta considers that the obligations imposed on the parties to the 2004 Contractual Arrangements are entirely consistent with the objective of the NGL and the requirements of the NGRs, and consequently the fact the DBP is now proposing to substantially alter these arrangements must be carefully examined by the Authority in assessing DBP's access arrangement proposal.

While Alinta cannot speak for other users or prospective users of the DBNGP, Alinta does not agree with DBP's claim at paragraph 4.8 of Submission 3 that the proposed R1 Reference Service will be more attractive to shippers, and will encourage shippers to access capacity on the DBNGP. Specifically, Alinta considers that for at least the following reasons, the proposed R1 Reference Service is significantly less attractive than the T1 Service and/or the T1 Reference Service.

- Omission of outer imbalance band and outer hourly peaking band.
- Significant increase in penalties for overrun, imbalance, hourly peaking excursions.
- Requirement that shippers agree to an Inlet Sales Agreement to nominate on behalf of another shipper.
- Monthly cashing out of imbalances.
- Significant expansion of the circumstances in which DBP can refuse to accept or deliver gas, or to curtail, without liability.
- Different methodology for determining capacity quantities.
- There is no equivalent to the concept of the Aggregated T1 Service.

Further comments on the terms and conditions on which the proposed R1 Reference Service would be offered by DBP to the market are provided in Attachment B.

As the comments above, and those in Attachment B illustrate, the proposed R1 Reference Service is fundamentally inferior to the current T1 Service and/or the T1 Reference Service. Given existing T1 Service shippers can gain access to further T1 Service by having DBP expand the capacity of the DBNGP under clause 16 of their shipper contracts, and that new shippers must be offered similar rights - obligations that were insisted on by the ACCC and the State in 2004 - Alinta considers it highly improbable that DBP's proposed R1 Reference Service could reasonably be expected to be sought by a significant part of the market for DBNGP pipeline services.

Capacity Trading Requirements

Issue 14 Capacity Trading Requirements

Submissions are invited from interested parties on:

- *the capacity trading requirements including whether they are consistent with rule 105 and the national gas objective;*
- *practical experience with the current capacity trading requirements; and*
- *any other matters in relation to capacity trading under the proposed revisions.*

The requirement at Clause 6.3(a) of DBP's proposed revised Access Arrangement that the Operator's consent to a transfer of Contracted Capacity to a Third Party will be conditional upon the Third Party complying with the Queuing Requirements in clause 5.4 is a new requirement.

Alinta considers this must be rejected, as it is objectionable for a number of reasons. Firstly it is an unwarranted interference with a shipper's right to deal with its property (i.e. contract interests) as it sees fit. It has never been, and should not be, a requirement that a transferee be the next applicant in the queue.

DBP has adequate safeguards as to the technical and financial capabilities of the transferee in the formal contractual provisions governing assignment, trading or transfer of Contracted Capacity. There is no basis to add this further condition which constrains a shipper's property rights considerably. This new requirement is also inconsistent with aspects of the existing regime. For example, a trade or transfer to an existing shipper does not require Operator's consent in certain circumstances. This is rendered meaningless if the existing shipper is required to be first in the queue. Further, the test for withholding consent in clause 6.2 on technical or commercial grounds is much broader than the existing criteria of financial capacity and technical expertise.

Alinta Pty Ltd
9 July 2010

ATTACHMENT B

DAMPIER BUNBURY PIPELINE - PROPOSED REVISIONS TO THE ACCESS ARRANGEMENT

SUBMISSION ON PROPOSED R1 REFERENCE SERVICE TERMS AND CONDITIONS

Clause Number	Provision / Issue	Comment
1	**B1 Service** is defined as a "Back Haul service which, under the terms of a contract for the Back Haul Service, is specified to rank equally to a R1 Service in the Curtailment Plan".	The B1 Service ranks ahead in priority to the R1 Service in the Curtailment Plan in Schedule 6. The definition of B1 Service is not correct.
1	The definition of **Force Majeure** has been amended to include an Insolvency Event in relation to a third party supplier of the Operator	The amendment should be deleted as the Operator should be able to and required to take steps in those circumstances to ensure its ability to perform its obligations under the Contract is not affected.
1	The definition of **Major Works** now includes the defined term **Planned Maintenance**. This means that Planned Maintenance is an additional exculpation from the Operator being liable for curtailing for more than 2% each year.	The definition should exclude Planned Maintenance from Major Works.
1	The definition of **Previous Verification** includes the capitalised term "Accurate" which is not defined.	The existing definition of Accurate should be reinstated.

Clause Number	Provision / Issue	Comment
1	Definitions of a **Related Body Corporate** and **Related Entity** have the meanings given to them in the Corporations Act as at the Execution Date.	Definitions incorporating terms as defined in the Corporations Act should be to those terms as they apply from time to time, and not as limited to a point in time. Limiting the definition to a point in time is difficult to administrate for Shipper and Operator.
1	**Retail Market Rules** is defined to mean the retail market rules that govern, or will govern when operative, the Retail Gas Market in Western Australia.	The Retail Market Rules are already operative.
1	The definition of **T1 Service** has been deleted.	T1 Service is still a term used in the Terms and Conditions (including in the Curtailment Plan) and a definition of the T1 Service should be retained. That Service should be, Alinta submits the service the subject of the Terms and Conditions. Firm Service has been retained as a definition and as an Other Reserved Service, when it is doubtful that any shipper has contracted for such service.
1	**Tp Service** is defined simply as an Other Reserved Service.	The definition does not actually identify or describe the Tp Service itself which should be identified by its essential characteristics, and that it was only available to Stage 5A shippers.

Clause Number	Provision / Issue	Comment
2.5(e)	The Operator must procure that the System operator complies with the requirements of section 4 (Ring Fencing Arrangements) of the *National Third Party Access Rules for Natural Gas Pipeline Systems*	The reference to the Code should be to Part 2 of Chapter 4 (Structural and operational separation requirements (ring fencing)) of the National Gas Access (Western Australia) Law.
2.6	Gas delivered to the BEP Inlet Point in excess of the BEP Inlet Point Capacity is deemed not to have been delivered.	DBP do not explain why this result is required. What happens if the Gas is out of specification, or the deeming results in an imbalance?
2.7	To avoid doubt, any provisions of the Access Regime and any requirements of the Regulator that prevail by force of law over an inconsistent clause of this Contract are Laws for the purposes of this Contract, but neither Party may seek to procure an amendment to an access arrangement under the Access Regime if the purpose for which such amendment is sought is to affect materially and adversely any of the other Party's rights and obligations under this Contract that are not general rights and obligations applicable to all shippers.	Amendments to the Access Regime must not be sought to affect materially and adversely any of the other Party's rights and obligations under the Contract regardless of their nature – "that are not general rights and obligations applicable to all shippers" must be deleted.

Clause Number	Provision / Issue	Comment
3.2(a)	The R1 Service is described as a Gas transportation service that gives the Shipper a right of access to Gas Transmission Capacity which (subject to clause 17.9) is treated the same in the Curtailment Plan as all other shippers with a R1 Service, P1 Service or a B1 Service and in the order of priority with respect to other Types of Capacity Services set out in clause 17.9.	The drafting in this provision is incorrect. The R1 Service is a different Type of Capacity Service and is lower in priority in the Curtailment Plan than the P1 and B1 Services, and it is therefore not correct to say the R1 Service is "treated the same in the Curtailment Plan". Clause 3.2(a)(ii) also states that the R1 Service is treated the same in the Nominations Plan as all other shippers with a R1, P1 or B1 Service which statement is also incorrect, as the Nominations Plan is based on the Curtailment Plan.
3.2(b)	R1 Capacity is quantified by reference to the Gas throughput at Kwinana Junction with the most critical compressor offline.	Alinta assumes that "critical" means the most important compressor in maximising Gas transmission capacity and this should be clarified. DBP has not provided any support for this quantification methodology such as the amount of capacity it will capture in addition to the T1 Capacity already captured by the quantification methodology in the existing shipper contracts, what is the likely annual percentage of curtailments (as it is curtailed before T1, P1 and B1) and how much does the average throughput in January (why January in the absence of evidence that January is the hottest month?) vary from the highest and lowest throughput which of course are dependent on gas demand downstream of Kwinana Junction? The estimate should remain as being with Operator acting as a Reasonable and Prudent Person and not just in accordance with Good Gas Industry Practice.

Clause Number	Provision / Issue	Comment
3.5	The Spot Capacity service has been deleted from the R1 Service Contract.	The Operator has stated in its supporting submissions that the Spot Capacity service has been removed from the reference R1 Service as Rule 109 of the National Gas Rules prohibits bundling of services. Alinta does not consider Rule 109 requires the removal of Spot Capacity from the reference service, as Rule 109 is intended to prohibit shippers having to pay for services they do not need. Spot Capacity is actually a service that most (if not all) shippers would like to use if and when it is available, which supports its inclusion in the reference service contract. Having a published and approved pricing structure and terms and conditions for Spot Capacity set out in the approved R1 Service Contract is beneficial for shippers. If Spot Capacity is not included in the reference service then there is no clarity at all as to the terms and conditions upon which Spot Capacity may be made available in the future – while there are Spot Capacity Service principles set out in the Revised Access Arrangement itself, they are stated to apply only "until otherwise advised by Operator". Additionally, the principles change a fundamental aspect of the Spot Capacity Service in that it is now take-or-pay once allocated. The present terms (in the T1 contract) provide that the Shipper must pay only when it uses the capacity unless the Operator would have sold the Spot Capacity to another shipper. There are also erroneous references to Westnet in the description of Spot Capacity in section 3.6 of the Access Arrangement.

Clause Number	Provision / Issue	Comment
4.1(a) and 4.2(a)	The Capacity Start Date is 08:00 hours on the date specified in the Access Request Form, and the Capacity End Date is 08:00 hours on the date specified in the Access Request Form.	The only relevant dates in the Access Request Form are referred to as the "Requested Reference Service Start Date" and the "Requested Reference Service End Date". There are several drafting problems with this clause. First the defined term "Access Request Form" is the form in the Schedule, which does not specify any dates. Secondly the date requested in the form on which the request is made may not be the date agreed by the Operator on which Capacity starts. Thirdly the terminology is inconsistent between this clause and the form; the form refers to "Reference Services" and the clause refers to "Capacity".
4.6 and 4.7	Provisions relating to the first and second option periods are based on the original Term being 15 years.	Why do the references to Term and Capacity End Date not simply refer to a 15 year period?
5.3(e) and 5.6(b)	This clause is now a basis on which the Operator can refuse to accept/deliver Gas rather than a basis on which the Operator can Curtail. It is therefore now outside the 2% allowance of Curtailments. Additionally the expansion of the definition of "Law" expands the residual non-specified powers of the Operator to refuse to accept or deliver gas.	The provision should be deleted from clauses 5.3 and 5.6 and reinstated in clause 17.2. The definition of "Law" from the T1 Service contract should be reinstated.
5.3(g)	The provision relates to the Operator's refusal to Receive Gas in certain circumstances.	The clause does not make sense. The words "the following" should be deleted and the words "all of the Shipper's Contracted Capacity" moved up to replace them.

Clause Number	Provision / Issue	Comment
5.5 and 5.9 (in the 2005 approved T1 Contract)	Clauses 5.5 and 5.9 from the T1 Contract have been deleted. These clauses provided that in certain circumstances where Operator could have taken steps to avoid or minimise the magnitude and duration of a refusal to Receive and/or Deliver Gas then such refusal to Receive and/or Deliver Gas constitutes a Curtailment for the purposes of the Contract and shall be taken into account in determining whether Curtailments aggregated over a Gas Year cause the Permissible Curtailment Limit to be exceeded.	There is no reason for these protections for the Shipper to be removed under the new R1 Contract. The provisions are important in protecting against the impact of an unreasonable refusal by Operator to Receive and/or Deliver Gas and should be reinstated.
5.9	This clause provides that a refusal to Deliver Gas under clause 5.6 does not affect the calculation of Charges payable by the Shipper.	Clause 5.9(a) should be subject to the reinstated clause 5.9 (from the T1 Contract) where refusal to Deliver Gas is a Curtailment in certain circumstances. Clause 5.9 should therefore be amended to reflect situations where the Capacity Reservation Charge must be refunded under clause 17.4 for a refusal to Deliver.

Clause Number	Provision / Issue	Comment
5.10	This clause provides an indemnity by the Shipper in favour of the Operator in respect of the cost of additional Gas incurred by the Operator in supplying System Use Gas in circumstances where the Shipper takes Overrun Gas or breaches the Accumulated Imbalance Limit or the Hourly Peaking Limit to the extent that the costs are not recovered by the Operator by Other Charges or Direct Damages paid by the Shipper. An independent verification process is established to confirm the relevant costs.	The auditor should be nominated by the Shipper (and agreed by the Operator) and the auditor should be required to hand down his or her decision within 30 days after having received all relevant information from the Operator in accordance with clause 5.10(g). A new provision should be inserted clarifying that the verification process in clause 5.10 is not a dispute over a Tax Invoice for the purposes of clause 21.5 (ie. is not subject to clause 21.5), and that no interest is payable by the Shipper in any circumstances for the period prior to the handing down of the auditor's decision. Clause 5.10(h) should provide exceptions for fraud and manifest error.
5.10(a)	The Operator must supply the Shipper's share of System Use Gas.	Should be clarified as being for no charge, as the SUG cost is included in the R1 Reference Tariff.

Clause Number	Provision / Issue	Comment
5.10(c)	The Shipper must indemnify the Operator in respect of the cost of additional Gas incurred by the Operator in supplying System Use Gas in accordance with this Contract to the extent to which that System Use Gas is required to be supplied, in accordance with Good Gas Industry Practice, because of the Shipper taking Overrun Gas or breaching the Accumulated Imbalance Limit or the Hourly Peaking Limit on any Gas Day, aggregated over a Contract Year, but only if that cost is not recovered by the Operator during that Contract Year by Other Charges or Direct Damages paid by the Shipper.	The concept of "share of System Use Gas" defined in clause 5.10(c) has no role in clause 5.10. Further there is no basis upon which the Operator is to determine whether System Use Gas is required to be supplied because of the shipper's identified conduct, other shippers' conduct or other operating conditions, such as exceptionally hot days or higher unaccounted for gas. System Use Gas is simply Gas used in the operation and maintenance of the DBNGP. Any attempt to allocate additional costs of System Use Gas to isolated episodes of one shipper's conduct will be artificial, arbitrary and unsupportable. This provision allows the Operator to include in a Tax Invoice the amount it considers it should be indemnified, and will be a source of constant dispute based on doubts as to the cause of the need for System Use Gas. In summary, the additional indemnity over and above the obligation to pay relevant "Other Charges" and Direct Damages is contentious, unnecessary and unreasonable and should be deleted.
5.11	An additional paragraph has been added referring to the Emergency Management Act 2005 (WA) which refers to the Minister or other persons declaring a state of emergency.	This paragraph should be amended to replace the reference to "the Minister or any other person, regulatory authority or body" with "a hazard management agency", and "a state of emergency" with "an emergency event"; and to delete "or any successor, supplementary or similar Law" which words are superfluous in the light of clause 2.1(e).

Clause Number	Provision / Issue	Comment
5.12	The Shipper is obliged to arrange inspections of certain gas installations installed or altered by the Shipper. The Operator should only be interested in policing this statutory requirement where gas is supplied directly to the gas installation from the DBNGP, as provided in section 13(1) of the Gas Standards Act 1972 (WA).	The words "to which Gas is supplied directly from the DBNGP" should be added after the words "gas installations" in 3 places in clause 5.12(b).
6.1(a)	The Inlet Points for the Contract are set out in the Access Request Form.	A previously commented, (eg, in relation to Capacity Start Date and Capacity End Date) the Access Request Form is not defined in any way which connects it to the request which resulted in the Contract. This connection must be established.
6.4(d)	Gas Delivered by the Shipper to an Inlet Point is deemed to be Received by the Operator in the order specified generally or for a particular Gas Day by the Shipper, and if the Shipper fails to specify for any Gas Day, then firstly is deemed to be Received for any available R1 Service.	This provision provides that R1 Service will in the absence of a Shipper specification be treated as a priority to T1 Service, which is not acceptable as a Shipper may have contracts for T1 and R1 Services.
6.7(d)	The issue, design and installation of Inlet Point Connection Facilities.	Clause 6.7(d) refers to a right of access for the purpose of maintaining and operating an Outlet Station – this should be a reference to an Inlet Station.

Clause Number	Provision / Issue	Comment
6.12(a)	Maintenance Charge means, with respect to a particular Inlet Station, Outlet Station or Gate Station Associated with a Sub-network, a charge determined by the Operator (acting as a Reasonable and Prudent Person) as being sufficient to allow the Operator (across all shippers who pay a charge for substantially the same purpose)…	"…across all shippers who pay a charge for substantially the same purpose" should be replaced with "…across all shippers who use the Inlet Station, Outlet Station or Gate Station Associated with a Sub-network…"
6.14(a)	Reference to Alinta Limited	This should be deleted.
7.2	Gas Delivered at an Inlet Point or an Outlet Point must be free, by normal commercial standards (as determined by the Operator), from dust and certain other constituents.	The test should be an objective one, and reference to "as determined by the Operator" should be deleted.
7.4(c)(ii)	If at any time the Shipper Delivers Gas to the Operator at that Inlet Point or the Shipper Receive Gas from Operator at that Outlet Point.	Typographical error – "Receive Gas" should be "Receives Gas".
7.9(b)	If any Out-of-Specification Gas is delivered to the Shipper at an Outlet Point without the Shipper's agreement under clause 7.9(a), then except to the extent that the Shipper caused the Gas in the DBNGP to be Out-of- Specification Gas the Operator is liable to the Shipper for Direct Damage arising in respect of the Out-of-Specification Gas.	The words "by Delivering Out-of-Specification Gas to the Inlet Point" should be added after the words "to be Out-of-Specification Gas".

Clause Number	Provision / Issue	Comment
7.12	The Operator will Deliver Gas to the Shipper at each Outlet Point at which odorising occurred as at 27 October 2004.	The Operator should also be required to Deliver odorised Gas at Outlet Points agreed in writing with the Shipper.
8.9	The clause refers to "Capacity Services for" and "Capacity Services in respect of the Shipper's Daily Nomination for"	As the only Capacity Service being scheduled under clause 8.9 is the R1 Services all these references are confusing, redundant and should be deleted.
8.10	The Operator may schedule a Capacity Service for R1 Service to the Shipper which is less than the Shipper's Initial Nomination for R1 Service at an Inlet Point or an Outlet Point.	A new clause 8.10(c) should be inserted, where Operator must endeavour as a Reasonable and Prudent Person to ensure that where the scheduled Capacity Services in respect of Daily Nominations is less than the Initial Nomination (calculated across all of the Shipper's R1 Contracts) the difference is kept to the smallest amount possible.
8.15 and 8.16 (in the 2005 approved T1 Contract)	The T1 Contract contemplated an Aggregated T1 Service for Services above Contracted Capacity at specific Inlet Points and Outlet Points.	There is no equivalent "Aggregated R1 Service". In the absence of provisions which govern the nomination, scheduling and curtailment of R1 Service at Outlet Points at which the Shipper does not have Contracted Capacity, or nominates in excess of its Contracted Capacity, it is unclear how the contract operates. For example there appears to be no restriction on nominating and being scheduled R1 Service at Outlet Points at which the shipper does not have Contracted Capacity or in excess of its Contracted Capacity (provided it does not exceed its Contracted Capacity across all Outlet Points) but in a Point Specific Curtailment such a scheduled R1 Service does not feature at all

Clause Number	Provision / Issue	Comment
		in the Curtailment Plan. Is this intended? If so, the value of the R1 Service is on this characteristic alone significantly less than the T1 Service, which must be reflected in the R1 tariff, being lower than the T1 tariff.
9	The Imbalance regime has been substantially amended from that which is contained in most shippers' 2004 Shipper Contracts and from that which was approved in 2005.	There was a threshold condition in the approved 2005 T1 Contract underpinning the Imbalance regime, which was the requirement that the Operator must first consider that: (i) a continuation of the Imbalance condition will have a material adverse impact on the integrity or operation of the DBNGP; or (ii) will adversely impact, or is likely to adversely impact, on any shipper's entitlement to its Daily Nomination for Capacity before the Operator may issue a notice requiring the shipper to reduce the Accumulated Imbalance and/or refuse to Receive or Deliver Gas. The threshold condition has been deleted. Deletion of the condition can result in the situation where the pipeline is in perfect balance on a Gas Day, with all shippers having a zero imbalance except two, which have equal offsetting positive and negative imbalances above the 8% threshold – and the Operator can levy Excess Imbalance Charges against the two shippers and/or refuse to Receive/Deliver Gas. Alinta considers this right of the Operator to be completely unacceptable, as it effectively provides for payments to be made to

Clause Number	Provision / Issue	Comment
		Operator where no possible loss has been incurred by Operator nor any adverse impact to the integrity or operation of the pipeline suffered nor to any other shipper. The Shipper could not agree to provide the statement in clause 20.4(a) that the Excess Imbalance Charges are genuine pre-estimates of the unavoidable additional costs, losses and damages that the Operator will incur as a result of the conduct entitling the Excess Imbalance Charges to be levied in those circumstances. Further, Operator is given the discretion in clause 9.5(c) to levy (or not) the Excess Imbalance Charge where the absolute value of the Shipper's Accumulated Imbalance is still above, but closer to, the Accumulated Imbalance Limit. There are no conditions at all placed on the exercise of the Operator's discretion – again this is not acceptable. The obligation on the Operator to endeavour to cooperate with the Shipper to ameliorate the impact of exceeding the Accumulated Imbalance Limit has also been deleted, as has the concept of the Outer Accumulated Imbalance Limit of 20%. These elements should be reinstated. The changes to the exceptions to the imposition of the Excess Imbalance Charge are not acceptable. Curtailment must remain an exception, and the Daily and Accumulated Imbalances must be calculated. Overall the existing Imbalance regime has been replaced with one that is very penal in its nature, and entirely out of keeping with the arrangements that

Clause Number	Provision / Issue	Comment
		have been in place since the introduction of third party access to the DBNGP. The cashing out of imbalances on a monthly basis is unfair and unreasonable. The provision penalises the Shipper by mandating a sale of gas to the Operator at a hugely discounted price, unless the Shipper takes a Storage Service. On the other hand, the price at which the Shipper must buy the imbalance quantity is a commercial price, and the Shipper may have no capability (within the physical constraints of the DBNGP) to deliver Gas to the Operator at a sufficient rate to restore the imbalance to zero. In clause 9.4 the reference should be to both clauses 6.4(c) and 6.5(c). If clause 9.9 is to remain, the Operator's purchase price under clause 9.9(c)(i) must be a price obtained by the Operator "acting as a Reasonable and Prudent Person".

Clause Number	Provision / Issue	Comment
10	The provisions governing Hourly Peaking Limits and Hourly Peaking Charges have been amended in much the same way as the Imbalance provisions in clause 9 discussed above.	The changes to the Hourly Peaking provisions, including the deletion of any conditions related to adverse impacts on the integrity and operation of the DBNGP before Hourly Peaking Charges can be levied and the removal of the Outer Hourly Peaking Limit, result in the Hourly Peaking regime becoming penal in nature – as discussed in relation to Imbalances above. In circumstances where breaching the Hourly Peaking Limit does not in any way impact on the integrity nor operation of the DBNGP, nor on any Capacity Services provided to any other Shipper, a charge for breaching such limit cannot be a genuine pre-estimate of the loss or damage resulting from breaching the relevant threshold and should not be approved. DBP does not currently provide accurate hourly data. It is offering a Peaking Service and a Metering Information Service as non-reference services. The draconian approach to Hourly Peaking Limits and Hourly Peaking Charges for the R1 Service seem transparently designed to create a paying market for its non-reference services; which services are unnecessary at present.

Clause Number	Provision / Issue	Comment
11.1(b)	The Overrun Rate is the greater of: (i) 500% of the R1 Tariff; and (ii) the highest price bid for Spot Capacity which was accepted for that Gas Day other than when the highest price bid was not a bona fide bid, in which case the highest bona fide bid. The percentage in 11.1(b)(i) under the 2005 approved T1 Contract was 115%. The Unavailable Overrun Charge is the greater of: (iii) 250% of the R1 Tariff; and (iv) the highest price bid for Spot Capacity which was accepted for that Gas Day other than when the highest price bid was not a bona fide bid, in which case the highest bona fide bid.	There has been a dramatic increase in the percentage in clause 11.1(b)(i). None of the submissions made by the Operator in support of the Revised Access Arrangement and R1 Terms and Conditions purport to give any justification for the increase. The Overrun Rate is twice the Unavailable Overrun Charge, which purports to deal with behaviour more detrimental to the pipeline. How can this be justified? Without any justification, a more than four-fold increase in the Overrun Rate is completely unacceptable to Alinta. Paying 750% of the reference tariff on the same quantity of Gas must be considered a penalty and unenforceable.

Clause Number	Provision / Issue	Comment
11.2(a)	Under the 2005 approved T1 Service Contract, the Operator could give an Unavailability Notice to the Shipper but only to the extent that the Shipper overrun will impact or is likely to impact on any other shipper's entitlement to its Daily Nomination for T1 Capacity, Firm Service, any Other Reserved Service or scheduled Spot Capacity. That condition to issuing an Unavailability Notice has been deleted.	The comments in relation to this change are similar to those in relation to the Excess Imbalance Charges and Hourly Peaking Charges discussed above. Where penalties for breaching certain thresholds are not related at all to the actual impact on the DBNGP or other shippers' capacity, they cannot be accepted as a genuine pre-estimate of damage or loss suffered by Operator due to the relevant Gas usage. The penalties become particularly hard to accept when they are increased arbitrarily and to a very significant extent (refer comment above).
11.4(a)(i)	"to" on third line	"to" should be deleted.
12.4	The Operator may satisfy its obligation to enable Gas to be Delivered to the Shipper by using any means other than the DBNGP provided that the Operator otherwise meets its obligations under the Contract.	The requirement in the 2005 approved T1 Service Contract that the Operator may use any means other than the DBNGP for Delivery only where there is no extra cost or risk to Shipper in doing so should be reinstated in clause 12.4.
14.2(c)(ii) & 14.2(d)(ii)	New Inlet Points to satisfy the Operator's technical and operational requirements.	The references to "proposed" should be replaced by "planned" in both sub clauses. Also, the Operator's technical and operational requirements should be set out in detail or reference made to the specific provisions of the Contract in which the requirements are set out.

Clause Number	Provision / Issue	Comment
14.2(d)(i)	A Requested Relocation to a New Outlet Point is an Authorised Relocation under the Contract if the Requested Relocation would result in a New Outlet Point being upstream of the Existing Outlet Point.	A New Outlet Point should be an Authorised Relocation if the New Outlet Point is upstream of the Existing Outlet Point or no greater than 2kms downstream of the Existing Outlet Point.
15.3(a)(i)(A)	Maximum metering uncertainty has been reduced to 0.75%	Alinta considers that the previous maximum uncertainty of 1% should be retained.
15.4(a)(i)(C)	Primary Metering Equipment must continuously compute and record any information required by the Operator from time to time to assist the Operator to comply with any Law.	This should be at Operator's cost.
15.4(c)(iv)	"reate"	Should be "rate".
15.5(e) & 15.5(f)	These provisions which relate to the availability of information to Distribution between Shippers have been deleted.	These provisions should be reinstated for the benefit of Distribution Network Shippers.
15.13(b) & 15.13(c)	Primary Metering Equipment in accuracy and Verification.	Clause 15.13(a)(i) is referred to twice in clauses 15.13(b) and (c) – one of the references in each clause should be deleted.
17.2(c)	The removal of this basis for curtailment and constituting it as a basis for refusing to accept or deliver Gas is a significant change in the characteristics of the R1 Service from the T1 Service.	The approach should be retained otherwise the R1 Service is devalued, which must be reflected in a lower tariff than the T1 tariff.

Clause Number	Provision / Issue	Comment
17.3(b)(ii)	Curtailment without liability includes a Curtailment for Major Works, which now includes Planned Maintenance.	Curtailment for Planned Maintenance has previously counted towards the Permissible Curtailment Limit and to change this is a significant devaluation of the R1 Service. Planned Maintenance should be treated separately to Major Works in relation to Curtailments without liability.
17.7(b)	An Initial Notice must specify the Operator's estimate of the starting time of the Curtailment and the portion of the Shipper's Contracted Capacity that is to be Curtailed.	An Initial Notice should also be required to include the reasons for the Curtailment, and if the Operator is not able to provide reasons at that time an explanation as to why not. Given the planning involved in Major Works the Operator will have information that it is able to provide to the Shipper as to why the Shipper's Capacity is to be Curtailed.
17.8(f) (in 2005 T1 Contract)	The existing T1 provision where Operator is obliged, other than when due to Force Majeure or by reason of an emergency it is unable to do so, to give effect to a Curtailment by a Curtailment Notice instead of, or prior to, doing so physically under clause 17.8(c) has been deleted.	This provision should be reinstated.
17.10(a)	Operator may apportion refusals to Receive or Deliver Gas or to Curtail in its discretion.	The apportionments should be made as determined by the Shipper, unless standing requirements under clause 17.10(b) have been proposed by the Shipper.

Clause Number	Provision / Issue	Comment
17.10(e)	If no apportionment mechanism has been proposed by the Shipper or agreed or determined under clause 17.10(c), and it becomes necessary to effect an apportionment of the kind referred to in clause 17.10(b), the apportionment may be effected by the Operator acting as a Reasonable and Prudent Person and must in that case be notified by the Operator to the Shipper as soon as practicable after the end of the relevant Gas Day.	Amendments to 17.10(a) suggested above make 17.10(e) redundant and it should be deleted.
18(d) & 18(e)	At the Shipper's request, the Operator must provide the Shipper with its estimate of the Curtailment to Capacity available to the Shipper on each day of the planned outages specified in the Annual DBNGP Maintenance Schedule.	Any information provided by the Operator following a request under clause 18(d) should not limit the Operator's obligation to give an Initial Notice within the timeframes required by clause 17.6(b)(i)(A) and this should be clarified.
18(g)	Despite clause 18(b), but subject to clauses 18(e) and 18(f), the Operator may determine the timing and extent of any Curtailment necessitated by Major Works in its discretion.	Curtailment for Major Works should also be expressed to be subject to clause 17.6(b)(b)(i)(A), and the obligation to give an Initial Notice not less than 60 days in advance of the Curtailment.

Clause Number	Provision / Issue	Comment
20.4(b)	The Parties agree that the Other Charges are genuine pre-estimates of the unavoidable additional costs, losses and damages that the Operator will incur as a result of the conduct entitling such charges to be levied. The Shipper will not be entitled to claim or argue (in any proceeding or otherwise), that any Other Charge is not a genuine pre-estimate of loss or damage that may be incurred by the Operator or is otherwise a penalty or constitutes penal damages.	See comments above in relation to the statement that the Excess Imbalance Charge, Hourly Peaking Charge and Overrun Rate are genuine pre-estimates of additional costs, losses and damages. Clause 20.4(b) to be deleted.
21.4(a) and 21.6(a)	Interest on unpaid amounts and incorrect amounts to be compounded.	Interest should not be compounded.
22.2 and 22.6	Default Notices previously needed to be given by certified mail.	Given their importance, the requirement to give Default Notices by certified mail should be reinstated.
22.9	The right of termination (with the right to recover Direct Damages) are the Shipper's sole and exclusive remedy in respect of a repudiation or disclaimer and the Operator (despite any provision of clause 23) is not liable to the Shipper for any other Indirect Damage arising in respect of a repudiation or disclaimer.	This is not satisfactory and should be deleted. In clause 23.2 the words “or wilfully defaults” should be added after the word “fraudulent” and the words “or wilful default” should be added after the word “fraud”.

Clause Number	Provision / Issue	Comment
23.6 and 23.7	Liability for death or injury to Party's personnel or damage to Party's property lies with the Party – the exception for liability for acts or omissions of the other Party has been deleted	The exception is an appropriate allocation of liability and should be reinstated.
25.1	Subject to this clause 25 and to clause 27, neither Party may assign any right, interest or obligation under this Contract (but this clause 25 does not prevent the creation of an interest for the Shipper).	What does "creation of an interest for the Shipper" mean in this context? This should be amended to read "(but this clause 25 does not prevent the Shipper from creating equitable or other interests in relation to its rights under the Contract)".
25.2	Party's may charge their interests under the Contract subject to entering into a tripartite deed in the form published on DBP's website from time to time.	The form of tripartite should be appended to the Contract itself.

Clause Number	Provision / Issue	Comment
25.3(a)(iii)	A Party may assign all or part of its rights and interests under the Contract without obtaining the consent of the other Party where that assignment is to a Related Body Corporate provided that: (i) where the assignor is the Shipper, such assignment does not release the assignor from liability; (ii) where the assignor is the Operator, such assignment does not release the assignor prior to the assignment date.	There is no reason for the treatment of liability following assignment to be different between the Shipper and the Operator. If the Operator as assignor is to be released from liability then it must be by way of a formal deed of assumption or novation which the Shipper has approved or is a party to. This is consistent with the operation of clause 25.4(a).
25.6	The ability of the Shipper to use its Daily Nominations on behalf of other shippers is now subject to the Shipper entering into an Inlet Sales Agreement, under which the Shipper will no doubt pay additional charges.	The provision should be reinstated as previously drafted, or this is a further devaluation of the R1 Service from the T1 Services, which must be reflected in a lower R1 tariff.
26 and 27.12 (in 2005 T1 Contract)	Relinquishment provisions have been deleted.	The provision enabling the Shipper to offer to relinquish Contracted Capacity should be reinstated. Why has it been deleted?
27.1(b)	The clause is subject to clause 25.6.	The reference to clause 25.6 should be deleted.

Clause Number	Provision / Issue	Comment
27.2	"contracted capacity"	This should be "Contracted Capacity".
27.4(a)	If the Shipper desires to transfer all or part of its Contracted Capacity to a Replacement Shipper, the Shipper must, prior to transferring or agreeing to transfer that Contracted Capacity (Tradeable Capacity), make a written request to the Operator for the approval of the Transfer of that Tradeable Capacity (Request for Approval).	In the T1 Contract the Shipper could request that the transfer be for a duration less than or equal to the remaining duration of the Period of Supply. It is implied from clause 27.4(b) that this is still an option, but if this is the case why not say so? This should be reinstated.
27.11 (in 2005 T1 Contract)	Operator could, if requested by Shipper, agree to provide marketing services for tradeable Capacity. This has been deleted.	This provision does not represent an onerous obligation on Operator and should be reinstated.
28.2(j)	Either Party may disclose Confidential Information which is requested by an operator of a pipeline which is inter-connected with the DBNGP.	The disclosure of Confidential Information must relate to and be necessary for the operation of the interconnected pipeline.
30.1(a)(i)	The Operator's warranty that it has complied with Environmental and Safety laws has been deleted.	This is an important warranty and should be reinstated.
30.4	DBNGP Trustee's warranties have been deleted.	The representations and warranties given by the DBNGP Trustee should be reinstated.

Clause Number	Provision / Issue	Comment
31(b) (in 2005 T1 Contract)	Shipper's right to request information on planned expansions has been deleted.	This right should be reinstated.

Alinta Pty Ltd
9 July 2010