



# Notice

1 April 2021

## Proposed revised access arrangement for the Dampier to Bunbury Natural Gas Pipeline

### Final decision and access arrangement

The Economic Regulation Authority has released its [final decision](#) for DBNGP (WA) Transmission's revised access arrangement for the Dampier to Bunbury Natural Gas Pipeline. The ERA has not approved the proposed changes to the access arrangement and has published a revised access arrangement and access arrangement information.

The Dampier to Bunbury Natural Gas Pipeline is the longest natural gas pipeline in Australia, extending approximately 1,600 kilometres from Dampier in the Pilbara region through to Perth and Bunbury in South West.

Under DBNGP (WA) Transmission's (DBP) May 2020 proposal, the combined increase in tariffs for its customers would have been 9.79 per cent. Under the ERA's final decision, tariffs will essentially remain flat, decreasing by 0.06 per cent in real terms.

A lower return on investment (or rate of return) due to conditions in the financial markets has placed a downward pressure on tariffs, but this is offset by accelerated depreciation of the pipeline and lower forecast demand.

The ERA's decision means that for end-use customers of gas including industrial gas users, gas-fired electricity generators and households, there will be no upwards pressure on gas prices from changes in transmission tariffs, other than economy-wide rates of price inflation.

The ERA's revised access arrangement, including tariffs, will take effect on 1 July 2021.

An access arrangement sets the terms and conditions under which third parties can access the pipeline.

This notice includes an explanatory statement that contains further information about the ERA's decision, its effect on tariffs and the access arrangement process.

### Further information

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## EXPLANATORY STATEMENT

This explanatory statement provides a summary of the ERA's final decision on proposed revisions to the access arrangement for the fifth access arrangement period (AA5) for the Dampier to Bunbury Natural Gas Pipeline (DBNGP).

This statement does not form part of the ERA's final decision or the reasons for the decision.

### The final decision

The ERA has not approved DBP's revised access arrangement and requires 29 amendments for the access arrangement to comply with the National Gas Rules and National Gas Law.

A summary of the required amendments is on pages (iii) to (vi) of the final decision.

The ERA has prepared and published its own approved access arrangement and access arrangement information in line with the required amendments. This approved access arrangement will take effect on 1 July 2021.

The ERA's final decision, approved access arrangement and access arrangement information is available at [www.erawa.com.au/DBP-AA5](http://www.erawa.com.au/DBP-AA5). This page also lists DBP's initial and revised proposals, the ERA's draft decision, and all submissions received from stakeholders during the review process.

**Table 1: Comparison of DBP's proposals and the ERA's draft and final decisions**

	DBP initial proposal <sup>1</sup> (updated May 2020)	ERA draft decision	DBP's revised proposal <sup>2</sup> (updated Jan 2021)	ERA final decision
Total revenue (\$ million nominal)	1,717.94	1,553.08	1,613.16	1,542.48
Weighted average cost of capital (nominal post tax %)	4.31	4.03	3.66	3.54
<b>Capital base</b>				
Opening capital base at the beginning of AA5 (\$ million real 31 December 2019)	3,329.03	3,327.39	3,344.09	3,331.50
Closing capital base at the end of AA5 (\$ million real 31 December 2019)	2,816.61	2,900.23	2,859.14	2,848.09
<b>Forecast expenditure</b>				
Capital expenditure (\$ million real 31 December 2019)	158.58	126.17	158.15	151.48

<sup>1</sup> DBP submitted its initial proposal to the ERA on 2 January 2020. In May 2020, DBP submitted updated demand forecasts that the ERA took into consideration.

<sup>2</sup> DBP submitted its revised proposal to the ERA on 7 October 2020. In January 2021, DBP submitted updated demand forecasts that the ERA took into consideration.

	DBP initial proposal <sup>1</sup> (updated May 2020)	ERA draft decision	DBP's revised proposal <sup>2</sup> (updated Jan 2021)	ERA final decision
Operating expenditure (\$ million real 31 December 2019)	439.76	456.44	433.07	426.62

## Pipeline use and demand

DBP expects demand for gas transmission to decrease due to increasing renewable generation of electricity displacing electricity generated from other sources including natural gas.

In the draft decision, the ERA was not satisfied with the level of information provided by DBP to demonstrate its forecasts of a significant fall in contracted capacity and throughput from 2020 to 2021 and continuing decline during AA5. Pipeline users also expressed concerns with the transparency of DBP's forecasting process, as well as the forecast reduction in demand.

Following the draft decision, DBP provided further information to the ERA explaining that some shippers had been over-contracted during AA4 and had relinquished excess gas from 2021 onwards. Submissions to the ERA's draft decision mostly supported DBP's proposal, following further engagement by DBP with its customers.

In January 2021, DBP submitted further revised demand forecasts following the announcement of the closure of BP's Kwinana refinery, which uses gas supplied from the DBNGP. These forecasts further reduced the expected throughput and contracted capacity of the pipeline.

The ERA accepted DBP's revised demand forecast with a correction to add the likely demand from a single customer that has only contracted for 2021 at this time but is projected to require transmission services for the entire access arrangement period. The demand forecast is for gas transmission contracted capacity to decline from 765.6 TJ per day in 2020 to 556.5 TJ/day in 2025 (full-haul equivalent quantities).

Demand forecasts are covered in pages 78 to 104 of the final decision.

## Reference tariffs

DBP provides three standard services, known as *reference services*, for which tariffs are regulated. These services are:

- The full haul "T1 Service", where gas is shipped south (downstream) along the full length of the pipeline.
- The part haul "P1 Service", where gas is shipped south (downstream) along part of the pipeline only (that is, the service is not a full haul service).
- The back haul "B1 Service", where gas is (notionally) shipped north (upstream).

For all of these services, DBP kept the same structure of tariffs as in the current (AA4) access arrangement, comprising a *capacity (reservation) charge* and *commodity (throughput) charge* to recover the fixed and variable costs of delivering reference services.

In its May 2020 proposal, DBP proposed that reference tariffs would increase by an average of 9.79 per cent from the current (2020) tariffs. DBP's proposed increases were:

- A 15.15 per cent increase to the capacity charge, which recovers DBP's fixed costs to operate the pipeline and is 94 per cent of the headline tariff.
- A 38.40 per cent decrease in the throughput charge, which recovers DBP's variable costs and is 6 per cent of the headline tariff.

The main reason for the proposed tariff increase was DBP's forecast of a 19.65 per cent fall in contracted capacity in AA5 from the previous access arrangement. A lower demand forecast has the effect of increasing reference tariffs because the costs of operating the pipeline are recovered over fewer units of contracted capacity.

The ERA's final decision results in an average tariff decrease of 0.06 per cent in real terms. Tariffs are indexed for inflation each year using the approved tariff variation mechanism.

**Table 2: Comparison of reference tariffs to apply from 1 July 2021 (\$ real as at 31 December 2019)**

Tariff component	Current tariff (2020)	DBP initial proposal (May 2020)	ERA draft decision	DBP revised proposal (January 2021)	ERA final decision
<b>Full Haul (T1 Service)</b>					
Capacity (reservation) charge (\$/GJ/day)	1.204764	1.387300	0.959110	1.385659	1.259781
Commodity (throughput) charge (\$/GJ/day)	0.133975	0.082527	0.088937	0.075504	0.078143
<b>Total</b>	<b>1.338739</b>	<b>1.469827</b>	<b>1.048047</b>	<b>1.461163</b>	<b>1.337924</b>
<b>Part Haul (P1 Service)</b>					
Capacity (reservation) charge (\$/GJ/km/day)	0.000861	0.000992	0.000686	0.000990	0.000900
Commodity (throughput) charge (\$/GJ/km/day)	0.000096	0.000059	0.000064	0.000054	0.000056
<b>Total</b>	<b>0.000957</b>	<b>0.001051</b>	<b>0.000749</b>	<b>0.001044</b>	<b>0.000956</b>
<b>Back Haul (B1 Service)</b>					
Capacity (reservation) charge (\$/GJ/km/day)	0.000861	0.000992	0.000686	0.000990	0.000900
Commodity (throughput) charge (\$/GJ/km/day)	0.000096	0.000059	0.000064	0.000054	0.000056
<b>Total</b>	<b>0.000957</b>	<b>0.001051</b>	<b>0.000749</b>	<b>0.001044</b>	<b>0.000956</b>

**Table 3: Comparison of AA5 tariff with current tariff (%)**

Tariff component	DBP initial proposal (May 2020)	Draft decision	DBP revised proposal (January 2020)	Final decision
<b>Full Haul (T1) / Part Haul (P1) / Back Haul (B1)</b>				
Capacity (reservation) charge (\$/GJ/day)	15.15	(20.39)	15.01	4.57
Commodity (throughput) charge (\$/GJ/day)	(38.40)	(33.62)	(43.64)	(41.67)
<b>Total</b>	<b>9.79</b>	<b>(21.71)</b>	<b>9.14</b>	<b>(0.06)</b>

Reference tariffs are covered in pages 426 to 466 of the final decision.

### **Rebateable services**

In addition to the three reference services described above, DBP provides additional services, most of which use the shared assets that provide the reference services. These are known as non-reference services.

The National Gas Rules require the ERA to allocate costs for shared assets between reference services and non-reference services. However, when there is uncertainty about the demand and revenue for these services, instead of allocating costs, the ERA may allow a rebate mechanism to reduce the reference tariff as part of the annual tariff variation process.

The final decision approves four services as rebateable (Spot Service, Peaker Service, Ullage Service and Other Reserved Services). DBP proposed a new rebateable Peaker Service for gas-powered generators providing greater flexibility with a lower fixed reserved capacity charge and higher throughput tariff.

Also, following the draft decision, DBP proposed an Ullage service to provide for gas to be transported from the onshore Perth Basin to the North West Shelf plant in Karratha for export. The ERA approves the introduction of this service.

The discussion of pipeline services is covered in pages 25 to 77 of the final decision.

### **Depreciation**

An access arrangement must include consideration of how assets in the capital base will be depreciated (that is, how capital is returned to the pipeline owner). Depreciation allowances form part of the total revenue that DBP can earn.

In its initial AA5 submission, DBP proposed to change depreciation schedules so that all pipeline assets were fully depreciated by 2059. DBP proposed that by 2059 the decarbonisation of the economy together with competition from renewable energy would constrain the prices able to be charged for gas transmission and prevent any further recovery of capital after that time.

In the draft decision, the ERA did not allow the changes to depreciation as proposed by DBP, determining that the National Gas Rules require depreciation over the economic life of the

pipeline (that is, the period over which the pipeline remains technically and commercially operable) and DBP did not project an early end to operating life.

DBP revised its proposal consistent with a projected end of the pipeline's economic life in 2063.

In the final decision, the ERA has accepted DBP's proposed estimate of the economic life and allowed a corresponding acceleration of depreciation.

This change in depreciation would, on its own, increase tariffs by 3.39 per cent. However, other elements of the ERA's final decision, particularly the lower weighted average cost of capital, offset this increase so that tariffs will remain flat over AA5 (in real terms).

The effect of technological and policy changes on the ability of a service provider to recover its investment in regulated assets is an emerging issue for the effective regulation of natural gas pipelines.

The ERA intends to raise with the Australian Energy Market Commission how the regulatory framework addresses asset stranding risk in an environment of increasing technological and policy change.

Depreciation is covered in pages 313 to 360 of the final decision.

### **Rate of return**

The rate of return provides a service provider with a return on the capital it has invested in its business. The rate, expressed as a weighted average cost of capital, is used in an access arrangement to determine part of the annual revenue that a regulated company can earn.

The ERA has published a guideline setting out the methods it uses to determine the rate of return for regulated gas pipelines. The ERA must comply with the guideline when determining the rate of return.

The ERA's final decision sets the weighted average cost of capital at 3.54 per cent (nominal after tax), down from 4.31 per cent in DBP's initial proposal and 5.83 per cent in the previous access arrangement.

The decline in the rate of return observed over this and other recent access arrangement review processes reflects conditions in financial markets, especially the falling yield on government bonds.

The rate of return is covered in pages 301 to 312 of the final decision.

### **Efficiency Factor scheme**

DBP proposed to introduce a new Efficiency Factor (E Factor) scheme as an incentive to improve operating expenditure efficiency. The purpose of the scheme is to provide DBP with time-neutral incentives to implement efficiency gains in each year over the access arrangement period.

Under the scheme, DBP will carry forward incremental operating expenditure savings (or decremental overspending) in some cost categories for five years following the year in which the efficiency gain (or loss) occurred.

In the draft decision, the ERA determined that the E Factor scheme was consistent with the rules and objectives governing gas pipelines in Australia, subject to some amendments to clarify the intent of the scheme and the eligibility of some types of expenditure for the scheme.

In its response to the draft decision, DBP mostly agreed with the ERA's amendments, but set out certain government fees and charges that it considered were outside its control, and therefore should not be included in the E Factor scheme.

In the final decision, the ERA has maintained its decision to include those government fees and charges in the scheme, following consideration of the requirements of the National Gas Rules and how the Australian Energy Regulator treats similar schemes in the eastern states.

The E Factor scheme is covered in pages 381 to 417 of the final decision.

## **Background**

The ERA is responsible for regulating third-party access to gas pipelines in Western Australia.

There are currently three fully regulated pipelines in Western Australia: the DBNGP, the Goldfields Gas Pipeline and the Mid-West and South-West Gas Distribution Systems.

The DBNGP is a transmission pipeline that extends approximately 1,600 kilometres from Dampier in the Pilbara region, through to Perth and Bunbury in the South West. It transports gas from offshore gas projects for domestic use, including for industry, energy generation and household consumption.

An access arrangement sets the terms and conditions, including prices, under which third parties can access services on a pipeline network. Those third parties generally include industrial gas users and gas retailers.

The National Gas Law and National Gas Rules set out the requirements for what should be included in an access arrangement, as well as the processes that the ERA must follow when considering whether to approve a service provider's proposal.

On 2 January 2020, DBP submitted a proposed revised access arrangement for the DBNGP, access arrangement information, and other supporting information for the period 1 January 2021 to 31 December 2025 (being the fifth access arrangement period or AA5).

The ERA published an issues paper for public comment on 17 March 2020, and a draft decision on 14 August 2020. DBP's revised proposal was published on 8 October 2020.

The ERA published a further position paper on pipeline and reference services on 20 November 2020, seeking further public submissions.

## **About the ERA**

The ERA is Western Australia's independent economic regulatory. The ERA aims to ensure that the delivery of water, electricity, gas and rail services in Western Australia is in the long-term interests of consumers.

The ERA also undertakes inquiries to provide recommendations to government on economic issues that are likely to have significant implications for the people and businesses of Western Australia.