SUBMISSION 52: Opening Capital Base

[redacted]

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1. INTRODUCTION

1.1. On 14 March 2011, the Economic Regulation Authority (**ERA**) made its draft decision (**Draft Decision**) in relation to the full access arrangement proposal filed by DBNGP (WA) Transmission Pty Ltd (**DBP**) on 1 April 2010 (**Original AA Proposal**).

1.2. The Draft Decision indicates that the ERA:

(a) is not prepared to approve the Original AA Proposal; and

(b) requires 109 amendments to the Original AA Proposal in order to make the access arrangement proposal acceptable to the ERA.

1.3. The Draft Decision also fixes a period for amendment of the Original AA Proposal (**revision period)**, which revision period expires on 18 April 2011.

1.4. On 18 April 2011, DBP submitted the following documents pursuant to Rule 60 of the NGR, which make up the amended access arrangement proposal (**Amended AA Proposal**):

(a) Amended Proposed Revised Access Arrangement; and

(b) Amended Proposed Revised Access Arrangement Information.

1.5. Rule 59(5)(c)(iii) of the NGR requires the ERA to allow at least 20 business days from the end of the revision period for submissions to be made (in relation to both the Draft Decision and the Amended AA Proposal). The ERA has advised that interested parties are able to make submissions on the ERA's Draft Decision up until 4:00pm (WST) Friday 20 May 2011.

1.6. While DBP has submitted to the ERA that the Amended AA Proposal contains the information that the NGA (which includes the WA National Gas Access Law text (**NGL**) and the National Gas Rules (**NGR**) requires to be included in order to enable it to be approved by the Economic Regulation Authority (**ERA**), on 18 April 2011, DBP also submitted that DBP will also be filing the following supporting submissions that explain and substantiate the amendments and additions in the Amended AA Proposal that have been made to address various matters raised in the Draft Decision:

(a) Submission (47) Revised Amended Access Arrangement Proposal (this was filed on 18 April 2011)

(b) Submission (48) Overarching

(c) Submission (49) Response to Specific Amendments

(d) Submission (50) Reference Service

(e) Submission (51) Terms & Conditions

(f) Submission (52) Opening Capital Base (being this Submission)

(g) Submission (53) Capital Expenditure

(h) Submission (54) Operating Expenditure

(i) Submission (55) Rate of Return

(j) Submission (56) Other Tariff Matters

(k) Submission (57) Non Tariff Matters

1.7. In this Submission, DBP:

(a) responds to a number of matters relating to the opening capital base that were raised in paragraphs 105 to 277 of the Draft Decision, being:

(i) the discretion afforded to the ERA in its assessment of the capital expenditure

(ii) the correct inflation escalator to be used;

(iii) the value of the conforming capital expenditure associated with the BEP Lease and the timing of that expenditure;

(iv) the value and timing of the conforming capital expenditure incurred from 2005-2010 and the verification of that expenditure;

(v) the inclusion of certain fees payable under the Operating Services Agreement; and

(b) substantiates its amendments and additions made in the elements of the Amended AA Proposal relating to the opening capital base as at 1 January 2011, including historical conforming capital expenditure.

1.8. As a final introductory matter, DBP also has issues with the manner in which the ERA has both exercised its discretion in relation to its assessment of the elements of the Access Arrangement relating to the opening capital base and undertaken its task under the NGL and NGR of assessing the relevant provisions of the Original AA Proposal's compliance and consistency with the requirements of the NGL and NGR that relate to the opening capital base. This matter is addressed in more detail in submission 48 filed on or about the date of this submission. Throughout this submission, DBP draws the ERA's attention to this point where relevant.

2. INFLATION FACTOR AND ITS IMPACT ON THE DERIVATION OF THE 2010 OPENING CAPITAL BASE

2.1. In paragraph 134 of the Draft Decision, the ERA states that it has two problems with the inflation escalation applied by DBP in the derivation of the opening capital base. They are outlined in paragraphs 135 & 136 of the Draft Decision.

2.2. The first is that DBP has applied different escalation factors to those used by the ERA (in its 2005 access arrangement approvals process) in rolling forward, to 31 December 2005, the value of the initial capital base for the DBNGP that was established for the pipeline as it existed at 31 December 1999 (**First Problem**).

2.3. The second problem identified in the Draft Decision (outlined in detail in paragraphs 105 and 106 and subsequently referenced in paragraph 136) is that DBP has used the wrong inflation escalation factor in the escalation of financial parameters from the 2005 to 2010 access arrangement period to the commencement of the 2011 to 2015 access arrangement period and that DBP should have used escalation factors derived from the “all-groups eight capital cities” CPI as opposed to the “all-groups’ Perth” CPI (**Second Problem**).

DBP Response to First Problem

2.4. Before responding to the First Problem, a preliminary issue needs to be addressed, being an issue raised by the ERA in paragraphs 138 & 139 of the Draft Decision – is it appropriate to recalculate the capital base from 1999 or should DBP simply apply the value of the capital base for 2005 set by the ERA in the 2005 Access Arrangement approvals process. If the answer to this issue is that DBP should apply the value of the capital base for 2005 set by the ERA in the 2005 Access Arrangement approvals process, then there is no need to address the First Problem.

2.5. In the Amended AA Proposal, DBP had not recalculated the opening capital base for 1 December 2011 consistently with Rule 77(2) of the NGR. In particular, DBP had not adopted the value of the capital base for the 2005 year that was approved by the ERA under the 2005 access arrangement approvals process. DBP recognises that this was an error on its part and has proposed to adopt the value of the capital base for the 2005 year that was approved by the ERA under the 2005 access arrangement approvals process. This has been corrected in a further amended AA Proposal lodged with the ERA on or about the date of this Submission.

2.6. Accordingly, there is no need to address the First Problem as it is no longer a problem.

DBP Response to Second Problem - Use of All Groups Perth CPI in rolling forward the 2005 capital base to 31 December 2010

2.7. DBP’s submissions concerning the appropriate CPI factor is contained in Section 4 its Submission 49 Response to Specific Amendments.

3. HISTORICAL CAPITAL EXPENDITURE – BEP LEASE CAPITAL EXPENDITURE

3.1. Paragraphs 151 to 178 of the Draft Decision deals with the BEP Lease and the inclusion in the capital base of capital expenditure incurred by DBP in connection with the BEP Capacity.

3.2. While DBP supports the conclusion of the ERA that the BEP Capacity should form part of the covered pipeline, DBP has a number of issues with the ERA's reasoning in relation to the amount of capital expenditure associated with the BEP Capacity allowed in the Draft Decision. They are:

(a) The timing of the capitalisation of the expenditure

(b) The categorisation of the expenditure

(c) The quantum of the expenditure and its substantiation.

3.3. In addition, the ERA raised an issue in the Draft Decision in relation to the operating expenditure associated with the BEP Lease.

3.4. Each of these issues is addressed in turn in this section of the submission.

BEP Capacity Expenditure – Timing of Capitalisation

3.5. DBP had originally (in its Original AA Proposal) assumed associated capital expenditure for the BEP Capacity would be incurred and capitalised in 2010. At the time of the filing of the Original AA Proposal however, it was not certain that this would occur because the BEP Lease was still conditional on certain conditions precedent being satisfied or waived by both parties.

3.6. DBP advised, in DBP's Submission 40, that the BEP Lease Agreement became unconditional on 17 December 2010. Therefore all the obligations and rights under the agreement have force and effect from that date (including the obligation of DBP to pay rent under the lease).

3.7. In response to the Draft Decision DBP has submitted an Amended AA Proposal for the DBNGP inclusive of:

(a) the BEP Capacity as part of the proposed Covered Pipeline (See Appendix 2 of the Access Arrangement); and

(b) the capital expenditure associated with the BEP Lease being incurred in 2011.

3.8. As shown in the audit reconciliation tables in section 4 of this submission, capital expenditure for the BEP Capacity is included in Capital Works in Progress (CWIP) for 2010 and is not forecast to be included in the capital base until 2011.

3.9. DBP has changed its position on the timing for the incursion of the capital expenditure associated with the BEP Capacity for the following reasons:

(a) It is consistent with the approach taken for all capital expenditure that is recorded as CWIP in the independently reviewed accounts for the calendar year 2010.

(b) Because the BEP Lease only became unconditional on 17 December 2010, to have included it in the capital base in 2010 would have meant DBP would have had to depreciate that expenditure for a full calendar year but without having had the benefit of an increase in the reference tariff for that calendar year.

The categorisation of the BEP Lease Expenditure

3.10. In the Amended AA Proposal, the amount of capital expenditure to be incurred in 2011 associated with the BEP Capacity is $23,117,293 ($2010). This is consistent with the amount included in the CWIP for the independently reviewed accounts for the calendar year 2010.

3.11. This in turn is the amount incorporated into forecast conforming capital expenditure to be rolled into the capital base in 2011 and which is proposed to be categorised as 'other depreciable assets' for the purposes of depreciation of the capital base.

3.12. The capital expenditure has been categorised in this asset category for the purposes of depreciation for the following reasons:

(a) The Primary Lease Term under the BEP Lease (being 20 years) is aligned most closely to the life of assets in this category (being 30 years);

(b) The term of each of the access contracts entered into with shippers for which the BEP Capacity was required (being 20 years) is aligned most closely to the life of assets in this category;

(c) There is no certainty that DBP will extend the term of the BEP Lease to the Extended Lease Term and even if it is, DBP will not be

The Correct Value for the BEP Lease Expenditure

3.13. This amount of capital expenditure for the BEP Capacity (ie $23,117,293 ($2010)) differs from the amount proposed in the Original AA Proposal and the amount proposed in the Draft Decision.

3.14. The reason for the difference between the amount of the BEP Capacity capital expenditure used in the Amended AA Proposal and the amount used in the Draft Decision is that the ERA has incorrectly applied the relevant accounting standard used to determine the capital expenditure attributable to lease payments of the kind in the BEP Lease.

3.15. In paragraph 171 of the Draft Decision, the ERA states that it is not satisfied that the capital expenditure associated with the lease of the BEP Capacity has been appropriately determined. While the ERA agrees with DBP that capital costs should be determined in accordance with Australian Accounting Standards AASB 117 (in particular paragraph 20 of that standard), the ERA has concluded, at paragraph 172 of the Draft Decision, that DBP:

(a) has not substantiated the discount rate it has used to determine the present value of the lease payments under the BEP Lease; and

(b) even so, has not applied the correct discount rate in determining the present value of the lease payments under the BEP Lease.

3.16. The ERA concludes that in the absence of an implicit interest rate in the BEP Lease, AASB 117 requires that the lessee's incremental borrowing rate to be used for the purpose of determining the present value of the minimum lease payments. Accordingly, the ERA recommends the use of the nominal pre-tax weighted average cost of capital approved in the Draft Decision as the proxy for DBP's incremental cost of funds – being a value of 10 per cent.

3.17. DBP submits that the ERA has incorrectly applied AASB 117 in a number of respects. The correct application of AASB 117 is outlined below.

3.18. In accordance with AASB 117 (para.20), at the date of commencement of the lease term DBP is required to recognise the finance lease as an asset and a liability in the Statement of Financial Position at an amount equal to the fair value of the leased asset, or if lower, the present value of the minimum lease payments (both determined at the inception of the BEP Lease being May 2008).

3.19. The standard goes on to provide that the discount rate to be used in the present value calculation is the interest rate implicit in the lease.

3.20. The BEP Lease agreement does not specifically disclose or determine the interest rate implicit in the lease. In such circumstances, AASB 117 para.4, provides that the interest rate implicit in the lease is the discount rate that, at the inception of the lease, causes the aggregate present value of the minimum lease payments to be equal to the fair value of the leased asset.

3.21. So the first step that must be undertaken is to determine both the minimum lease payments and the fair value of the BEP Capacity.

3.22. The second step then involves determining an implicit interest rate which causes the present value of the minimum lease assets to equal to the fair value of the leased asset

3.23. There is a third step that applies only where there is a delay between the inception of the lease and the commencement of the lease. In that situation, interest expense is calculated for this period prior to the commencement of the lease using the interest rate implicit in the lease. It is then added to the fair value at inception when recognising the lease asset/liability in the Statement of Financial Position.

3.24. Turning back to the first step, AASB 117 para.4 provides that the minimum lease payments are the payments over the lease term that the Lessee is or can be required to make and excludes contingent rents. Contingent rent is defined as the portion of the lease payment that is not a fixed amount, but is based on the future amount of a factor that changes other than with the passage of time (eg. future CPI escalation). [redacted]

3.25. In relation to the fair value of the leased asset, AASB 117 para.4 defines "Fair Value" as the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

3.26. As the BEP Capacity is an unusual asset, there is a lack of similar assets or similar sale/lease transactions that would provide an indication as to the fair value of the asset. For this reason DBP has estimated the fair value of the asset by determining the depreciated replacement value of the BEP Capacity, based on the premise of constructing a similar asset.

3.27. As stated in DBP's prior submissions, the BEP covers 23.7km from the North West Shelf gas pant through the environmentally and culturally sensitive Burrup Peninsula to MLV7.

3.28. DBP's recent history with the construction of Stage 5B Looping, provides evidence of an average construction cost for looping of approximately $0.95 million per kilometre. Based on the 23.7km length of the BEP this would equate to approximately $22.5m in construction costs.

3.29. The construction of looping through the Burrup Peninsula would however, be much more expensive than the average cost of construction incurred by DBP for stage 5B. This is so due to the following factors:

(a) Terrain – The Burrup Peninsula is predominantly comprised of rock & would require 100% rock excavation, including 3km of man made causeway in order to cross the salt flats at the Dampier Mud Flats.

(b) Environmental & Cultural Heritage - The Dampier Archipelago was included in the National Heritage List on 3 July 2007. As a result construction through this area would incur significant additional costs in legal and approval processes as a result of the heritage listing as well as Native Title/Cultural approvals. Additionally, this cultural & heritage exposure along the easement requires "slow" construction techniques so as to preserve and re-instate cultural artefacts.

3.30. [redacted].

3.31. Assuming the pipeline has a similar asset life to that which has been assumed for the DBNGP for the purposes of depreciation – being 70 years – at the date of the lease inception the asset would have been depreciated for approximately 9.6 years. On this basis the depreciated replacement value of the asset would be approximately $39.1m.

3.32. The initial leased capacity taken up by DBP under the BEP Lease is 49% of the total capacity of the BEP. Applying this factor would result in a value of approximately $19.2m. Although it must be noted that a replacement asset would involve construction of the asset as a whole and not just a percentage of the asset.

3.33. Alternatives to accessing the BEP Capacity but still providing the incremental contracted capacity and ensuring DBP meets its contractual pressure obligations would be to construct a compressor station at MLV7 or to increase the capacity at CS1 via the addition of another compressor. [redacted]

3.34. Based on the above, it is reasonable to conclude that the fair value of the BEP can be reasonably determined based on the depreciated replacement value (DORV) to construct a replacement asset.

3.35. Applying the second step, it could be reasonably argued that the fair value of the BEP Capacity as at May 2008 (being the inception of the BEP Lease) was approximately $19.2m.

3.36. Thus, based on the aggregated value of the minimum lease payments over the 20 year lease term, this equates to an implicit interest rate of approximately 6.78%pa.

3.37. Applying the third step, AASB 117 para.20 provides that the lease asset/liability is recognised in DBP's financial statements at the commencement of the lease term rather than the lease inception date. Between the lease inception date and the commencement date interest expense (calculated at the interest rate implicit in the lease – ie 6.78%) accrues on the lease and is 'capitalised' to the lease asset liability. During the period 18 May 2008 to 18 December 2010 $3.6m of interest expense is incurred.

3.38. Given the above, the DORV ($19.2m) plus the value of the accrued interest incurred from the lease inception date to the lease commencement date ($3.6m) delivers a lease asset/liability of $22.8m that is required to be recognised in the Statement of Financial Position.

3.39. This amount and methodology was reviewed by DBP's independent auditor and signed off as appropriate as part of the auditor's review of DBP's half yearly accounts to 31 December 2010.

3.40. Additionally, AASB 117 allows for any initial direct costs of the lessee to be added to the capital asset. In the case of the BEP lease, these costs totalled [redacted] and were made up of the following cost items:

(a) The payment of an option fee of [redacted] to Epic Energy to enable the period for the satisfaction of the conditions precedent to be extended

(b) The balance was for external consultants engaged to assist in the preparation, negotiation and obtaining board approval for the BEP Lease, which covered legal, tax and regulatory advisers.

3.41. Accordingly, the total amount of capital expenditure for the BEP Capacity is $23,117,293.

3.42. DBP submits that it has determined the amount of capital expenditure for the BEP Capacity consistently with AASB 117 and that this amount should correctly be considered as forecast conforming capital expenditure for 2011 under rule 79(1)(a) of the NGL.

Operating Expenditure associated with the BEP

3.43. In paragraph 168 of the draft decision the Authority presumes operating and capital costs for the BEP are included in the forecasts of capital and operating expenditure for the entire DBNGP for the 2011 to 2015 access arrangement period. In paragraph 177 of the Draft Decision, the ERA then queries whether the whole of the operating and capital costs forecast to be incurred by DBP in operation and maintenance of the BEP from 2011-15 should be included in the forecasts of costs used to calculate total revenue given that DBP leases only part of the capacity of the BEP for the provision of transmission services via the DBNGP.

3.44. DBP responds to this issue in two parts – the first part deals with the capital expenditure assumptions relating to the BEP and the second part deals with operating expenditure assumptions associated with the BEP.

3.45. In relation to capital expenditure, the only capital expenditure that DBP has included in the Amended AA Proposal is the capital expenditure associated with the lease payments under the BEP Lease. DBP has not included any stay in business capital expenditure associated with the BEP Lease in its forecast capital expenditure. Under the terms of the BEP Lease, to the extent that there is any capital expenditure to be incurred, it will be shared between DBP and Epic Energy in the proportions of [redacted] respectively, unless DBP does not exercise its lease interest option under the BEP Lease, in which case, the proportions revert to [redacted] respectively.

3.46. In such circumstances, DBP would propose to roll into the capital base its portion of the capital expenditure.

3.47. [redacted]

3.48. DBP has previously submitted to the ERA (in submissions 34 and 37 and in its presentation made to the ERA on 2 December 2010) that the physical operation of the BEP is fully integrated into the operation of the DBNGP as if it were another loop of the DBNGP. Without its full integration, DBP would not be able to meet its contractual obligations to shippers to provide contracted capacity and minimum pressure. Accordingly, DBP has included the fuel gas associated with the integration of the entire BEP into the operation of the DBNGP.

3.49. However, DBP has not assumed any other operating expenditure associated with the operation of the BEP or the BEP Capacity because at the time, there was uncertainty as to whether the BEP Capacity would form part of the covered pipeline and also, at the time of the filing of the Original AA Proposal, [redacted]

3.50. DBP has not however sought to add, in its Amended AA Proposal, further costs to the forecast operating expenditure that are associated with the operation and maintenance of the BEP lease.

3.51. In relation to expenditure for non routine maintenance, the same principles that apply to the sharing of capital expenditure apply.

4. VERIFICATION OF CAPITAL EXPENDITURE

4.1. Paragraphs 183 to 187 and 274 of the draft decision introduces the requirements for DBP to provide independent audit reports for the expansion capital expenditure, stay-in-business capital expenditure and capital contributions and to only allow audited values of this expenditure to be approved for addition to the capital base.

4.2. Regarding the requirement to provide independent audit reports, as the ERA is aware, this requirement comes as somewhat of a surprise to DBP given that, in the months leading up to the filing of DBP's Original AA Proposal in April 2010, the ERA dispensed with this requirement. This was previously outlined by DBP in correspondence with the ERA in early 2010.

4.3. Accordingly, DBP has only had since 14 March to:

(a) understand what the ERA meant by the requirement to provide independent audit reports; and

(b) have an independent auditor undertake the audits and have the audit reports finalised and issued for review by the ERA.

4.4. The ERA has indicated that an audit which follows the following procedure is likely to address the ERA's requirement that the expenditure be independently audited:

(a) DBP reconciles capital expenditure information provided in DBP's submission, to financial records that have previously been subject to either independent review or audit by DBP's external auditor, [redacted]

(b) Reconciling items will be necessary due to the fact that DBP's regulatory and statutory financial year ends do not coincide, as well as the fact that regulatory and statutory treatments for some capital and operating expenditure items differ.

(c) The independent auditor will then prepare a report in accordance with Auditing Standards applicable to agreed-upon-procedures engagements. The procedures undertaken by the independent auditor should be designed to ensure that the following information has been adequately reconciled to underlying financial information that has previously been subjected to review/audit: Total capital expenditure for each year from 2005 to 2010 (inclusive), broken down between stay-in-business and expansion, as follows:

- Pipeline
- Compression
- Metering
- Linepack
- Other

(d) The procedures should include:

(i) Agreeing each submitted capital and operating expenditure amount in the above categories to schedules which reconcile these amounts to underlying financial information that has been previously subjected to review/audit.

(ii) Agree reviewed/audited information included in the reconciliation to source (e.g. general ledger/full year or interim financial reports).

(iii) Document the nature and amount of reconciling items relating to differences between regulatory and statutory accounting treatments identified by DBP management in the reconciliations.

(iv) For expansion capital expenditure, agree amounts submitted to amounts subjected to separate procedures performed by independent auditors [redacted] where possible. Note reasons where this is not possible.

4.5. DBP has therefore reconciled its actual capital expenditure included in the corrected Amended AA Proposal (lodged on or about the date of this submission) with the capital expenditure included in the audited financial (annual and half yearly) statements and this reconciliation has been independently audited by DBP's external financial auditors [redacted] by adopting the above agreed upon procedures. A copy of the work scope adopted by [redacted] is attached (Attachment 3).

4.6. The following tables summarise the independent audit report which reconciles the actual capital expenditure in the annual and half yearly financial statements with the actual capital expenditure included in the corrected Amended AA Proposal.

Table 1: DBP Statutory Reports

Reconciliation of Asset Cost (Excludes depreciation & amortisation)

(Inclusive of Land, Buildings Plant & Equipment, Motor Vehicles, Gas Linepack, Information Systems and Assets Under Construction)

	6 Mths 30-Jun-05	12 Mths 30-Jun-06	12 Mths 30-Jun-07	12 Mths 30-Jun-08	12 Mths 30-Jun-09	12 Mths 30-Jun-10	6 Mths 31-Dec-10	Total
Opening Balance (cost)	**1,488,550**	**1,488,564**	**1,535,793**	**1,920,554**	**1,921,207**	**2,565,143**	**2,586,580**	
Additions and Transfers from C	30	54,732	384,819	676	644,004	21,678	622,316	**1,728,256**
Disposals (cost)	- 15	- 6,823	- 58	- 23	- 69	- 241	-	**- 7,230**
Asset Impairment (cost)	-	- 680	-	-	-	-	-	**- 680**
Closing Balance (cost)	**1,488,564**	**1,535,793**	**1,920,554**	**1,921,207**	**2,565,143**	**2,586,580**	**3,208,896**	**1,720,346**
Linepack (Opening) (cost)	4,172	4,172	3,473	4,052	7,262	7,262	8,589	
- Additions / movement (cost)	-	699	579	3,210	-	1,327	-	**4,417**
Linepack (Close) (cost)	**4,172**	**3,473**	**4,052**	**7,262**	**7,262**	**8,589**	**8,589**	
Assets under Construction (cos	**27,532**	**321,050**	**267,511**	**683,610**	**373,079**	**696,716**	**129,357**	
	1,520,268	**1,860,316**	**2,192,118**	**2,612,079**	**2,945,485**	**3,291,885**	**3,346,842**	

4.7. Table 1 reconciles to DBP's statutory accounts for property plant and equipment.

4.8. The independent auditor in its Report of Factual Finding (Attachment 3) in paragraphs (I, ii, iii, iii, iv, v, vi & vii) agreed amounts in Table 1 to the audited consolidated financial consolidated statements of the Trust.

Table 2: Breakdown of additions & Transfers from Table 1

Breakdown of Additions (cost)	6 Mths 30-Jun-05	12 Mths 30-Jun-06	12 Mths 30-Jun-07	12 Mths 30-Jun-08	12 Mths 30-Jun-09	12 Mths 30-Jun-10	6 Mths 31-Dec-10	Total
Stage 4-Compression	-	41,621	153,622	-	9,534	-	-	**204,777**
Stage 4-Pipeline	-	6,185	229,784	-	160	-	-	**236,129**
Stage 4-Other	30	108	-	-	910	-	-	**1,047**
Stage 5A-Compression	-	-	-	-	117,142	-	-	**117,142**
Stage 5A-Pipeline	-	-	-	-	493,382	-	-	**493,382**
Stage 5A-Other	-	-	-	-	1,522	-	-	**1,522**
Stage 5B-Compression	-	-	-	-	-	-	52,261	**52,261**
Stage 5B-Pipeline	-	-	-	-	-	-	489,960	**489,960**
Stage 5B-Other	-	-	-	-	-	-	75,315	**75,315**
Stage 5B-Metering	-	-	-	-	-	-	4,756	**4,756**
SIB-Compression	-	844	4	34	-	328	-	**1,210**
SIB-Pipeline	-	-	328	-	-	915	-	**1,243**
SIB-Metering	-	-	-	-	-	76	-	**76**
SIB-Other	-	3,383	785	563	86	5,221	24	**10,063**
Shippers-Shipper Funded	-	2,592	-	79	21,268	-	-	**23,939**
Opex-Compression	-	-	295	-	-	14,297	-	**14,592**
Opex-Other	-	-	-	-	-	841	-	**841**
	30	**54,732**	**384,819**	**676**	**644,004**	**21,678**	**622,316**	**1,728,256**

4.9. The table above contains a detailed breakdown of the Additions and Transfers line from table 1 consistent with its reconciliation to statutory accounts.

4.10. The independent auditor in its Report of Factual Finding (Attachment 3) in paragraph (viii) agreed the additions in Table 2 to the underlying accounting records of the Trust prepared by Management.

Table 3: Regulatory Submission - Breakdown of Additions

Breakdown of Additions (cost) - Per Regulatory Submission

		12 Mths 31-Dec-05	12 Mths 31-Dec-06	12 Mths 31-Dec-07	12 Mths 31-Dec-08	12 Mths 31-Dec-09	12 Mths 31-Dec-10	Total	Notes
Capital Expenditure									
Stage 4-Compression		40,372	153,622	-	9,534	-	-	**203,529**	
Stage 4-Pipeline		7,434	229,784	-	160	-	-	**237,378**	
Stage 4-Other		138	-	-	910	-	-	**1,047**	
	-	**47,943**	**383,407**	**-**	**10,604**	**-**	**-**	**441,954**	1
Stage 5A-Compression		-	-	-	117,142	-	-	**117,142**	
Stage 5A-Pipeline		-	-	-	493,382	-	-	**493,382**	
Stage 5A-Other		-	-	-	1,522	-	-	**1,522**	
	-	**-**	**-**	**-**	**612,047**	**-**	**-**	**612,047**	2
Stage 5B-Compression		-	-	-	-	-	52,261	**52,261**	
Stage 5B-Pipeline		-	-	-	-	-	489,960	**489,960**	
Stage 5B-Other		-	-	-	-	-	75,315	**75,315**	
Stage 5B-Metering		-	-	-	-	-	4,756	**4,756**	
	-	**-**	**-**	**-**	**-**	**-**	**622,292**	**622,292**	3
SIB-Compression		844	79	136	151	-	-	**1,210**	
SIB-Pipeline		-	96	1,146	-	-	-	**1,243**	
SIB-Metering		-	-	-	-	76	-	**76**	
SIB-Other		3,383	785	2,149	3,201	544	-	**10,063**	
Shippers-Shipper Funded		2,592	12,584	7,752	1,011	-	-	**23,939**	
	-	**6,819**	**13,545**	**11,184**	**4,363**	**620**	**-**	**36,531**	
	-	**54,762**	**396,952**	**11,184**	**627,013**	**620**	**622,292**	**1,712,823**	
Expenditure Recognised as OPEX (Reconciling Item)									
Opex-Compression		-	295	588	2,361	12,189	-	**15,433**	
	-	**-**	**295**	**588**	**2,361**	**12,189**	**-**	**15,433**	
Total Expenditure	**-**	**54,762**	**397,247**	**11,772**	**629,374**	**12,809**	**622,292**	**1,728,256**	

Reconciliation Expansion Costs to [redacted] Audit Reports

	Regulatory Submission	[redacted] Verified	Variance
1 Stage 4	441,954	439,373	- 2,581
2 Stage 5A	612,047	630,578	18,531
3 Stage 5B	622,292	661,626	39,334
	1,676,292	**1,731,577**	**55,285**

Notes

1 Variance due to transactions that were unable to be obtained due to time constraints and system issues.
2 Consistent with [redacted] audit report (variance due to assets recognised in CWIP waiting to be capitalised)
3 Consistent with [redacted] audit report (variance due to assets recognised in CWIP waiting to be capitalised)

4.11. Table 3 above contains DBP's regulatory treatment of additions.

4.12. DBP notes that its independent auditor in its Report of Factual Finding (Attachment 3) in paragraph (ix) have agreed the amount in Table 3 to the underlying accounting records of the Trust prepared by Management.

4.13. DBP notes that its independent auditor in its Report of Factual Findings (Attachment 3) in paragraph (xvi) have agreed amounts included for "adjustments – Overhauls recognised in OPEX" to the corresponding amount on the Reconciliation of Asset Costs included under the heading Opex – Compression.

4.14. DBP notes that its independent auditor in its Report of Factual Findings (Attachment 3) in paragraph (x) has agreed amounts in "[redacted] Verified" (contained in Table 3) to amounts verified by [redacted] in their Reports on Factual Findings as provided to the auditors by Management.

4.15. Variances between [redacted] verified figures and figures preposed in DBP's regulatory submission are explained in notes 1 to 3. It should also be noted that these amounts differ from the amounts included in the [redacted] reports previously submitted by DBP to the ERA prior to the Draft Decision. The reasons for the differences in values between both the original [redacted] reports and the reports contained in Attachments 1 & 2 and between the audited accounts and the [redacted] reports contained in Attachments 1 & 2 are explained in the following paragraphs of this submission.

4.16. In relation to the [redacted] audit for stage 4 expansion:

(a) The differences between the values in the original stage 4 report and the values in the report attached in Attachment 1 are due to the fact that in the original report, not all invoices were reviewed. The second stage 4 report from [redacted] confirms that they have not reviewed invoices twice. The second report outlines the procedures undertaken by [redacted] in its review.

(b) The difference between the [redacted] report attached in Attachment 1 and the amounts in the [redacted] report are due to the fact that some invoices were unable to be accessed in the time available because they reside in an accounting system that is no longer used by DBP and was held by the prior owner, [redacted]. DBP does not have ready access to that system. However, the fact that the amount not audited by [redacted] has been verified by [redacted] as part of its audit of annual and half yearly financial accounts means that it should still be rolled into the capital base as conforming capital expenditure. DBP has adopted this approach in its corrected Amended AA Proposal.

(c) The difference in values between the original stage 5B report and the most recent stage 5B report contained in Attachment 2 is attributable to the fact that the original [redacted] Stage 5B report was based on invoices up to October 2010. The report attached in Attachment 2 was based on invoices up to 31 December 2010. This is explained in the [redacted] report contained in Attachment 2.

(d) The reason for the difference in values between the [redacted] reports for both stages 5A and 5B and the values in the audited financial statements as being entered into the asset register is due to the fact that [redacted] audited based on invoices paid. The amounts that had not been audited but which were not in the asset register are recorded in the CWIP report. Accordingly, these values are being treated in the corrected Amended AA Proposal as conforming capital expenditure to be rolled into the capital base in 2011.

Table 4: Statutory Reporting - Breakdown of Disposals

Breakdown of Disposals Per Statutory Accounts at Cost

	6 Mths 30-Jun-05	12 Mths 30-Jun-06	12 Mths 30-Jun-07	12 Mths 30-Jun-08	12 Mths 30-Jun-09	12 Mths 30-Jun-10	6 Mths 31-Dec-10	Total
Land		- 1,856						**- 1,856**
Buildings		- 4,597						**- 4,597**
Vehicles	- 15	- 26	- 58	- 23	- 69	- 241		**- 432**
Network Assets		- 298						**- 298**
Software		- 46						**- 46**
Asset Impairment		- 680						**- 680**
	- 15	**- 7,503**	**- 58**	**- 23**	**- 69**	**- 241**	**-**	**- 7,910**

4.17. The table above contains DBP's break down of disposals per its statutory accounts. Note table 4 also includes asset impairments.

4.18. DBP notes that its independent auditor in its Report of Factual Finding (Attachment 3) in paragraph (xi & xii) have agreed disposals in "Breakdown of Disposals per Statutory Accounts" to the consolidated audited financial statements of the Trust for the applicable years and unaudited fixed asset register of the Trust at 30 June 2005 and 31 December 2010 prepared by Management.

Table 5: Regulatory Submission - Breakdown of Disposals

Breakdown of Disposals Per Regulatory Submission

	2005	2006	2007	2008	2009	2010	TOTALS
Pipelines	-	-	-	-	-	-	-
Compressors	3.509	-	-	-	-	-	3.509
Meters	-	-	-	-	-	-	-
Other	0.064	-	0.034	0.027	0.086	0.010	0.221
Land	1.933	-	-	-	-	-	1.933
	5.505	**-**	**0.034**	**0.027**	**0.086**	**0.010**	**5.662**

4.19. The table above contains DBP's regulatory treatment of disposals per its statutory accounts. Table 5 and Table 4 are not directly comparable. DBP's treatment for regulatory purposes is explained in paragraphs 5.10 to 5.14 of this submission.

5. EXPLANATION OF VARIANCES BETWEEN THE OPENING CAPITAL BASE IN THE ORIGNINAL AA PROPOSAL AND AMENDED AA PROPOSAL

5.1. As is apparent from tables 8 - 12 in the corrected Amended Access Arrangement Information contained in the Amended AA Proposal filed on or about the date of this submission, there is a difference between the value of the opening capital base for 1 January 2011 proposed in the Original AA Proposal and the value of the opening capital base for 1 January 2011 as proposed in the Amended AA Proposal. There are a number of reasons for this difference. They are the following :

(a) Disposals - DBP's Original AA Proposal did not identify any disposals of assets during the period 2005 to 2010. As a result of the independent audit undertaken in relation to DBP's capital expenditure, DBP has identified a small number of assets were in fact disposed of during the period. DBP makes a number of submissions on this point in paragraphs 5.2 to 5.14 of this submission.

(b) Capital contributions – as was previously outlined in submissions made by DBP prior to the draft decision, DBP identified early on in the assessment process, that in the Original AA Proposal, DBP had included values for capital contributions in incorrect years. This occurred because the value of assets were physically entered into the book accounting asset register some time after they had been commissioned but were recorded as having been entered into the asset register on the date they were in fact physically entered, rather than on the date of commissioning. Whereas for regulatory purposes, DBP should have adopted the approach that capital expenditure incurred in relation to an asset which was to be treated as conforming capital expenditure was to be rolled into the capital base in the year in which the asset was commissioned or first put into service. In this regard, this resulted in a timing error. The total in the Original AA Proposal for capital contributions does not differ from the total in the Amended AA Proposal.

(c) Conforming capital expenditure – there are a number of reasons for the differences in actual conforming capital expenditure. These are explained later in this section of the submission.

(d) Depreciation – as a consequence of the change to the values for the actual conforming capital expenditure and the disposals, the depreciation schedule has changed, as shown in Table 11 of the amended proposed access arrangement information.

Disposals

5.2. As stated above, DBP has now identified that certain assets were, in fact, disposed of in the prior access arrangement period. This is contrary to the position it outlined in the Original AA Proposal. DBP makes the following submissions to substantiate the amounts proposed to be removed from the capital base as disposals in the Amended AA Proposal.

5.3. In the Amended AA Proposal, DBP valued these disposals at $10.7m ($2010) over the period (see Table 12). This is in fact an error. The correct total value (in $2010) of assets disposed of the purposes of the access arrangement is outlined in the following table. The error in the figures reported as disposals in 2005 was due to the fact that DBP had included the same value for buildings disposed of in 2005 under two different asset categories – once under Compression and the second time under Other Depreciable Assets – when they should only have been recorded once and under the asset category of Compression.

Year ending 31 December	2005	2006	2007	2008	2009	2010	Total
Pipelines	0.00	0.00	0.00	0.00	0.00	0.00	**0.00**
Compression	4.10	0.00	0.00	0.00	0.00	0.00	**4.10**
Metering	0.00	0.00	0.00	0.00	0.00	0.00	**0.00**
Other depreciable assets	0.07	0.00	0.04	0.03	0.09	0.01	**0.24**
Non-depreciable assets	2.26	0.00	0.00	0.00	0.00	0.00	**2.26**
Sub Total	**6.43**	**0.00**	**0.04**	**0.03**	**0.09**	**0.01**	**6.60**

5.4. Accordingly, a further amended proposed revised access arrangement information document is being issued to the ERA at or about the same time as this submission with updated tables to correct the value of disposals in 2005.

5.5. With this error corrected, the details of the assets disposed of during the prior access arrangement period (and their regulatory values in nominal$) were as follows:

Year ending 31 December	2005	2006	2007	2008	2009	2010
Compression Assets Disposed						
• Disposal of buildings forming part of the Karratha Depot	[redacted]					
• Disposal of buildings forming part of the Geraldton Depot						
• Disposal of buildings on 3 residential properties in Karratha						
Subtotal for Compression	**3.51**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Other Depreciable Assets Disposed						
• Disposal of motor vehicles	[redacted]					
• Disposal of software						
Subtotal for Other depreciable assets	**0.06**	**0.00**	**0.03**	**0.03**	**0.08**	**0.01**
Non-depreciable Assets Disposed						
• Disposal of depot site at Geraldton	[redacted]					
• Disposal of properties at Karratha (1 depot site and 3 residential properties)						
Subtotal for Non-depreciable assets	**1.93**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Total	**5.5**	**0.00**	**0.03**	**0.03**	**0.08**	**0.01**

5.6. In relation to the assets included in the "other depreciable assets" category that were disposed of in 2005, DBP does not have records in its possession to enable it to discern the specific assets that were disposed of in that year. This is due to the fact that there was a change to a new accounting system in 2006 and the asset manager at the time who was responsible for the accounting system did not retain sufficiently detailed information in the transfer to the new accounting system. DBP is however, able to discern that these assets should be grouped into this asset category because the description in the audited financial accounts for that year attribute the assets to three particular classes of assets, all of which, DBP has to date included in the "other depreciable assets" category for regulatory purposes.

5.7. In relation to the disposals of the properties in 2005 and which have been recorded in both the non depreciable asset category (for the value of the land) and the compression category (for the value of the buildings), they were disposed of as a result of a review by DBP which concluded that they were no longer required as part of the long term operational and asset management strategy of the pipeline. Accordingly, they were sold through a market based sale process.

5.8. DBP submits that it was appropriate to deduct from the capital base an amount from the asset category of compression equal to the regulatory value of the buildings disposed of because DBP has traditionally categorised all buildings in this asset category.

5.9. The value that has been attributed to each asset that has been disposed of during the prior access arrangement period has been determined using the following methodology.

Asset Disposal Treatment

5.10. In determining the value to be attributed to individual assets for regulatory purposes a number of assumptions were made:

(a) that all disposed of items were included in the Regulator's original opening capital base of $1,550 million as at 1 January 2000;

(b) that all building assets were included in the Regulator's 'Compressors' asset category;

(c) that all vehicles and software were include in the Regulator's 'Other depreciable' asset category; and

(d) that all disposed items of would have been depreciated based on the initial capital base's average life remaining for the relative category.

5.11. Making these assumptions disposal figures were sourced from those used in DBP's statutory accounts.

5.12. The values have been pro-rated based on the capital base at the time of disposal. DBP used the following formula:

Undepreciated Regulatory Asset Value (Undepreciated RAV) = Statutory Account Value x ($1,550m / capital base at the time of disposal)

5.13. An adjustment was then made for depreciation based on the assumed asset category and the average life remaining for the relative category. DBP used the following formula:

Depreciated Regulatory Asset Value = Undepreciated RAV - (Undepreciated RAV / average life remaining as at 1 Jan 2000) x Number of years since 2000

5.14. The regulatory value has been included in the reconciliation undertaken by the independent auditor (see section 4 of this Submission)

Reasons for variance in actual conforming capital expenditure

5.15. The following table contains a high level comparison of the actual capital expenditure incurred by DBP and included in DBP's Original AA Proposal and the actual capital expenditure incurred by DBP and included in its Amended AA Proposal, broken into the following expenditure types and by asset categories for each expenditure type:

(a) Expenditure capitalised for regulatory purposes but expensed for accounting purposes

(b) Shipper funded capital expenditure – capital contributions

(c) Stay in business capital expenditure

(d) Stage 4 Expansion capital expenditure

(e) Stage 5A Expansion capital expenditure

(f) Stage 5B Expansion capital expenditure

Comparison of Actual Capital Expenditure filed in the Original AA Proposal and that filed in the Amended AA Proposal

	2005		2006		2007		2008		2009		2010		TOTAL	
	Actual Apr '10 filing	Actual Current filing	Actual Apr '10 filing	Actual Current filing	Actual Apr '10 filing	Actual Current filing	Actual Apr '10 filing	Actual Current filing	Actual Apr '10 filing	Actual Current filing	Forecast Apr '10 filing	Actual Current filing	Actual Apr '10 filing	Actual Current filing
LINEPACK Total	-	-	-	-	-	-	-	-	4,450,252.25	-	-	-	4,450,252.25	-
Opex Compression Total	-	-	-	294,756.70	-	587,827.63	-	1,520,302.83	-	12,188,818.55	-	-	-	14,591,705.71
Opex Other Total	-	-	-	-	-	-	-	841,006.98	-	-	-	-	-	841,006.98
Shipper Funded Total	-	2,591,855.62	-	12,583,896.13	-	7,752,098.36	-	1,011,001.82	-	-	-	-	-	23,938,851.93
SIB Compression Total	-	844,264.00	160,318.62	79,465.31	-	135,718.48	26,216.02	150,551.78	-	-	171,703,131.00	-	171,889,665.64	1,209,999.57
SIB Metering Total	-	-	50,815.60	-	-	-	-	-	76,179.76	76,179.76	50,000.00	-	176,995.36	76,179.76
SIB Other Total	38,090.01	3,382,743.62	3,175,983.68	785,498.06	2,149,487.74	2,149,487.74	3,285,990.76	3,201,175.68	520,054.78	544,292.60	35,007,276.33	-	44,176,883.30	10,063,197.70
SIB Pipeline Total	648,355.79	-	313,064.26	96,299.95	914,587.20	1,146,387.20	-	-	-	-	-	-	1,876,007.25	1,242,687.15
Stage 4 Compression Total	-	40,372,058.78	50,297,488.13	153,622,428.67	153,622,428.67	-	-	9,534,363.08	9,534,363.08	-	-	-	213,454,279.88	203,528,850.53
Stage 4 Other Total	-	107,847.96	-	-	-	-	-	909,634.79	898,550.01	-	-	-	898,550.01	1,017,482.75
Stage 4 Pipeline Total	-	7,433,603.48	2,404,435.37	229,784,242.94	229,784,242.94	-	-	159,683.33	170,768.11	-	-	-	232,359,446.42	237,377,529.75
Stage 5A Compression Total	-	-	-	-	-	-	117,142,159.10	117,142,159.10	-	-	-	-	117,142,159.10	117,142,159.10
Stage 5A Other Total	-	-	-	-	-	-	1,437,548.43	1,522,363.51	-	-	14,000,000.00	-	15,437,548.43	1,522,363.51
Stage 5A Pipeline Total	-	-	-	-	-	-	493,382,071.81	493,382,071.81	-	-	-	-	493,382,071.81	493,382,071.81
Stage 5B Compression Total	-	-	-	-	-	-	-	-	-	-	-	52,260,917.14	-	52,260,917.14
Stage 5B Metering Total	-	-	-	-	-	-	-	-	-	-	-	4,755,536.71	-	4,755,536.71
Stage 5B Other Total	-	-	-	-	-	-	-	-	-	-	15,900,000.00	75,315,456.32	15,900,000.00	75,315,456.32
Stage 5B Pipeline Total	-	-	-	-	-	-	-	-	-	-	450,000,000.00	489,959,899.98	450,000,000.00	489,959,899.98
TOTAL of OSA fees Capitalised Total	-	-	-	-	-	-	-	-	2,283,360.00	-	2,331,504.00	-	-	-
Grand Total	686,445.80	54,732,373.46	56,402,105.66	397,246,587.76	386,470,746.55	11,771,519.41	615,273,986.12	629,374,314.71	17,933,527.99	12,809,290.91	688,991,911.33	622,291,810.15	1,761,143,859.45	1,728,225,896.40

Note: that Apr 2010 Filing figures do not include shipper funded capital contributions.

5.16. A more detailed breakdown of the comparison for each of these expenditure types is contained in Attachment 4.

5.17. As is noted in the above table, there are differences in the amounts incurred for each expenditure type between the Original AA Proposal and the Amended AA Proposal:

(a) in total;

(b) in each year; and

(c) in the various asset categories for each expenditure type.

5.18. This leads to a difference between the total capital expenditure incurred between 2005 and 2010 and as reported in the Original AA Proposal and the total reported in the corrected Amended AA Proposal (once allowing for the capital contributions expended in 205-2010 and that were recorded in the Original AA Proposal) of approximately $86M. So, DBP's corrected Amended AA Proposal includes $86m less in capital expenditure than was included in the Original AA Proposal.

5.19. There are a number of reasons for the variances. However, it is important to note that all of the figures included in the corrected Amended AA Proposal have been audited by an independent auditor in accordance with the ERA's requirements for auditing, as outlined in section 4 of this submission.

5.20. The reasons are as follows.

5.21. Firstly, in relation to the Stage 4 expansion capital expenditure, the amount included in the Original AA Proposal was based on the amounts included in DBP's financial statements and not what was in the original [redacted] report.

5.22. Secondly, there are some variances between the proposals on a small number of individual capital projects. A table is provided summarising these variances (attachment 5).

ASSET No	Description	Included in Original AA Proposal	Included in Revised AA Proposal	Explaination
116832	Engel Fridge 40Litre	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
116833	Case Roller*12	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117108	Connector Plug 500v	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117109	Connector*3/Cable4mm*50	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117110	Blue Tongue Compressor	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117111	Wrench adjustable*4	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117112	Nylon/Copper Hammer*4	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117113	Tool Set Sidchrome 340pieces	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117114	Frame 3Drawer Rola Case*4	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117115	Air Tool Kit 5pce incl Wrench	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117116	Needle File Set (10) Chinese	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117117	ATX Plug 440 - 460V *3	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117198	Tetra Atmosphere Gas Tester*7	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117199	Tetra Atmospheric Gas Tester*7	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117200	Line Tracer TW7700	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117395	2*RSLOGIX 5000 Pro Edition	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117396	3*375 Field Communicator	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117398	NWSG Metering RTU upgrade	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117399	DBNGP Provide Scrubber Alarms	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117400	Turbine exchange series ESN 0058M CS1 un t 1	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
117401	Turbine exchange series ESN 0085M CS5 un t 1	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
119755	Pipeline Efficiency Calibration Instruments	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
128439	Site Improvements	[redacted]		Included from Asset Register, but not as a Statutory addition for the period
119678	CS-1 Pressure Maintenance Main Line Valve	[redacted]		Included in 2011 filing to ensure totals agreed back to Statutory Accounts, but not included in 2010 filing
128126	GEA's for CS9		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
128127	GEA's for CS6		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
128128	GEA's for CS2		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000573	CS6 GEA1 Deutz TBG616 V12 Major Overhaul SN9296219		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000574	CS6 GEA2 Deutz TBG616 V12 Major Overhaul SN9296204		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000575	CS8 GEA1 Waukesha L5108 Major Overhaul		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000576	CS9 GEA1 Deutz TBG616 V12 Major Overhaul SN9296187		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000577	CS9 GEA2 Deutz TBG616 V12 Major Overhaul SN9296220		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000590	CS6/2 Nuova Pignone Major Overhaul		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000591	CS5/2 Solar Mars 100 Replacement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000594	CS6/2 Nuova Pignone Low Pressure Turbine		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000596	CS4/1 GEA Major Overhaul		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000597	CS1 -> CS9 GEA Partial Upgrades		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000598	CS10/2 Turbine Vibration Control Enhancement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000599	CS2/3 Solar Mars 100 Replacement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000600	CS9/2 Solar Mars 100		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000656	CS2 GEA1 12000H Major Upgrade Service		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000657	CS2 GEA1 12000H Major Upgrade Service		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000658	CS3 GEA2 24000H Major Upgrade Service		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000659	CS5 GEA2 24000H Major Upgrade Service		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000660	CS6 GEA2 48000H Major Upgrade Service		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000661	CS2/2 Solar Mars 100		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000662	CS8/2 Solar Mars 100		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000572	CS9 Turbine Exhaust Stack Major Overhaul		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
131634	DBP - Throttling Vibration Study		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000544	CS6 Nuova Pignone Demister Replacement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000545	CS9 Nuova Pignone Demister Replacement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000552	CS6 Nuova Pignone D20 RTU Interface		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000553	CS9 Nuova Pignone D20 RTU Interface		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000554	CS1 Solar Turbine Lube Oil System Pipework		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000555	CS3 Solar Turbine Lube Oil System Pipework		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000556	CS5 Solar Turbine Lube Oil System Pipework		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000557	CS8 Solar Turbine Lube Oil System Pipework		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000589	CS6/2 Nuova Pignone Dry Gas Seals Replacement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000595	CS10 Vibration Monitoring Equipment		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
2000601	CS6/3 Solar Pressure Sensing Tube Replacement		[redacted]	Included in 2011 filing, however, omitted from 2010 filing due to being classified as OPEX
117406	Maintenance Vehicles - 1CCT734		[redacted]	This asset was included in the Statutory additions, but omitted in the original filing
2000718	L6 A lendale - 6 grey filing cabinets - finance		[redacted]	This asset was capitalised in 2010, w th a backdated commissioning date of 2009
2000719	L6 A lendale - Fuji Xerox C4400 serial 682601		[redacted]	This asset was capitalised in 2010, w th a backdated commissioning date of 2009
		3,888,479.05	15,850,513.50	

5.23. Finally, for the 2010 actual expenditure in all expenditure types, there is a difference between the amounts included in the Original AA Proposal and the corrected Amended AA Proposal. This is so for two reasons:

(a) DBP now knows what it has incurred in 2010 whereas at the time of the filing of the Original AA Proposal (ie April 2010), DBP only had available to it a forecast of what it expected to be the actual expenditure for 2010.

(b) DBP is now not capitalising in 2010 items of capital expenditure which are recorded in the audited financial accounts for that year as being “Construction Work in Progress” or “Assets under Construction”. These items will therefore be capitalised in 2011 instead.

5.24. The large variances between balances in each year are explained by a shift in its approach to reporting figures in its regulatory submissions. Variances are explained by shifting expenditure to align with the date of commissioning (or that at which depreciation commences) as opposed to the timing of capitalisation for accounting purposes. The detailed breakdown of the table above in attachment 4 demonstrates how the timing for expenditure has been adjusted.

6. JUSTIFICATION UNDER 79(2)

Rule 79(2)(c)(iii) - Expenditure to comply with a regulatory obligation or requirement

6.1. The NGR prescribes that the ERA's discretion in making decisions relating to the element of an access arrangement proposal governed by rule 79 is limited. Accordingly, the ERA cannot withhold its approval to an element of an access arrangement proposal that is governed by rule 79 if the ERA is satisfied that it:

(a) complies with applicable requirements of the Law; and

(b) is consistent with applicable criteria (if any) prescribed by the Law.

6.2. In paragraph 250 of the Draft Decision, the ERA states that it agrees with Alinta Pty Limited's submission which contests DBP's reliance on the ACCC Undertakings as a justification for capital expenditure in accordance with rule 79(2)(c)(iii). The ERA agrees that the ACCC Undertakings "*do not constitute a regulatory obligation that compelled DBP to expand the DBNGP and do not justify capital expenditure under rule 79(2)(c)(iii)*".

6.3. It is not clear from the ERA's statement whether the ERA is disputing that the obligations imposed on DBP under the ACCC Undertakings were regulatory obligations or, alternatively, that the obligations *are* regulatory obligations but these obligations did not *compel* DBP to expand the DBNGP and therefore do not meet the criteria in rule 79(2)(c)(iii). A review of other language in paragraph 250 seems to support the alternative as being the correct interpretation of the ERA's position.

6.4. In either case, the DBP submits that the ERA has incorrectly interpreted the obligation which is imposed on DBP under the ACCC Undertakings.

6.5. In particular, at paragraph 250 the ERA states that under clause 5.7 of the ACCC Undertakings DBP was only required to expand the capacity of the DBNGP to "*meet known capacity requirements of users that enter into standard shipper contracts*" and that this obligation was limited by clause 5.6 (presumably clause 5.6(b)(i), although this is not expressly stated) which includes a proviso that DBP is not required to enter into a Shipper Contract (sic) with a prospective shipper if it would not be required to do so under the Gas Access Law and Access Arrangement. As a result of this apparent limitation, the ERA concluded that:

(a) clause 5.6 and 5.7 did not create any obligation which was additional to any expansion obligations it might have under the Gas Access Law, in particular under section 6.22 of the Gas Code; and

(b) that the expansion obligations imposed under the ACCC Undertakings would compel DBP to expand the DBNGP only in limited circumstances; that is, where the expansion is economically feasible and the service provider is not required to fund part or all of the expansion (which appears to be inconsistent with its earlier statement that the obligations in the ACCC Undertakings did not compel DBP to expand the DBNGP).

6.6. The ERA appears to have made a number of errors in reaching this conclusion.

6.7. First, clause 5.7 is not subject to, or conditioned by, clause 5.6 other than in the respect that any Standard Shipper Contract must include capacity expansion obligations (clause 5.6(a)).

6.8. Second, clause 5.6(b)(i) is not relevant for the purpose of the ERA's consideration of whether the obligations imposed under the ACCC undertakings meets the criteria set out in clause 79(2)(c)(iii) to justify new capital expenditure during the Access Arrangement Period (i.e. for the Stage 4 expansion). This is because the Stage 4 expansion was necessary to meet the capacity requirements of *contracted* shippers (and not *prospective* shippers), as DBP demonstrated in section 2.14 of Submission 9; whereas clause 5.6(b)(i) of the undertakings applies only to *prospective* shippers - it does not apply to *contracted* shippers. This is true also in respect of *contracted* shippers who sought expansion capacity under Stage 5A and Stage 5B expansions.

6.9. Third, it is not correct to say that clause 5.6 and 5.7 of the ACCC Undertaking did not compel DBP to undertake any expansions. Clause 5.7 clearly imposes an obligation on DBP to expand the DBNGP by a certain capacity (i.e. minimum of 100 TJ in aggregate) to meet the known capacity requirements of contracted shippers or prospective shippers within a certain timeframe (i.e. 5 years), subject only to:

(a) an assessment by DBP as to whether such an expansion was technically or economically feasible;

(b) the shipper who requested the expansion having a standard shipper contract (which meets the requirement in clause 5.6(a) that the contract include non-discriminatory capacity expansion rights as compared to other shipper contracts for a T1 service); and

(c) the expansion being carried out in accordance with the terms of that contract.

6.10. That is, if DBP's feasibility assessment found that any requested expansion satisfied the feasibility criteria and the requesting shipper had a relevant existing contract, DBP was, in fact, compelled by clause 5.7 to undertake an expansion to meet the required capacity in accordance with the terms of the shipper contract (which in the case of the standard shipper contract includes at clause 16 provisions dealing with funding contributions by the shipper) and the ACCC Undertaking. In the case of the Stage 4 expansion:

(a) DBP's feasibility assessment indicated that expansion to meet requested capacity from contracted shippers was both economically and technically feasible; and

(b) each of the shippers requesting expansion capacity had an existing shipper contract which included expansion capacity rights (clause 16).

6.11. Finally, whether or not the obligations imposed on DBP under the ACCC Undertakings were additional to any other statutory obligation that may have required DBP to expand the DBNGP is an irrelevant consideration in circumstances where those other obligations did not, in fact, apply for the purpose of new expenditure during the Access Arrangement Period (e.g. section 6.22 of the Gas Code which the ERA refers to but which did not impose an obligation with respect to the Stage 4 expansion). Rule 79(2)(c)(iii) confines the ERA to considering whether capital expenditure was necessary in order for DBP to comply with the ACCC Undertakings, on the basis that the obligations contained in the undertakings are regulatory obligations or requirements which were imposed on DBP during the Access Arrangement Period. If the obligations under the ACCC Undertakings comply with that criteria, which DBP submits they did, then the ERA must not withhold its approval of that element of the access arrangement proposal.

Rule 79(2)(a) - Overall Economic Value of Expenditure is Positive

6.12. Only conforming capital expenditure may be added to the capital base of a covered pipeline and recovered via reference tariffs. In accordance with Rule 79(1) of the NGR, conforming capital expenditure is capital expenditure which:

(a) 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;

(b) is justifiable on a ground stated in Rule 79(2).

6.13. Rule 79(2) sets out four "grounds" on which capital expenditure may be justifiable:

(a) the overall economic value of the expenditure is positive; or

(b) the present value of the expected incremental revenue to be generated exceeds the present value of the capital expenditure; or

(c) the capital expenditure is necessary:

(i) to maintain and improve the safety of services; or

(ii) to maintain the integrity of services; or

(iii) to comply with a regulatory obligation or requirement; or

(iv) to maintain the service provider's capacity to meet levels of demand for services existing at the time the capital expenditure is incurred; or

(d) the capital expenditure is an aggregate amount divisible into two parts, one referable to incremental services and the other referable to a purpose referred to in paragraph (c), and the former is justifiable under paragraph (b) and the latter under paragraph (c).

6.14. Rule 79(3) limits the extent of "economic value" in the context of Rule 79(2)(a): in deciding whether the overall economic value of capital expenditure is positive, consideration is to be given only to economic value directly accruing to the service provider, gas producers, users and end users.

6.15. Certain transitional provisions also apply in the case of capital expenditures by DBP because the DBNGP is a Western Australian gas transmission pipeline. In particular, clause 7(2) of Schedule 1 to the NGR requires:

In making a relevant decision under rule 79(3) on whether the overall economic value of capital expenditure is positive, the AER must consider not only economic value directly accruing to the service provider, gas producers, users and end users (as required by rule 79(3)) but also material economic value that is likely to accrue directly to electricity market participants and end users of electricity from additional gas fired generation capacity.

Draft Decision

6.16. In paragraph 251 of the Draft Decision, the ERA stated:

DBP submits that the expenditure associated with each of stages 4, 5A and 5B of expansion of the DBNGP, when considered as separate investments, meets the requirement of rule 79(2)(b) of the NGR.

6.17. This is not correct. In support of this statement, the ERA referred to paragraphs 18.9 and 18.10 DBP's *Submission 9: Justification of Expansion Related Capital Expenditure* (**Submission 9**). However, paragraph 18.9 did not assert that the expenditure associated with each of Stages 4, 5A and 5B, when considered as separate investments, met the requirement of Rule 79(2)(b). Paragraph 18.9 only advised of a possible interpretation of Rule 79(2)(b): that the total expansion expenditure during the period 2005 to 2010 could be found to be justifiable if each of the three stages of expansion were found to satisfy the test of Rule 79(2)(b). Paragraph 18.10 then noted only that DBP's consultant, Marsden Jacob Associates, agreed with this view. Neither DBP, nor Marsden Jacob Associates, was of the view that the expenditure associated with each of Stages 4, 5A and 5B, when considered as separate investments, met the requirement of rule 79(2)(b).

6.18. On the basis of advice from its consultant, DBP submitted, in Submission 9, that the total capital expenditure on the Stage 4, Stage 5A and Stage 5B expansions of the DBNGP was justified under Rule 79(2)(a). (This was noted in paragraph 257 of the Draft Decision.) However, in paragraph 264, the ERA advised that it considered the analysis which had been provided in support of this submission was too simplistic and inexact to be relied upon as an indication of the economic benefits.

6.19. The ERA advised that the shortcomings of the analysis were:

- *The analysis considers only very simplistic scenarios of direct physical substitution of gas for other energy sources for both retail gas customers and electricity generators. The Authority considers that this fails to adequately address the effects of a greater gas supply to the south west of Western Australia (enabled by expansions in capacity of the DBNGP) on relative prices of energy sources, investments in energy infrastructure, competition in energy markets and costs of energy supplies to end users.*
- *The analysis of substitution between gas and electricity by retail gas customers was undertaken applying unjustified assumptions on the substitutability of electricity and gas and derives unreliable estimates of the benefits to retail energy customers of a greater gas supply.*
- *The analysis of substitution between gas and other fuel types in electricity generation involves too simplistic an assessment of the cost effects of substitution of generation types in the electricity market (gas, coal and diesel-fired) by failing to take into account both capital and operating costs of generation with different fuel types and the investment decisions in generation plant that would be affected by the additional DBNGP capacity.*[1]

6.20. DBP agrees that the analysis which has been provided only considers scenarios of direct physical substitution of gas for other energy sources for both retail gas customers and electricity generators, and does not address the wider economic effects of a greater gas supply to the south west of Western Australia. However, to do so would be contrary to the limitations on the assessment of overall economic value imposed by Rule 79(3) as modified by the transitional provisions of clause 7(2) to Schedule 1 to the NGR.

6.21. To the extent that these effects are restricted to the gas and electricity markets, if a greater gas supply were to stimulate investment in energy infrastructure, and were to promote competition with the effect of lowering gas and electricity prices, then the overall economic benefits of pipeline expansion would be larger than DBP and its consultant have indicated.

6.22. There are, however, substantial difficulties in considering the effects of a greater gas supply to the south west of Western Australia. The market for gas transportation services

[1] Draft Decision, paragraph 264.

served by the DBNGP is a market in which there is a relatively small number of buyers of larger volumes of gas. Those buyers are quite diverse (minerals processors operating in a range of commodity markets, electricity generators, and energy retailers), making inferences about what they might, or might not, do when faced with change is difficult, if not impossible. DBP and its consultant have made simple assumptions about substitutability because the commercial options which might be available to these market participants, and the costs and benefits of these options, are known – if at all – only to the individual participants. The market does not comprise a large number of relatively homogeneous buyers for whom assumptions about similar preferences, and smooth and continuous substitution in response to price change, are appropriate.

6.23. Simple, but obvious, assumptions were made in respect of behaviour in the retail sectors of electricity and gas markets. Refinement is difficult. DBP notes that, in Western Australia, these remain markets in which the Government, through the Minister of Energy, retains a role in price setting, injecting a political element which complicates prediction of the effects of change. Moreover, (predominantly) [redacted] clearly believed it could sell more gas through its contracting long term for additional pipeline capacity. Given the relatively inelastic nature of retail energy demand it is most likely that under the counterfactual situation this energy demand would be met through electricity. If other alternatives are considered – such as bottled gas, then due to its high cost, this would only increase the economic benefit of additional pipeline capacity to retail consumers.

6.24. DBP accepts that on a day to day basis existing retail gas consumers would only able to substitute the use of gas for electricity in space heating. However, over a longer timeframe, existing homes with a gas connection and new-build homes or renovations with gas available in the street would be able to compare gas and electric products for a range of uses such as water heating and cooking.[2]

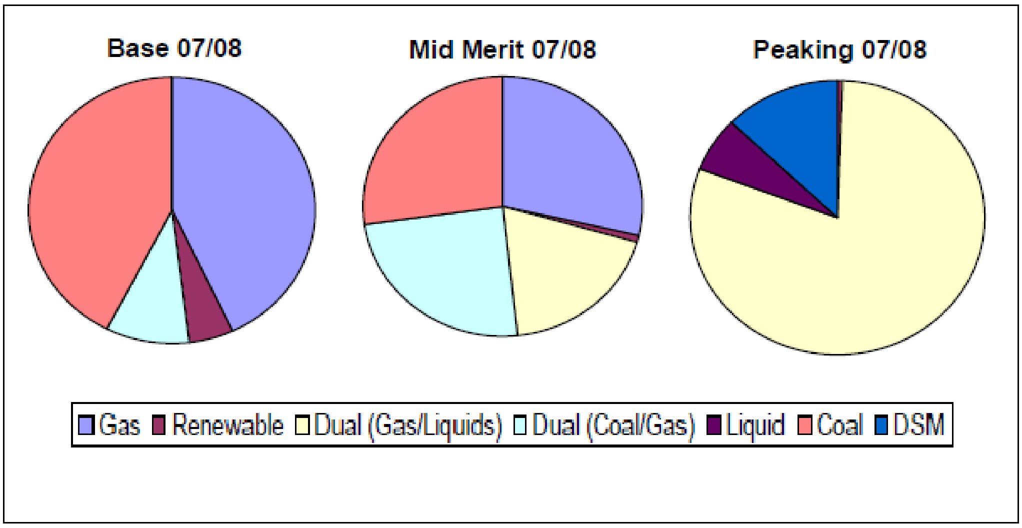
6.25. A “fully informed” and non time constrained consumer would compare gas and electric appliances for both hot water and cooking and consider the costs and benefits over a whole of life basis. Through this process the ideal consumer would consider the energy cost differential as well as the upfront product costs, installation costs, product life and other factors (such as a personal preference for or against cooking with gas). In this manner substitution could occur across a broad range of uses over a longer timeframe as DBP’s consultant has assumed.

6.26. In considering the market for electricity generation, provision of the additional gas capacity coincides approximately with the implementation of the Wholesale Electricity Market for the South West Interconnected System. Since 2005 the Independent Market Operator has published a Statement of Opportunities outlining the need for additional capacity in the electricity generation market. In considering the counterfactual situation the impact of the additional capacity on the capacity credits market is impossible to accurately predict – especially as this market is competitive but only partially transparent.

6.27. As noted by Marsden Jacob Associates in its report, gas-fired generation, and dual fuel generation that includes gas, account for almost 66% of the increase in capacity over the period 2005/06 to 2010/11. Furthermore, although coal is substantially cheaper than the alternatives, it makes up a relatively small proportion of mid merit generation and is not used for peaking (See figure Figure 1).

[2] For new houses or renovations with gas available in the street the cost of installing gas would be a relatively small addition to the building cost, particularly as the installation could occur during construction by tradesman already on site.

6.28. **Figure 1: Fuel composition servicing different generation load types**



Source: Independent Market Operator of Western Australia, Reserve Capacity Mechanism Progress Report, May 2009.

6.29. On the basis of this assessment, Marsden Jacob Associates assumed that any reduction in gas generation would be made up through an even split of coal and distillate.

6.30. Given the prevalence of coal, distillate and dual fuel generation (coal/gas and liquids/gas), particularly in the mid merit and peaking segments of the generation market, this was a reasonable starting assumption. Any other scenarios put forward as the counterfactual would be difficult to justify.

6.31. DBP also notes that for dual fuel generation (shown,Figure 1), to be around 45% of mid merit generation, and 80% of peaking generation) the fuels would appear to be directly substitutable, further indicating that the assumptions made by its consultant were reasonable.

6.32. DBP does not agree with the ERA's assertion, in paragraph 265 of the Draft Decision, that it has not presented a reliable quantification of the economic benefits from the expansions in capacity of the DBNGP. Rule 79(2)(a) does not require a reliable quantification of the economic benefits. Rule 79(2)(a) requires only that the economic value of the expenditure be shown to be positive. DBP and its consultant have shown a substantially positive, although not precisely estimated, overall economic value.

6.33. DBP notes that, in paragraph 266 of the Draft Decision, the ERA has argued that:

> *. . . inferences on economic benefits can be drawn from the contractual arrangements under which the expansions to capacity have occurred.*

6.34. In paragraphs 267 to 269, the ERA set out reasons for this view. In this context, reference to the specific arrangements of the Standard Shipper Contracts is not particularly relevant. The fact is, as the ERA correctly identified in paragraph 269, a number of businesses entered into commercial arrangements with DBP for access to additional capacity in the DBNGP. That these arrangements were entered into by businesses which can reasonably be assumed to be acting rationally and commercially is evidence of expected positive economic benefits from pipeline expansion.

6.35. DBP notes that the “test” which the ERA which has applied is the same as the “test” which DBP applied: demonstration of positive overall economic benefits. The ERA has not sought – because it did not need to – a reliable estimate of the economic benefits.

6.36. In paragraph 270 of the Draft Decision, the ERA qualified its argument that contracting for additional capacity by parties acting rationally and commercially provided direct evidence of positive economic benefits from pipeline expansion. The scope and cost of expansion may have been greater than anticipated by some shippers – shippers not requiring additional capacity – and, for these shippers, there may be a reduction in economic value when they become subject to the closest equivalent reference tariff in 2016. This qualification does little more than highlight the fact that, in a market – the market for gas transportation services – where buyers, and the customers of those buyers, are clearly heterogeneous, making inferences about what they might, or might not, do when faced with change is difficult, if not impossible.

6.37. In these circumstances, DBP and its consultant have made simple assumptions about substitutability because the commercial options which might be available to market participants, and the costs and benefits of these options, are not generally known. Those simple assumptions do not allow the precise quantification of the overall economic value of pipeline expansion. They do allow the conclusion that the overall economic value is positive.

7. CONFIDENTIALITY

[redacted]

ATTACHMENTS

Attachment 1 – Updated [redacted] report for stage 4 expansion
Attachment 2 – Updated [redacted] for stage 5B expansion
Attachment 3 – [redacted] agreed upon procedures report
Attachment 4 – Detailed breakdown of capital expenditure variances between Original AA Proposal and corrected Amended AA Proposal
Attachment 5 – List of projects included in Amended AA Proposal and not in the Original AA Proposal and vice versa