

Final Approval

Access Arrangement proposed by NT Gas Pty Ltd for the Amadeus Basin to Darwin Pipeline

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1. Background

NT Gas submitted an access arrangement for the Amadeus Basin to Darwin Pipeline (ABDP) to the Australian Competition and Consumer Commission (the Commission) on 25 June 1999. It sought approval under section 2.2 of the *National Third Party Access Code for Natural Gas Pipeline Systems* (the Code). The access arrangement describes the terms and conditions on which third parties will gain access to the pipeline.

The ABDP transports gas from the Palm Valley and Mereenie gas fields to Darwin. The pipeline is fully contracted until 2011, with the majority of gas transported (99.7 per cent) used in the generation of electricity. In 1988 the AGL Group acquired through wholly owned subsidiaries¹ 96% of NT Gas. Later, AGL floated its pipeline interests including its share of NT Gas through a transfer to the Australian Pipeline Trust, in June 2000.

The Commission's assessment of the access arrangement has been conducted in accordance with the Code. It has involved public consultation, examination of information provided by NT Gas and interested parties and has included:

- The release of a Draft Decision (pursuant to s. 2.13 of the Code) on the proposed access arrangement on 2 May 2001, in which the Commission proposed sixteen amendments to be made for the access arrangement to be approved; and
- The release of a Final Decision (pursuant to s. 2.16 of the Code) on 4 December 2002, in which the Commission required seventeen amendments to be made for the access arrangement to be approved.

Following the release of the Commission's Final Decision, NT Gas submitted revisions to its access arrangement and access arrangement information on 5 February 2003.

This Final Approval assesses NT Gas' revised access arrangement and access arrangement information. It relates to the facts and analysis set out in the Commission's Final Decision and should be read in conjunction with that decision.

¹ Agex Pty Ltd and Sopic Pty Ltd

2. NT Gas' Revised Access Arrangement

2.1 Assessment

Having received the revised access arrangement and access arrangement information, the Commission is required under section 2.19 of the Code to issue a further final decision (this Final Approval).

The Commission has assessed NT Gas' revised access arrangement and considers that NT Gas has incorporated the amendments specified in the Commission's Final Decision. Accordingly, the Commission approves the revised access arrangement and access arrangement information submitted by NT Gas.

The following section identifies the required amendments as per the Final Decision and discusses their incorporation in the revised access arrangement and access arrangement information.

2.1.1 The initial Capital Base

Initial Capital Base

Amendment FDA2.1

In order for NT Gas' access arrangement for the ABDP to be approved, the value of the initial capital base must be adjusted to the value derived by the Commission of **\$228.5m** as at 1 July 2001.

The Commission determined an Optimised Deprival based initial Capital Base (ICB) of \$228.5m as at 1 July 2001.

Following the release of the Final Decision, NT Gas adopted this ICB valuation in its revised access arrangement information. This is also reflected in its access arrangement.

Depreciated Optimised Replacement Cost

The Commission notes that NT Gas included a Depreciated Optimised Replacement Cost (DORC) estimate of \$336.3m as at 1 July 2001 in its revised access arrangement information. This estimate is NT Gas's opinion of a DORC valuation for the ABDP. No rationale, underpinning assumptions or methodology in support of the derivation of this DORC value have been provided in the revised access arrangement or access arrangement information.

The Commission is concerned that NT Gas' inclusion of its DORC value has the potential to confuse users and prospective users as to the relevant valuation of the ICB. It needs to be clarified that NT Gas' DORC value is not the ICB and does not affect the calculation of reference tariffs to which this Final Approval relates.

Section 8.10 of the Code identifies the factors that should be considered in establishing an ICB for a pipeline in operation at the commencement of the Code. A DORC valuation is one of a range of matters the regulator is required to consider in determining an ICB. In accordance with the provisions of the Code, the Commission has determined an ICB using a methodology other than DORC. NT Gas adopted the Commission's ICB valuation.

This Final Approval does not endorse NT Gas' DORC value nor any of the assumptions or methodology which presumably underpin its derivation. The Commission has set out in detail the relevant considerations for determining the ICB in its Final Decision.

The Commission affirms that the ICB is \$228.5m as at 1 July 2001.

2.1.2 New facilities investment and capital redundancy

New facilities investment

Amendment FDA3.1

In order for NT Gas' access arrangement for the ABDP to be approved, clause 4 of section 4 of the access arrangement must state that new facilities investment that does not satisfy the requirements of the Code may be undertaken by NT Gas. However, only that portion of the investment that satisfies the requirements of the Code may be included in the capital base.

In order for NT Gas' access arrangement for the ABDP to be approved, clause 6 of section 4 of the access arrangement must be amended to clearly specify that any new facilities investment must meet the requirements of the Code before it can be included in the capital base.

The Commission was concerned that clause 4 of section 4 of NT Gas' original access arrangement implied all new facilities investment could be included in the Capital Base whether it satisfied the requirements of section 8.16 of the Code or not. Though the Code has precedence over the access arrangement, the Commission believed there was potential for clause 4 of section 4 to confuse prospective users.

Following the release of the Commission's Final Decision, NT Gas agreed to make this amendment. NT Gas incorporated the amendment in its revised access arrangement with minor wording variations from the requirements contained in the Commission's Final Decision. In the Commission's view the revised access arrangement and access arrangement information substantially incorporates the amendment required by the Final Decision.

Capital redundancy

Amendment FDA3.2

In order for NT Gas' access arrangement for the ABDP to be approved, the reference tariff policy must be amended to allow the Commission at the commencement of the subsequent access arrangement period to review, and if necessary adjust, the asset base for wholly or partially redundant assets within the meaning of the Code.

The Commission was concerned that the reference tariff policy in NT Gas' original access arrangement did not allow redundant capital assets to be removed from the asset base at the start of the subsequent access arrangement period. As a result of the Commission's Final Decision, NT Gas agreed to adjust the asset base for wholly or partially redundant assets. Such a mechanism has been included in the reference tariff policy of NT Gas' revised access arrangement.

NT Gas has complied with this amendment in its revised access arrangement and reflected this in its access arrangement information.

2.1.3 Depreciation and inflation

Depreciation

Amendment FDA3.3

In order for NT Gas' access arrangement for the ABDP to be approved, NT Gas should adopt the depreciation schedule given in Table 3.2.

As a result of the Commission's Final Decision, NT Gas has amended its revised access arrangement information and reflected changes in its access arrangement according to the following depreciation schedule.

Depreciation schedule (nominal) for 2002-2011[#]

Year ending 30 June	Depreciation (\$m)
2002	14.12
2003	15.53
2004	17.09
2005	18.80
2006	20.75
2007	14.44
2008	12.49
2009	13.09
2010	13.71
2011	14.35

[#]This schedule is in nominal terms. Forecast total revenues and reference tariffs have been derived from a normalised depreciation schedule.

Working capital

Amendment FDA3.4

In order for NT Gas' access arrangement for the ABDP to be approved, for the purpose of calculating NT Gas' return on capital assets, the working capital component must not be included in the capital base.

In its original access arrangement, NT Gas included a working capital component in its calculation of capital costs. For the reasons set out in its Final Decision, the Commission required NT Gas to remove the working capital component. NT Gas agreed and as a result has amended its access arrangement information and reflected relevant changes in its access arrangement.

2.1.4 Rate of return

Amendment FDA3.5

In order for NT Gas' access arrangement for the ABDP to be approved:

- the WACC estimates and associated parameters forming part of the access arrangement and access arrangement information must be amended to reflect the current financial market settings by adopting the parameters set out by the Commission in Table 3.5 and Table 3.6; and
- the target revenues and forecast revenues must be based on these new parameters.

NT Gas proposed a range of possible values for WACC parameters in its original access arrangement. The Commission assessed the parameters proposed by NT Gas against the requirements of the Code. After considering all relevant factors, the Commission arrived at the values listed in the Final Decision.

NT Gas has amended its values for WACC parameters according to the Commission's calculations and reflected these in its revised access arrangement and access arrangement information.

2.1.5 Legitimate business interests and existing contractual obligations

Amendment FDA3.6

In order for NT Gas' access arrangement to be approved, allowances for the additional tariff component (as detailed in Table D.1 of Confidential Annexure D) must be included in the calculation of forecast revenues.

NT Gas did not include two cost components in its original access arrangement. One is a capital cost. The other is a non-capital cost which is referred to as the additional tariff component. NT Gas advised the Commission of these costs and provided relevant information about them after the release of the Commission's Draft Decision. The Commission determined in its Final Decision that the inclusion of an additional tariff component was necessary for the appropriate calculation of forecast total revenues. Consequently, NT Gas has amended its access arrangement information and reflected relevant changes in its access arrangement.

2.1.6 Forecast revenue and pipeline capacity

Amendment FDA3.7

In order for NT Gas' access arrangement for the ABDP to be approved, the [Optimised Replacement Cost] ORC valuations for each zone used for the calculation of tariffs should be amended as follows:

Zone One	\$171.6m
Zone Two	\$118.6m
Zone Three	\$83.5m

The Commission accepted the methodology outlined in NT Gas' original access arrangement for the allocation of costs to each zone. However, the Commission has calculated zonal costs using its own estimates of ORC. Following the Commission's Final Decision, NT Gas amended its access arrangement information, with changes also reflected in the access arrangement, to correspond with the Commission's ORC valuation as the basis for calculating zonal tariffs.

2.1.7 Tariff path and incentive structure

Reference tariffs and tariff path

Amendment FDA3.8

In order for NT Gas' access arrangement for the ABDP to be approved, NT Gas must amend the reference tariff proposed in Section 3 of the access arrangement. The amendment must have the effect that:

- the initial tariff (in 2001/02) is derived from the cost of service revenue resulting from the amendments proposed by the Commission in this *Final Decision*; and
- in each subsequent year, with the exception of the 2007/2008 financial year, the reference tariffs will be calculated using the CPI-X tariff escalator:

$$t_n = t_{n-1} (1 + (CPI_n - CPI_{n-1}) / CPI_{n-1}) \cdot (1 - X)$$

where X = 1.51 per cent

- In the 2007/2008 financial year a once off tariff adjustment will occur and the tariff will be derived in accordance with the following formula:

$$t_n = t_{n-1} (1 + (CPI_n - CPI_{n-1}) / CPI_{n-1}) \cdot (1 - X) \cdot Y$$

where Y = 0.74

X = 1.51 per cent

Section 3 of the access arrangement must be amended to remove the reference to CPI adjustment of NT Gas' proposed reference tariff for the year to 30 June 2004. In the event that there is a gap between the reference tariff years specified in the access arrangement and the revisions commencement date, the interim reference tariff will be determined by adjusting the final year's reference tariff in accordance with the CPI-X tariff escalator discussed in point two of this amendment.

In accordance with the Final Decision, NT Gas determined reference tariffs for the first year of the access arrangement based on the Commission's decision and accepted that all subsequent reference tariffs would be based on the reference tariff escalator formula except in 2007/2008. NT Gas also agreed to the Commission's "X" factor of 1.51%.

NT Gas has incorporated a once off tariff adjustment for the 2007/2008 financial year. This recognises the termination of an additional cost component for NT Gas in June 2006.

NT Gas was concerned about the calculation of reference tariffs after 1 July 2011 if there was a gap between that date and the revisions commencement date. The Commission considers it appropriate for the access arrangement to state that interim reference tariffs will be calculated using the same formula as reference tariffs in the access arrangement period.

Following the release of the Commission’s Final Decision, NT Gas agreed to make these amendments and has done so in its revised access arrangement information with changes reflected in the access arrangement.

Incentive mechanism

Amendment FDA3.9

In order for NT Gas’ access arrangement for the ABDP to be approved, the following statement must be deleted from Clause 9 of the reference tariff policy:

‘and to provide other Users of the Pipeline with a share in gains from additional sales of Services.’

In its original access arrangement, NT Gas proposed that revenue from interruptible services be distributed according to the Amadeus Gas Trust agreement. It was the Commission’s view that the phrase ‘share in gains from additional sales of services’ may have misled users or prospective users as to likely benefits of the incentive mechanism. NT Gas agreed with this amendment and has changed its access arrangement and access arrangement information accordingly.

Fixed principle

Amendment FDA3.10

In order for NT Gas’ access arrangement for the ABDP to be approved, the fixed principle (section 4.8) must be deleted.

Section 4.8 of the reference tariff policy in the original access arrangement included a reference to one fixed principle. The Commission regarded the inclusion of this fixed principle as unnecessary given that section 4.6 of the reference tariff policy satisfied section 8.22 of the Code.

Following the release of the Commission’s Final Decision, NT Gas agreed to remove this reference and has done so in its revised access arrangement with changes also reflected in the access arrangement information.

2.1.8 Terms and Conditions

Gas quality specifications

Amendment FDA4.1

In order for NT Gas' access arrangement for the Amadeus Basin to Darwin Pipeline to be approved, NT Gas must amend the access arrangement to require adoption of a revised gas specification, subject to:

- the enactment of any legislation necessary to facilitate the change in specification;
- recognition and preservation of existing contractual rights and obligations; and
- the specification not precluding continued transportation of gas from existing fields.

NT Gas incorporated these amendments in its revised access arrangement with minor wording variations from the requirements contained in the Commission's Final Decision. In the Commission's view the revised access arrangement substantially incorporates the amendment required by the Final Decision.

Standard service agreement

Amendment FDA4.2

In order for NT Gas' access arrangement for the Amadeus Basin to Darwin Pipeline to be approved, NT Gas must clearly specify that schedule 2 of the access arrangement prevails over the standard service agreement.

The Commission was concerned that the original access arrangement proposed by NT Gas did not specifically state that schedule 2 of the access arrangement takes precedence over the standard service agreement. The Commission considered that such a clause is needed to clarify the status of the access arrangement in the event of inconsistency between the standard service agreement and the access arrangement. NT Gas agreed and has made the required amendment in its revised access arrangement.

Prudential requirements

Amendment FDA4.3

In order for NT Gas' access arrangement for the Amadeus Basin to Darwin Pipeline to be approved, NT Gas must include in the access arrangement the prudential requirements set out below:

- the user or prospective user must be resident in, or have a permanent establishment in, Australia.;
- the user or prospective user must not be under external administration as defined in the Corporations Act or under any similar form of administration in any other jurisdiction; and
- the user or prospective user may be required to provide reasonable security in the form of a parent company guarantee or a bank guarantee or similar security. The nature and extent of the security will be determined having regard to the nature and extent of the obligations of the user or prospective user under the Service Agreement.

In response to the Commission's Draft Decision, NT Gas proposed that users and prospective users must meet certain prudential requirements to gain access to services from the ABDP.

In its Final Decision, the Commission found these requirements to be reasonable. NT Gas has reflected these amendments in its revised access arrangement.

2.1.9 Extensions and Expansions policy

Amendment FDA4.4

In order for NT Gas's access arrangement for the Amadeus Basin to Darwin Pipeline to be approved, NT Gas must amend section 7.2(b) and insert (c) to its proposed access arrangement to read:

- (b) that the expanded capacity will not be treated as part of the pipeline for the purposes of this Access Arrangement and NT Gas will lodge a separate Access Arrangement in respect of that expanded capacity; or
- (c) that the expansion will not be covered, subject to the consent of the Commission prior to the expansion coming into service.

NT Gas agreed to make the amendment outlined in the Commission's Final Decision and has done so in its revised access arrangement.

2.1.10 Review and expiry of the access arrangement

Amendment FDA4.5

In order for NT Gas's access arrangement for the Amadeus Basin to Darwin Pipeline to be approved, NT Gas must amend clause 9.2 of the access arrangement:

- to specify 1 January 2011 as the Revisions Submission Date; and
- to include the following trigger mechanism:

NT Gas is required to submit revisions to this access arrangement within one month of receiving written notification by the Commission that one of the following major events has occurred:

- (i) the interconnection of another pipeline with the ABDP; or
- (ii) the introduction of a significant new source of gas supply to one of the ABDP's markets;

that substantially changes the types of Services that are likely to be sought by the market or has a substantial effect on the direction of the flow of natural gas through all or part of the pipeline.

Following the release of the Commission's Draft Decision, NT Gas proposed a ten year access arrangement so the subsequent revisions date coincides with the end of NT Gas' lease on pipeline assets. The Commission accepted this proposal in its Final Decision but considered a review mechanism necessary to reassess the access arrangement if specific major events occur.

NT Gas agreed with the inclusion of a review mechanism, but incorporated the amendment in its revised access arrangement with minor wording variations from the requirements contained in the Commission's Final Decision. In the Commission's view the revised access arrangement substantially incorporates the amendment required by the Final Decision.

2.1.11 Information provision and performance indicators

Amendment FDA5.1

For the access arrangement to be approved, the Commission requires NT Gas to revise its access arrangement information so that it is consistent with the most recent information provided to the Commission as part of the completion of the *Final Decision*, and incorporate relevant amendments specified in this *Final Decision*.

NT Gas agreed with this requirement and has reflected these amendments in its revised access arrangement and access arrangement information.

3. Final Approval

For the reasons expressed in this Final Approval and in the Commission's Final Decision, pursuant to section 2.19 of the Code, the Commission approves NT Gas' revised access arrangement for the Amadeus Basin to Darwin Pipeline.

The access arrangement commences on 28 March 2003.

This Final Approval document and NT Gas' revised access arrangement and access arrangement information for the Amadeus Basin to Darwin Pipeline are available on the Commission's website at <http://www.accc.gov.au> under 'Gas'.