

Draft decision:

Australian Petroleum Pipelines Pty Ltd (APTPL) Roma to Brisbane Pipeline 2017–22

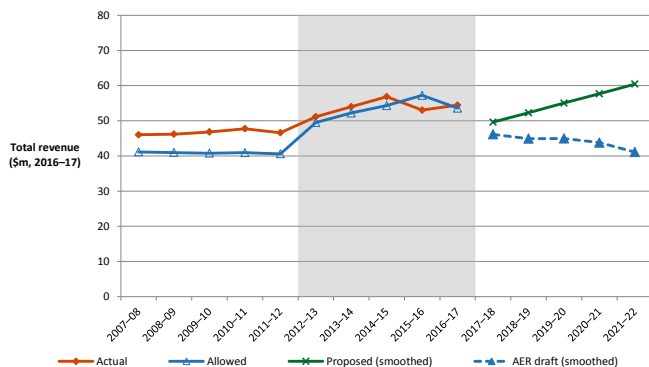
Overview

The Australian Energy Regulator (AER) approves access arrangements for APTPL and other major gas networks in most of Australia under the National Gas Law (NGL) and National Gas Rules (NGR). APTPL is the owner and operator of the Roma to Brisbane Pipeline (RBP).

Our draft decision allows APTPL to recover \$237.4 million (\$nominal) from its customers over five years commencing 1 July 2017. If implemented, the forecast revenue requirement approved in this draft decision would allow APTPL to recover 9.6 per cent less revenue than its 2012–17 allowance of \$262.7 million (\$ nominal, smoothed).

The figure below shows the difference between APTPL's proposed revenue, and what we have allowed for each year of the access arrangement period.

APTPL's past and proposed total revenue and AER draft decision revenue allowance (\$million, 2016–17)



The revenue we determine affects the transmission component of a customer's gas bill. Transmission charges make up approximately 3 per cent of a Queensland residential or small business customer's annual gas bill.

Other components of customer bills include the cost of sourcing the gas, distribution network charges and retailer costs. The AER does not set retail prices.

Estimated impact on customer bills

If implemented, we expect that our draft decision will result in no material change to the transmission component of the average annual gas bills for residential customers in Queensland over the 2017–22 access arrangement period. Similarly, bill impacts for large directly connected customers will be minimal because our draft decision is for relatively flat transmission tariffs.

Key elements of our decision

We made our assessment of APTPL's proposed revenue by separately considering its components. These include expenditures to maintain and operate the pipeline, and the return to shareholders on their investment. Together, these determine the revenue that APTPL may recover from its customers.

Our draft decision accepts APTPL's opex forecast of \$72.1 million (\$2016–17) over the 2017–22 access arrangement period. We made slight reductions in APTPL's proposed capex over the access arrangement period. Our draft decision approves \$61.1 million (\$2016–17) of APTPL's proposed total net capex of \$69.0 million (\$2016–17) for the 2012–17 access arrangement period.

Two elements of our draft decision drive most of the difference between the revenue that APTPL was allowed to recover in the 2012–17 access arrangement period, and the level of revenue approved for the 2017–22 access arrangement period: rate of return, and depreciation on assets. We discuss each of these below.

Our draft decision also makes an assessment on forecast demand and on the services covered by APTPL's access arrangement. The key elements of our draft decision in respect to these matters are also discussed below.

Rate of return

Significant investment is required to build a transmission pipeline. The return that APTPL must pay lenders and investors is referred to as the rate of return. Even a small difference in the rate of return can have a big impact on revenues.

Our draft decision sets the allowed rate of return (or 'cost of capital') at 5.75 per cent for 2017–18. We have not accepted APTPPL's proposed 7.72 per cent. The rate of return approved in our draft decision is a significant decrease compared to the rate of return for the 2012-17 access arrangement period of 7.31 per cent.

We consider that APTPPL has sought a rate of return that is higher than necessary given the current investment environment which includes low interest rates compared to previous years. This translates to lower financing costs necessary to attract efficient investment.

We have not accepted the methodology proposed by APTPPL to set its rate of return. Instead, we have used the methodology we developed through extensive consultation during our Better Regulation program in 2013. We consider that our approach provides for a rate of return that better reflects the allowed rate of return objective.

The lower rate of return in this decision will reduce APTPPL's average annual revenue requirement compared to the previous regulatory period.

Depreciation of assets

Depreciation is the amount that APTPPL recovers over time to pay for the cost of an asset. Our decision on depreciation affects the timing of APTPPL's revenue recovery, but not the amount of depreciation in total. Our draft decision does not approve APTPPL's proposed regulatory depreciation allowance of \$18.1 million (\$nominal) for the 2017–22 access arrangement period. Our draft decision on APTPPL's regulatory depreciation allowance is \$19.9 million (\$nominal).

Our draft decision allowance for regulatory depreciation reflects our decision to update APTPPL's calculation of remaining asset lives as at 1 July 2017 and also reflects the effect of our determinations on other components of APTPPL's proposal. These determinations include the opening capital base and the forecast capex.

Demand

Tariff levels depend on estimates of forecast total demand (GJ/day). In simple terms, tariffs are determined by dividing cost by total demand (GJ/day), such that an increase in forecast demand has the effect of reducing tariffs and vice versa.

Based on the information before us, we are satisfied that APTPPL's forecast of an average of 200TJMDQ/day long term equivalent demand on the RBP for the 2017-22 AA period is the best estimate in the circumstances. We note the Queensland Government recently announced the reopening of Swanbank E gas fired power station in 2018. While we have not incorporated Swanbank E in our draft decision, we will consider this further in the context of our final decision.

Services

Underlying our draft decision for the RBP is an increasingly dynamic market for natural gas. While the RBP traditionally provided long haul and mostly long term services from west to east, RBP users are increasingly demanding bidirectional services to also send gas west to the Wallumbilla gas trading hub. APTPPL responded to this by proposing new bidirectional and short term reference services to complement the existing

eastbound long term reference service.

We agree a bidirectional long term firm reference service is appropriate. With respect to short term services however, RBP users are already successfully negotiating terms and conditions with APTPPL. Intervening in the emerging market for short term services may not be in users' best interests. Therefore, our draft decision is to approve only a bidirectional long term firm service and allow RBP short term services to continue to evolve.

We propose to retain the existing postage stamp pricing for the long term firm reference service in this draft decision. This approach minimises upwards pressure on the reference tariff for the long term firm service. An alternative approach would be to establish multiple pricing zones which would advantage users seeking part-haul services but lead to higher prices for full-haul services. We note that full-haul services are expected to remain the predominant type of service demanded by users. Having said that, this decision is finely balanced and we seek further views from interested parties on this matter.

Demand for other types of services is also growing, but demand is uncertain. For that reason our draft decision is to make the following services rebateable services; in-pipe trading, capacity trading, and park and loan services. Part of the revenue earned by APTPPL from these services will be rebated to users.

More information about our consultation process

APTPPL will submit a revised proposal in response to this draft decision by 14 August 2017. Interested parties are invited to make submissions on both our draft decision and APTPPL's revised proposal by 15 September 2017.

More information on APTPPL's proposal, our draft decision and how to make a submission is on our website: www.aer.gov.au.