

# Final Decision

## Roma to Brisbane Pipeline

### Access Arrangement 2022 to 2027

(1 July 2022 to 30 June 2027)

## Attachment 5

### Capital expenditure

May 2022

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## Note

This attachment forms part of the AER's final decision on the access arrangement that will apply to APT Petroleum Pipelines Pty Limited's (APTPPL) Roma to Brisbane Pipeline for the 2022–27 access arrangement period. It should be read with all other parts of the final decision.

The final decision includes the following documents:

Overview

Attachment 3 – Rate of return

Attachment 5 – Capital expenditure

Attachment 6 – Operating expenditure

Attachment 9 – Reference tariff setting

Attachment 12 – Demand

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## 5 Capital expenditure

Capital expenditure (capex) refers to the capital costs and expenditure incurred in the provision of pipeline services.<sup>1</sup> This investment mostly relates to assets with long lives and these costs are recovered over several access arrangement periods.

This attachment outlines our assessment of APTPPL's proposed conforming capex for the Roma to Brisbane Pipeline (RBP) over the 2017–22 access arrangement period (2017–22 period), which forms part of its opening capital base.<sup>2</sup> It also outlines our assessment of forecast capex for the 2022–27 access arrangement period (2022–27 period), which forms part of its projected capital base.<sup>3</sup>

### 5.1 Final decision

#### 5.1.1 Conforming capex for 2016–17 and the 2017–22 period

Our final decision indicates whether we approve the access arrangement proposal as submitted, based on the information that we have available at the time.<sup>4</sup>

We approve APTPPL's total net capex of \$83.6 million (\$2021–22) for the RBP for the 2017–22 period as conforming capex under rule 79(1) of the National Gas Rules (NGR).<sup>5</sup>

We also approve APTPPL's actual capex of \$20.0 million (\$2021–22) for the RBP in the 2016–17 year as conforming capex for the purpose of establishing the opening capital base for the 2017–22 period.<sup>6</sup>

#### 5.1.1 Conforming capex for the 2022–27 period

We accept APTPPL's proposed total net capex for the RBP for the 2022–27 period, with adjustments to reflect its updated capex model to account for modelling errors, real cost escalations and inflation. This results in conforming capex of \$39.0 million (\$2021–22) as conforming capex under rule 79(1) of the NGR, which is \$1.5 million higher than the revised proposal.

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<sup>1</sup> NGR, r. 69.

<sup>2</sup> Ibid, r. 77.

<sup>3</sup> Ibid, r. 78(b).

<sup>4</sup> Ibid, r. 59(2).

<sup>5</sup> We have not assessed 2021–22 amounts as approved capex under this decision. This is because this value is an estimate. We will undertake an assessment of whether 2021–22 is conforming as part of our next access arrangement decision.

<sup>6</sup> NGR, r. 77(2).

**Table 5.1 AER approved capital expenditure, by category, for the RBP over the 2022–27 period (\$ million, 2021–22)**

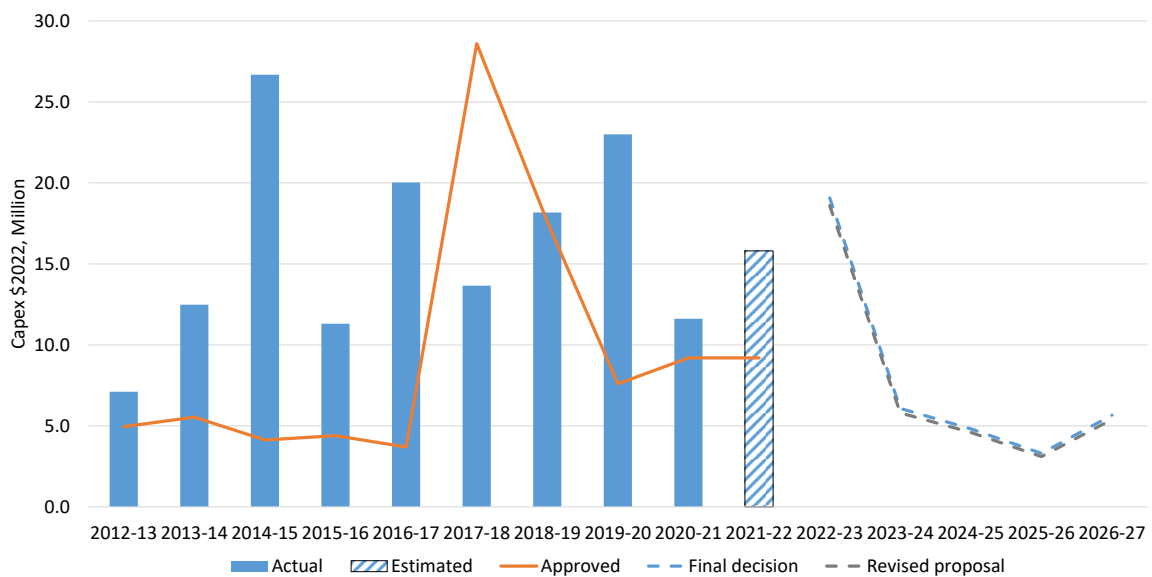
Category	2022–23	2023–24	2024–25	2025–26	2026–27	Total
Expansion	–	–	–	–	–	–
Replacement	14.6	2.3	1.6	1.4	3.1	22.9
Non-network	4.5	3.8	3.3	1.9	2.6	16.0
Gross Total Capex	19.1	6.1	4.8	3.3	5.7	39.0
Contribution	–	–	–	–	–	–
Asset disposals	–	–	–	–	–	–
Net Total capital expenditure	19.1	6.1	4.8	3.3	5.7	39.0

Source: AER analysis; and APTPPL, *Response to information request IR020*, 8 March 2022. Numbers may not add up to totals due to rounding.

## 5.2 APTPPL’s RBP revised proposal

### 5.2.1 Capex over the 2017–22 and 2022–2027 periods

**Figure 5.1 APTPPL’s RBP capex trends**



APTPPL's RBP revised proposal updated its total conforming net capex for the 2017–22 period to \$83.6 million (\$2021–22). This is a \$0.5 million reduction from our draft decision to better reflect its estimated capex for 2021–22.<sup>7</sup>

The revised proposal also forecasts \$37.5 million (\$2021–22) in total net capex for the 2022–27 period. This increase from our draft decision of \$29.2 million (\$2021–22) reflects updates to real cost escalations and additional capex for security of critical infrastructure and information technology (IT).<sup>8</sup>

## 5.3 Assessment approach

We must make two decisions regarding APTPPL's capex for the RBP.

First, we are required to assess past capex and determine whether it is conforming capex that we should add to the opening capital base.<sup>9</sup>

Secondly, we are required to assess APTPPL's forecast of required capex for the RBP for the 2022–27 period to determine whether it is conforming capex. Capex will be 'conforming' if it meets the NGR's new capex criteria.<sup>10</sup>

The following sections set out our approach and the tools and techniques we employed in forming a view on these two issues. We also need to take into account timing issues associated with the lag between actual capex data being available in the last year of the 2017–22 period and the need to forecast the opening capital base for the 2022–27 period. We explain this in the next section.

### 5.3.1 Capex in the 2017–22 period

We reviewed APTPPL's revised proposal and supporting material to assess its proposed capex for the RBP for the 2017–22 period. This included information on APTPPL's reasoning and, where relevant, business cases, responses to information requests and other relevant information.

We used this information to identify whether capex over the 2017–22 period was conforming capex and, in turn, whether that capex should be included in the opening capital base.<sup>11</sup>

Generally, we use the same approach to assess whether both historical and forecast or estimated capex conforms with the new capex criteria. We have set out this approach in more detail in section 5.3.2 below.

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<sup>7</sup> APTPPL, *Roma to Brisbane Pipeline 2022–27 access arrangement, Revised proposal*, January 2022, p. 10. The \$0.5 million does not take into account the conversion to real \$2021-22.

<sup>8</sup> *Ibid*, p. 23.

<sup>9</sup> NGR, r. 77(2)(b).

<sup>10</sup> *Ibid*, r. 79.

<sup>11</sup> *Ibid*, r. 77(2)(b).

We consider the following when determining the opening capital base for the 2022–27 period:

- 2016–17 capex: when we conducted the previous access arrangement review, we did not yet have actual capex for 2016–17. Consequently, we need to adjust for the difference between actual and estimated capex for 2016–17 in the capital base.<sup>12</sup> Since actual capex for 2016–17 is now available, we have assessed whether this capex is conforming capex.
- 2017–21 capex: since we have actual capex data for these years, we have assessed whether this is conforming capex.<sup>13</sup> We have included conforming capex in the opening capital base for 2017–22.<sup>14</sup>
- 2021–22 capex: we do not yet have actual capex for 2021–22 and so must include an estimate in the opening capital base. We have assessed whether APTPPL’s proposed estimate is conforming capex under the NGR. At the next access arrangement review, we will assess whether APTPPL’s actual capex for 2021–22 is conforming capex under the NGR, and adjust for any differences between actual and estimated capex.<sup>15</sup>

### 5.3.2 Capex in the 2022–27 period

We have assessed the key drivers of forecast capex to consider whether APTPPL’s proposed capex for the RBP complies with the new capex criteria.<sup>16</sup> In doing so, we relied on the following information, including:

- the access arrangement submission and access arrangement information, which outline APTPPL’s capex program and the main drivers of those programs
- business cases that detail the expenditure requirements for specific projects
- APTPPL’s regulatory information notice (RIN) template response
- APTPPL’s capex forecast model
- responses to information requests

For each category of capex we considered the scope, timing and cost of the proposed capex in order to form a view on whether it complies with the new capex criteria. We also considered whether cost forecasts were arrived at on a reasonable basis and represent the best forecast possible in the circumstances.<sup>17</sup>

### 5.3.3 Interrelationships

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<sup>12</sup> Ibid, r. 77(2)(a).

<sup>13</sup> Ibid, rr. 77(2)(b) and 79.

<sup>14</sup> Ibid, r. 77(2)(b).

<sup>15</sup> Ibid, rr. 77(2)(a) and 79.

<sup>16</sup> Ibid, r. 79(1)

<sup>17</sup> Ibid, r. 74(2).



In assessing APTPPL's total forecast capex for the RBP, we took into account other components of its access arrangement proposal, including:

- possible trade-offs between capex and operating expenditure (opex)
- any differences between capitalisation policies applied in the 2017–22 and 2022–27 periods
- the growth in the price of labour for opex and capex.

## 5.4 Reasons for final decision

### 5.4.1 Conforming capex for 2016–17 and the 2017–22 period

APTPPL proposed capex for 2016–17 and 2017–22 of \$19.5 million and \$81.9 million, respectively, for the RBP.

Our final decision reflects our draft decision assessment of APTPPL's RBP capex for 2016–22. There has been no material change to this except for a \$0.5 million reduction to 2021–22 to reflect updated actual capex information.

We are satisfied with APTPPL's adjustment. However, we have also updated its 2020–21 actual capex to be consistent with the RIN and updated for actual inflation. This results in \$83.6 million in capex for the 2017–22 period. This is consistent with our roll forward model.

We are satisfied with the use of more updated actual capex information.

### 5.4.2 Conforming capex for the 2022–27 period

APTPPL proposed forecast capex of \$37.5 million for the RBP for the 2022–27 period. This is an increase from its initial proposal of \$29.2 million, which we approved in our draft decision.

We have accepted APTPPL's revised capex forecast but adjusted to account for modelling errors, updated inflation and real cost escalations. This results in a forecast capex of \$39.0 million for the 2022–27 period.

The incremental increase from our draft decision relates to \$5.7 million for security of critical infrastructure (SoCI) and \$4.0 million for additional IT Cloud capex as part of APTPPL's IT transformation program for the RBP that was previously included as opex. The remaining difference is due to updates to inflation and real cost escalation.

Although we have some concerns with APTPPL's proposed IT costs, we are satisfied that APTPPL's overall capex forecast for the RBP is reasonable. We have placed greater weight on our top-down assessment rather than category specific concerns. This is because forecast capex for the 2022–27 period is 54% lower than the current 2017–22 period capex and materially lower than the long term capex trend as shown in Figure 5.1.

### 5.4.2.1 Security of critical infrastructure

We have assessed APTPPL's SoCI capex and consider that not all the capex proposed is required under the *Security of Critical Infrastructure Act 2018* (SoCI Act). APTPPL's forecast SoCI capex is comprised of physical security and cyber security components.

We consider the cyber security requirements have been established as part of the *Security Legislation Amendment (Critical Infrastructure) Act 2021*<sup>18</sup> and we have found these costs to be reasonable. However, we are not satisfied by the physical security aspects which are based on *Security Legislation Amendment (Critical Infrastructure Protection) Act 2022* (the SLACIP Act) in April 2022.<sup>19</sup> The physical security aspects included in APTPPL's revised proposal accounts for \$2.8 million of APTPPL's forecast capex are based on an earlier version of the SLACIP Bill which have now changed.

Our review of APTPPL's supporting information in its revised proposal concluded that APTPPL did not demonstrate that there is a material risk (excluding cyber security) that requires any change to its current risk management practices, as contemplated by the SLACIP Act. We note that despite these concerns at the individual project level, this project forms a part of APTPPL's total capex which we consider is reasonable based on our top-down analysis.

More information on our assessment of cyber security costs is discussed in our opex attachment (Attachment 6).

### 5.4.2.2 Group IT

We have assessed the additional capex related to APTPPL's Enterprise Program Management Office (EPMO) which is a part of APTPPL's IT transformation program.

APTPPL originally proposed this cost as part of its opex forecast. However, APTPPL considers that since this product has been exclusively built for the APA Group and not shared with any other customers, it can be capitalised.<sup>20</sup>

We are satisfied that these costs can be capitalised. However, we note that APTPPL's forecast IT costs are shared across both capex and opex. We have taken capex/opex substitution into account by assessing both opex and capex as total costs.

We note total forecast IT in the current period is \$13.7 million. APTPPL's total forecast IT for the 2022–27 is \$12.0 million. As the total forecast is lower than the current period to provide the same IT functions, we are satisfied by the forecast.

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<sup>18</sup> Australian Government, *Security Legislation Amendment (Critical Infrastructure) Act 2021*, December 2021.

<sup>19</sup> Australian Parliament House, *Security Legislation Amendment (Critical Infrastructure Protection) Bill 2022*, February 2022.

<sup>20</sup> APTPPL, *Roma to Brisbane Pipeline 2022–27, Attachment 10 – Information Technology Information Paper*, January 2022, p. 9.

### 5.4.2.3 Modelling adjustments

We have adjusted APTPPL's forecast capex to reflect more up to date information and modelling errors.

Consistent with our approach for the roll forward model and the weighted average cost of capital we have adopted the March quarter consumer price index. This increases the inflation figure for 2021–22 from 1.5% in APTPPL's capex model to 5.09%.

We have also updated the real cost escalations to take into account Deloitte Access Economics March report.<sup>21</sup> We note APTPPL did not commission its own real cost escalation forecasts and instead used BIS Oxford Economics forecasts<sup>22</sup> produced for Powerlink's 2022–27 revenue proposal. We have also updated the 2021–22 wage price index to be consistent with our forecast approach. We do not consider APTPPL's methodology of using forecasts from previous decisions<sup>23</sup> is reasonable when more up to date information is available.

In response to our information request on IT costs, APTPPL provided an updated capex model to account for some modelling errors.<sup>24</sup> We have acknowledged these adjustments and used the updated model as the basis of our capex forecast.

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<sup>21</sup> Deloitte Access Economics, *Wage Price Index forecasts*, March 2022, p. 36.

<sup>22</sup> BISOE, *Labour cost escalation forecasts to FY2027 Report*, November 2020, p. 5.

<sup>23</sup> APTPPL, *Response to information request AER IR002*, 3 August 2021, p. 5.

<sup>24</sup> APTPPL, *Response to information request AER IR020*, 8 March 2022.

## A. Shortened forms

Shortened form	Extended form
AER	Australian Energy Regulator
APTPL	Australian Petroleum Pipelines Pty Limited
capex	Capital expenditure
EPMO	Enterprise Program Management Office
IT	Information technology
opex	Operating expenditure
RBP	Roma to Brisbane Pipeline
RIN	Regulatory Information Notice
SLACIP Bill	Security Legislation Amendment (Critical Infrastructure Protection) Bill
SoCI	Security of Critical Infrastructure