



APT Petroleum Pipelines Ltd

Capital contributions Precedent in setting the Initial Capital Base of regulated transmission assets

October 2006



Introduction

The Roma to Brisbane Pipeline (RBP) was originally built in 1969, and has been subject to additional compression and looping to increase its capacity since that time.

The RBP was included in Schedule A of the *National Third Party Access Code For Natural Gas Pipeline Systems* (the national Gas Code or the Code), which meant it was to be considered a Covered pipeline for the purposes of the Code.

The *Gas Pipelines Access Act (Queensland) 1998* established a number of derogations from the National Gas Code. In particular, section 58 of the *Act* provides that the Reference Tariffs for several transmission pipelines (notably the Roma to Brisbane pipeline) were to be approved and gazetted by the Queensland Minister for Mines and Energy rather than complying with the access pricing principles – and related regulatory process – in the National Gas Code. This means that the Reference Tariffs are non-reviewable for the term of the relevant derogation. For the RBP, this derogation expires in 2006.

On 31 August 2006, the ACCC issued its draft decision on the Roma to Brisbane pipeline revised access arrangement proposed by APTPPL. This is the first time the ACCC has set the reference tariff for this pipeline since the gas code began in 1998. The draft decision proposes a number of changes to APTPPL's revised access arrangement.

Of note, the ACCC decided the Initial Capital Base (ICB) should be \$250.63m rather than the \$342.6m proposed by APTPPL.

The ACCC's ICB decision is based on its interpretation of the gas code with respect to two key issues:

- DORC: The ACCC proposes to calculate DORC according to the straight line approach.
- Capital contributions: The ACCC found that, in some cases, past expansions of the RBP have been funded by users through 'users' contributions'. The ACCC does not consider that it is reasonable for users to continue to pay for these expansions. Accordingly, in calculating the value of the ICB the ACCC has deducted the value of these 'contributions' from the DORC.

Scope and approach

This document surveys and comments on regulator decisions regarding the treatment of historic capital contributions in setting the Initial Capital Base (ICB) of



regulated gas and electricity transmission assets. The documents reviewed are summarised in the Appendix to this report.

The review was conducted as a desktop review, referencing relevant public record regulatory decision documents. IRS did not conduct interviews of regulatory officers or pipeline staff.

Findings

Of the regulatory decisions reviewed, there was little discussion on the treatment of past capital contributions in the context of setting the Initial Capital Base for tariff setting purposes. The most complete discussion reviewed was contained in a 1997 IPART decision on the AGL distribution network.

IPART noted that capital contributions could equally have been recovered in the form of higher charges in the past, and concluded that where the nature of any additional payments could not be clearly ascertained, it was not appropriate characterise the past payments as capital contributions in setting the Initial Capital Base.

While other decisions, both in gas and electricity, discussed capital contributions in a forward-looking sense in the discussion of future reference tariffs, none of the initial access arrangement decisions discussed capital contributions in the context of setting the Initial Capital base.

In summary, our review did not uncover any instances in which the economic regulator applied capital contributions to reduce the Initial Capital Base of a regulated gas or electricity transmission asset.



Appendix: Decisions reviewed

ACCC decisions

Decision: GasNet 1998 (initial draft decision)

Document reference: Draft Decision 28 May 1998:

<http://www.aer.gov.au/content/item.phtml?itemId=679517&nodeId=337654be5aba07683237abbe3cfb270a&fn=Draft%20decision.zip>

Capital contributions

Section 3.2.2: This draft decision does not discuss capital contributions at all in developing the Initial Capital Base, it only discusses user contributions in the context of new facilities investment:

Decision: GasNet 1998 (initial final decision)

Document Reference: Final Decision 6 October 1998:

[http://www.aer.gov.au/content/item.phtml?itemId=679519&nodeId=512ce2a1f3de9c4c5f1fe9a7f5a81479&fn=Final%20Decision%20\(6%20October%201998\).zip](http://www.aer.gov.au/content/item.phtml?itemId=679519&nodeId=512ce2a1f3de9c4c5f1fe9a7f5a81479&fn=Final%20Decision%20(6%20October%201998).zip)

The Final Decision also discusses capital contributions only in term of new facilities investment. See required change 4.12:

Decision: GasNet 2003

Document link:

<http://www.aer.gov.au/content/item.phtml?itemId=679321&nodeId=57794ebde349b974407f93c695319001&fn=Revised%20Access%20Arrangement%20Information.pdf>

Capital contributions: No discussion¹

Decision: Moomba-Adelaide 2001

Document link: <http://www.aer.gov.au/content/index.phtml/itemId/679550/fromItemId/678759>

Capital contributions: No discussion

Decision: Moomba-Sydney 2003

Document link: <http://www.aer.gov.au/content/index.phtml/itemId/679651/fromItemId/679638>

Capital contributions: No discussion

¹ It would be reasonable to expect that there would be no discussion of capital contributions and the Initial Capital base, as this decision did not relate to an initial Access Arrangement.



Decision: TransGrid 2000

Document link:

[http://www.aer.gov.au/content/item.phtml?itemId=680093&nodeId=eeb60f7e1d2efc71912ad3bd0be7e2d1&fn=NSW%20and%20ACT%20revenue%20cap%20decision%20\(25%20January%202000\).pdf](http://www.aer.gov.au/content/item.phtml?itemId=680093&nodeId=eeb60f7e1d2efc71912ad3bd0be7e2d1&fn=NSW%20and%20ACT%20revenue%20cap%20decision%20(25%20January%202000).pdf)

Capital contributions: No discussion

Decision: PowerLink Queensland November 2002

Document link:

[http://www.aer.gov.au/content/item.phtml?itemId=660927&nodeId=40997ccc447cc5c287698da7616d2ec6&fn=Powerlink%20revenue%20cap%20decision%20\(1%20November%202002\).pdf](http://www.aer.gov.au/content/item.phtml?itemId=660927&nodeId=40997ccc447cc5c287698da7616d2ec6&fn=Powerlink%20revenue%20cap%20decision%20(1%20November%202002).pdf)

Capital contributions: No discussion

Decision: ElectraNet 2002

Document link:

[http://www.aer.gov.au/content/item.phtml?itemId=660987&nodeId=49408c8eddf5ec2d4f2fdcd0fb5772c&fn=Decision%20\(11%20December%202002\).pdf](http://www.aer.gov.au/content/item.phtml?itemId=660987&nodeId=49408c8eddf5ec2d4f2fdcd0fb5772c&fn=Decision%20(11%20December%202002).pdf)

Capital contributions: No discussion

Decision: SP AusNet December 2002

Document link:

[http://www.aer.gov.au/content/item.phtml?itemId=661095&nodeId=277999bc508cfd27aed9b6cfd56067e&fn=Victorian%20transmission%20network%20revenue%20cap%20decision%20\(11%20December%202002\).pdf](http://www.aer.gov.au/content/item.phtml?itemId=661095&nodeId=277999bc508cfd27aed9b6cfd56067e&fn=Victorian%20transmission%20network%20revenue%20cap%20decision%20(11%20December%202002).pdf)

Capital contributions: No discussion

WA ERA decisions

Decision: EPIC 2003/04

Document link: <http://www.era.wa.gov.au/library/DBNGPFD23May2003Web.pdf>

Capital contributions: No discussion

Goldfields Gas Pipeline Final Decision 17 May 2005

Document Link: <http://www.era.wa.gov.au/library/GGP%5FFinal%5FDecision%5F17May2005.pdf>

Capital Contributions

The GGT decision discusses capital contributions in the context of the capacity expansion policy, but does not discuss capital contributions in the context of setting the Initial Capital Base.



NSW IPART decisions

Decision: AGL 1997

Document link: <http://www.iprt.net/pdf/gas97-2.pdf>

Depreciation: Straight line depreciation preferred

Capital contributions: Past capital contributions excluded from consideration (i.e. no reduction in initial capital base)

NSW IPART AGL 1997 final decision page 97

Past user contributions

In the past, several gas customers contributed toward the cost of having natural gas service made available to them. The contributions took a variety of forms, primarily minimum bill arrangements and standing charges. However, these contributions could equally have been collected through higher per unit charges.

Some customers who have made contributions to the network operator have argued that the price for providing service to them should be reduced by the effect of the contribution. That is, the contributing customer's tariff should be reduced by an amount representing the amortisation of the contribution, and by an amount representing a return on the remaining portion of the contribution. The customer making the contribution, it is argued, should be compensated for investing the capital, rather than the pipeline owner's investing the capital on the customer's behalf.

... all other things being equal, if a customer has provided capital, then for the life of that capital, the tariff to that customer must be lower than to another customer by virtue of the capital injection.

In the tariff setting regime in which the customer contributions were made, prices were negotiated directly by AGL and each customer. It is not clear whether or how these contributions were reflected in the price charged by the network operator for service. Since tariffs were previously set in an environment of negotiation, any reflection of these contributions in tariffs cannot be identified. In practice, it appears that previous regulators effectively passed the benefit of capital contributions on to tariff market customers.

The Tribunal considers that an unregulated monopoly Service Provider would be likely to package the revenue stream in the way most palatable to the customer, with the caveat of maintaining the same total revenues. The Tribunal considers that a customer contribution, either through a minimum bill arrangement or lump sum payment, is, in essence, an alternative form of revenue collection. The Tribunal is not seeking to compensate customers for higher prices paid per unit in the past. Nor is it seeking to compensate customers for making additional payments that may have been labelled capital contributions. Therefore, the



Tribunal has not taken capital contributions into account in determining reference tariffs.

It is not possible for the Tribunal to reflect capital contributions in this manner in its Determination of an Access Undertaking. Section 3.3 of the Code requires that:

3.3 The Service Provider must include in the proposed Access Undertaking one or more Reference Tariffs. At least one Reference Tariff must relate to a Service that is likely to be sought by a significant part of the market.

A tariff which reflected a particular customer's contribution would not be available to "a significant part of the market", and therefore could not be classed as a Reference Tariff. As the Tribunal's Determination relates to an Access Undertaking and the related Reference Tariffs, it is not possible to reflect the circumstances of particular customers which have made capital contributions.

Accordingly, the Tribunal believes it would not be appropriate to reflect past customer contributions by reducing the Service Provider's capital base, or by adjusting the Reference Tariff. The Tribunal notes that customers which have made contributions may still negotiate prices. The Tribunal's comments on this matter are not meant to exempt the Service Provider from good faith negotiations in this area, or to constrain the scope for such negotiation.

In future, the tariff treatment of any capital contributions will have to be specified in the contract for service agreed by the user and the Service Provider. Consistent with this approach, the Tribunal expects that user contributions will be reflected in the price for service to the contributing user. Assets funded from user contributions will not be included in the Capital Base for regulatory purposes.

Decision: AGLGN 2005

Document link:

http://www.ipart.nsw.gov.au/gas/documents/RevisedAccessArrangementforAGLGasNetworks-AGLGN-April2005-FinalDecision-PDFversion_000.PDF

Capital contributions: Excluded from roll forward of capital base

Page 71, IPART excludes capital contributions from the calculation of new facilities to be rolled into the capital base in the roll forward calculation.



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