

Alinta EA Pty Ltd
54 083 353 495

*Level 8 IBM Tower
60 City Road
Southbank VIC 3006*

*Tel: +61 3 9685 1000
Fax: +61 3 9685 1001*

12 November 2004

Mr Michael Walsh
Director, Gas Group
Regulatory Affairs Divisions
Australian Competition and Consumer Commission
GPO Box 3648
Sydney NSW 2001

Dear Mr Walsh

Draft regulatory reporting guidelines for gas pipeline service providers

Alinta welcomes the opportunity to comment on the Australian Competition and Consumer Commission's (ACCC's) draft Regulatory Reporting Guidelines for Gas Pipeline Service Providers (the guidelines).

Alinta's interest in the guidelines arises as a result of its ownership of the Queensland Gas Pipeline (QGP) and as owner of a number of gas distribution pipelines throughout Australia. While it is recognised that the ACCC is not the relevant regulator with respect to the latter, Alinta's interest extends from a distribution perspective due to the potential for the guidelines to influence future arrangements for the national regulation of gas distribution businesses by the Australian Energy Regulator (AER).

Alinta has the following concerns with the guidelines:

- The extent to which the guidelines are beyond power;
- The significant costs associated with complying with the guidelines in the absence of a demonstrated need; and
- The need for any guidelines to contain a cost benefit assessment mechanism.

Each of these is considered below.

ACCC's power under the Code

Alinta recognises that the *National Third Party Access Code for Natural Gas Pipeline Systems* (the Code) empowers the ACCC to issue general accounting guidelines with which service providers are obliged to comply. However, Alinta has significant concerns that a number of aspects of the guidelines go beyond the power granted to the ACCC under the Code.

Given the significance of these concerns Alinta has obtained legal advice which we have attached for the Commission's information. The key conclusions of this advice are:

- The scope of the accounting guidelines contemplated by section 4.2 is limited to matters going to ring fencing (that is matters addressed in sections 4.1(c), (d) and (e) of the Code and the collection of sufficient information as would enable the verification by the ACCC of the calculation of existing Reference Tariffs for consistency with an appropriate cost allocation methodology).
- Even if the scope of the guidelines could be broader, encompassing general accounting guidelines, the obligation to comply with the guidelines extends only in so far as they address sections 4.1(c), (d) and (e) and the collection of sufficient information as would enable the verification by the ACCC of the calculation of existing Reference Tariffs for consistency with an appropriate cost allocation methodology.
- There is no power for the requirement for submission and approval of a Regulatory Accounting Manual under section 4.2(b).
- Sections 4, 5 and 6 of the Guidelines deal with reporting requirements and are beyond power.

Significant compliance costs and no demonstrable need

Notwithstanding Alinta's concerns expressed above, and even should the guidelines be within power, Alinta notes that the guidelines place intensive and intrusive obligations on service providers. Concomitant with the extensive nature of the guidelines is a substantial compliance cost. This cost is of significant concern to Alinta particularly given the absence of any demonstrable need for the guidelines, at least in the form as currently drafted.

It would also appear that the ACCC's proposed approach in relation to ring fencing compliance, in particular the Annual Reporting Requirement, disregards the findings of the Productivity Commission in its recent Review of the Gas Access Regime¹:

"Regulators are currently seeking to have their powers under the Gas Access Regime extended so that can obtain information between access arrangement reviews. This extension has the potential to add unnecessarily to service providers' compliance costs."

Not only does the Annual Reporting Requirement require annual submission of a Regulatory Financial Statement, but also annual Statements of Compliance and annual Auditors reports. It is of concern to Alinta that despite the Productivity Commission explicitly identifying the imposition of such obligations as unnecessary the ACCC continues to pursue such an approach.

Alinta notes that historically service providers have complied with their obligations under section 4.12 and 4.13 of the Code through completion of the ACCC's pro forma Ring Fencing Compliance Report. Alinta is not aware that there have been any complaints from users or prospective users regarding compliance with service providers' ring fencing obligations and therefore questions the need for a move to such an extensive, and expensive, compliance regime.

Need for a cost benefit assessment

It is appreciated that despite the absence of any complaints regarding existing ring fencing reporting arrangements the ACCC may nonetheless desire to issue guidelines within the

¹ Productivity Commission Review of the Gas Access Regime – Inquiry Report, June 2004, Finding 7.7

allowed legal scope. To that extent, Alinta is happy to work with the ACCC to develop guidelines consistent with the ACCC's powers under the Code.

To that end, Alinta notes that any revised guidelines would need to be substantially reworked and considered in the light of the attached legal advice. Any revised guidelines should also contain a cost benefit analysis mechanism that would be used to establish whether a service provider is obliged to comply with the guidelines. Implementing such a mechanism would ensure that the costs of the more extensive compliance approach (as compared with the current ring fencing reporting requirements) would only be incurred where the associated benefits dictate.

The need for such a cost benefit assessment is no more clearly demonstrated than in the case of certain transmission pipelines located in Queensland. As the ACCC is aware the *Gas Pipelines Access (Queensland) Act 1998* contains derogations from the Code which apply to certain Queensland transmission pipelines, including the QGP. In the case of the QGP the derogations effectively mean that its Reference Tariffs for Reference Services are set and are to remain in place until the Revisions Commencement Date (that is, the earlier of 2016 or when the capacity of the pipeline is greater than the nominal capacity of the pipeline).

As such, the ACCC's regulatory role does not extend to the verification (or setting for that matter) of tariffs, and therefore, the ACCC has no reason to require the provision of detailed financial information in respect of the QGP. Given this, the expensive, time consuming and intrusive information requirements contained in the guidelines would serve no useful purpose. In such a circumstance it is clear that a cost benefit analysis would reveal that costs of compliance would far outweigh the benefits (if any).

Where any analysis identifies that the costs of compliance outweigh the benefits the service provider would continue reporting its compliance with its ring fencing obligations via the current ACCC pro forma Ring Fencing Compliance Report.

Alinta also notes that in the event the QGP was obliged to comply with the guidelines as currently drafted, not only would the costs exceed the benefits, but the QGP would also have no ability to pass-through the associated compliance costs. While ordinarily it would be expected that the relevant regulator would allow full pass-through of the costs associated with complying with the guidelines, in the case of the QGP there is no existing legislative or contractual provisions that would allow this to occur. This is simply due to the nature of the derogations and the fact that the tariffs cannot be changed until the Revision Commencement Date.

Conclusion

Given the materiality of the issues raised in this letter and the attached legal advice Alinta believes it would be inappropriate for the ACCC to proceed to issue the guidelines in its current form. Accordingly, and given the imminent commencement of the AER, it is Alinta's view that further work on the guidelines should be delayed until the AER assumes its responsibilities and the Ministerial Council on Energy determine its position in response to the Productivity Commission's Review of the Gas access Regime.

To the extent the ACCC intends to proceed with developing the guidelines Alinta would appreciate the opportunity to work with the ACCC to ensure any such guidelines are appropriate and consistent with the powers under the Code.

Should you have any queries in respect of this submission please do not hesitate to contact me on (03) 9685 1061.

Yours sincerely

Stephen Livens

Manager Government and Regulatory Affairs

Freehills

12 November 2004

Our ref Rohan Madders
Phone +61 3 9288 1362
Email rohan.madders@freehills.com
Matter no 20932920
Doc no Melbourne\004570202

Ms Julie Buckland-Bull
Manager
Regulation & Government Relations Group
Alinta Limited
422 Warrigal Road
MOORABBIN VIC 3189

By email

Dear Julie

ACCC draft Regulatory reporting guidelines for gas pipeline service providers

1 Purpose

You have sought our advice in relation to the publication by the Australian Competition and Consumer Commission (**ACCC**) of draft *Regulatory reporting guidelines for gas pipeline service providers* (**Guidelines**) purportedly in reliance upon sections 4.1, 4.2, 4.12 and 4.13 of the *National Third Party Access Code for Natural Gas Pipeline Systems* (**Code**).

In particular, you have asked us to consider what aspects of the Guidelines are beyond the power of the ACCC.

For ease of reference in reading this letter we have set out the relevant sections of the Code in an Appendix.

2 Key conclusions

- (a) The scope of the accounting guidelines contemplated by section 4.2 is limited to matters going to ring fencing (that is matters addressed in sections 4.1(c), (d) and (e) of the Code and the collection of sufficient information as would enable the verification by the ACCC of the calculation of existing Reference Tariffs for consistency with an appropriate cost allocation methodology).
- (b) Even if the scope of the guidelines could be broader, encompassing general accounting guidelines, the obligation to comply with the guidelines extends only in so far as they address sections 4.1(c), (d) and (e) and the collection of sufficient information as would enable the verification by the ACCC of the calculation of existing Reference Tariffs for consistency with an appropriate cost allocation methodology.
- (c) There is no power for the requirement for submission and approval of a Regulatory Accounting Manual under section 4.2(b).

- (d) Sections 4, 5 and 6 of the Guidelines deal with reporting requirements and are beyond power.

3 Issues of interpretation - Scope of guidelines and obligations

3.1 Scope

A governing principle for interpretation of a provision is that it must be read in the context of the whole document. There are other sections of the Code that deal with general regulatory and miscellaneous provisions (section 7) and approval of Access Arrangements (sections 3 and 8), where a power to issue guidelines of general application could have been placed. Accordingly, the placement of sections 4.1 and 4.2 suggests that their operation should be confined to ring fencing. All the other provisions in Part 4 of the Code relate only to ring fencing.

Headings to Parts of the Code form a part of the Law¹ and so are relevant for the interpretation of it. Sections 4.1 and 4.2 are contained within Part 4 of the Code which is headed “Ringfencing Arrangements”. That heading establishes the context in which sections 4.1 and 4.2 should be interpreted. Where it is argued that a heading to a Part is too narrowly stated to encompass the effect of the sections of that Part, the heading will not limit the operation of those sections if they are unambiguous and it would be inappropriate in the context of the Act to confine them by reference to the heading. However, if the language of the sections is doubtful or ambiguous, the meaning which is consistent with the headings is to be adopted. We consider that, in the context of the Code as a whole, the heading to this Part can be used to constrain any broader construction of those sections. Furthermore, to the extent that the meaning of these provisions is ambiguous, the overview to the commencement of section 4 of the Code can be used in the interpretation of that section².

Moreover, if the architects of the Code had intended to confer on the Relevant Regulator a broad power to issue general accounting guidelines (and to compel compliance with such guidelines by Service Providers) then the power should have been conferred expressly and in terms sufficient to clearly define the objects and scope of the power.

Accordingly, as a general proposition, we consider that the requirements of section 4.2 should be read in the overall context of a series of provisions which require a Service Provider to segregate or “ring fence” its business of providing Services using a Covered Pipeline; in particular the requirements that a Service Provider not carry on a Related Business (as defined – essentially producing, purchasing or selling Natural Gas), and that the Service Provider maintain separate accounts for the Services provided by each Covered Pipeline that is the subject of an Access Arrangement.

Viewed in this context, the scope of the general accounting guidelines contemplated by section 4.2 is limited to matters going to:

- compliance with sections 4.1(c), (d) and (e) and that these sections in turn must be read in their context so that the ‘set of accounts’ and cost allocation methodologies must relate to ring fencing (rather than, for example, the approval of an Access Arrangement); and
- the collection of sufficient information as would enable the verification by the Relevant Regulator of the calculation of the Reference Tariffs for Covered Pipelines.

¹ Clause 4 of the Appendix to Schedule 1 of the Gas Pipelines Access Law (**Law**).

² Section 10.5 of the Code.

3.2 Compliance

A second limb of an approach to consider guidelines which might be published under section 4.2 relates to the scope of the compliance obligation.

We consider that even if section 4.2 contemplates the publication of accounting guidelines having a more general application, the *obligation to comply* with those guidelines imposed by section 4.2 is confined to the extent that those guidelines relate to the matters addressed in sections 4.1(c), (d) and (e).

Importantly, although the final paragraph of section 4.2 indicates that the general accounting guidelines may require the accounts to contain sufficient information, and be presented in such a manner as would enable verification of the calculation of Reference Tariffs, the obligation to comply with any such guideline is in our view limited as described above.

Therefore, it is our view that the extent of the obligation imposed on a Service Provider by section 4.2 to comply with such guidelines as may have been published under paragraph (a) (or approved or advised under paragraph (b)) is to comply with such guidelines to the extent that they relate to the matters which are the subject of sections 4.1(c), (d) and (e). The requirement imposed by the last paragraph in section 4.2 must be complied with to the same extent; i.e. accounts may be required to contain sufficient information, and to be presented in such a manner, as to enable verification by the Relevant Regulator that Reference Tariffs for a Covered Pipeline have been calculated in compliance with sections 4.1(c), (d) and (e). In practical terms we think this means that it could be required that the accounts for each Covered Pipeline should be maintained and presented so as to enable the Regulator to verify that existing Reference Tariffs reflect an allocation of costs that has been done consistently with the principles in section 8.1 and otherwise on a fair and reasonable basis (as required by section 4.1(e)).

Any aspects of guidelines which go beyond these limitations are either beyond power or have that status of guidelines only with no accompanying obligation to comply.

4 Issues as to power

The Guidelines have two broad requirements:

- the requirement for approval of a Regulatory Accounting Manual which is to set out the procedures and processes that will instruct the Service Provider's preparation of its Regulatory Financial Statements and which is to:
 - incorporate by reference section 2 and Appendices 4 and 5 of the Guidelines;
 - address the additional matters in section 3 and Appendix 1 of the Guidelines; and
- the requirement for a Service Provider to prepare and submit an Annual Regulatory Report consisting of the Regulatory Financial Statements prepared in accordance with the Manual, a pro-forma Statement of Compliance (approved by the Board and signed by the CEO and a director) and a pro-forma independent Auditor's Report. The ACCC may also require an Agreed-Upon Procedures Report from the auditor where it requires further information.

4.1 Submission and approval of a Regulatory Accounting Manual

In relation to the Manual the ACCC says "it is intended that the Regulatory Accounting Manuals be submitted to the Commission for approval under section 4.2(b) of the Code".

There is no power for the requirement for submission and approval of such a Manual under section 4.2(b). Sections 4.2(a) and 4.2(b) provide for a scheme with the following features:

- compliance with general accounting guidelines or, if there are no such guidelines,

- compliance with guidelines prepared by the Service Provider and approved by the Regulator (the drafting suggests no power in the Relevant Regulator to require the Service Provider to prepare the guidelines for approval), or, if there are no such guidelines
- compliance with Service Provider specific guidelines that apply to the Service Provider as advised by the Relevant Regulator.

4.2 The allowed scope of guidelines

As discussed above, guidelines published by the ACCC must be confined to matters relating to the ‘ring fencing’ requirements of sections 4.1(c), (d) and (e) or, in any event, a Service Provider would only need to comply with guidelines in so far as they went to matters contained within those paragraphs of section 4.1.

The preparation of statements

Section 2 of the Guidelines provides for:

- (1) Preparation of General Purpose Financial Statements (we understand these to be in the nature of consolidated accounts);
- (2) “Disaggregation Statements”, deconsolidating the General Purpose Financial Statements into stand alone financial statements for each Covered Pipeline and in total for all other non-regulated businesses; and
- (3) Special Purpose (Regulatory) Financial Statements for each Covered Pipeline.

Careful examination of the detailed requirements in relation to these three statements would be necessary to ensure that those requirements did not go beyond the allowed scope under section 4.1(c), (d) and (e) of the Code.

We have not conducted such an examination because our primary view is that the requirement to submit a Manual for approval is beyond power. However, we make the following observations.

In some instances, the ACCC seems to have stepped beyond its own statement of objectives. In particular we have some doubts about aspects of Appendix 1. For example, sections 5 (product and service definitions), section 10 (attribution of asset values) and section 11 (depreciation schedule) appear to be directed to the approval of an access arrangement rather than the requirement for separate accounts and the verification of existing Reference Tariffs for consistency with an appropriate cost allocation methodology.

The requirements in Section 2 in relation to an ‘Asset Schedule’, “Related party transactions”, “Provisions” and related ‘regulatory accounting adjustments’ are questionable. The ACCC says it “would expect that such [regulatory accounting adjustments] would principally comprise adjustments to asset values and movements in those values, to bases that would be consistent with the bases of calculation of Reference Tariffs”³. Furthermore the ACCC says “a purpose of these guidelines is to record the financial position and performance of a Covered Pipeline in a way that will assist the Commission in verifying the calculation of Reference Tariffs. It provides a base of information that will help the Commission to assess an Access Arrangement for a Covered Pipeline, but it does not pre-empt the basis on which the Commission may approve any Access Arrangement”⁴.

In making this statement the ACCC seems to rely on the last paragraph of section 4.2, however, as discussed above, we think the proper construction of this paragraph is constrained by its

³ See page 14 of the Guidelines.

⁴ See page 15 of the Guidelines.

context. It allows for information to be sought that assists the Relevant Regulator to verify that existing Reference Tariffs have been calculated in a manner which reflects the requirements of sections 4.1(c), (d) and (e) (in other words that the Reference Tariffs have been calculated based upon an appropriate cost allocation) and does not extend to general information gathering for Access Arrangement approval purposes.

Reporting requirements

Sections 4, 5 and 6 of the Guidelines deal with reporting requirements. In relation to the Annual Regulatory Report, the ACCC relies on sections 4.2(a), 4.12 and 4.13. In relation to an Agreed Upon Procedures Report it is not clear what provision it relies on – presumably section 4.13.

We do not think these provisions support these requirements.

Section 4.2(a) requires a Service Provider to comply with general accounting guidelines. As discussed above, the ***obligation to comply*** with those guidelines imposed by section 4.2 is confined to the extent that those Guidelines relate to the matters addressed in sections 4.1(c), (d) and (e). In other words, in so far as the guidelines address establishing and maintaining separate accounts for each Covered Pipeline, consolidated accounts for the business of the Service Provider and the allocation of shared costs, the Guidelines must be complied with.

We considered the argument that the Guidelines could deal with reporting on the required accounts and the allocation of costs on the basis that without such a scope the Guidelines would ‘have no teeth’, but think this should be rejected. The provisions of clause 4.1 could have easily dealt with the issue if that was intended (for example, clause 4.1(c) could read “establish, maintain and report on a separate set of accounts...”). So too could section 4.2 have dealt with the issue by specifically providing for the guidelines to deal with reporting – such an approach (clarification of scope) was adopted in the last paragraph of section 4.2. In so far as the Guidelines address reporting requirements, section 4.2(a) does not support that requirement and compel compliance.

Section 4.12 requires the Service Provider to establish and maintain internal procedures for compliance with the ring fencing requirements and the Relevant Regulator may require the Service Provider to demonstrate the adequacy of these procedures. Section 4.13 requires the Service Provider to provide a report, at reasonable intervals, describing the measures taken to ensure compliance with the ring fencing requirements and to provide an accurate assessment of the effect of those measures. These sections go to “procedures” and “measures” of compliance and a report on the effectiveness of them. The sections allow a Relevant Regulator to seek comfort about compliance programs and their effect. The sections do not support detailed financial reporting.

It is difficult to see on what basis at all the Code could support the requirements for the Relevant Regulator to meet and discuss issues with an auditor or to direct an auditor to conduct an Agreed Upon Procedures Report.

Sections 4, 5 and 6 of the Guidelines are beyond power.

Peter Rose
Partner

Rohan Madders
Special Counsel

Attachment

APPENDIX

Relevant provisions of the Code

Ring Fencing Minimum Obligations

- 4.1 A person who is a Service Provider in respect of a Covered Pipeline (regardless of whether they are also a Service Provider in respect of a Pipeline that is not Covered) must comply with the following (but in the case of paragraphs (a), (b), (h) and (i), as from the date that is 6 months after the relevant Pipeline became Covered):
- (a) be a legal entity registered under the Corporations Law, a foreign company within the meaning of the Corporations Law that has appointed a local agent in accordance with sections 601CF and 601CG of the Corporations Law, a statutory corporation, a government or an entity established by royal charter;
 - (b) not carry on a Related Business;
 - (c) establish and maintain a separate set of accounts in respect of the Services provided by each Covered Pipeline in respect of which the person is a Service Provider;
 - (d) establish and maintain a separate consolidated set of accounts in respect of the entire business of the Service Provider;
 - (e) allocate any costs that are shared between an activity that is covered by a set of accounts described in section 4.1(c) and any other activity according to a methodology for allocating costs that is consistent with the principles in section 8.1 and is otherwise fair and reasonable;
- 4.2 In complying with sections 4.1(c), (d) and (e) a Service Provider must:
- (a) if the Relevant Regulator has published general accounting guidelines for Service Providers which apply to the accounts being prepared, comply with those guidelines; or
 - (b) if the Relevant Regulator has not published such guidelines, comply with guidelines prepared by the Service Provider and approved by the Relevant Regulator or, if there are no such guidelines, comply with such guidelines (if any) as the Relevant Regulator advises the Service Provider apply to that Service Provider from time to time.

Such guidelines may, amongst other things, require the accounts to contain sufficient information, and to be presented in such a manner, as would enable the verification by the Relevant Regulator of the calculation of the Reference Tariffs for Covered Pipelines.

Compliance Procedures and Compliance Reporting

- 4.12 A Service Provider must establish and maintain appropriate internal procedures to ensure it complies with its obligations under this section 4. The Relevant Regulator may require the Service Provider to demonstrate the adequacy of these procedures upon reasonable notice. However, any statement made or assurance given by the Relevant Regulator concerning the adequacy of the Service Provider's compliance procedures does not affect the Service Provider's obligations under this section 4.
- 4.13 A Service Provider must provide a report to the Relevant Regulator, at reasonable intervals determined by the Relevant Regulator, describing

the measures taken by the Service Provider to ensure compliance with its obligations under this section 4, and providing an accurate assessment of the effect of those measures.