APA Group

APT Petroleum Pipelines Limited

Access Arrangement Revised Proposal Submission

Effective
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Contents

1 Introduction

On 30 April 2012, the AER issued its draft decision on the proposed revisions to the Access Arrangement for the Roma to Brisbane Pipeline, as filed by APT Petroleum Pipelines Pty Ltd (APTPPL) on 11 October 2011.

The AER did not accept the proposed revisions to the AA, requiring a number of amendments to the proposed AA, as outlined below.

This submission addresses the AER's required amendments.

This submission and the proposed amendments to the Access Arrangements are subject to a further round of submissions from industry participants. APTPPL reserves the right to make further submissions on this matter.

1.1 Amendments index

AER required amendment	Reference
Amendment 1.1: Amend the access arrangement submission to: - demonstrate that revenue is allocated between reference and non-reference services (negotiated) in the ratio in which costs are allocated between reference and non-reference services - demonstrate that costs are allocated between reference and non-reference services according to r. 93(2) of the NGR	*Section 9*
Amendment 1.2: Revise the 2012–13 reference tariffs to a capacity reference tariff ($/GJ of MDQ/day) of $0.5149 and a throughput reference tariff ($/GJ) of $0.0344.	*Section 9*
Amendment 2.1: Delete the first paragraph of clause 4.5.2 of the access arrangement proposal and replace with the following: Subject to the approval of the AER under the National Gas Rules, Reference Tariffs may be adjusted after one or more Cost Pass-through Event/s occurs, in which each individual event materially increases or materially decreases the cost of providing the Reference Service. Any such adjustment will take effect from the next 1 July.	*Section 9*
Amendment 2.2: Delete the definition of an insurance cap cost pass through event in clause 4.5.2 of the access arrangement proposal and include the following: An event that would be covered by an insurance policy but for the amount that	*Section 9*

materially exceeds the policy limit, and as a result Service Provider must bear the amount of that excess loss. For the purpose of this Cost Pass-through Event, the relevant policy limit is the greater of the actual limit from time to time and the limit under Service Provider's insurance cover at the time of making this Access Arrangement. This event excludes all costs incurred beyond an insurance cap that are due to Service Provider's negligence, fault or lack of care. This also excludes all liability arising from the Service Provider's unlawful conduct.	
Amendment 2.3: Amend clause 4.5.4 of the access arrangement proposal by deleting the following: If Service Provider proposes adjustments to the Reference Tariffs (other than as a result of a Cost Pass-through Event) and those adjustments have not been approved by the next 1 July, then the Reference Tariffs will be adjusted with effect from that next 1 July, until such time as adjustments to reference tariffs are approved by the AER.	*Section 9*
Amendment 3.1: Amend clause 1.3 of the access arrangement proposal to change the definition of existing capacity as follows: Existing capacity refers to the capacity of the Covered Pipeline as at the commencement of this access arrangement.	*Section 2*
Amendment 3.2: Amend clause 2.2.1 of the access arrangement proposal by inserting the word 'Covered' before the word 'Pipeline'.	*Section 2*
Amendment 4.1: Make all necessary amendments to reflect the AER's draft decision on capacity utilisation forecasts for the access arrangement period as set out in table 4.8.	*Section 3*
Amendment 4.2: Make all necessary amendments to reflect the AER's draft decision on capacity requirement forecasts for the access arrangement period as set out in table 4.9.	*Section 3*
Amendment 4.3: Make all necessary amendments to reflect the AER's draft decision on throughput forecasts for the access arrangement period as set out in table 4.10.	*Section 3*
Amendment 5.1: Make all necessary amendments to reflect the AER's draft decision on standard economic lives and remaining economic lives of assets for the access arrangement period, as set out in table 5.3.	*Section 4.1, Section 4.3*
Amendment 5.2: Make all necessary amendments to reflect the AER's draft decision on regulatory depreciation allowance for the access arrangement period, as set out in table 5.1.	*Section 4.1, Section 4.3*

Amendment 6.1: Make all necessary amendments to reflect the AER's draft decision on corporate income tax allowance for the access arrangement period, as set out in table 6.1.	*Section 7*
Amendment 6.2: Make all necessary amendments to reflect the AER's draft decision on the opening tax asset base as at 1 July 2012, the standard tax asset lives and the remaining tax asset lives for the access arrangement period, as set out in table 6.3.	*Section 4.1, Section 7*
Amendment 7.1: Make all necessary amendments to reflect the AER's draft decision on the rate of return on capital for the access arrangement period, as set out in table 7.1.	*Section 6*
Amendment 8.1: Make all necessary amendments to reflect the AER's draft decision on opening capital base for the access arrangement period, as set out in table 8.1.	*Section 4.3*
Amendment 8.2: Make all necessary amendments to reflect the AER's draft decision on capital expenditure by asset class over the earlier access arrangement period, as set out in table 8.2.	*Section 4*
Amendment 8.3: Make all necessary amendments to reflect the AER's draft decision on projected capital base for the access arrangement period, as set out in table 8.3.	*Section 4.3*
Amendment 8.4: Make all necessary amendments to reflect the AER's draft decision on forecast capex by asset class over the access arrangement period, as set out in table 8.4.	*Section 4.3*
Amendment 9.1: Make all necessary amendments to reflect the AER's draft decision on opex in relation to the RBP8 expansion project, as set out in table 9.5.	*Section 8.1*
Amendment 9.2: Amend Lytton Lateral forecast opex to zero as provided in section 9.4.3, and make all other necessary changes to reflect this amendment.	*Section 8.2*
Amendment 9.3: Make all necessary amendments to reflect the AER's draft decision on corporate cost forecasts, as set out in table 9.1.	*Section 8*
Amendment 9.4: Make all necessary amendments to reflect the AER's draft decision on debt raising cost forecasts, as set out in table 9.6.	*Section 8*
Amendment 10.1:	*Section 10*

Make the queuing requirements for the access arrangement period identical to those in the earlier access arrangement, except for amendments 10.2, 10.3 and 10.4.	
Amendment 10.2: Delete clause 6.1(d) of the access arrangement proposal.	*Section 10*
Amendment 10.3: Amend clause 6.3(a) of the access arrangement proposal to the following: An Existing Capacity Queue will include all relevant Requests which can be satisfied from the spare capacity of the covered pipeline.	*Section 10*
Amendment 10.4: Replace 'queuing policy' and 'queuing', wherever occurring, with 'queuing requirements'.	*Section 10*
Amendment 11.1: Delete the text 'An example of such grounds might be if a reduction in the amount of the Delivery Point MDQ at the initial Delivery Point will not result in a corresponding increase in Service Provider's ability to provide that service to the alternative Delivery Point.' from clause 5.4 of the access arrangement proposal.	*Section 11*
Amendment 11.2: Provide a definition of the term 'reasonable commercial and technical' For the purposes of clause 5.4 'reasonable commercial grounds' and 'reasonable commercial conditions' include allowing APTPPL to deliver the same amount of the Service, receive the same amount of revenue and bear no additional capital or non-capital costs, as applied before the trade. Examples of items that would be reasonable are: (a) APTPPL refusing to agree to a User's request to change its Delivery Point where a reduction in the amount of the Service provided to the original Delivery Point will not result in a corresponding increase in APTPPL's ability to provide Services to the alternative Delivery Point; and (b) APTPPL specifying that, as a condition of its agreement to a change in the Delivery Point or Receipt Point, APTPPL must receive the same amount of revenue, and bear the same or a reduced level of costs that it would have received or borne before the change.	*Section 11*
Amendment 11.3: Amend clause 1.5 of the access arrangement proposal as below: This Access Arrangement will commence on the date on which the approval of the AER takes effect under Rule 62 or Rule 64.	*Section 11*
Amendment 11.4:	*Section 11*

Amend clause 1.6 of the access arrangement proposal as below: Service Provider will submit revisions to this Access Arrangement to the AER on or before 1 July 2016, or four years from the commencement date of this Access Arrangement, whichever is the later (Revisions Submission Date). The revisions to this Access Arrangement will commence on the later of 1 July 2017 and the date on which the approval by the AER of the revisions to the Access Arrangement takes effect under the National Gas Rules (Revisions Commencement Date).	
Amendment A.1: Amend the legislative references in the access arrangement proposal as under: - Petroleum and Gas (Production and Safety) Act 2004 (QLD) - Gas Supply Act 2003 (QLD) - Petroleum Act 1923 (QLD).	*Section 12*
Amendment A.2: Adopt the definition of 'Wilful Misconduct' as follows: Wilful misconduct means any act or omission done or omitted to be done with deliberate or reckless disregard for foreseeable, harmful and avoidable consequences which is not otherwise an act or omission done in good faith.	*Section 12*
Amendment A.3: Delete following definitions from definitions and interpretation schedule 2: - Existing Capacity Notice - Notice of Auction for Developable Capacity - Notice of Auction for Existing Capacity -Open Season Existing Capacity Closing Date	*Section 12*
Amendment A.4: Amend definition of Relevant Tax as follows: 'Relevant Tax' means any royalty, duty, excise, tax, impost, levy, fee or charge (including, but without limitation, any goods and services tax) imposed by the Commonwealth of Australia, any State or Territory of Australia, any local government or statutory authority or any other body (authorised by law to impose such an impost, tax or charge) on or in respect of the Network (or any part of it) or on or in respect of the operation, repair, maintenance, administration or management of the Network (or any part of it) or on or in respect of the provision of any Network Service (other than a levy, fee or charge that arises as a result of APTPPL's breach of a law or failure to pay a tax or charge by the due date for payment).	*Section 12*
Amendment A.5:	*Section 12*

Delete clause 8(b) from the access arrangement proposal.	
Amendment A.6: Maintain the original wording of clause 16 as follows: If Service Provider interrupts or curtails receipts or deliveries of quantities of Gas under clause 15, Service Provider is not liable to the User in respect of interruption or curtailment if the interruption or curtailment:	*Section 12*
Amendment A.7: Amend clause 20 as follows: If the provision of a Transportation Service under the Gas Transportation Agreement causes or would cause an imbalance which exceeds or would exceed the Cumulative Imbalance Limit then Transporter may, in its absolute discretion, cease to provide or suspend the MOS Decrease Service and/or the MOS Increase Service to Shipper.	*Section 12*
Amendment A.8: Delete clause (60(b)).	*Section 12*
Amendment A.9: Amend clauses 87(a), 88, 89(a) and 90 to replace Gross Negligence/Wilful Misconduct with the phrase 'gross negligence or wilful misconduct'.	*Section 12*
Amendment A.10: Amend clause 91 as follows: Nothing in this Access Arrangement limits Service Provider's rights under Queensland STTM from time to time which limit or avoid Service Provider's liability to the User or any other person.	*Section 12*
Amendment A.11: Delete the word 'reasonable' from clause 92.	*Section 12*
Amendment A.12: Amend clause 92(a) to include the words "other acts caused" as per original clause.	*Section 12*
Amendment A.13: Delete the word 'loss or damage' from clause 92(g).	*Section 12*
Amendment A.14: Amend clause 93(c) as follows: the inability of the User or a person supplying Gas at or upstream of the Receipt Points to obtain a supply of Gas for transportation under the Transportation Agreement; or	*Section 12*
Amendment A.15:	*Section 12*

Amend clause 93(d) as follows: the inability of a person, other than the User, consuming the Gas at or downstream of the Delivery Points to take gas due to any event or circumstance within the control of that person.	
Amendment B.1: Delete clause 7.4 of the access arrangement proposal which relates to the inclusion in the extension and expansion requirements of certain fixed principles.	*Section 11*
Amendment F.1: Make all necessary amendments to reflect the AER's draft decision on forecast capacity requirement for the RBP, as set out in table F.5.	*Section 3*
Amendment F.2: Make all necessary amendments to reflect the AER's draft decision on forecast throughput for the RBP, as set out in table F.6.	*Section 3*
Amendment I.1: Make all necessary amendments to reflect the AER's draft decision on labour cost escalators, as set out in table I.3.	*Section 8*
Amendment I.2: Amend the superannuation guarantee escalator to zero as provided in section I.4.4, and make all other necessary changes to reflect this amendment.	*Section 8*

2 Pipeline services

Amendment 3.1: *Amend clause 1.3 of the access arrangement proposal to change the definition of existing capacity as follows:* *Existing capacity refers to the capacity of the Covered Pipeline as at the commencement of this access arrangement.*
Amendment 3.2: *Amend clause 2.2.1 of the access arrangement proposal by inserting the word 'Covered' before the word 'Pipeline'.*

APTPPL accepts these amendments and has reflected them in the Access Arrangement.

3 Demand forecasting

In its draft decision, the AER approved APTPPL's estimate (for 2011–12) and forecasts of RBP capacity over the access arrangement period. The AER considered that the methodology and assumptions APTPPL used to arrive at these forecasts and estimate are reasonable and therefore meet the requirements of Rules 74(1) and 74(2) of the NGR. For the same reason, the AER approved APTPPL's capacity utilisation forecasts and estimate for the RBP from 2011–12 to 2015–16.

However, the AER did not approve APTPPL's capacity utilisation and throughput forecasts for 2016–17. The AER considered that APTPPL's forecast did not take into account a number of factors which suggest that any capacity to be freed on the RBP is likely to be acquired by the market in 2016–17.

The AER considered that APTPPL's capacity utilisation forecast for the RBP for 2016–17 is not arrived on a reasonable basis and does not represent the best forecast possible in the circumstances.

The AER therefore required the following amendments:

Amendment 4.1: *Make all necessary amendments to reflect the AER's draft decision on capacity utilisation forecasts for the access arrangement period as set out in table 4.8.*
Amendment 4.2: *Make all necessary amendments to reflect the AER's draft decision on capacity requirement forecasts for the access arrangement period as set out in table 4.9.*
Amendment 4.3: *Make all necessary amendments to reflect the AER's draft decision on throughput forecasts for the access arrangement period as set out in table 4.10.*
Amendment F.1: *Make all necessary amendments to reflect the AER's draft decision on forecast capacity requirement for the RBP, as set out in table F.5.*
Amendment F.2: *Make all necessary amendments to reflect the AER's draft decision on forecast throughput for the RBP, as set out in table F.6.*

APTPPL addresses these amendments as discussed below.

Confidential information

The Required Amendments appearing in confidential Appendix F mirror those appearing in Chapter 4 of the AER's draft decision, save for additional detail surrounding confidential information relating to particular users.

In its October 2011 submission, APTPPL sought to mask some information from its load forecast in order to conceal commercial information related to those shippers. That information is similarly masked in this submission.

3.1 2016/17 step down

As discussed in section 5.4 of the SKM MMA Report,[1] the 2016/17 step down in contracted capacity and annual volumes is related to the expiry of a contract with a particular shipper. While the majority of this section of the public version of SKM MMA's report is redacted, the analysis hinges on SKM MMA's assessment of the expected future behaviour of that particular user.

In summary, APTPPL and SKM MMA differ in terms of their knowledge of the alternate supply arrangements for that particular shipper, the circumstances surrounding the existing contract, and the probability of that contract being extended. While SKM MMA's analysis is based on the available public information and supposition, APTPPL has more intimate knowledge gained through its ongoing relationship with the user.

[Confidential text redacted]

3.2 Updated forecast

At the time of filing the proposed AA revisions in October 2011, APTPPL reported that the capacity created by the RBP8 expansion was largely contracted, save for 4TJ/day which was identified as being under negotiation.

[1] SKM MMA, Roma to Brisbane Pipeline - Review of demand forecasts, 20 April 2012.

APTPPL advises that the 4TJ/day that was under negotiation has not been contracted and is available to provide pipeline services. At this stage APTPPL forecasts a further 7TJ/day becoming available in 2016/17. This is reflected in Table 3.1 below.

3.3 Capacity utilisation

One aspect of Required Amendment 4.1 is to amend the capacity utilisation from 93%, as shown in Table 4.2 of APTPPL's October 2011 Access Arrangement Information, to 100%. APTPPL largely accepts this component of Required Amendment 4.1, albeit for different reasons.

In its October 2011 submission, APTPPL advised that a particular load, located towards the western end of the pipeline was expected to cease taking service in 2016/17. It is the location of this user's injection and offtake points, both being at the western end of the pipeline, that allow this service to be provided.

The nature of pipeline flow dynamics is such that, if that load were to fall away, there would not be any capacity "freed up" for other users to take supply at other points along the pipeline. APTPPL conducted, and provided to the AER,[2] detailed hydraulic load flow modelling analysis which indicates that the pipeline pressure at the Ellen Grove gate station is largely the same with or without this load on the system. Capacity would only be available if the pipeline pressure were greater at the Ellen Grove gate station with the particular load removed from the load flow modelling

As discussed in the information provided to the AER in response to its queries, it is the particular locations of the supply and load in this case that means the RBP will not be able to sell that capacity to any other shipper.

The capacity of the pipeline therefore falls by the amount of this load reduction.

APTPPL therefore acknowledges that AAI Table 4.2 was incorrect and should have shown the capacity of the pipeline falling to 215 TJ/day in 2016/17, and capacity utilisation at 100% for all years of the proposed AA period. This reduction in capacity is reflected in Table 3.1 below.

The capacity and utilisation forecasts, as updated, are shown below.

[2] Clarification of response to query AER.APTPPL.43, filed 04 January 2012.

Table 3.1: Forecast RBP demand and utilisation

(TJ/day)	2012/13	2013/14	2014/15	2015/16	2016/17
GPG	c-in-c	c-in-c	c-in-c	c-in-c	c-in-c
Non-GPG	c-in-c	c-in-c	c-in-c	c-in-c	c-in-c
Available capacity	**5**	**4**	**4**	**4**	**11**
Total capacity	**232**	**232**	**232**	**232**	**215**
Capacity utilisation	**98%**	**98%**	**98%**	**98%**	**95%**

The resulting throughput forecast, applying the same average load factors as approved by the AER in its draft decision, are as follows:

Table 3.2: Forecast RBP throughput

(TJ)	2012/13	2013/14	2014/15	2015/16	2016/17
GPG	c-in-c	c-in-c	c-in-c	c-in-c	c-in-c
Non-GPG	c-in-c	c-in-c	c-in-c	c-in-c	c-in-c
Total	**68,755**	**69,604**	**69,752**	**70,607**	**63,222**

4 Capital expenditure

The AER has accepted APTPPL's historical and forecast capital expenditure, with two exceptions:

- The AER has disallowed the historical capital expenditure associated with the buyout of the Pipeline Management Agreement (PMA) to bring the operation of the pipeline in house. This matter is discussed below; and
- The AER has not approved some components of forecast non-system (IT) capital expenditure on the grounds that it may be recoverable under another mechanism (STTM MOS cost recovery). This matter is

These matters are discussed below. It should be noted that these matters are not required amendments *per se*, but are the root causes to the following required amendments:

Amendment 8.1: *Make all necessary amendments to reflect the AER's draft decision on opening capital base for the access arrangement period, as set out in table 8.1.*
Amendment 8.2: *Make all necessary amendments to reflect the AER's draft decision on capital expenditure by asset class over the earlier access arrangement period, as set out in table 8.2.*
Amendment 8.3: *Make all necessary amendments to reflect the AER's draft decision on projected capital base for the access arrangement period, as set out in table 8.3.*
Amendment 8.4: *Make all necessary amendments to reflect the AER's draft decision on forecast capex by asset class over the access arrangement period, as set out in table 8.4.*

The PMA buyout affects the opening capital base of the AA period (Amendment 8.1) and the historical capital expenditure (Amendment 8.2), and consequently impacts the projected capital base (Amendment 8.3).

The IT capital expenditure only affects the projected capital base (Amendment 8.3).

4.1 Historical capital expenditure

Amendment 8.2: *Make all necessary amendments to reflect the AER's draft decision on capital expenditure by asset class over the earlier access arrangement period, as set out in table 8.2.*

The AER required two amendments to the proposed AA revisions in this area. The first was to reject the capital expenditure on the PMA contract buyout, which is discussed below.

The second was to remove a small amount of IT capex related to the Queensland Short Term Trading Market, on the grounds that it may be subject to another form of cost recovery.[3]

At the time of filing its original submission in October 2011, the process for recovery of Market Operating System (MOS) costs was unclear. Some clarity has now been added to this process, and APTPPL estimates that it will be seeking recovery of $360,519 related to corporate IT through the MOS cost recovery process. APTPPL has removed this amount from the APTPPL historical IT capex forecast.

4.2 PMA buyout

A feature of the previous AA was that APTPPL contracted the planning, design, capex project management, and operation and maintenance of the pipeline to a third party, Agility Asset Management (Agility). The costs associated with this form of service provision, including a margin paid to Agility, were extensively examined, approved and included in the operating expenditure forecast approved by the ACCC.

In June 2007, APA Group acquired the Agility asset management business from Alinta. The acquisition effectively internalised the construction, management and services functions by acquiring the various asset management contracts as well as some items of property, plant and equipment. In addition, APA Group took over all 270 employees working in the business.

Among other things, the acquisition of the Agility business meant that APTPPL was no longer required to pay a margin on operating and capital expenditure, resulting in a direct reduction in ongoing costs. This reduction in costs is reflected in the operating and capital cost forecasts included in this AA revision submission and will ultimately accrue fully to shippers.

In this AA revision, APTPPL seeks to capitalise a portion of the costs associated with the purchase of the PMA.

It should be noted that, through the PMA acquisition, APTPPL also avoided the costs associated with recruiting and training a qualified workforce to operate the pipeline. APTPPL has not sought to capitalise the costs associated with recruitment of staff and acquisition of intellectual property. APTPPL considers that, while this would be difficult to accurately quantify, on any reasonable approach it would nonetheless ne a substantial amount. APTPPL, by not seeking to include such an

[3] AER draft decision p190. $315,820 has been removed from historical IT capex in the AER's version of the APTPPL revenue model, but not clearly identified in the draft decision.

amount, has embedded a large margin for error to provide assurance to the AER that APTPPL is not seeking to over capitalise the value of the PMA buyout.

In its draft decision, the AER did not accept the capitalisation of the PMA buyout. In reaching its draft decision, the AER received advice from two consultants, RSM Bird Cameron,[4] and Frontier Economics.[5] The AER's concerns appear to be in the following areas:

- Whether the PMA buyout payment is capital in nature;[6]
- Whether it is reasonable to include a value for intangible assets in the regulatory capital base;[7]
- Whether the costs avoided through the purchase of the PMA were efficient in the first instance;[8]
- Whether the PMA buyout is an expenditure for the provision of pipeline services in accordance with Rule 69;[9]
- Whether the PMA buyout is conforming capital expenditure under Rule 79 (in particular whether the value is NPV positive);[10] and
- Given that the points above are made, what value should be calculated (in particular whether the PMA should be calculated having regard to expansion capex).[11]

APTPPL will address each in turn below. In responding to the AER's concerns, APTPPL has sought the assistance of KPMG, whose expert report is included as Attachment 4.1

In addressing the AER's concerns, APTPPL notes that capital expenditure is defined in Rule 69 as follows:

> **capital expenditure** means costs and expenditure of a capital nature incurred to provide, or in providing, pipeline services.

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[4] RSM Bird Cameron Chartered Accountants, *Appendix 1– Review of capital expenditure for the Roma to Brisbane Pipeline access arrangement*, (not dated).

[5] Frontier Economics. *Review of capital expenditure on the Roma to Brisbane Pipeline access arrangement*, A Report Prepared For The Australian Energy Regulator, April 2012.

[6] Draft decision p353.

[7] Draft decision p355.

[8] Draft decision p356.

[9] Draft decision p360.

[10] Draft decision p362.

[11] Draft decision p362 *et seq*.

4.2.1 Expenditure of a capital nature

There appears to be little controversy as to whether the expenditure on the PMA contract buyout is capital in nature.

Chartered Accountants RSM Bird Cameron, who could reasonably be regarded as having experience in this field, clearly agree with KPMG that the expenditure on the PMA contract buyout is capital in nature:[12]

> The goodwill is deemed an intangible asset under AASB 3 which is known as being capital in nature. As a result, the allocation made to the RBP and conclusions drawn in the KPMG report are reasonable.

And:[13]

> As per Scope 1 of this paper, in accordance with the Australian Accounting standards, the nature of the expenditure is clearly capital– this cannot be refuted. Under the National Gas Rules, we feel it also cannot be refuted, as when interpreting relevant definitions the cost associated with the goodwill is directly linked to pipeline assets.

Frontier Economics, while acknowledging that they are not expert in the field of accounting, agree:[14]

> from a first-principles economic perspective, we see no reason why these costs should not be regarded as capital expenditure. They are costs incurred at a particular time in order to provide a stream of future benefits, those benefits being the avoided charges payable for future capital investment and for operations and maintenance services under the PMA.

And from a regulatory perspective:[15]

> In our view, the classification of the PMA buyout premium as capital expenditure is consistent with the Tribunal's decision [in the Jemena mine subsidence case].

KPMG also discusses this issue in Attachment 4.1 and concludes that the PMA contract buyout is clearly an expenditure of a capital nature.

In the end, the AER agreed with APTPPL's submissions and the advice of its consultants that the PMA buyout is an expenditure of a capital nature.[16]

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[12] RSM Bird Cameron p7.
[13] RSM Bird Cameron p16.
[14] Frontier Economics, p5.
[15] Frontier Economics, p7.
[16] AER draft decision p360.

4.2.2 Intangible assets in the regulatory capital base

One of the AER's concerns[17] appeared to be that the PMA buyout has been classified as Goodwill in the APA Group audited financial statements. The AER then expends considerable effort on analysis of whether "goodwill" can be included in the capital base of a regulated service provider.[18] APTPPL submits that:

- first, as a legal matter, the Rules do not differentiate between types of capital expenditure (tangible or intangible) and the Rules do not provide the AER with a relevant discretion to exclude capital expenditure from the capital base on the basis that the capital expenditure is of an intangible nature; and
- second, in any case, the nature of the expenditure in the current case is markedly different from those cases in which regulators have denied inclusion of goodwill in the capital base.

4.2.2.1 Rule requirements

As noted above, capital expenditure is defined as meaning "costs and expenditure of a capital nature incurred to provide, or in providing pipeline services". The Rules do not distinguish between tangible and intangible assets. Therefore, the only question is whether the expenditure is of a capital nature and not whether the asset acquired by virtue of that expenditure is tangible or intangible.

An amendment to the Rules would be required to permit an enquiry into whether the capital expenditure is in respect of a tangible or intangible asset for the purposes of determining whether that expenditure should form part of the capital base. This is in a sense recognised by RSM Bird Cameron in their report where they comment as follows:

> In addition to the lines of inquiry stated above, from our research, we have identified areas where we feel need to be addressed as a result of this case:
>
> (1) Proposed amendments to the National Gas Rules, including to:
>
> - explicitly state that intangible assets, such as goodwill, directly attributable to the pipeline can or cannot be included in the regulatory opening capital base and provide justification as to this determination. If goodwill is to be included, determine some rules around how to amortise this amount over a contract period, notwithstanding the fact that current accounting standards do not require goodwill to be amortised...[19]

[17] AER draft decision p351.
[18] AER draft decision pp351-355.
[19] RSM Bird Cameron p18.

The Rules also do not provide the AER with any relevant discretion to elect not to treat new capital expenditure as conforming capital expenditure on the basis that the expenditure was for goodwill. To the extent it can be demonstrate that the expenditure is of a capital nature, was incurred to provide or in providing pipeline services, and was conforming capital expenditure, the Rules require that amount to be added to the opening capital base. The AER cannot elect to exclude certain expenditure on the basis that there are "particular problems in fitting the notion of goodwill in the building block model"[20] or that the recognition of expenditure on goodwill in a regulatory capital base "does not fit well in the regulatory scheme"[21].

APTPPL submits that the AER would commit a legal error if it rejected the capitalisation of the PMA on the basis that it represents expenditure on goodwill.

4.2.2.2 Previous determinations re inclusion of goodwill

Regulators have previously denied inclusion of goodwill on the grounds that it is not related to the provision of services[22] and that it is not possible to reasonably value the assets:[23]

> it is difficult to determine an 'efficient" value of goodwill as the underlying assets are unidentifiable
>
> even if such payments were justifiable, the process of separating out the portion of those payments which reflect specific factors (such as potential efficiency gains) would be subjective and arbitrary

In this case, the value of the PMA buyout can be determined with a high degree of certainty, as the capital expenditure is directly related to identifiable savings in operating costs.

APTPPL has only sought to capitalise that proportion of the PMA buyout costs that are capable of being accurately quantified and which are supported by the operating cost savings.

The amortisation of the PMA value will ensure that the "self fulfilling circle of increasing asset values and revenue streams" does not occur.

The AER also discussed the point made by the New Zealand Commerce Commission, that[24]

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[20] AER draft decision p355.

[21] AER draft decision p 356.

[22] AER draft decision p353. The question of the expenditure being related to the provision of services is addressed in section 4.2.3.

[23] AER draft decision p352.

[24] AER draft decision p353.

· in markets subject to workable competition suppliers are generally unable to earn an additional rate of return simply as the result of the goodwill included in their payments to acquire assets

APTPPL agrees with this point, in a regulatory context, where the goodwill is related to the acquisition of a network business, such as in the case of the privatisation of the Victorian electricity distribution businesses. However, as discussed in the Bird Cameron report,[25] the goodwill in this case is entirely attributable to operating cost savings associated with the continued operations of the RBP.

4.2.2.3 The potential to capitalise inefficiencies

The AER expressed concern that allowing the PMA buyout to be capitalised would amount to allowing APTPPL to capitalise inefficiencies.[26] In reaching this decision, the AER reasoned that:

> the KPMG report submitted that APA could provide the outsourced services in-house at a cost substantially less than charged by Agility at around the time the ACCC made its decision

APTPPL has reviewed the KPMG report and concludes that the AER has misinterpreted KPMG's comments, which were of a general introductory nature.[27] APTPPL considers that there may be some scope for confusion in the Introduction to the KPMG report. KPMG describes, in general terms, the APA Group experience on the acquisition of the Victorian GasNet business,[28] which preceded the PMA buyout.[29] The acquisition of the GasNet workforce (being located wholly in Victoria) did not enable APTPPL to operate the Roma to Brisbane Pipeline.

Moreover, APTPPL's submission[30] is clear that APTPPL did not have the internal capability to operate the Roma to Brisbane pipeline at the time of the PMA contract buyout:

> the acquisition or enhancement of the in-house pipeline management capability was effectively an acquisition of a new business and represents an asset or advantage which was not present prior to the making of the PMA Termination Payment

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[25] RSM Bird Cameron p7.

[26] AER draft decision p356.

[27] For clarity, this matter is not included in the Terms of Reference and therefore cannot be considered to be part of the opinion of the expert. KPMG has not collected evidence or done work to facilitate an Expert Opinion under the guidelines on this matter.

[28] APA Group media release 18 December 2006, *APA Completes Compulsory Acquisition of GasNet*

[29] APA Group media release, 29 June 2007, *APA finalises negotiations with Alinta*

[30] APTPPL submission October 2011, Attachment 4.3, p4.

APTPPL did not have the internal capability to operate the Roma to Brisbane Pipeline at the time of acquiring the PMA contract. As recently as January 2012, the Australian Competition Tribunal found that fees paid to access the services of a larger, more efficient operator were clearly costs that would be incurred by a prudent service provider, acting efficiently, in accordance with accepted industry practice and that it was "inappropriate for the AER to maintain that the [Network Management Fee] is necessarily an inefficient cost".[31]

As APTPPL did not have the internal capability to operate the Roma to Brisbane pipeline at the time of acquiring the PMA contract, it cannot be said that "demonstrating that services can be performed in house at a lower cost shows that the PMA did not result in an outcome that achieved the lowest sustainable cost of providing services".[32]

APTPPL submits, for the reasoning above, that the acquisition of the PMA contract in no way represents the capitalisation of inefficiencies.

4.2.3 Incurred in providing pipeline services

ACCC findings

The ACCC, in its 2008 decision approving the current Access Arrangement for the Roma to Brisbane Pipeline,[33] approved a Reference Tariff based on a total revenue requirement including the operating costs provided through the PMA under clause 8.36 and 8.37 of the then *National Gas Code*:[34]

> 8.36 Non Capital Costs are the operating, maintenance and other costs incurred in the delivery of the Reference Service. ...
>
> 8.37 A Reference Tariff may provide for the recovery of all Non Capital Costs (or forecast Non Capital Costs, as relevant) except for any such costs that would not be incurred by a prudent Service Provider, acting efficiently, in accordance with accepted and good industry practice, and to achieve the lowest sustainable cost of delivering the Reference Service.

[31] Australian Competition Tribunal, *Application by Envestra Ltd (No 2)* [2012] ACompT 3 at [261]–[262].

[32] AER draft decision p356.

[33] ACCC, *Final Approval - Revised access arrangement by APT Petroleum Pipelines Ltd for the Roma to Brisbane Pipeline*, 28 March 2007

[34] *National Third Party Access Code for Natural Gas Pipeline Systems*, November 1997.

The ACCC undertook considerable analysis of the costs associated with the PMA contract in the context of the 2008-12 Access Arrangement. In the extensive analysis supporting its draft decision,[35] the ACCC commented that:

> In the course of its examination of APTPPL's non-capital costs the ACCC sought and obtained detailed information from the company about its costs. …
>
> The ACCC also held discussions directly with Agility to obtain detailed information on the operating and maintenance costs and all aspects of operation of the RBP. …
>
> The costs to be paid by APTPPL to Agility for operations and maintenance and hence APTPPL's forecast operations and maintenance costs for the period 2006–11 are considered to be consistent with s. 8.37 of the code.

The ACCC's approval of these costs demonstrates its assessment that:

- the costs incurred through the PMA were incurred in the delivery of the Reference Service; and
- the costs incurred through the PMA were such as would be incurred by a prudent Service Provider, acting efficiently, in accordance with accepted and good industry practice, and to achieve the lowest sustainable cost of delivering the Reference Service.

As the costs incurred under the PMA were clearly costs incurred in providing pipeline services, APTPPL submits that by any reasonable, logical interpretation, capital incurred to reduce these costs is equally clearly incurred in providing pipeline services.

AER consultants' findings

AER consultants Bird Cameron analysed the question of whether the PMA buyout was incurred in relation to the provision of pipeline services. Bird Cameron concluded:[36]

> Scope 1 determined that the cost incurred on the goodwill from acquisition of Agility was capital in nature, where the cost was incurred by APTPPL to deliver their pipeline services. In proving that this relates to delivering pipeline services, it is clear that the circumstances under which the costs were incurred relate directly to APTPPL deciding that it was more economically viable to bring the conduct of pipeline services in-house, rather than retain them under an outsourcing arrangement. We therefore conclude that this definition is met. …

[35] ACCC, *Draft decision - Revised access arrangement by APT Petroleum Pipelines Ltd for the Roma to Brisbane Pipeline* 23 August 2006 pp75-76

[36] Bird Cameron, p11, p16.

> Pipeline assets are defined in Rule 69 as capital assets that constitute the pipeline, or are otherwise used by the service provider to provide services. The goodwill asset (payment for termination of PMA) was, and is, used by APTPPL to reduce the cost of services, by bringing the services in-house.

Frontier Economics did not analyse in detail the question of whether the buyout of the PMA contract was incurred in the provision of pipeline services. Rather, Frontier Economics appears to have taken this matter as self-evident, concluding:[37]

> Part 9 of the NGR (Rule 69) simply defines capital expenditure to be "costs and expenditure of a capital nature incurred to provide, or in providing, pipeline services". While no further elaboration is provided, this implies that there needs to be a nexus between the expenditure and the provision of pipelines services.
>
> … However, from a first-principles economic perspective, we see no reason why these costs should not be regarded as capital expenditure. They are costs incurred at a particular time in order to provide a stream of future benefits, those benefits being the avoided charges payable for future capital investment and for operations and maintenance services under the PMA.

Objective of Rule 69

The requirement in Rule 69 that the expenditure must be incurred to provide, or in providing, pipeline services is concerned with ensuring that expenditure which is *not* incurred by the service provider in connection with its business of owning, operating and controlling the pipeline that is the subject of the access arrangement does not form part of the building block approach that ultimately determines reference tariffs and a service provider's revenue requirement for a relevant period. This is necessary as service providers (increasingly so) are not always "standalone" providers just operating one regulated asset. Rather, most modern service providers undertake a range of activities that may not be associated with the pipeline services provided by the pipeline that is the subject of the access arrangement, including for example, asset management services to other owners of pipelines.

In its draft decision, the AER alluded to this objective when rejecting that the PMA buyout constituted capital expenditure for the purposes of Rule 69 on the basis that it was not clear that it was incurred with providing pipeline services.[38] In particular, the AER pointed to a confidential APA Board paper dated 26 February 2007, which indicated that there were many motivations other than the maintenance and operation of pipeline services that would be properly attributable to the PMA buyout.[39]

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[37] Frontier Economics p5.

[38] AER Draft Decision, p358-361.

[39] Ibid, at 349.

As discussed more fully above at 4.1.2, APTPPL has only sought to capitalise that proportion of the PMA buyout costs that are quantifiable and which are supported by the operating cost savings. Furthermore, APTPPL has sought a further opinion from KPMG to (among other things) further consider whether the PMA buyout could be regarded as expenditure "incurred to provide, or in providing, pipeline services" for the purpose of Rule 69. KPMG's opinion has been set out in its report.

Looking at the calculation of the amount of the goodwill payment to be allocated between the relevant pipelines, and the amount that is ultimately allocated to the RBP, it is clear that the expenditure that APTPPL is seeking to capitalise only relates to matters that are directly connected to provide, or in providing, pipeline services on the RBP. These are:

- operating cost savings;
- margins on capital works savings;
- overheads on capital works savings; and
- tax benefit from purchase.[40]

It is clear that no portion of the amount APTPPL is seeking to capitalise in respect of the PMA relates to any of the advantages outlined in the 2007 Board Paper other than allowing APA to optimise the long term management of its key assets in an economic and operational manner. There is no doubt that other advantages may have been achieved as a result of the PMA contract buyout, but no value has been attributed to advantages other than the achievement of operating cost savings, margins on capital works savings, overheads on capital works savings and tax benefits from the purchase. This is entirely appropriate and consistent with the requirements of the Rules.

The KPMG May 2012 report highlights that:

- the regulatory value of the PMA premium asset attributed to the RBP is solely predicated on economic benefits resulting from savings in costs of operating and maintaining the RBP of a kind that are recoverable by a reference tariff; and
- the actual or hypothetical existence of any additional reasons not connected with the provision of pipeline services neither invalidates nor changes the valuation of the PMA premium asset and the expenditure attributable to the RBP.[41]

[40] KPMG, *Pipeline Management Agreement Termination*, October 2011, pp 31 – 32.

[41] KPMG, *APA Group – Regulatory accounting treatment of Pipeline Management Agreement termination payment – Further information,* May 2012, pp 4-5.

Accordingly, APTPPL submits that (consistent with the underlying objective of Rule 69) the amount of the PMA buyout attributed to the RBP only relates to expenditure which was incurred to provide, or in providing, pipeline services.

Causative nexus between PMA buyout and the provision of pipeline services

In APTPPL's view, the correct approach to be taken in determining whether the expenditure incurred in the PMA buyout was "incurred to provide, or in providing, pipeline services" would be to apply a "causation test". More specifically, to establish a causative nexus by asking the question: was the PMA buyout was incurred because of APA's role as a declared transmission system service provider in respect of the RBP? If this question is answered in the affirmative, it would follow that the PMA buyout is capital expenditure incurred to provide, or in providing, pipeline services, in accordance with Rule 69.

When considering the proposed question in light of the points previously raised, it is clear that the PMA buyout was incurred by APTPPL as a consequence of its role as a declared transmission system service provider in respect of the RBP. Absent this role, APTPPL would not have incurred the expenditure associated with the PMA buyout.

Conclusion

In summary,

- the ACCC and the AER's consultants are clear in their findings that the Agility operating cost was incurred in the provision of pipeline services;
- the AER's consultants agree that, by any reasonable, logical interpretation, capital incurred to reduce these costs is equally clearly incurred in providing pipeline services;
- there is a clear causative nexus between the PMA buyout and the provision of pipeline services; and
- therefore the expenditure associated with the PMA buyout is capital expenditure in accordance with Rule 69.

4.2.4 Conforming capital expenditure

Under the construct of the Rules, once an expenditure is considered to be capital in nature, and it is determined that the capital expenditure was made for the purpose of providing pipeline services, the next hurdle is whether the capital expenditure is *conforming capital expenditure*. In Rule 69:

conforming capital expenditure means capital expenditure that complies with the new capital expenditure criteria.

The capital expenditure criteria are located in Rule 79:

79 New capital expenditure criteria

(1) Conforming capital expenditure is capital expenditure that conforms with the following criteria:

(a) the capital expenditure must be such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of providing services;

(b) the capital expenditure must be justifiable on a ground stated in subrule (2).

(2) Capital expenditure is justifiable if:

(a) the overall economic value[42] of the expenditure is positive; or

(b) the present value of the expected incremental revenue to be generated as a result of the expenditure exceeds the present value of the capital expenditure; or

(c) the capital expenditure is necessary:

(i) to maintain and improve the safety of services; or

(ii) to maintain the integrity of services; or

(iii) to comply with a regulatory obligation or requirement; or

(iv) to maintain the service provider's capacity to meet levels of demand for services existing at the time the capital expenditure is incurred (as distinct from projected demand that is dependent on an expansion of pipeline capacity); or

(d) the capital expenditure is an aggregate amount divisible into 2 parts, one referable to incremental services and the other referable to a purpose referred to in paragraph (c), and the former is justifiable under paragraph (b) and the latter under paragraph (c).

[42] "Overall economic value" is discussed below.

Frontier Economics

Frontier Economics concluded that the PMA would be conforming capital expenditure under Rule 79(2)(a):[43]

> In other words, the economic value from the PMA buyout would be positive if the net cost savings from terminating the contract are greater than the buyout premium.

Frontier Economics concludes emphatically that the PMA buyout should be eligible for capitalisation:[44]

> the transaction appears likely to reduce the costs of providing gas to end consumers. If one accepts the proposition that APTPPL can perform certain activities more cheaply in-house than by contracting out those activities, one must also accept that the buyout is likely to promote efficiency compared to the pre-existing arrangements. **Having regard to the National Gas Objective, we consider that it would be unfortunate if service providers were deterred from pursuing cost savings because to do so would reveal that their original processes were sub-optimal and hence that their efforts to reduce costs were not worthy of reward.** (emphasis added)

APTPPL notes that the present value of the future cost savings is indeed higher than the amount it seeks to capitalise. As discussed more fully in the attached supplementary report from KPMG, APTPPL has used the present value of the demonstrated margin savings as a test to ensure the amount capitalised for the buyout of the PMA contract is supported.

Bird Cameron analysis

Bird Cameron did not adequately consider this issue. Rather, it relied upon the AER's preliminary analysis and discussion with the AER indicating the AER did not consider the PMA contract buyout qualified as conforming capital expenditure under Rule 79(2)(a):[45]

> AER provided us with preliminary calculations on the comparison of what the assumed tariff would be when including the goodwill and then compared this to the tariff if the old arrangement was still in place. …
>
> The results of this analysis indicate that the tariff would be higher under the inclusion of the goodwill in the opening capital base, as opposed to the previous arrangement of outsourcing.

[43] Frontier Economics p8

[44] Frontier Economics, p13. Frontier Economics had additional comments on the valuation of the PMA, which are discussed below.

[45] Bird Cameron p1.

> On discussions with AER, it was concluded that, as this analysis resulted in a negative conclusion, the condition under clause (a) … could not be met for the costs incurred on goodwill to be identified as "conforming capital expenditure".

In a teleconference held between the AER, APTPPL and KPMG on 11 May, 2012, the AER agreed that the comparative analysis it provided to Bird Cameron, which it also provided to APTPPL on 3 May 2012, it is clear that the AER only considered the access period 2012-2017.

APTPPL submits that this analysis does not form a sufficient basis for either the AER or Bird Cameron to reach a valid conclusion regarding the whether the overall economic value of the expenditure is positive, because it did not consider the full period over which the PMA buyout will deliver benefits to users of pipeline services. APTPPL submits, as demonstrated in in section 4.2.5, that when the full period is correctly considered, the economic value is clearly positive.

This error of analysis would be tantamount to assessing the net economic benefits of a new pipeline asset, with a life of 80 years, over a single AA period. Just as it would be unreasonable to expect the overall economic value of that pipeline asset to be positive over a five-year AA period, it is unreasonable to expect the overall economic value of any long-lived asset to be positive over a time horizon shorter than its useful life.

Had the AER's analysis covered a longer period (over the remaining life of the PMA buyout) then Bird Cameron would have reached the same conclusion as KPMG, consistent with its conclusion that:[46]

> We reviewed the logic of the KPMG valuation and agreed with the overall approach adopted.

APTPPL submits that, had the AER provided its consultant with a valid analysis as part of its brief, the consultant would have been in a position to provide a valid conclusion on whether the PMA buyout met the requirements of Rule 79(2)(a).

4.2.5 Overall economic value

Rule 79(2)(a) provides that:

> (2) Capital expenditure is justifiable if:
>
> (a) the overall economic value of the expenditure is positive

And Rule 79(3) on Conforming Capital Expenditure provides that:

[46] Bird Cameron p17.

(3) In deciding whether the overall economic value of capital expenditure is positive, consideration is to be given only to economic value directly accruing to the service provider, gas producers, users and end users.

APTPPL has interpreted this provision as having two key implications:

- in calculating the overall economic value, consideration should not be given to benefits accruing to the market as a whole, or the Australian economy in general. That is, there is no broader "market benefits test" associated with this leg of Rule 79.

- "Overall economic value" must be interpreted in net terms. That is,

  - the total of any positive economic value directly accruing to the service provider, gas producers, users and end users

  must be greater than

  - the total of any negative economic value directly accruing to the service provider, gas producers, users and end users

In particular, APTPPL has applied this provision as follows:

Item	Economic Value to Service Provider	Economic Value to users
1. the cost saving delivered to users as a result of the PMA buyout *during the period of the PMA buyout amortisation*		Positive $33.2m[47]
2. the capital outlay on the part of the Service provider	Negative $30.1m[48]	
3. the return on and of capital arising from including the asset in the capital base	Positive $30.1m	
4. present value of the net increase in tariffs accruing to users as a result of the transaction		Negative $30.1m[49]
5. the cost saving delivered to users as a result of the PMA buyout *following the period of the PMA buyout amortisation*		Positive (not valued)
Total	**Neutral**	**Positive**

1. The starting point for the calculation is the value of cost savings passed on to users over the remaining life of the PMA contract (that is, to 2020). This is shown in the red-striped rectangle in the diagram below. This saving is NPV positive to users.

2. This value determines the maximum amount of the PMA buyout that can be demonstrated to be associated with future economic benefits directly attributable to the PMA buyout. Representing the capital outlay to buy out the PMA contract, this is classified as a negative economic value to the Service Provider.

   The AER reports that IPART was concerned that goodwill should not be capitalised because of the "self-fulfilling circle" concern[50] – the value of an expenditure will always be positive so long as tariffs are allowed to

[47] KPMG, *Regulatory accounting treatment of Pipeline Management Agreement termination payment,* October 2011, p 14, p32.

[48] This is the amount that APTPPL seeks to capitalise as a result of the PMA contract buyout. See APTPPL's October 2011 submission, Attachment 4.3.

[49] This is the present value of the increase in tariffs attributable to the return on and of capital arising from including the value of the PMA contract in the Service Provider's regulatory capital base.

[50] AER draft decision p353 referring to IPART, "Goodwill for a regulated business is influenced by the value of future net earnings, which in turn depend on future regulated revenue streams. If regulated revenue streams included returns on and of goodwill, it would initiate a self-fulfilling circle of increasing asset values and revenue streams."

increase to provide a fair return on and of capital to the service provider. Limiting the value of the PMA contract to the demonstrated savings to users addresses this concern.

3. The Service Provider will then earn a return on and of capital associated with the capital investment. As the PMA buyout is being amortised over the remaining term of the contract (that is, to 2020), the return on and of capital is shown as the light blue triangle in the diagram below.

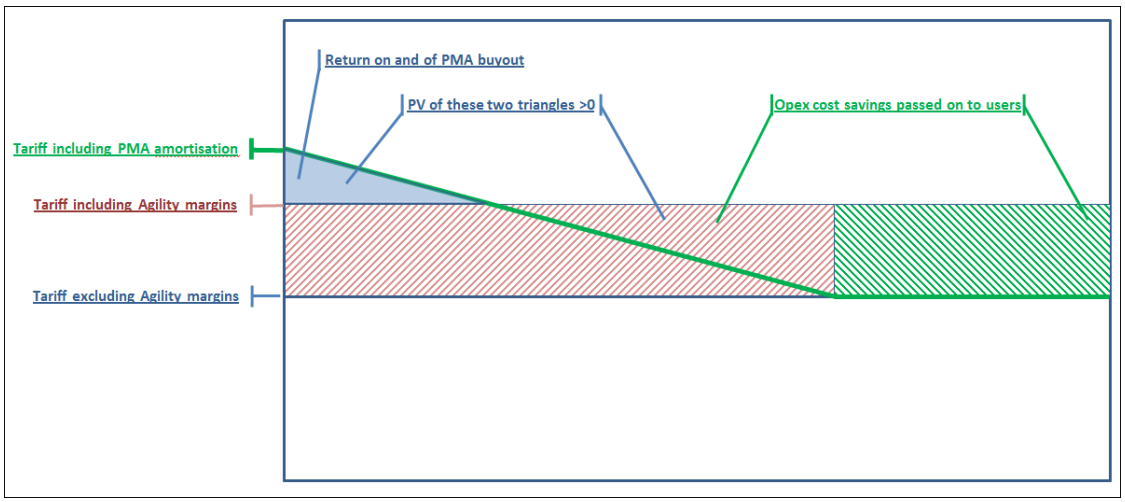
4. APTPPL acknowledges that, in the early years of the PMA contract amortisation, the Reference Tariff is higher than would have been the case had APTPPL continued to operate under the PMA and pay the margins to Agility. This is clearly a negative value to users, and is represented in the diagram below as the portion of the light blue triangle above the red-striped rectangle described above.

   But as the PMA asset decays through amortisation, the tariff falls below the counterfactual "margin-loaded" tariff, and users begin to benefit from the transaction. In the diagram below, this is represented by the red-striped triangle. It is important to understand that the net value described by these two triangles is NPV positive in the favour of users, in accordance with the requirements of Rule 79(2)(a).

   At this stage, once the amortisation of the PMA buyout has been completed, Users would be NPV positive relative to the counterfactual case of retaining the PMA contract and continuing to pay the margins.

5. Once the amortisation of the PMA contract is complete, all operating cost savings accrue directly to users. This is represented in the diagram below by the green-striped rectangle. While not necessary to clear the Rule 79(2)(a) hurdle, this represents an additional benefit to users.

Figure 4.1 Customer benefits from PMA buyout



In summary,

as	the amount capitalised in the regulatory capital base (*Item 1 above*) and the return on and of capital over the amortisation period (*Item 2 above*) is NPV neutral;
and if	the increased tariff resulting from the return on and of capital (*Item 3 above*) is, in PV terms over the life of the asset, less than the value of the operating cost savings passed on to users over the life of the asset (*Item 4 above*);
and if	Operating cost savings continue to be passed on to users after the life of the asset (*Item 5 above*);
then	any savings passed on to users as a result of the PMA buyout will render the overall economic value of capital expenditure positive.

4.2.6 The value of the PMA asset

APTPPL acknowledges that the valuation of the PMA buyout asset is somewhat unusual relative to the valuation of the acquisition of a physical asset.

Where a physical asset is purchased, there is clear documentary evidence of the item purchased and the consideration paid. There is then a presumption (indeed an assertion) that the future economic value of the asset is greater than the

consideration paid. But even with a physical asset, the amount paid may not reflect its value – that still depends on the PV of the future economic benefits.[51]

In the case of an intangible asset, the consideration may be clear, but defining the item purchased is made by reference to the contractual and other rights acquired.[52] In the context of an intangible asset, the presumption that the consideration is less than the future economic benefits is more tenuous. It is therefore necessary to place relatively more reliance on the value of the future economic benefits than the consideration paid.

In its draft decision, the AER appears to be somewhat unclear on the consideration paid to buy out the PMA and the amount that APTPPL seeks to capitalise as representative of the value of the future economic benefits:[53]

> In June 2007, APA acquired the Agility business from Alinta Limited (Alinta) for $206.2 million ($nominal) of which $30.1 million of goodwill was attributed to the RBP.

Indeed of the total consideration paid to buy out the PMA, $35.2 million was allocated to the RBP.[54] However APTPPL seeks to capitalise only $30.1 million into the regulated capital base (as opposed to the statutory financial accounts), representing the value of the future economic benefits supported by the reduction in margin costs as a result of buying out the contract.

As discussed more fully in the KPMG supplementary report, APTPPL's estimation of the value of the PMA buyout is based solely on demonstrable cost savings that accrue to replacing pipeline operations and maintenance services formerly provided by Agility with services provided in house.

Inclusion of expansion capital expenditure

Frontier Economics disagrees with the value attributable to the PMA on the grounds that savings associated with growth related capital expenditure have been included in the valuation. Where KPMG assessed the value of the PMA on an average level of growth related capex, Frontier Economics was of the view that, as expansion capex was infrequent and lumpy, this approach would overstate the value of the PMA.[55]

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[51] This is fundamentally the purpose of asset impairment testing conducted in the course of a financial audit.

[52] In this case, to a contractual right embodying future economic benefits, and transfer of employees and intellectual property.

[53] AER draft decision p176, and p361.

[54] KPMG, *Regulatory accounting treatment of Pipeline Management Agreement termination payment,* October 2011 , p 14, p25.

[55] Frontier Economics p10.

Frontier Economics also expressed concern that the value associated with the PMA buyout was calculate with reference to the savings on growth related capital expenditure when the capacity provided by recent growth capex was being used to provide Negotiated Services.[56]

APTPPL has addressed both these concerns in this response to the AER's draft decision. In response to the AER's decision to include the RBP8 and Lytton Lateral in the covered pipeline for the purposes of calculating the Reference Tariff, APTPPL has allocated all costs and volumes evenly between Reference and Negotiated Services.[57] Under this approach, Reference Service users benefit from the greater economies of scale associated with the expansion. Under this approach, there is no weighting of PMA capital costs in favour of either Reference or Negotiated Services.

As Reference Service users benefit from the increased economies of scale in the calculation of the Reference Tariff, and as users of the Negotiated Services carry a proportionate share of the PMA capital costs, APTPPL submits that it is reasonable to calculate the value of the PMA buyout having regard to expansion capital expenditure.

There remains a question of which measure of growth related capex should be reflected in the valuation of the PMA. In its draft decision[58], the AER expressed concern with the use of average growth related capex, instead focusing on incurred growth related capex (RBP8 and the Lytton Lateral) and market-signalled growth capex (in particular the metro loop).

On balance, APTPPL believes that either these approaches (average vs identified growth capex) are supportable.

4.2.7 Conclusion

In this section, APTPPL has demonstrated that:

- the PMA buyout payment is capital in nature;
- it is reasonable to include a value for intangible assets in the regulatory capital base;
- the costs avoided through the purchase of the PMA were efficient in the first instance;

[56] Frontier Economics p10.
[57] See response to Required Amendment 1.1.
[58] AER draft decision p365.

- the PMA buyout is capital expenditure for the provision of pipeline services in accordance with Rule 69;
- the PMA buyout is conforming capital expenditure under Rule 79; and
- the value of the PMA should be calculated having regard to expansion capex).

4.3 *Forecast capital expenditure*

Amendment 8.4:

Make all necessary amendments to reflect the AER's draft decision on forecast capex by asset class over the access arrangement period, as set out in table 8.4.

Regarding forecast capital expenditure, the AER's approved APTPPL's forecast capital expenditure, but required adjustments to the inflation applicable to the project costs:[59]

> The AER is satisfied that APTPPL's proposed stay in business capex is necessary to maintain the safety, reliability and integrity of the pipeline. The AER also considers that this expenditure is broadly in line with the ACCC approved stay in business capex over the earlier access arrangement period. The AER, however, requires APTPPL to make inflation adjustments to its proposed capex over the access arrangement period.

APTPPL accepts this amendment. These adjustments are of a mechanical nature and are reflected in APTPPL's revenue model.

[59] AER draft decision p186.

5 Capital base

The AER has required a number of amendments to the capital base, many of which are consequential on amendments addressed in other areas of this submission.

5.1 Depreciable lives

Amendment 5.1:

Make all necessary amendments to reflect the AER's draft decision on standard economic lives and remaining economic lives of assets for the access arrangement period, as set out in table 5.3.

The AER requires two amendments to the Access Arrangement in this area:

- To amend the depreciable life of easement from an arbitrarily long life to being non-depreciable;[60]
- To amend the depreciable life of the PMA contract buyout from 8 years to "n/a";[61] and
- Amend the economic life of the RBP8 expansion group of assets from 35 to 46 years, to reflect the weighted average life of the composite group of assets constructed.[62]

APTPPL agrees with the correction to the depreciable life of easements.

Regarding the PMA buyout, the AER notes in the footnote to its Table 5.3 that "The AER did not approve APTPPL's proposed PMA capex. Therefore, there is no expenditure amount to be depreciated for this asset class. For modelling purposes, the AER has changed the remaining and standard economic life inputs for the 'PMA' asset class in APTPPL's revenue model to 'n/a'."

The PMA buyout is discussed in section 4.1 of this submission. Its value has been included in APTPPL's historical capital expenditure, and impacts the regulatory depreciation building block accordingly.

RBP8 weighted average asset life

In its October 2011 proposal, APTPPL grouped the RBP8 project costs into a single project file for ease of tracking costs. When the RBP8 project is completed and commissioned, APTPPL will classify the relevant assets to the correct asset classes.

[60] AER draft decision p111.
[61] AER draft decision p108.
[62] AER draft decision p112.

APTPPL submits that the remaining life of RBP8 pipeline assets should not exceed the remaining life of the upstream N400 mainline. However, APTPPL agrees that the AER has made a reasonable approximation of the proportion of project costs applicable to each asset class, and for the purposes of these revisions to the AA, APTPPL will adopt the 46 year weighted average life for the RBP8 project.

5.2 Regulatory depreciation allowance

Amendment 5.2:

Make all necessary amendments to reflect the AER's draft decision on regulatory depreciation allowance for the access arrangement period, as set out in table 5.1.

This Required Amendment hinges on many other decisions throughout the AA assessment process.

In particular, the AER notes in the footnote to its Table 5.3 that "The AER did not approve APTPPL's proposed PMA capex. Therefore, there is no expenditure amount to be depreciated for this asset class. For modelling purposes, the AER has changed the remaining and standard economic life inputs for the 'PMA' asset class in APTPPL's revenue model to 'n/a'."

The PMA buyout is discussed in section 4.1 of this submission. Its value has been included in APTPPL's historical capital expenditure, and impacts the regulatory depreciation building block accordingly.

The change in the RBP8 weighted average asset life, as discussed above, will also impact the calculation of the regulatory depreciation allowance.

The regulatory depreciation calculation is also impacted by the inflation forecast used to index the capital base.

All these factors have been reflected in the APTPPL revenue model.

5.3 Opening capital base

Amendment 8.1:

Make all necessary amendments to reflect the AER's draft decision on opening capital base for the access arrangement period, as set out in table 8.1.

Required Amendment 8.1 is the outturn result of the application of Required Amendment 8.2, addressed above.

Table 5.1 – Opening capital base for the access arrangement period

$m (Nominal)	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
Opening capital base	296.35	300.22	340.88	345.66	359.98	374.80
Plus capex	2.67	34.38	3.18	11.45	10.50	51.30
Plus speculative capex						
Plus reused redundant assets						
Less depreciation	(6.02)	(6.46)	(6.81)	(7.12)	(7.68)	(8.02)
Plus indexation	7.22	12.73	8.41	9.98	12.00	9.37
Less redundant assets						
Less disposals						
Closing capital base	**300.22**	**340.88**	**345.66**	**359.98**	**374.80**	**427.45**

5.4 *Projected capital base*

Amendment 8.3:

Make all necessary amendments to reflect the AER's draft decision on projected capital base for the access arrangement period, as set out in table 8.3.

The AER's Required Amendment on the projected capital base is a function of the required amendments on the opening capital base, the regulatory depreciation, and the forecast capital expenditure, all discussed above.

Where amendments have been proposed in any of those subject areas, they will be consequentially reflected in the projected capital base.

Table 5.2 – Projected capital base for the access arrangement period

$m (Nominal)	2012/13	2013/14	2014/15	2015/16	2016/17
Opening capital base	427.4	426.6	425.0	420.9	417.0
Plus indexation	11.1	11.1	11.1	10.9	10.8
Plus forecast capex	4.2	4.9	3.7	4.1	3.5
Less forecast depreciation	(16.2)	(17.5)	(18.9)	(18.9)	(18.3)
Less forecast disposals	-	-	-	-	-
Less forecast redundant assets	-	-	-	-	-
Closing capital base	**426.6**	**425.0**	**420.9**	**417.0**	**413.0**

6 Weighted Average Cost of Capital

The AER's draft decision requires the following amendment:

> *Amendment 7.1:*
>
> *Make all necessary amendments to reflect the AER's draft decision on the rate of return on capital for the access arrangement period, as set out in table 7.1.*

APTPPL is unable to directly comply with this Required Amendment.

The footnote to Table 7.1 regarding the Weighted Average Cost of Capital clearly indicates that "The risk free rate, debt risk premium and inflation forecast will be updated closer to the date of the final decision."[63] Until these updates have been implemented, the outturn approved WACC cannot be determined.

APTPPL has some further commentary to add to the AER's assessment of the Weighted Average Cost of Capital, as discussed below.

In summary, APTPPL and the AER agree on:

- the AER's approach to setting the rate of return on the RBP by reference to a nominal 'vanilla' post-tax WACC using the Capital Asset Pricing Model;
- the approach to measuring the debt risk premium;
- the approach to measuring the risk free rate.
- the methodology to estimate expected inflation.
- the gearing ratio;
- the corporate tax rate and the utilisation of imputation credits (Gamma);

APTPPL and the AER disagree on:

- Equity beta;
- Market risk premium;
- The application of the Capital Asset Pricing Model using of a long term average market risk premium with a currently observed risk free rate.

These matters are discussed below.

[63] AER draft decision p121.

6.1 Debt margin

APTPPL agrees with the benchmark used by the AER to estimate the debt risk premium (DRP). Specifically, that the appropriate debt benchmark is Australian corporate bonds with a credit rating of BBB+ and a term to maturity of 10 years.

Furthermore, APTPPL considers that the methodology adopted by the AER in its draft decision for estimating the debt benchmark is correct. That is, the debt benchmark should be measured by reference to an independent market based estimates as opposed to a small sample of bonds. The extrapolated BBB Bloomberg fair value curve estimate is supported by the CEG.[64]

This approach is consistent with recent decisions by the Australian Competition Tribunal that endorse the use of extrapolated BBB Bloomberg fair value curves.[65] We also note that the methodology set out in the draft decision is consistent with the approached adopted in the AER's final decision for Powerlink and Aurora.[66]

6.2 Market risk premium

In its original proposal, APTPPL proposed to adopt a market risk premium (MRP) of 7.0% based on the analysis undertaken by SFG Consulting. However, the AER in its draft decision proposed a MRP of 6.0%.

The AER's MRP estimate was derived with consideration: to historical estimates of excess returns; survey based estimates; market commentary and economic outlook; dividend growth models; and implied volatility analysis.[67] However, the AER states that it places limited weight on the final three of these methods – ie, market commentary and economic outlook, dividend growth model estimates and implied volatility analysis.[68] Further, the AER have predominantly determined the MRP based on historic excess returns "on the assumption that investors base their forward looking expectations on past experience".[69]

It is inconsistent to use a historical value of the MRP in combination with a current estimate of the risk-free rate in the calculation of the return on equity. This inconsistency means that there is no economic or financial theory to support the

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64 CEG estimated a 10-year DRP of 3.92% using an averaging period of 21 November 2011 to 16 December 2011. See Attachment 6.1: CEG, *Estimating the Regulatory Debt Risk Premium for Victorian Gas Businesses*, March 2012, page 60.

65 See *Application by APT Allgas Energy Limited (No 2) [2012] ACompT 5 (11 January 2012).*

66 AER, *Powerlink Transmission determination 2012-13 to 2016-17: Final decision*, April 2012, page 183; and AER, *Final Distribution Determination Aurora Energy Pty Ltd 2012-13 to 2016-17*, April 2012, page, 31.

67 AER Draft Decision pp127-128.

68 AER Draft Decision, pp137,138 and 140,

69 AER Draft Decision, p132.

resulting return on equity figure. Indeed, using a current estimate of the risk-free rate and a historical value of the MRP will in the current investment climate result in a return on equity that is biased downward.

The AER's approach to estimating the cost of equity was evaluated by CEG[70] for the Victorian gas networks. CEG finds evidence that:

- the MRP varies over time, and is negatively correlated to the CGS yield (ie, the MRP increases when the risk free rates are low); and
- the current conditions in the market are one of heightened risk premiums and scarcity premiums for CGS (ie, the risk free rate is below, and the MRP is above, their respective historical long term averages).

The implication of this finding is that the AER's normal application of the CAPM is inappropriate. In other words, adding a MRP measured by reference to a historical excess returns together with a current ('spot') measure of the risk free rate will result in a downwardly biased estimate of the expected return that an asset with an equity beta of 1.0 (ie, the return on the market portfolio). CEG concludes that:[71]

> the AER's methodology is not valid in current market conditions. Specifically, the assumption, implicit in the AER methodology, that the cost of equity has moved one-for-one with CGS yields and is currently at historically low levels is invalid.

This issue becomes a material error during unstable markets conditions such as we are experiencing. The negative relationship between the MRP and the risk free rate was illustrated by CEG in Figure 11 of its report, which is reproduced below. This figure shows the equity risk premium for Australian publically listed entities estimated using the AMP method against the yield on 10 year CGS.

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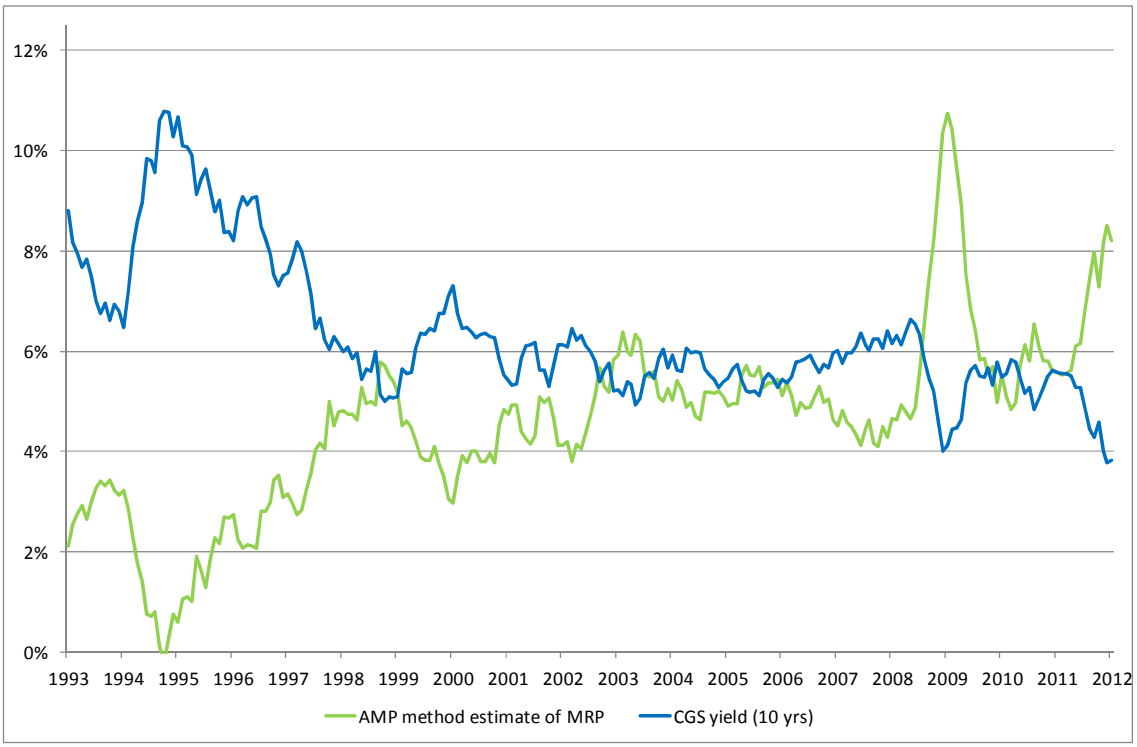
70 See Attachment 6.2: CEG, *Internal consistency of risk free rate and MRP in the CAPM - Prepared for Envestra, SP AusNet, Multinet and APA,* March 2012.

71 CEG, *Internal consistency of risk free rate and MRP in the CAPM - Prepared for Envestra, SP AusNet, Multinet and APA,* March 2012, page vi.

Figure 6.1 Risk premiums on listed equities (AMP method) vs 10 year yields on CGS



Source: RBA, CEG analysis

CEG explains that the negative relationship between the MRP and the yields on CGS can be intuitively understood as follows:[72]

> In periods of high investor risk aversion there is a flight from risky assets to safe assets. This tends to push up the price and push down the yields on safe assets. For this reason, falling risk free rates tend to be associated with rising investor risk premiums (and vice versa).

CEG also supports this inverse relationship by demonstrating that equity returns have remained relatively stable, although the risk free and risk premium components have varied over time:[73]

An important feature of US regulatory decisions is the predominate use of dividend growth models (DGM). An important aspect of DGM models is that they are purely forward looking estimates (ie, no component of the model is computed using

[72] CEG, *Internal consistency of risk free rate and MRP in the CAPM - Prepared for Envestra, SP AusNet, Multinet and APA,* March 2012, page iii.

[73] CEG, *Internal consistency of risk free rate and MRP in the CAPM - Prepared for Envestra, SP AusNet, Multinet and APA,* March 2012, Figure 13, page 38.

historical data). The above figure shows that equity returns have remained relatively constant over time and do not exhibit the variation seen in the underlying ten year risk free rate. In contrast, the AER's approach requires that equity returns on the market is locked as a fixed premium above the risk free rate.

APTPPL finds this evidence compelling and submits that the AER's approach to estimating the cost of equity is not sustainable. It follows that the AER must either:

- estimate the prevailing forward looking CAPM, ie, applying a spot measure of the risk free rate together with forward looking indicators of the MRP; or
- estimate a long term CAPM, ie, applying a long term average risk free rate and long term average MRP.

APTPPL submits that the first approach, the prevailing forward looking CAPM, better meets the requirements of Rule 87(1) that the return on capital is to be commensurate with *prevailing* conditions in the market for funds.

Further, APA GasNet undertook substantive work to derive an appropriate estimate of the MRP in its access arrangement proposal, resulting in a MRP value of 8.5%.[74] APTPPL considers that this value of the MRP provides the best current estimate of the MRP and has therefore adopted an MRP value of 8.5%.

6.3 Beta

APTPPL proposed an equity beta estimate of 1.0 in its original submission. However, the AER's current equity beta estimate (based on 60% gearing) for gas transmission and distribution businesses is 0.8, which is derived from the AER's 2009 Review of WACC Parameter Estimates.

In adopting an equity beta of 0.8, the AER has disregarded substantial evidence that the benchmark equity is best approximated by at least 1.0. [75] Notwithstanding the AER's proposed equity beta of 0.8, APTPPL continues to advocate an equity beta of at least 1.0.

6.4 WACC estimate

Based on the parameter estimates set out in this chapter, the resulting indicative estimate of the nominal post-tax WACC to apply to the RBP is summarised in *Table 6.1*.

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74 APA GasNet Australia, *Access Arrangement Submission 1 January 2013 to 31 December 2017*, March 2012, pages 139-147

75 CEG, WACC Estimation: A report for Envestra, March 2011.

Table 6.1: Indicative WACC estimate

Parameter	Estimate
Risk free rate	3.99%*
Forecast inflation	2.60%
Real risk free rate	1.57%*
Gearing (debt to value)	60%
Debt risk margin	4.03%*
Nominal pre-tax cost of debt	**8.02%**
Market risk premium	8.5%
Equity beta	1.0
Nominal post-tax cost of equity	**12.49%**
Gamma	0.25
Nominal Vanilla WACC	**9.81%**

* APTPPL accepts that these parameters will be updated with market-observed values prior to the Final Decision.

7 Taxation

Amendment 6.1: *Make all necessary amendments to reflect the AER's draft decision on corporate income tax allowance for the access arrangement period, as set out in table 6.1.*
Amendment 6.2: *Make all necessary amendments to reflect the AER's draft decision on the opening tax asset base as at 1 July 2012, the standard tax asset lives and the remaining tax asset lives for the access arrangement period, as set out in table 6.3.*

APTPPL is not able to directly comply with Amendment 6.1.

The corporate tax allowance is calculated by APTPPL's revenue model, and is a consequence of the other decisions made in assessing the Access Arrangement, Of note, the tax allowance will vary depending on the final WACC parameters measured at the time of the defined market observation period.

APTPPL has calculated the tax allowance using APTPPL's revenue model, reflecting the amendments made throughout this submission. As discussed in section 4.1, APTPPL has provided further information to allow the AER to capitalise the PMA contract buyout. APTPPL also noted that, as the amended RBP8 useful life is longer than the standard tax asset life, no change is required to the RBP8 standard tax life.

Table 7.1 – Tax asset base roll forward for the access arrangement period

$m (nominal)	2012/13	2013/14	2014/15	2015/16	2011/12
Opening TAB	134.4	121.0	113.4	103.7	94.6
Capital expenditure	4.1	4.7	3.6	3.9	3.4
Tax depreciation	17.5	12.3	13.2	13.0	12.4
Total	**121.0**	**113.4**	**103.7**	**94.6**	**85.6**

Table 7.2 – Tax allowance for the access arrangement period

$m (nominal)	2012/13	2013/14	2014/15	2015/16	2016/17
Total	2.60	4.48	4.61	4.65	4.59

8 Operating expenditure

The AER required a number of amendments to operating costs, which are discussed below.

8.1 RBP8 operating costs

Amendment 9.1:

Make all necessary amendments to reflect the AER's draft decision on opex in relation to the RBP8 expansion project, as set out in table 9.5.

APTPPL addresses this required amendment by providing the detailed information required by the AER as discussed in the text surrounding this required amendment.

In its draft decision, the AER did not accept the level of operating costs associated with the RBP8 expansion. In estimating its draft approved level of operating costs it took the advice of Wilson Cook[76] and Ross Calvert Consulting[77] to apply 75% of the average per km cost of operating the pipeline to the RBP8 project.[78]

However, the AER commented that this may not adequately reflect the cost of operating the compressor included as part of the RBP8 expansion project:[79]

> The AER notes that because its RBP8 expansion project opex forecast is based on average pipeline opex it may understate costs associated with operation of the new compressor. As advised by Wilson Cook, inclusion of a compressor within the expansion project would be expected to add a further margin to additional opex forecast costs. However, in the absence of sufficient information from APTPPL the AER is unable to specify the appropriate additional opex margin.

In December 2011, APTPPL provided a spreadsheet detailing the opex calculations used to support its October 2011 filing. However, that particular spreadsheet did not include the page detailing the buildup of the operating costs associated with the compressor constructed as part of the RBP8 expansion. APTPPL has provided this information to the AER as an attachment to this submission. As this document

[76] Wilson Cook, *Review Of Expenditure Forecasts For Roma-Brisbane Gas Pipeline Access Arrangement For FYS 2013-2017,* 25 January 2012.

[77] Ross Calvert Consulting, *GasNet – Assessment of proposed operating expenditure scope and workload changes*, September 2007, p. 4.

[78] AER draft decision p212.

[79] AER draft decision p213.

contains commercial information relating to APTPPL's compressor operational strategies, it has been filed confidentially.

8.2 Lytton Lateral operating costs

Amendment 9.2:

Amend Lytton Lateral forecast opex to zero as provided in section 9.4.3, and make all other necessary changes to reflect this amendment.

APTPPL has confirmed that the Lytton lateral came into service in June 2010, and therefore it would be reasonable to expect that the related operating costs were included in the base year 2011/12 costs.

While APTPPL's October 2011 submission did not indicate that the Lytton lateral opex costs were a step change,[80] APTPPL has ascertained that the operating costs associated with the Lytton lateral were incorrectly included in step change costs in the operating cost modelling used to support the AA forecast.

APTPPL accepts this Required Amendment and has removed the Lytton lateral operating cost step change from the calculation of forecast opex.

8.3 Carbon costs

The *Clean Energy Act 2011* received royal assent on 18 November 2011. The *Act* introduces a carbon trading scheme in Australia designed to impose a price on carbon emissions from 1 July 2012. The first three years of the carbon pricing scheme has a fixed price path; after that the scheme moves to a floating price period. Under the floating price period the price path forecast by the Australian Treasury is the price path required to meet the emission reduction target of 5% by 2020 on 2000 emission levels.

APTPPL expects to incur considerable costs in the current access arrangement period associated with purchasing permits to be surrendered to the Clean Energy Regulator under the *Clean Energy Act 2011*. These costs arise in relation to direct emissions, from fuel gas and fugitive emissions, and also from indirect costs such as increased electricity prices and administration costs for managing compliance and procuring permits.

[80] For example, Table 8.8 of the October 2011 submission indicates only the operating costs associated with RBP8 as a step change.

APTPPL has calculated its liability on the basis of the methodology set out in the *National Greenhouse and Energy Reporting Act 2007*, based on expected sales volumes and fugitive emissions.

For the first three years of the scheme APTPPL has applied the fixed carbon price set out in the *Clean Energy Act*, and after that date has adopted a carbon price consistent with Australian Treasury modelling. The Deputy Prime Minister and Treasurer and the Minister for Climate Change and Energy Efficiency released the Strong growth low pollution: modelling a carbon price (SGLP) report on 10 July 2011. An update to the SGLP report was released on 21 September 2011. APTPPL has used the updated price path from 21 September 2011.

Forecast direct carbon costs associated with this step change are set out in below.

Table 8.1: Forecast RBP carbon costs

($ 2011/12)	2012/13	2013/14	2014/15	2015/16	2016/17
Throughput (TJ)	**68,755**	**69,604**	**69,752**	**70,607**	**63,222**
Fuel gas emissions (tCO_2e)	26,169	26,492	26,548	26,874	24,063
Fugitive emissions (tCO_2e)	4,901	4,901	4,901	4,901	4,901
Total liable emissions (tCO_2e)	**31,070**	**31,393**	**31,449**	**31,774**	**28,964**
Permit price	$23.00	$23.00	$23.00	$24.60	$25.60
Total RBP carbon cost	**$714,601**	**$722,039**	**$723,326**	**$781,649**	**$741,473**

As discussed in section 9, APTPPL proposes a mechanical calculation to adjust for the difference between forecast and actual carbon costs as part of the tariff variation mechanism.

APTPPL understands that the revised Access Arrangement and associated tariffs will commence on 01 September 2012, leaving ten months of the first year of the regulatory period available to recover the fiscal 2012/13 carbon costs. As these carbon costs will have been accruing since 01July 2012, APTPPL has included 12/10 of the forecast 2012/13 carbon costs in the operating cost modelling to ensure they can be recovered over the remaining ten months of the 2012/13 fiscal year.

8.4 Debt raising costs

Amendment 9.4: *Make all necessary amendments to reflect the AER's draft decision on debt raising cost forecasts, as set out in table 9.6.*

APTPPL accepts this Required Amendment and has made the necessary change in APTPPL's revenue model.

8.5 Labour cost escalators

Amendment I.1: *Make all necessary amendments to reflect the AER's draft decision on labour cost escalators, as set out in table I.3.*
Amendment I.2: *Amend the superannuation guarantee escalator to zero as provided in section I.4.4, and make all other necessary changes to reflect this amendment.*

The AER did not accept APTPPL's proposed labour escalators in its draft decision and required APTPPL to adopt escalators prepared on a different basis by its own consultant, Deloitte Access Economics, for the following reasons:

- APTPPL's proposed escalators are premised on inappropriate labour cost indices and industries (use of AWOTE or LPI, and inclusion of waste services in the EGW measure);
- Productivity adjustments to labour cost forecasts, as proposed by APTPPL, may distort forecast labour cost outcomes and may double-count economies of scale; and
- The Australian Government's superannuation guarantee rate changes are not expected to increase APTPPL's total labour costs (inclusive of superannuation payments) as proposed by APTPPL.

APTPPL discusses each of these reasons below.

8.5.1 Appropriate labour cost indices

APTPPL proposed to use productivity-adjusted EGW AWOTE to escalate internal labour other than corporate labour. Corporate labour was escalated by a General

labour escalator, which was comprised of professional (90%) and administrative (10%) indices. Contract labour (construction) was escalated by a contractor escalator.

The AER's draft decision did not accept APTPPL's use of an EGW labour escalator for its non-corporate internal labour, as it considered using this index involved adjustment of the ABS EGWWS labour force series that introduced scope for error. The AER instead required use of the unadjusted ABS EGWWS labour force series to derive escalators for this labour category.

While APTPPL remains of the view that skills and price movements associated with the waste services sector are not well aligned with skills and price movements associated with the electricity, gas and water sectors, the adjustment to the escalator to remove waste services represents an additional adjustment to published values and increases the risk of error. APTPPL has therefore applied BIS Shrapnel escalators prepared on the basis of the ABS EGWWS labour force series without adjustment.

The AER further considered that the separation of the internal RBP labour force into EGW and General labour was not appropriate, as the EGWWS labour force series captured wage movements for all professions associated with the sector. APTPPL accepts this change, and has applied the EGWWS escalator to all external labour.

The AER's draft decision requires APTPPL to use non-productivity adjusted LPI measures for EGWWS and Construction sector to derive real price escalators.

APTPPL has not adopted this approach, and has instead retained use of productivity-adjusted AWOTE to derive its labour escalator for internal and contractor labour. LPI is a measure of underlying wage inflation in the economy or in a specific industry, as the LPI only measures changes in the price of labour, or wage rates, for specific occupations or job classifications, which are then aggregated into a measure of the collective variations in wage rates made to the current occupants of the same set of specific jobs.

The LPI, therefore, reflects pure price changes, but does not measure variations in the quality or quantity of work performed, that is, it holds labour composition effects as fixed. The LPI also does not reliably measure the changes in total labour costs which a particular enterprise or organisation incurs, because the LPI does not reflect the changes in the skill levels of employees within an enterprise or industry. As skills are acquired, employees will be promoted to a higher grade or job classification, and with this promotion will move onto a higher base pay. So the change in the cost of labour over, say a year, includes increases in the base pay rates (which the LPI measures) and the higher average base pay level. The AWOTE captures both these elements, while the LPI only captures the first element. Basically, promoting employees to a higher occupation does not necessarily show up in the LPI, but the employer's total wages bill (and average unit labour costs) is higher, is AWOTE.

AWOTE is a better measure of the change in overall costs per employee, because it takes into account movements of employees to higher grades, changes in compositional effects from entry/exits of higher skilled/lower skilled (ie higher paid/lower paid) workers in an enterprise or industry, and also the payments above base rates of pay, such as bonuses, incentives, penalty rates and other allowances that are a normal part of an employee's earnings over the quarter or year. With regard to the latter, many enterprises in the utilities (and other industry) sectors(s) regularly include bonuses or incentive payments which are linked to a range of objectives, such as up skilling, additional training, productivity targets, safety targets, etc. These 'extra' payments — or changes in the quantum of payments — are not included in changes in the LPI, but can make a material difference to an enterprise's overall labour costs.

Further discussion as to the appropriate application of these two labour measures can be found in the BIS Shrapnel real labour cost escalation report and the report prepared for Envestra Pty Ltd by Professor Borland[81], both of these accompany this submission.

Rule 91(1) provides that "Operating expenditure must be such as would be incurred by a prudent service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of delivering pipeline services."

APTPPL considers that use of the AWOTE measure best reflects efficient labour costs incurred and expected to be incurred in relation to the RBP, and is therefore the most appropriate measure to use in this revenue proposal;

8.5.2 Productivity adjustments

APTPPL has adopted productivity-adjusted AWOTE values as it considers that these best reflect expected actual labour costs over the period. The reasons for this approach are discussed further in the BIS Shrapnel real cost escalation report that accompanies this submission (Attachment 9.1).

APTPPL notes that Rule 91(1) is a limited discretion Rule.

APTPPL agrees with the AER's analysis that it is not appropriate to adjust the LPI measure for productivity. It remains appropriate, however to adjust the AWOTE measure for productivity, as discussed in the report prepared by Professor Borland:

> The AWOTE measure remains, in my opinion, the best series to be used as the basis for future labour costs.

[81] Professor Borland 2012, Labour Cost Escalation: Choosing between AWOTE and LPI: Report for Envestra Ltd, March.

> First, theory and empirical evidence support this opinion. Take the rate of change in AWOTE and subtracting the rate of change in labour productivity gives a measure of labour costs that appropriately adjusts for the effects of labour productivity in a firm's costs.[82]

While APTPPL considers that its proposal to use productivity-adjusted AWOTE real cost escalators is consistent with the National Gas Rules and should be approved by the AER, APTPPL has also included non-productivity adjusted LPI values in the attached BIS Shrapnel report. In the event that the AER does not approve APTPPL's proposed use of productivity-adjusted AWOTE real cost escalators, it considers that the AER should use the non-productivity adjusted LPI values as set out in the BIS Shrapnel report. APA considers that these values have been derived on a reasonable basis and represent the next best option to using productivity-adjusted AWOTE real cost escalators.

8.5.3 Australian Government's superannuation guarantee rate changes

APTPPL is a firm believer in the importance of superannuation to an ageing workforce. APTPPL expects that the Australian Government's decision to increase the superannuation guarantee rate will change APTPPL's labour costs during the access arrangement period and therefore is appropriately included in its forecast operating expenditure allowance.

The AER cites an expectation by the Australian Government that the increase in the superannuation guarantee will be offset by a reduction in an employee's take home wages as the basis for not accepting APTPPL's superannuation guarantee escalator. APTPPL notes this expectation, but considers that it is not based on any grounding in fact relevant to APTPPL's circumstances. The AER have provided no evidence to demonstrate that the increase in the superannuation guarantee will not increase APTPPL's costs, and therefore that APTPPL's inclusion of these costs in its operating expenditure forecast is inconsistent with the Rules (the requirement under limited discretion rules).

APTPPL considers that the AER's exclusion of costs associated with this new regulatory obligation would be inconsistent with the Revenue and Pricing Principles which provide for a service provider to be given reasonable opportunity to recover at least the efficient costs the service provider incurs in complying with a regulatory obligation or payment.

APTPPL has therefore retained its proposed superannuation guarantee escalator in its revision proposal.

The real cost escalators used in developing APTPPL's proposed program operating and capital expenditures are set out in Table 8.2.

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[82] Professor Borland 2012, Labour Cost Escalation: Choosing between AWOTE and LPI: Report for Envestra Ltd, March, p 18

Table 8.2 – Project cost escalators 2013-17 (annual movement, %)

Type	2012/13	2013/14	2014/15	2015/16	2016/17
EGWWS Labour	2.0%	2.2%	1.9%	1.2%	8.0%

8.6 Corporate costs

Amendment 9.3:

Make all necessary amendments to reflect the AER's draft decision on corporate cost forecasts, as set out in table 9.1.

In its October 2011 proposal, APTPPL escalated corporate costs using a weighted average of the Professional and Scientific escalator and the Administrative Services escalator. The weighting was chosen to approximate the ratio of professional to administrative staff providing the corporate services. The AER rejected this approach.

For the purposes of this revision APTPPL has applied the EGWSS escalator to corporate costs in the same manner as to other operating costs as described in section 8.5.

8.7 Summary

In summary, APTPPL's forecast operating costs are provided below:

Table 8.3 – Forecast operating costs

$m (June-2012)	2012/13	2013/14	2014/15	2015/16	2016/17
Labour	6.48	6.63	6.75	6.84	7.38
Contractors	1.12	1.14	1.16	1.18	1.27
Insurance, Licences and Fees	0.63	0.63	0.63	0.63	0.63
Other operating costs	1.42	1.45	1.48	1.58	1.62
Corporate costs	4.38	4.47	4.56	4.62	4.99
Carbon costs	0.71	0.72	0.72	0.78	0.74
Debt raising costs	0.28	0.27	0.27	0.26	0.25
Total operating costs	**15.03**	**15.33**	**15.58**	**15.88**	**17.73**

9 Tariffs

Tariffs are based on an allocation of total costs across forecast utilisation.

9.1 Total Revenue

The total revenue requirement for the RBP, culminating from the revisions discussed above, is as follows:

Table 9.1 – Forecast total revenue

$m (Nominal)	2012/13	2013/14	2014/15	2015/16	2016/17
Return on capital	41.91	41.83	41.68	41.27	40.88
Depreciation	5.09	6.40	7.90	7.98	7.42
Opex allowance	15.42	16.13	16.83	17.60	20.15
Tax payable	3.47	5.97	6.15	6.20	6.13
Less imputation credits	(0.87)	(1.49)	(1.54)	(1.55)	(1.53)
Annual building block revenue	**65.03**	**68.84**	**71.02**	**71.50**	**73.05**
Smooth revenue profile	**52.87**	**61.33**	**71.11**	**82.50**	**88.48**

9.2 Cost allocation

Amendment 1.1:

Amend the access arrangement submission to:

- demonstrate that revenue is allocated between reference and non-reference services (negotiated) in the ratio in which costs are allocated between reference and non-reference services

- demonstrate that costs are allocated between reference and non-reference services according to r. 93(2) of the NGR

In its October 2011 submission, APTPPL allocated the capital and operating costs associated with the RPB8 expansion and Lytton Lateral to the Negotiated Service. APTPPL also allocated the demand and volumes associated with the Negotiated Services provided by this capacity to the Negotiated Service. The balance of the costs and volumes were then used to calculate the Reference Tariff. The AER has questioned this approach.

In this submission, APTPPL has not sought to distinguish the Reference and Negotiated Services for cost allocation purposes. That is, all capital and operating costs, and all volumes, are included in the calculation of the Reference Tariff.

This is consistent with the requirements of the AER's Required Amendment 3.1, in which the AER required the definition of "Existing Capacity" to be reset at the commencement of each Access Arrangement period.

Amendment 1.2:

Revise the 2012–13 reference tariffs to a capacity reference tariff ($/GJ of MDQ/day) of $0.5149 and a throughput reference tariff ($/GJ) of $0.0344.

APTPPL is unable to directly comply with this Required Amendment.

Reference Tariffs are, by their nature, the culmination of a multitude of decisions made in the process of developing an Access Arrangement. To the extent that any of those decisions is not finalised, the Reference Tariff cannot be finalised.

For example, the footnote to Table 7.1 regarding the Weighted Average Cost of Capital clearly indicates that "The risk free rate, debt risk premium and inflation forecast will be updated closer to the date of the final decision."[83] Until these updates have been implemented and the approved WACC determined, the outturn tariffs cannot be determined.

The Reference Tariffs proposed after reflecting all the amendments discussed in this submission are provided below:

Table 9.2 – Proposed Reference Tariffs

	2012/13	2013/14	2014/15	2015/16	2016/17
Capacity ($/GJ/day)	0.5922	0.6865	0.7960	0.9228	1.0699
Throughput ($/GJ)	0.0396	0.0459	0.0532	0.0617	0.0715

[83] AER draft decision p121.

9.3 Cost pass through

Amendment 2.1:

Delete the first paragraph of clause 4.5.2 of the access arrangement proposal and replace with the following:

Subject to the approval of the AER under the National Gas Rules, Reference Tariffs may be adjusted after one or more Cost Pass-through Event/s occurs, in which each individual event materially increases or materially decreases the cost of providing the Reference Service. Any such adjustment will take effect from the next 1 July.

AER draft decision

The AER found that APTPPL's proposed tariff variation mechanisms were consistent with the requirements of the NGL and NGR. The AER considered, however, that for some elements, a more preferable alternative existed that would better promote the purpose of the NGL and NGR.[84] The AER requires amendments in respect of the following before approving the tariff variation mechanism in the revised access arrangement:

- Removal of forward looking cost pass through;
- The definition of an insurance cap event; and
- Removal of automatic variation of tariffs where the AER does not make a decision before the relevant 1 July.

APTPPL's responses to these amendments are set out below.

9.3.1 Forward looking cost pass through

The AER has not accepted APTPPL's proposal that costs approved under a cost pass through event may include costs that are reasonably expected to be incurred by APTPPL.

The first reason given by the AER for this decision that the expected pass through event may not eventuate, or that the expected costs under that pass through event do not match the expected quantum.

[84] AER draft Decision, p69

APTPPL does not consider that the first part of this concern is warranted given APTPPL's proposed original drafting in clause 4.5.2 of the access arrangement. Clause 4.5.2 as proposed in October 2011 stated:

> Subject to the approval of the AER under the National Gas Rules, Reference Tariffs may be adjusted after one or more Cost Pass-through Event/s occurs, in which each individual event materially increases or materially decreases, or is reasonably expected to materially increase or decrease, the cost of providing the Reference Service. Any such adjustment will take effect from the next 1 July.

This formulation required the event to have occurred before adjustment of reference tariffs under the cost pass through mechanism. Therefore, the AER's concerns that a proposed event may not eventuate is unfounded.

Following the occurrence of an event, APTPPL considers that it is efficient, both in respect of streamlined cost recovery processes and in relation to the reduction of administrative costs, for a cost pass through claim to be able to include an element of forecast. The efficiency of this approach can be demonstrated by way of an example.

Consider a new legislative obligation that comes into law on 1 January during the access arrangement period and that imposes an obligation on APTPPL to pay a fee or charge for the following financial year 1 July to 30 June, and that fee or charge is known before the relevant 1 July. These circumstances allow both the AER and APTPPL to have a considerable degree of certainty in relation to the costs of the event before they are incurred. There is therefore opportunity to align cost recovery with the year in which the costs are incurred, reducing complexity and administrative costs (such as that which would arise in the calculation of the time value of money) and ensure that APTPPL does not suffer unnecessary (and potentially costly) burdens in relation to cash flow. APTPPL considers that users, the AER and service providers would benefit from this scope in the tariff variation mechanism by reducing administrative costs and complexity in the tariff variation process.

APTPPL further notes that the scope to include forecast costs applies equally to forecast reductions in costs, which are more likely to be able to be determined in advance (for example the removal of an impost). The AER's revisions to the tariff variation mechanism would mean that users would not be able to benefit from a known future reduction in costs until the following regulatory year.

APTPPL recognises that not all cost pass through events and associated costs have characteristics that are conducive to this treatment. In many cases, for example costs incurred in relation to a natural disaster event, it may not be appropriate to recover forecast costs. APTPPL notes that the AER would have discretion under the tariff variation mechanism to not approve forecast costs if it did not consider those costs were reasonably expected to be incurred. APTPPL therefore does not consider that the AER or users would incur significant administrative costs arising

from the inclusion of scope in the access arrangement for recovery (or return) of costs that contain an element of forecast.

APTPPL has made amendments to clause 4.5.2 to accommodate the inclusion of a carbon cost pass through event to which no materiality threshold applies (see discussion below). Changes to clause 4.5.2 in no way undermine the limited application of the clause to events that have occurred, however these changes do mean that the AER's required amendment is no longer relevant to this clause. The AER's amendment does have relevance, however, to the inclusion of the new clause 4.6 referring to pass through amounts which incorporate a forecast. APTPPL considers this new clause is necessary to allow for further adjustments to be made at future annual tariff changes to reflect actual costs once these are known.

APTPPL notes the AER's confirmation that compensation for cost pass through events would include compensation for the time value of money. While this confirmation is welcome, later compensation for incurred costs does not address the potentially immediate cash flow implications of delayed recovery that can occur in relation to significant cost pass through events.

APTPPL has therefore not adopted the AER's amendment 2.1 to its tariff variation mechanism, and has made further adjustments to the proposed access arrangement to provide for future adjustments to tariffs to take account of actual costs (where a cost pass through amount incorporated a forecast) after those costs become known (new clause 4.6).

9.3.2 Insurance cap event

Amendment 2.2:

Delete the definition of an insurance cap cost pass through event in clause 4.5.2 of the access arrangement proposal and include the following:

An event that would be covered by an insurance policy but for the amount that materially exceeds the policy limit, and as a result Service Provider must bear the amount of that excess loss. For the purpose of this Cost Pass-through Event, the relevant policy limit is the greater of the actual limit from time to time and the limit under Service Provider's insurance cover at the time of making this Access Arrangement. This event excludes all costs incurred beyond an insurance cap that are due to Service Provider's negligence, fault or lack of care. This also excludes all liability arising from the Service Provider's unlawful conduct.

The AER has not accepted APTPPL's proposed definition of an insurance cap event which excludes recovery through the pass through mechanism of costs incurred beyond an insurance cap that are due to Service Provider's Gross Negligence/Wilful Misconduct. The AER considers that this exclusion would raise moral hazard issues, by removing incentives for APTPPL to effectively manage risks and operate the pipeline safety and reliably.

In place of Gross Negligence/Wilful Misconduct, the AER have set a lower bar for exclusion of cost recovery at the service provider's negligence, fault or lack of care.

APTPPL considers that the AER have overestimated the degree to which the availability of cost pass-through mechanisms influence business behaviour. A finding of negligence against APA Group is likely to have profound implications for the business. A finding of negligence can be expected to increase APA Group's overall cost of doing business by substantiality increasing insurance premiums. A successful claim is also likely to have an impact on APA Group's share price by undermining market confidence in the business, as well as the willingness of its contractual partners to enter into arrangements with the business. Given this, scope to recover costs above an insurance cap is unlikely to change APA Group's approach to risk management, particularly where it will remain exposed to gross negligence and wilful misconduct claims.

APTPPL also notes that the AER's reasoning for amending the insurance cap event focuses on the difference between negligence and gross negligence. Its amendments, however, go much further, to also include exclusions fault or lack of care. The AER's reasons for this are not set out. APTPPL does not consider that extension to fault or lack of care is appropriate, as it does not provide a clear basis on which the AER will assess proposed insurance cap cost pass through claims.

A limitation to negligence (or gross negligence) implies established legal liability that can be independently verified. The concepts of fault and lack of care are comparatively not well defined. It is unclear how the AER would establish fault or lack of care and on what basis. It is therefore not appropriate to include these concepts in the cost pass through definition.

APTPPL has therefore adopted the AER's amendment 2.2 in part, replacing reference to Gross Negligence/Wilful Misconduct with reference to negligence.

9.4 Tariff adjustment

Amendment 2.3:

Amend clause 4.5.4 of the access arrangement proposal by deleting the following:

If Service Provider proposes adjustments to the Reference Tariffs (other than as a result of a Cost Pass-through Event) and those adjustments have not been approved by the next 1 July, then the Reference Tariffs will be adjusted with effect from that next 1 July, until such time as adjustments to reference tariffs are approved by the AER.

The AER has not accepted APTPPL's proposal that where the AER have not approved an annual tariff variation by the relevant 1 July, the tariff variation as proposed will apply until such time as the AER reaches a decision.

The AER has rejected this proposal on the basis that it does not consider that it is consistent with Rule 97(4), which requires that a tariff variation mechanism give the

AER adequate oversight or powers of approval over reference tariff variations. The AER also considers that the proposal would give rise to a significant risk that tariffs may not be efficient.

APTPPL's inclusion of this clause is consistent with the access arrangements recently approved by the AER for the Allgas and Amadeus Gas Pipeline access arrangements, approved in June 2011 and July 2011 respectively. APTPPL notes that the Rules were not changed 2-3 months between the AER making these decisions, and the submission of the RBP access arrangement revision proposal. APTPPL therefore considers that it is reasonable to conclude that these arrangements remain consistent with the Rules, and that APTPPL appropriately included this mechanism in its access arrangement proposal.

APTPPL further notes that the 'automatic' tariff change relates only to the annual tariff adjustment formula mechanism, and does not extend to the automatic adjustment of tariffs related to cost pass through claims. The annual tariff adjustment formula mechanism is a very simple calculation involving the application of known CPI values and a pre-set X-factor. As such, the automatic variation of tariffs each 1 July where the AER fails to make a decision before that 1 July is very unlikely to lead to inefficient tariffs being imposed.

APTPPL has therefore not adopted AER amendment 2.3.

9.4.1 Inclusion of carbon cost pass through event

APTPPL proposes to include an additional cost pass through event in its access arrangement revision proposal related to the pass through of carbon costs as they vary from those forecast in APTPPL's operating expenditure.

The NGR (Rule 60) permits the AER to approve amendments to the access arrangement revision proposal in response to the draft decision to address matters not otherwise raised in the AER's draft decision. The specific example used in the Rules is amendments to the access arrangement proposal to deal with a change in circumstances of the service provider's business since the submission of the access arrangement proposal.

The Clean Energy Act 2011 received royal assent on 18 November 2011. The Act introduces a carbon trading scheme in Australia designed to impose a price on carbon emissions from 1 July 2012. There was significant uncertainty related to the likelihood of this scheme up until very shortly before the passage of this legislation. As a result, APTPPL did not include forecast costs in its access arrangement revision proposal related to its likely carbon cost liability.

As discussed above in relation to forecast operating expenditure, APTPPL proposes to include carbon liability costs in its forecast revenue. Alongside this forecast, APTPPL considers that it would be appropriate to provide for a cost pass-through event that will permit differences between the forecast of total carbon costs and the

actual total carbon costs incurred by APTPPL in each year of the access arrangement period to be passed through. The carbon cost event seeks to deal with two uncertainties: (a) the volume of the gas to which the carbon cost will attach; and (b) the carbon price itself, which is fixed for the first three years of the scheme, and after this period is set by the market.[85]

APTPPL submits that treating this difference as a cost pass-through is particularly appropriate in circumstances where the shape and operation of the carbon market is still uncertain, and there is considerable scope for the carbon price to vary significantly from that forecast by the Australian Treasury (either in positive or negative terms).

In these circumstances, APTPPL does not consider that it is appropriate for itself or users of the pipeline to bear forecasting risks associated with substantially different carbon costs from those forecast.

As noted above, the carbon price will be fixed for the first three years of the scheme and therefore APTPPL's carbon costs are relatively predictable (variability will mainly be related to compressor usage, which responds to customer demand). In the later years, however, the price moves to a floating market price and is highly uncertain. APTPPL is likely to be a price taker in this market, as its carbon liability is relatively small compared to other businesses such as coal-fired generators. The ability to pass through actual carbon costs is therefore unlikely to materially change the costs incurred by APTPPL in procuring carbon certificates, even where it does not face direct incentives to minimise its costs.

APTPPL also notes that it will incur carbon liabilities across a number of its assets, including those that are not subject to regulated pass through mechanisms. APA Group will manage the purchase and trade of carbon certificates through its centralised corporate function, and therefore it can be expected that any efficiencies that APA Group can achieve in relation to its total carbon costs will be passed on to regulated assets regardless of the specific pass through arrangements in place.

APTPPL does not propose that a materiality threshold would attach to the carbon cost event. The relevant costs to be passed through will be verifiable and the administrative costs associated with the assessment of the pass-through amount should be minor. This approach is consistent with that taken by the AER in similar circumstances, including the ETSA Utilities 'feed-in tariff event' pass through and a number of pass through events in the Jemena Gas Networks access arrangement.[86] Therefore, the inclusion of a carbon cost pass through event as discussed here also requires consequential amendments to the materiality threshold approved by the AER in the draft decision, as well as to clause 4.5.2 of the access arrangement.

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[85] *Clean Energy Act 2011* (Cth), section 100.

[86] AER, *South Australia Distribution Determination 2010-11 to 2014-15 Final Decision*, May 2010, pp 231 – 242; AER, *Jemena Gas Networks: Access Arrangement Proposal for the NSW Gas Networks 1 July 2010 – 30 June 2015 - Final Decision*, June 2010, pp 363 – 392.

In the ETSA Utilities distribution determination, the AER noted that in some circumstances it may be appropriate to avoid the potentially significant forecast errors in relation to some events that are anticipated during a regulatory period. These circumstances arise for events that are subject to significant uncertainty and therefore potential forecast error, where the consequence of including these costs in the capital or operating expenditure forecast could be to the disadvantage of customers where, for example, those costs do not materialise. Similarly, the AER recognised that the service provider would be disadvantaged if the actual costs were higher than those forecast. The AER stated that in these circumstances a pass through of costs with a notional (in that case, administrative cost) is in the interests of customers.[87]

APTPPL submits that the total carbon cost incurred by APTPPL in relation to the RBP is a particular circumstance that supports the inclusion of a pass-through event where the forecast costs differs from actual costs. As some component of the difference between the forecast costs and the actual costs will be an estimate, there would be a further adjustment or 'true up' in the following year when the actual cost for the full regulatory year is known. This is reflected in a new clause 4.6 in the revised access arrangement.

9.4.2 Application of the materiality threshold to cost pass through claims

APTPPL has made a further change to its access arrangement regarding the applicability of the materiality threshold to individual pass through events.

APTPPL considers that the materiality threshold should apply only once in relation to each annual tariff change, reflecting the limitation of tariff changes to each 1 July, such that the materiality threshold is met where application pass through event amounts in that year in total exceed the materiality threshold. APTPPL considers that this approach provides an appropriate balance between:

1. limiting the administrative costs of users, the AER and the service provider by having only a single tariff adjustment in any year, and ensuring that this tariff adjustment reflects a material amount (NGR 97(3)(b)); and

2. ensuring that tariffs are efficient (NGR 97(3)(a)) by ensuring that APTPPL can recover its efficient costs in providing pipeline services.

Applying the materiality threshold to each individual cost pass through event risks APTPPL incurring potentially significant costs associated with recognised pass through events that are material in total, while not being able to recover those costs where those events individually do not satisfy the materiality threshold. APTPPL does not consider that this outcome would be consistent with the Revenue and Pricing Principles which provide for a service provider to be given reasonable

[87] AER 2011, *South Australia Distribution Determination 2010-11 to 2014-15 Final Decision*, May 2010, pp 234 – 235

opportunity to recover at least the efficient costs the service provider incurs in complying with a regulatory obligation or payment and providing reference services.

10 Queuing requirements

In its October 2011 submission, APTPPL proposed moving from a First Come First Served (FCFS) queue to a publicly notified auction as allowed under Rule 103(4)(b).

In its April 2012 draft decision, the AER rejected APTPPL's proposal, requiring it to re-institute the FCFS queue with some amendments:

Amendment 10.1: *Make the queuing requirements for the access arrangement period identical to those in the earlier access arrangement, except for amendments 10.2, 10.3 and 10.4.*
Amendment 10.2: *Delete clause 6.1(d) of the access arrangement proposal.*
Amendment 10.3: *Amend clause 6.3(a) of the access arrangement proposal to the following:* *An Existing Capacity Queue will include all relevant Requests which can be satisfied from the spare capacity of the covered pipeline.*
Amendment 10.4: *Replace 'queuing policy' and 'queuing', wherever occurring, with 'queuing requirements'.*

APTPPL's approach to Queuing Requirements in response to Amendments 10.1, 10.2 and 10.3 is discussed below.

APTPPL accepts Amendment 10.4.

10.1 Rule requirements

Rule 103(1)(a) requires an access arrangement to contain queuing requirements if the access arrangement is for a transmission pipeline. APTPPL's proposed access arrangement contains the queuing requirements discussed below.

Rule 103(3) provides that queuing requirements must establish a process or mechanism (or both) for establishing an order of priority between prospective users of spare or developable capacity (or both) in which all prospective users are treated on a fair and equal basis. APTPPL submits that the queuing requirements in the access arrangement meet this requirement.

The queuing requirements for spare (existing) capacity provides for the order of priority to be determined on a first-come-first served basis (the example in Rule 103(4)). An "open season" type approach is proposed for developable capacity. This approach enables the grouping together of requests for capacity in the most

efficient and economic way and is a process or mechanism which establishes the order of priority between prospective users of developable capacity in a manner that treats prospective users on a fair and equal basis.

Rule 103(5) provides that queuing requirements must be sufficiently detailed to enable prospective users to understand the basis on which an order of priority between them has been or will be determined and if an order of priority has been determined, to determine the prospective user's position in the queue. APTPPL submits that the details of the queuing requirements in the proposed access arrangement meet these requirements.

10.2 Purpose of queuing requirements

In assessing APTPPL's response to the AER's draft decision, it is important to understand the purpose of the queuing requirements and distinguish Existing Capacity from Developable Capacity. Importantly, Existing Capacity is about access to capacity created by sunk investment; Developable Capacity invariably requires further capital investment in pipeline assets.

They key distinction is that, as the capital value of the pipeline decays over time, the Reference Tariff is unlikely to support the development of new capacity; in the context of the Rules, that new capacity must therefore be developed to serve a Negotiated Service at a negotiated tariff.

The purpose of the Developable Capacity queuing arrangements is therefore not to allocate Existing Capacity in an economically efficient manner, but to aggregate sufficient demand for pipeline expansion to develop economically efficient expansion projects.

This suggests that the Queuing Requirements for Existing Capacity need to serve a different purpose than those for Developable Capacity. The queuing requirements therefore need to be fit for purpose.

10.3 Queue v auction

In its October 2011 submission, APTPPL outlined the difficulties associated with the queuing arrangements in the previous AA. In particular, that the queue did not deliver an efficient allocation of pipeline capacity, and that the queue was subject to "squatting" by non-genuine shippers.

With its proposal submission, APTPPL filed an expert report by NERA, which clearly indicated that an auction approach was the more economically efficient way to allocate capacity.

APTPPL proposed to move to an auction format, as allowed under Rule 103. In January 2012, APTPPL and the AER conducted a workshop with shippers and other interested parties, who indicated mixed feelings about the move to an auction, and some concerns with the process for assessment of auction bids. High level notes from this workshop are available on the AER's website.

While acknowledging that the Rules provide for the queuing requirements to be met by an auction process, the AER, in its draft decision dated 30 April 2012, rejected the APTPPL proposal to adopt an auction process, requiring it to revert to its previous Fist Come First Served queue, with some amendments.

APTPPL considers that the AER's concerns with APTPPL's proposed move to an auction format can be grouped in two general categories:

- concerns over the relationship of an auction process within the National Gas Rules' negotiate/arbitrate framework; and
- concerns over the detailed rules surrounding the conduct of the auction.

The AER also expressed some concern, following on from the ACCC's experiences with recent grain port capacity auctions,[88] in the ability to develop sufficiently robust auction processes in the time available for the APTPPL AA process.

APTPPL conducted a further workshop with the AER and shippers on 17 May 2012, with a follow-up teleconference on 21 May 2012 to work through the AER's concerns with shippers.

Matters raised by the AER and shippers are discussed below, followed by APTPPL's revised proposal relating to queuing requirements.

10.3.1 Negotiate/arbitrate framework

Within the context of the negotiate/arbitrate framework, the AER's concerns appear to be that a shipper who acquires capacity at auction would not be able to launch an access dispute.[89] This stems largely from the auction requirements that a bid is required to be irrevocable, and capable of being considered a binding contract.

APTPPL acknowledges that there is a degree of circularity in the framework. Section 189 of the NGL requires the dispute resolution body to "give effect to the

[88] See ACCC, *Auction Objection Notice in response to Viterra Operations Limited's Auction Variation Notice*, 11 April 2012

[89] AER draft decision p225.

applicable access arrangement". Were that AA to include an auction process for allocating capacity, then the dispute resolution process would be required to give effect to the auction process included in the Access Arrangement, thus ending the access dispute.

APTPPL considers that a more reasonable reading is that the auction process obviates the need for the access dispute provisions to be in place.

APTPPL considers that an auction is an alternative to negotiation as a means to allocate scarce capacity. In the auction format proposed by APTPPL, shippers have full control to define the features of the service bid, and the price they are willing to pay for those services.

Under the auction format proposed, the auction outcomes, as defined in the winning shipper's bid, would be binding on both users and APTPPL. It is not clear then, the circumstances under which a user would launch an access dispute.

APTPPL also notes that a 'publicly notifiable auction' is expressly contemplated as an appropriate queuing mechanism under Rule 103(4)(b). APTPPL can only presume that the Rules' authors understood the implications of allowing an auction on the scope to launch an access dispute.

10.3.2 Auction processes

The AER expressed a number of concerns surrounding auction processes, primarily surrounding the methodology for assessment of competing bids and the definition of the product being auctioned.

At the workshops, it also became clear that there were concerns over the detailed rules associated with mismatches between available capacity and bids, and tie-breaking between bids. Following on from the ACCC's experience in the Fonterra auction, there were also concerns about the scope for shippers to exercise strategic behaviour in the auction process,[90] and for inefficient outcomes to occur as a result.

The experience from the workshops has made it clear that the auction rules that would need to be in place to address all eventualities, and to avoid strategic bidding behaviour, would be quite detailed and require extensive development with shippers and the AER. In this regard, APTPPL concludes in agreement with the AER that a robust auction process would require a more detailed development process than the current time available in the context this Access Arrangement revisions process allows.

[90] The Fonterra auction featured "auction brinkmanship" behavior driven by the increasing price nature of the auction and the ability to access spare capacity not allocated through the auction process. A similar type of behaviour could be envisioned in the RBP capacity auction as proposed.

However, inasmuch as there may not be scope to develop a robust auction process for the purposes of the proposed revised RBP Access Arrangement, simply reverting to the previous FCFS queue remains an unsatisfactory option.

10.4 APTPPL revised proposal

As discussed above, APTPPL considers that the AER's draft decision indicates a level of discomfort with an auction process that is unlikely to be able to be resolved in the short time available to assess amendments to a particular pipeline access arrangement. APTPPL therefore proposes to revert to a queuing process.

However, the AER's required amendments (primarily to re-institute the previous queuing process in its entirety) do not address the concerns with the operation of the previous queue which drove APTPPL to propose an alternative approach in the first instance.

In the context of the workshops on the queuing process, several recommendations were made to improve the effectiveness of the previous queuing process, which APTPPL proposes to take up in the response to the AER's required amendments:

- A deposit is required to secure a position on the Existing Capacity queue;
- Shippers on the Existing Capacity queue may be required to confirm every three months that the capacity is still required. Failure to confirm would result in removal from the queue;
- Shippers interested in Developable Capacity are welcome to lodge an expression of interest which will inform APTPPL regarding the needs of the market. Developable Capacity will be subject to an open season process subject to bilateral negotiation.

10.4.1 Existing capacity

The proposed Existing Capacity queue will remain a "First Come First Served" (FCFS) queue. However, to address to concerns raised in the original AA revision proposal, APTPPL proposes some changes to improve the operation and integrity of the queue.

APTPPL has long been concerned that a position on the queue could be secured by simply filing a letter requesting to join the queue. This did not necessarily require the endorsement of senior management of the business, and had considerable scope to block access to other, genuine, shippers. APTPPL therefore considers that the deposit needs to be sufficient to require expenditure approval by a suitably senior level of management.

The deposit is proposed to be calculated as follows:

Existing Capacity Queue Deposit

= Volume of capacity sought x Reference Tariff x 365 x 10%

In APTPPL's view, this will result in a more efficient outcome, as the deposit will ensure that only genuine shippers seek entry to the queue.

The Existing Capacity queue will be "grandfathered" such that shippers currently holding places on the queue will continue to hold those positions. However, a deposit will be required to be lodged within three months of the commencement of this AA to secure that position.

The other major concern with the FCFS queue was the scope for "queue-sitting", where by shippers holding a position on the queue could hold that position and block or delay access to other shippers. APTPPL considers that this also leads to inefficient outcomes, and proposes to include provision for periodic confirmation by shippers that they wish to remain on the queue.

10.4.2 Developable capacity

As discussed above, the purpose of developable capacity queuing arrangements is to aggregate sufficient demand to construct efficient expansions. The concept of a "queue" sits uncomfortably with the bespoke nature of pipeline expansions.

The purpose of Developable Capacity Queuing Requirements is to monitor the market and aggregate demand for pipeline expansions in order to expand the pipeline in the most efficient way.

The expressions of interest filed by potential users will inform APTPPL regarding the level of interest in developable pipeline capacity. APTPPL will then be able to develop a pipeline expansion project to serve that market interest.

APTPPL therefore proposes an "open season" process for developable capacity. The open season will identify those shippers seeking additional capacity on the pipeline, and APTPPL will enter into bilateral negotiations to develop the optimally sized capacity expansion. Further, APTPPL also proposes to dissolve the Developable Capacity Queue as it existed on the day before the commencement of this Access Arrangement.

11 Non tariff components

Amendment B.1: *Delete clause 7.4 of the access arrangement proposal which relates to the inclusion in the extension and expansion requirements of certain fixed principles.*

As discussed in section 2 APTPPL accepts the AER's Required Amendment 3.1 to amend the definition of Existing Capacity to be the capacity at the commencement of the AA period.

As this would be inconsistent with the Fixed Principle proposed to be included in clause 7.4 of the proposed AA, APTPPL accepts the required amendment to remove the fixed principle.

11.1 Capacity trading requirements

Amendment 11.1: *Delete the text 'An example of such grounds might be if a reduction in the amount of the Delivery Point MDQ at the initial Delivery Point will not result in a corresponding increase in Service Provider's ability to provide that service to the alternative Delivery Point.' from clause 5.4 of the access arrangement proposal.*
Amendment 11.2: *Provide a definition of the term 'reasonable commercial and technical'* *For the purposes of clause 5.4 'reasonable commercial grounds' and 'reasonable commercial conditions' include allowing APTPPL to deliver the same amount of the Service, receive the same amount of revenue and bear no additional capital or non-capital costs, as applied before the trade.* *Examples of items that would be reasonable are:* *(a) APTPPL refusing to agree to a User's request to change its Delivery Point where a reduction in the amount of the Service provided to the original Delivery Point will not result in a corresponding increase in APTPPL's ability to provide Services to the alternative Delivery Point; and* *(b) APTPPL specifying that, as a condition of its agreement to a change in the Delivery Point or Receipt Point, APTPPL must receive the same amount of revenue, and bear the same or a reduced level of costs that it would have received or borne before the change.*

The AER in large part accepted APTPPL's proposed capacity trading requirements. The AER however, requires inclusion of a definition of 'reasonable commercial grounds' as part of clause 5.4 of the access arrangement (AER amendments 11.1 and 11.2).

APTPPL notes that the approach proposed in its revised access arrangement in relation to the RBP access arrangement for the specification of reasonable commercial and technical grounds is identical to that approved by the AER in respect of both the Allgas access arrangement and the Amadeus Gas Pipeline access arrangement in June 2011[91] and July 2011[92] respectively. In both of these cases the AER explicitly determined that relevant service provider's approach was appropriate in its final decision.[93]

APTPPL has amended the RBP access arrangement to adopt the AER's required amendments 11.1 and 11.2, with some further amendments for consistency in drafting style with the rest of the access arrangement[94]. APTPPL notes, however, that the changes to the AER's approach in relation to these provisions create considerable uncertainty for APA Group in relation to its access arrangements where it seeks to submit revision proposals that it considers have maximum potential to be accepted by the AER as they reflect previous AER decisions.

11.2 Commencement and review dates

Amendment 11.3: *Amend clause 1.5 of the access arrangement proposal as below:* *This Access Arrangement will commence on the date on which the approval of the AER takes effect under Rule 62 or Rule 64.*
Amendment 11.4: *Amend clause 1.6 of the access arrangement proposal as below:* *Service Provider will submit revisions to this Access Arrangement to the AER on or before 1 July 2016, or four years from the commencement date of this Access Arrangement, whichever is the later (Revisions Submission Date).* *The revisions to this Access Arrangement will commence on the later of 1 July 2017 and the date on which the approval by the AER of the revisions to the Access Arrangement takes effect under the National Gas Rules (Revisions Commencement Date).*

[91] AER 2011, APT Allgas Energy Pty Limited Access Arrangement effective 01 July 2011 – 30 June 2016, Amended by order of the Australian Competition Tribunal, 10 February 2012, June, clause 5.4

[92] AER 2011, Access Arrangement for the Amadeus Gas Pipeline 01 August 2011 to 30 June 2016, July, clause 5.4

[93] AER 2011, APT Allgas Access Arrangement proposal for the Qld gas network 1 July 2011 – 30 June 2016: Final Decision, June, p 99; AER 2011, NT Gas Access arrangement proposal for the Amadeus Gas Pipeline 1 August 2011 – 30 June 2013: Final Decision, July, p 132

[94] For example, by changing references to 'APTPPL' to 'Service Provider'

The AER requires APTPPL to revise clause 1.5 and 1.6 of its access arrangement revision proposal to, respectively:

- Explicitly provide scope for the revisions commencement to be determined in accordance with an AER-imposed access arrangement made under Rule 64(6); and

- Make clear that the revisions to the access arrangement will be submitted to the AER.

APTPPL has adopted both of these amendments in its access arrangement revision proposal.

12 Terms and conditions

The AER requires APTPPL to make a number of amendments to its access arrangement definitions (Schedule 2) terms and conditions (Schedule 3) as per Appendix A of the Draft Decision. APTPPL responds to each of these required amendments in Table 12.1 below.

Table 12.1 Required Amendments to terms and conditions

No	Matter	AER Amendment	APTPPL response
Definitions			
A.1	Gas Law definition	*Amend the legislative references in the access arrangement proposal as under:* *- Petroleum and Gas (Production and Safety) Act 2004 (QLD)* *- Gas Supply Act 2003 (QLD)* *- Petroleum Act 1923 (QLD).* However, the AER considers 'QLD' should be inserted after relevant legislative references to avoid uncertainty.	APTPPL accepts this amendment
A.2	Gross Negligence/Wilful Misconduct	*Adopt the definition of 'Wilful Misconduct' as follows:* *Wilful misconduct means any act or omission done or omitted to be done with deliberate or reckless disregard for foreseeable, harmful and avoidable consequences which is not otherwise an act or omission done in good faith.* The AER considers that the inclusion of the definition of Gross Negligence/Wilful Misconduct fails to provide clarity and certainty around the meaning of the term. The AER is of the opinion that gross negligence and wilful misconduct are two separate concepts, and the AER considers that the definition proposed by APTPPL fails to capture the two different concepts clearly. The AER has approved a definition of 'Wilful Misconduct' in the AGP access arrangement and requires the APTPPL to adopt the same definition as set out in amendment A.2.	APTPPL accepts the deletion of the definition of 'Gross Negligence/Wilful Misconduct' and inclusion of the AER's proposed definition of Wilful Misconduct. APTPPL proposes to include a definition of 'Gross Negligence' to provide certainty and clarity regarding the two concepts of Gross Negligence and Wilful Misconduct. This responds to the specific concerns raised by the AER in its Draft Decision that the combined definition increased uncertainty, as well as to clarify the difference between negligence and gross negligence as the difference is not clear under Australian common law. Gross Negligence means a negligent act or omission, committed with reckless disregard for the consequences and the circumstances where the negligent party knows or ought to know that those consequences would likely result from the act or omission, and which is not due to an honest mistake, oversight, error of judgement or accident. APTPPL has also made consequent amendments to the references to Gross Negligence and Wilful Misconduct in clauses 16(d), 57, 87(a), 88, 89(a), 90 and 96.

A.3	Queuing Policy	*Delete following definitions from definitions and interpretation schedule 2:* *- Existing Capacity Notice* *- Notice of Auction for Developable Capacity* *- Notice of Auction for Existing Capacity* *-Open Season Existing Capacity Closing Date* Definition pertain to proposal for auction-based queuing policy which is rejected by the AER. Relevant definitions to be deleted	APTPPL accepts the deletion of definitions of 'Existing Capacity Notice', 'Notice of Auction for Developable Capacity', 'Notice of Auction for Existing Capacity' and 'Open Season'. In light of the matters raised in the draft decision, APTPPL does not propose to have an auction-based queuing policy, but instead proposes the following. - In respect of Existing Capacity, maintain an Existing Capacity Queue (see clauses 6.1 – 6.4). APTPPL requires Requests to be placed on the Existing Capacity Queue to include an Existing Capacity Queue Deposit (see clause 6.2(b)). - In respect of Developable Capacity, adopt an open season process to determine the most economic and efficient manner for undertaking investment in Developable Capacity (see clauses 6.5 – 6.6). Clause 6.7 (Transitional arrangements) has also been inserted to deal with the transition from the previous Access Arrangement..

A.4	Relevant Tax	*Amend definition of Relevant Tax as follows:* *'Relevant Tax' means any royalty, duty, excise, tax, impost, levy, fee or charge (including, but without limitation, any goods and services tax) imposed by the Commonwealth of Australia, any State or Territory of Australia, any local government or statutory authority or any other body (authorised by law to impose such an impost, tax or charge) on or in respect of the Network (or any part of it) or on or in respect of the operation, repair, maintenance, administration or management of the Network (or any part of it) or on or in respect of the provision of any Network Service (other than a levy, fee or charge that arises as a result of APTPPL's breach of a law or failure to pay a tax or charge by the due date for payment).* The AER does not accept APTPPL's proposed definition of relevant tax. The AER considers that the proposed definition excludes some of the categories of tax but it is not clear what relevant tax is included in tax payable by Service Provider. The AER also states that no justification is provided for the proposed definition. The AER has approved a definition of 'relevant tax' for the other APA companies and requires APTPPL to amend this definition in line with those decisions.	APTPPL's proposed definition for 'Relevant Tax' is based on that included in the National Electricity Rules with changes limited to differences in nomenclature between the electricity and gas rules. The AER has previously stated a preference for consistency in cost pass through arrangements between electricity and gas, and in line with this preference, APTPPL adopted the definition in the National Electricity Rules for a Relevant Tax. This reasoning is stated on page 104 of APTPPL's revision proposal. APTPPL accepts this amendment, however makes some amendments to the drafting to refer to transmission pipelines as opposed to networks, and Service as opposed to Network Service.

Terms and conditions			
A.5	Nominations	*Delete clause 8(b) from the access arrangement proposal.* The AER requires deletion of clause 8(b) as it considers that it creates additional obligations for the Users to comply with, which is not essential to support the Queensland STTM in the presence of clause 8(a).	APTPPL has not accepted the AER's amendment and provides the following additional information in support of its original drafting of this clause. There may be circumstances where APTPPL is given a direction by AEMO or by another government or semi-governmental authority not relating to Queensland STTM. For example, gas examiners and emergency services (Police, Fire Bridge) could give APTPPL a directive to shut-in a particular delivery point if they considered it endangered lives or property. Therefore APTPPL submits that the wider reference to an Authority is needed. APTPPL has also identified the need for a further clause (clause 10A) dealing with contingency gas quantities as contingency gas will affect users' nominations. The need for this clause has only become apparent since the commencement of the STTM in Queensland. APTPPL submits the following clause 10A be included in the access agreement User must revise any Nominations necessary to account for any quantities of contingency gas which are scheduled by AEMO for Shipper's account under the STTM Rules.

A.6	Curtailment	*Maintain the original wording of clause 16 as follows:* *If Service Provider interrupts or curtails receipts or deliveries of quantities of Gas under clause 15, Service Provider is not liable to the User in respect of interruption or curtailment if the interruption or curtailment:* The AER does not accept inclusion of 'failure to schedule' for allowable reasons listed in clause 16. The AER considers that the proposed amendment is not consistent with the NGO because scheduling provides reliability and security to the user for supply of gas. In case the service provider fails to schedule the gas, the user may be required to purchase the gas from the STTM market at a higher price. The AER considers that the proposed amendment does not promote efficient operation and use of gas services for the long term interests of consumers of gas with respect to reliability and security of supply of gas.	APTPPL does not accept the AER's amendment A.6. The inclusion of 'failure to schedule' in the limitation of liability is intended to permit APTPPL to be relieved of the obligation to Schedule (clause 11) in certain circumstances, namely the circumstance where an allowable event occurs. These are events which are specifically set out in the agreement - such as a planned interruption undertaken in accordance with clauses 35 or 36 - that means that APTPPL cannot schedule gas for a particular shipper. The AER's exclusion of 'failure to schedule' would mean APTPPL is in breach of the agreement for failure to schedule for such an allowable event. APTPPL would instead need to schedule and then interrupt gas (before any has flowed) to ensure that flows do not exceed pipeline capacity (which would be administratively cumbersome). APTPPL considers that this approach would undermine rather than contribute to certainty for shippers as to expected pipeline flows. In all cases (failure to schedule, interruption or curtailment), the shipper may be required to purchase gas from an alternative source or curtail demand, as the end result from all such events would be that gas did not flow as nominated by the shipper. APTPPL considers that it would be preferable for the shipper to be advised as soon as possible that nominated gas flows could not be scheduled because of an event listed in clause 16, such that they can make alternative arrangements, rather than schedule and then interrupt or curtail gas, which would be the only alternative available to APTPPL under clause 16 as amended by the AER.

A.7	Market Operator Service (MOS)	*Amend clause 20 as follows:* *If the provision of a Transportation Service under the Gas Transportation Agreement causes or would cause an imbalance which exceeds or would exceed the Cumulative Imbalance Limit then Transporter may, in its absolute discretion, cease to provide or suspend the MOS Decrease Service and/or the MOS Increase Service to Shipper.* AER redrafting of clause to correspond with new allocation methodology during the recent QLD STTM Market Trial.	APTPPL accepts the amended clause 20 in part, however makes amendments to the drafting to refer to the terminology/ definitions in STTM Rules ie use of 'allocate' instead of receive/ supply, so as to ensure consistent with terminology used in the access arrangement. The terminology in clauses 18 and 19 has also been amended.

A.8	Warranties and representations	*Delete clause (60(b)).* AER requires deletion of clause 60(b) which requires shippers to provide contract reference information to APTPPL that is accurate. The AER does not accept this clause as it considers that it absolves the service provider from verifying the authenticity and correctness of information. The AER considers that it is not consistent with the NGO because it does not promote efficient operation and use of natural gas service services for the long term interest of consumers of gas with respect to safety, reliability and security of supply gas.	APTPPL does not accept the AER's amendment. Rule 380 requires contract holders to provide information to the AEMO as listed in Rule 381. As this obligation rests on both APTPPL and the shipper, APTPPL retains responsibilities under the rules to ensure that information provided to AEMO is accurate. APTPPL's only source of that information is from users and therefore users should be required to provide correct information. APTPPL does not agree that this provision absolves APTPPL of obligations to verify the authenticity or correctness of information provided to AEMO. Further, APTPPL does not agree with the AER that including an obligation on a user to ensure that information provided to APTPPL is accurate could be contrary to the long term interests of consumers. On the contrary, the absence of such an obligation on users to provide accurate information to APTPPL is likely to lead to additional costs for APTPPL where inaccurate information is provided to either itself or AEMO. APTPPL has already been required to deal with circumstances where users have provided incorrect contract reference information to AEMO in their MOS offers which had the potential to cause APTPPL's MOS allocations for the day to be rejected and default allocations applied. This outcome would have distorted intended market outcomes and resulted in unintended wealth transfer amongst STTM Users. APTPPL has also included a definition of Contract Reference Information in the clause to clarify what information must be provided by users with accuracy.

A.9	Limitation of Liability and indemnity	*Amend clauses 87(a), 88, 89(a) and 90 to replace Gross Negligence/Wilful Misconduct with the phrase 'gross negligence or wilful misconduct'.* The AER does not accept APTPPL's proposed inclusion of the defined term 'Gross Negligence/Wilful Misconduct' as it does not consider the definition provides certainty or clarity of the meaning of the term. The AER states that it considers that gross negligence and wilful misconduct are two separate concepts and should not be merged into one definition. In its place, the AER have included a definition for Wilful Misconduct that aligns with that approved in relation to the Amadeus Gas Pipeline access arrangement, but retained gross negligence as an undefined term.	As discussed above in relation to amendment A.2, APTPPL accepts the AER's removal of the combined definition for Gross Negligence/Wilful Misconduct, as well as the AER's inclusion of a definition for Wilful Misconduct as approved in the Amadeus Gas Pipeline access arrangement. APTPPL considers, however, that certainty and clarity is improved by including a definition in the access arrangement for Gross Negligence, in place of leaving this as an undefined term. APTPPL has therefore included a definition for Gross Negligence in the revised access arrangement as follows: 'Gross Negligence means a negligent act or omission, committed with reckless disregard for the consequences and the circumstances where the negligent party knows or ought to know that those consequences would likely result from the act or omission, and which is not due to an honest mistake, oversight, error of judgement or accident'
A.10	Limitation of Liability and indemnity	*Amend clause 91 as follows:* *Nothing in this Access Arrangement limits Service Provider's rights under Queensland STTM from time to time which limit or avoid Service Provider's liability to the User or any other person.* The AER revision to clause 91 as it considers that the clause protects APTPPL's rights under any laws from time to time which limit or avoid APTPPL's liability to the User or any other person and is not limited to changes introduced to support the Queensland STTM as proposed by APTPPL. The AER therefore considers that this clause should be limited to preserving Service Provider's rights under Queensland STTM and should not limit or avoid Service Provider's liability to the User or any other person.	APTPPL accepts the AER's amendment and has included additional words at the commencement of the clause 'without limiting Service Providers' other rights,..' APTPPL considers these additional words add certainty and clarity for users as they inform users that APTPPL may have other rights which limit its liability and that these other rights are not affected.

A.11	Force Majeure	*Delete the word 'reasonable' from clause 92.* The AER requires deletion of the word 'reasonable' from the chapeau of clause 92 to change form events 'not within the reasonable control' to events 'not within the control' of a Party. The AER states its understanding that such an event is typically one over which a party to a contract has no control, for example, an event such as a cyclone, and also notes that the qualifying phrase 'that Party is not reasonably able to prevent or overcome' adds the necessary element of reasonableness to the test.	APTPPL does not accept the AER's required amendment that the word 'reasonable' be deleted. The clause is drafted with a condition precedent of 'reasonable' so that neither party is able to rely on it without first having implemented reasonable and prudent processes for dealing with events that are partly within their control. APTPPL does not agree that Force Majeure Events are limited to events for which the parties have absolutely no control. Many events which are commonly included in commercial Force Majeure clauses of this nature may be, to some extent, in the control of a Party. For example, strikes and lockouts in clause 92(b) are to some extent within the control of a party - ie a party with prudent management processes and policies may avoid a strike. For this reason, other safeguards are inserted into the clause (to prevent the spurious calling of Force Majeure) such that its effect must not be able to overcome by the exercise of due diligence, not able to be reasonably overcome or prevented. In the case of a strike, if a party could reasonably control the event or prevent or overcome it (say by settling the dispute on reasonable terms) the party would not be in a position to call Force Majeure.

A.12	Force Majeure	*Amend clause 92(a) to include the words "other acts caused" as per original clause.* The AER requires insertion of the phrase 'other acts caused by' in clause 92(a) to cover both acts caused by the elements and acts of the elements. The AER considers that originally the clause includes two types of acts: - acts of god (earthquakes, floods, washouts, landslides, lightning, storms); and - other acts caused by the elements but not necessarily the acts of the elements. With the deletion of the phrase 'other acts caused by', other acts caused by the elements are no longer covered by Force Majeure Events themselves in the amendment proposed by APTPPL. The AER does not accept the amendment as it will reduce the scope of the clause and potentially increase the liability of the parties.	APTPPL accepts the AER's amendment A.12.
A.13	Force Majeure	*Delete the word 'loss or damage' from clause 92(g).* The AER requires deletion of 'loss or damage' from clause 92(g) has it considers that a force majeure event may cause loss or damage and that the inclusion of loss or damage as Force Majeure Events themselves is illogical and unnecessary.	APTPPL accepts the AER's amendment A.13.

A.14	Force Majeure	*Amend clause 93(c) as follows:* *the inability of the User or a person supplying Gas at or upstream of the Receipt Points to obtain a supply of Gas for transportation under the Transportation Agreement; or* The AER requires deletion of 'a supply of Gas' and reinstatement of previous text which covered proving gas at a receipt point in clause 93(c). The AER considered that the replacement of 'a supply of Gas' with 'provide gas at a Receipt Point' broadens the scope of the clause and may have been intended to pick up situations where the User or a person supplying the gas can obtain a supply of Gas but for some reason may still be unable to provide gas at a Receipt Point for transportation. The AER considered that this potentially increased the liability of the User or a person supplying the gas since it reduces the scope of clause 92.	APTPPL does not accept the AER's amendment A.14 and submits the clause as previously drafted be reinstated, as follows: 'the inability of the User or a person supplying Gas at or upstream of the Receipt Points to provide gas at a Receipt Point for transportation under the Transportation Agreement;' APTPPL intends that the clause deal with all circumstances where the User is unable to provide gas at a Receipt Point, including circumstances where an upstream gas supplier fails to supply gas to the user, or where upstream facilities not owned by APTPPL have constraints eg a gas processing facility upstream of the Receipt Point shuts down or a pipeline upstream of APTPPL's pipeline has capacity constraints. Users are able to manage these risks under their contracts with gas suppliers and facility and pipeline service providers. APTPPL has no ability to manage these risks as it is not a party to these agreements. Further, APTPPL has not accepted the AER's revisions as they place certain circumstances where the User is unable to provide gas at a Receipt Point potentially within the definition of Force Majeure. The terms and conditions are necessarily limited to Force Majeure Events affecting the pipeline. It is not appropriate for the Service Provider to be required to take on the risk of Force Majeure of other parties, effectively assuming risk that sits outside the operation of the pipeline itself such as upstream producer risk.

A.15	Force Majeure	*Amend clause 93(d) as follows:* *the inability of a person, other than the User, consuming the Gas at or downstream of the Delivery Points to take gas due to any event or circumstance within the control of that person.* The AER requires amendment to clause 93(d) to remove exclusion of force majeure for situations where a person contracted with the shipper cannot take gas. The AER considered that the deletion of the phrase 'due to any event or circumstance within the control of that person' effectively means that the inability to take gas by the User or a person consuming the gas will be excluded from the consideration of a Force Majeure Event even if the circumstances giving rise to this inability are outside the control of the person. The AER considered that the proposed amendment appears to broaden the scope of clause 93(d), so that a Force Majeure Event does not apply to the inability to take gas at all. The AER therefore did not accept deletion of phrase 'due to any event or circumstance within the control of that person' as it would affect the substance of clause 93(c) and appears to increase the liability of the User or other persons consuming the gas. The AER considers that the qualification 'due to any event or circumstance within the control of that person' is reasonable for the exclusion to clause 92, for both the User and other persons consuming the gas. The AER therefore accepts the first part of the proposed amendment which changes the phrase 'a person other than the User' to 'the User or a person'. The AER does not accept the second part of the proposed amendment because it attempts to increase the liability of the User and other persons consuming the gas, which is not in the long term interest of consumers with respect to price, reliability and security of the supply of gas.	APTPPL does not accept the AER's amendment A.15 and submits the clause as previously drafted be reinstated. 'the inability of the User or a person consuming the Gas at or downstream of the Delivery Points to take gas', The reference needs to be to Users taking the gas as well as persons downstream of the Users. This is because contractually the Users are obligated to take the gas at delivery points and it is entirely within their control whether or not they take the gas whatever the downstream circumstances eg their own intended use or a third party's use of the gas. Also Users manage risks under their own insurances and with third parties under their own contractual arrangements which Service Provider is not a party to. Again, APTPPL has not accepted the AER's revisions as they place certain circumstances where the User in unable to take delivery of the gas at a Delivery Point potentially within the definition of Force Majeure. The terms and conditions are necessarily limited to Force Majeure Events affecting the pipeline. It is not appropriate for the Service Provider to be required to take on the risk of Force Majeure of other parties, effectively assuming risk that sits outside the operation of the pipeline itself such as downstream end user risk.