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Dr Mike Vertigan
Chair
Gas Market Reform Group
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Dear Dr Vertigan

DRAFT FINANCIAL REPORTING GUIDELINES FOR NON-SCHEME PIPELINES

DBP Transmission (**DBP**), DBP Development Group (**DDG**), Australian Gas Networks (**AGN**) and Multinet Gas (**MG**), as members of the Australian Gas Infrastructure Group (**AGIG**), appreciate the opportunity to respond to the Gas Market Reform Group's (**GMRG**) *Draft Financial Reporting Guidelines for Non-Scheme Pipelines Consultation Paper* (**Consultation Paper**).

About AGIG

AGIG is one of Australia's largest gas infrastructure businesses comprising a number of gas distribution and transmission pipeline businesses, including:

- DBP, the owner and operator of the Dampier to Bunbury Natural Gas Pipeline (**DBNGP**), Western Australia's most important piece of energy infrastructure. The DBNGP is WA's key gas transmission pipeline stretching almost 1600 kilometres, linking the gas fields located in the Carnarvon Basin off the Pilbara coast with population centres and industry in the south-west of the State;
- DDG, the owner and operator of a number of gas transmission pipelines and associated gas infrastructure connected to the DBNGP; and
- AGN and MG, which together make AGIG Australia's largest natural gas distribution company with around 2 million customers and over 33,000km of distribution pipelines located in five Australian states and territories.

AGIG's vision is to be the leading gas infrastructure business in Australia by delivering for customers, remaining sustainably cost efficient and being a good employer.

Focus of this submission

The Consultation Paper seeks responses to 42 specific questions contained in the provided feedback template. Our responses to these questions are contained in **Attachment A** to this letter. While these responses form the substantive component of our submission, there are two points that are made in this letter which we see are key to ensuring that the financial guidelines are implemented in a way that is consistent with and work towards achieving the overall objective stated at NGR 546(1) in Part 23 of the National Gas Rules (**NGR**). These are:

- It is important that the guideline requirements should limit the regulatory burden and additional compliance requirements for non-scheme pipelines in a way that the requirements will demonstrably progress the achievement of the stated objective of the new framework and can be practically completed by service providers. Requirements that don't demonstrably progress the objective should not be included in the first version of the financial reporting guidelines; and

- The requirement for the guidelines to include the asset valuation methodology described in NGR 569(4) conflates the information disclosure framework and the arbitration framework. The information disclosure framework has been implemented to assist parties achieve a commercially negotiated outcome. Asset valuation methodologies are relevant to the arbitration process, not the information disclosure and commercial negotiation parts of the framework. We are of the view that including the NGR 569(4) asset valuation methodology in the financial reporting guidelines is inconsistent with the objective in NGR 546 and the intent in establishing a commercial negotiation framework.

Meeting the Objective

Whenever implementing any new regulatory requirement, we consider it an important goal that compliance costs are minimised to those necessary to meet the objective of the regime. As new regulations are implemented, it is important to be mindful of the impact that they will have on the cost of providing services and eventual prices for customers. Furthermore, any new regulatory obligation should demonstrably contribute to the achievement of stated objectives of the new law.

We are of the view that there are a number of requirements in the Draft Financial Reporting Guidelines that either present a challenge for the pipeline service providers to comply with without having to incur additional costs, or they do not seem to be relevant the objective of the framework. While more detail is contained response to some of the GMRG's questions in Attachment A, we raise two key examples here:

1. The requirement to publish entity level financial reports, which by their nature, consolidate the financial information of a number of assets, which may or may not be non-scheme pipelines. We do not see a clear explanation of the relevance to the objective in NGR 546 in the consultation paper.

   We understand from the round table discussion held with pipeline service providers on 18 October that one of the reasons to require the publication of such reports may be for stakeholders to compare the return being earned by the consolidated entity with the commercial return of the specific non-scheme pipeline subject to the regime. However, we believe that a comparison of this nature will most likely be inconsistent with the intent of the regime and will be misleading.

   If implemented, it would suggest that if the consolidated entity level return is, or is even perceived to be, higher than the return to be earned under the specific service being negotiated on a particular non scheme pipeline, the shipper (or similarly the arbitrator) should be entitled to negotiate/determine a lower tariff (or implied lower return on capital) so as to somehow make up for a perceived over-recovery somewhere else. There could be a number of reasons why an entity may have a consolidated rate of return that is higher than the return to be earned for the particular service that is the subject of a negotiation. For example, the entity may be engaged in several businesses which are not gas pipelines.

   We note that the framework in Part 23 seeks to achieve prices and other terms that as far as reasonably practical reflect the outcomes of a workably competitive market. In that regard, when it comes to the rate of return for a non-scheme pipeline, the framework requires it to be one that is *"a commercial rate of return that is commensurate with the prevailing conditions in the market for funds and reflects the risks the service provider faces in providing the pipeline service"*[1], rather than a return that is influenced by perceived under/over-recovery at a group or parent level.

   While we acknowledge that these sorts of reports may well be, in most cases, freely available to anyone through ASIC – and therefore prospective users can make these comparisons if they so wish – the inclusion of this requirement in the reporting guidelines implies they have relevance to the shipper or arbitrator decision-making when evaluating a service provider's offer.

[1] NGR 569(3)

2. In regards to pipeline financial reports, we think that many challenges with practically complying with the financial reporting requirements for a specific pipeline would be avoided if the report is restricted to reporting only the information required to report Earnings Before Interest and Tax (EBIT). This is because, in practice, it is common to finance assets at a group level. Under this commonly deployed approach, interest costs are therefore not recorded against specific assets. The same applies with respect to service providers who form part of a consolidated tax group of a business – the actual tax expense quite often are not reported against specific assets.

NGR 569(4) Asset Valuation

The inclusion of the asset valuation methodology described in NGR 569(4) as a reporting requirement contained in pipeline financial reports, we believe, is inconsistent with the intention of Part 23 of the NGR, the objective in NGR 546 - that is that this is a framework seeking to encourage a commercially negotiated outcome with limited recourse to the arbitration framework.

We say this because:

- The draft financial reporting guidelines, if adopted, would require the service provider to report two asset base values - one in the balance sheet consistent with accounting standards and the other prepared to the GMRG's recovered capital method.

  Requiring two asset valuations is inconsistent with the intent articulated by the GMRG throughout the consultation process that all prospective shippers needed was access to enough information to easily establish as 'rough and ready tariff' for a non-scheme pipeline. Having two asset bases reported, one in the balance sheet based on book value and the other based on NGR 569(4) seems to be unnecessary to achieve this aim.

- Within the overall context of the new Part 23 framework, NGR 569(4) is a rule relevant to the pricing and other principles that the arbitrator is to take into consideration when making a final access determination. Arbitration is intended to be used after the parties have been unable to negotiate a commercial outcome. Requiring this information to be available before the commercial negotiation stage has even commenced will create a real risk that the parties will not only not adopt a commercial approach to the negotiation stage but are likely to move to arbitration at the earliest opportunity, thereby shortcutting the process outlined in Part 23 of the NGR..

  Furthermore, this type of information is not the type of information that would be available during negotiations in a workably competitive market.

  We also note that the framework requires the arbitrator to contemplate whether "*the value of any assets used in the provision of pipeline service must be determined using asset valuations consistent with the objective of the Part set out in rule 546(1)*". We suggest that it is only where the value of any assets determined is inconsistent with the **objective** is the value to be calculated by way of the GMRG's recovered capital method, prescribed in NGR 569 (4)(b).

I hope the key points made above are received in the constructive way they are intended and we look forward to continuing to work collaboratively with the GMRG in its future work. Finally, I refer you to the points made in response to the GMRG's specific questions in **Attachment A.**

Yours sincerely

Anthony Cribb
General Manager – Corporate Services and Company Secretary