# Draft Financial Reporting Guidelines

## Submission to the Gas Market Reform Group

03/11/2017

## Introduction

The Australian Pipelines and Gas Association (APGA) welcomes the opportunity to respond to the Gas Market Reform Group's (GMRG) Draft Financial Reporting Guideline.

APGA is the peak body representing Australasia's pipeline infrastructure, with a focus on gas transmission, but also including transportation of other products, such as oil, water and slurry. Our members include constructors, owners, operators, advisers, engineering companies and suppliers of pipeline products and services.

APGA's members build, own and operate the gas transmission infrastructure connecting the disparate gas supply basins and demand centres of Australia, offering a wide range of services to gas producers, retailers and users. The replacement value of Australia's gas transmission infrastructure is estimated to be $50 billion.

APGA is an active participant in the GMRG's process to develop the new information disclosure and arbitration framework for non-scheme pipelines. APGA is concerned that the reform has established a framework that is more prescriptive and interventionist that the recommendation, made to the CoAG Energy Council in December 2016, for a regime of enhanced commercial negotiation with the backstop of binding arbitration. There are a number of issues arising in this consultation that continue the trend.

Commercial negotiations between service providers and shippers are fundamental to the gas transportation agreements that set out the terms and conditions under which gas is transported around Australia. Ensuring an appropriate balance between information to support these negotiations and promoting timely and effective negotiations is vital.

An overemphasis on historical costs and detailed information may only serve to slow negotiations as parties waste considerable time debating the relevance and accuracy of information that is not relevant to the service being sought. Commercial entities are far more focussed on future business conditions and appropriate allocation of risk.

APGA discussions with service providers and shippers indicate that there is much confusion as to the relevance and utility of the information proposed in the Guideline.

## Key issues with matters raised in Draft Guidelines

### Level of detail proposed

The objective of the information disclosure and arbitration regime is set out in rule 546 of Part 23 of the National Gas Rules:

*546 Objective*

*(1) The objective of this Part is to facilitate access to pipeline services on non-scheme pipelines on reasonable terms, which, for the purposes of this Part, is taken to mean at prices and on other terms and conditions that, so far as practical, reflect the outcomes of a workably competitive market.*

*(2) This Part is intended to contribute to achieving the objective in subrule (1) by means of:*

> *(a) requirements for the publication and exchange of information to facilitate timely and effective commercial negotiations in relation to access to non-scheme pipelines;*
>
> *(b) a commercially-orientated arbitration process to resolve access disputes in a cost-effective and efficient manner; and*
>
> *(c) principles that the arbitrator must have regard to when determining access disputes,*

The Consultation Paper states on page 1:

*Financial and weighted average price information is intended to assist prospective users to carry out a high-level assessment of the reasonableness of the service provider's standing price, as well as the terms and conditions associated with the service.*

APGA supports the intent of the information to be assistance in carrying out a high-level assessment of the reasonableness of the service provider's standing price.

The level of detail proposed in the draft Guidelines for the publishing of information is well beyond that required to:

- facilitate timely and effective commercial negotiation as set out in 546(2)(a); or
- carry out a high-level assessment of the reasonableness of any offer as set out in the consultation paper.

APGA members report that the information proposed for publication is not consistent with the information that shippers have requested during past commercial negotiation nor is APGA aware of any current or prospective users calling for such a level of detail during the progress of these reforms.

## Examples

By way of example, when reporting direct costs as part of the income sheet, a service provider is expected to report:

- Repairs and maintenance;
- Wages;
- Depreciation;
- Insurance;
- Licence and regulatory costs;
- Directly attributable finance charges;
- Leasing and rental costs; and
- Other direct costs.

The report for indirect costs is similarly granular.

All of this information is *historical* in nature. It is unclear how such a breakdown could assist in the carrying out of a high-level assessment of reasonableness of proposed *future* tariffs. With regard to costs, APGA would expect that a prospective user is interested in:

1. A single line item: operating expenses; and
2. An appropriate level of certification by an independent auditor or company officer.

Other examples of unnecessary detail include most of the notes to the pipeline statements; the liability components of the balance sheets and other detailed line items in the income statements.

## Impact on cost

It is clear that the new information obligations, and the requirement to certify them, will add significant costs to the provision of pipeline services. It is also clear that preparation and certification costs will increase as granularity increases.

As noted above, it is not clear that the level of granularity proposed will materially improve:

- the facilitation of timely and effective commercial negotiation as set out in 546(2)(a); or
- the carrying out a high-level assessment of the reasonableness of any offer as set out in the consultation paper.

APGA recommends that the GMRG work closely with stakeholders, including auditors, to establish a relevant set of information that will achieve the intent of the regime at lowest cost.

It is important that both the information to be provided and the level of certification required fairly balances the benefit a prospective user derives from that data and its certification against the costs of providing it.

## Requirement to publish an asset valuation in accordance with rule 569(4)

Rule 569 sets out the principles that an arbitrator must apply during an access dispute.

Rule 569(4) sets out the principles that an arbitrator must apply in determining an asset value during an access dispute, primarily that the asset valuation technique used must be consistent with the objective of Part 23, being that pipeline services on non-scheme pipelines are accessible on reasonable terms which is taken to mean at prices that so far as practical reflect the outcomes of a workably competitive market.

As rule 546(2) sets out, the purpose of information publication (covered under 2(a)) and the pricing principles (covered under 2(b)) are not the same. The pricing principles relate to the price of access to a particular pipeline service whereas information is published at an entity or pipeline level of detail.

APGA has three key concerns:

1. Requiring service providers to publish an estimate of an asset valuation following the recovered capital methodology may undermine negotiations by encouraging the party who perceives its position to be supported by that value to seek arbitration. Further, any 569(4) asset valuation published by a service provider would not binding on the arbitrator, and it is therefore premature to report it. The arbitrator will publish the asset value (if relevant to the arbitration) under 581(g).
2. There is significant uncertainty over what asset valuation techniques may actually satisfy rule 569(4). Different data, assumptions and methodologies will produce different results which will still being consistent with the rule. Different arbitration decisions on the same pipeline will also potentially determine different values.
3. Any requirements for certification of a valuation following the recovered capital method is likely to be highly complex and costly for older pipelines. Initial feedback from auditors is that the certification requirements are outside those required under the relevant Australian standards and will be very costly to implement.

APGA is aware that the GMRG holds the view that, as arbitration is 'on the papers', any information required during arbitration must be presented through publication or negotiation. This is not the case.

Rule 568(1) sets out that is a party to an access dispute must seek leave to rely on any information that was not provided during negotiation. It does not bind the arbitrator to also only use information provided during negotiation.

Rule 568(3) sets out that arbitrator can direct a party to provide information that it did not provide during a negotiation.