

IN THE WESTERN AUSTRALIAN ELECTRICITY REVIEW BOARD (IN ITS CAPACITY AS THE LOCAL APPEALS BOARD PURSUANT TO THE NATIONAL GAS ACCESS (WA) ACT 2009, THE NATIONAL GAS ACCESS (WA) (PART 2) REGULATIONS 2009 AND THE ENERGY ARBITRATION AND REVIEW ACT (WA) 1998)

No 1 of 2010

Re Application for review of the decision by the Western Australian Economic Regulation Authority dated 5 August 2010 to draft and approve its own revised Access Arrangement to apply to the Goldfields Gas Pipeline

Application by:

BHP BILLITON NICKEL WEST PTY LTD

Applicant

No 2 of 2010

Re Application for review of the decision by the Western Australian Economic Regulation Authority dated 5 August 2010 to draft and approve its own revised Access Arrangement to apply to the Goldfields Gas Pipeline

Application by:

**SOUTHERN CROSS PIPELINES AUSTRALIA PTY LTD
SOUTHERN CROSS PIPELINES (NPL) AUSTRALIA PTY LTD
ALINTA DEWAP PTY LTD
GOLDFIELDS GAS TRANSMISSION PTY LTD**

Applicant

**BHP BILLITON NICKEL WEST PTY LTD
OUTLINE OF SUBMISSIONS IN NO 1 OF 2010**

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Capitalised terms used in this document utilise the definitions contained in the National Third Party Access Code for Natural Gas Pipeline Systems contained in Schedule 2 of the Gas Pipelines Access (Western Australia) Act 1998 (WA) (Code), and the defined terms in the applicant's statement of issues facts and contentions, unless otherwise defined in this document.

MERITS REVIEW OF THE REGULATOR'S DECISION

- 1 BHPB applies for Review by the Board of the Regulator's decision to approve its own access arrangement pursuant to section 2.26 of the Code (being a decision pursuant to sections 2.41 and 2.20(a) and accordingly within section 2.26).
- 2 Pursuant to section 57 of the *Gas Pipelines Access (Western Australia) Act 1998 (GPA Act)*:
 - (a) the Review is to be conducted by way of a fresh hearing;¹ and
 - (b) the Board is not bound by the rules of evidence and must act according to equity, good conscience and the substantial merits of the case and without regard to technicalities and forms.
- 3 Section 39(2)(a)(i), (ii) & (iii) of Schedule 1 to the GPA Act (**GPA Law**) provide that an application for a review of a Regulator's decision to approve its own access arrangement may be made only on the grounds:
 - (a) of an error in the Regulator's finding of facts; or
 - (b) that the exercise of the Regulator's discretion was incorrect or was unreasonable having regard to all the circumstances; or
 - (c) that the occasion for exercising the discretion did not arise.
- 4 The Board may make an order affirming, or setting aside or varying immediately or as from a specified future date the decision under review and may exercise the same powers as may be exercised by the Regulator: section 38(9) of the GPA Law.²

¹ Once error is established on a permissible ground of review the Board is required to reach its own view on the facts and discretions which are to be decided and exercised: *Bradshaw v Medical Board (WA)* (1990) 3 WAR 322 at 325-328 per Kennedy J.

² which applies by virtue of section 39(6) of the GPA Law.

5 BHPB submits that, in approving its own access arrangement, the Regulator exercised its discretion incorrectly and unreasonably having regard to all the circumstances.

6 BHPB accepts that the exercise of discretion by the Regulator will not be incorrect or unreasonable simply because the Board considers that a different decision would be preferable.³ BHPB is required to and will establish:

- (a) that there was an error made in exercising the discretion in that the Regulator acted upon a wrong principle, allowed extraneous or irrelevant matters to guide or affect it, mistook the facts and/or did not take into account a material consideration;⁴ and/or
- (b) that the decision of the Regulator was so “unreasonable or plainly unjust” in all the circumstances that failure properly to exercise the discretion will be inferred from the character of the result.⁵

7 Incorrectness and unreasonableness within the meaning of section 39(2)(a)(ii) of the GPA Law are to be determined by reference to applicable criteria contained in the Code applied to the matters which were before the Regulator before the decision under review was made.⁶

THE CODE

8 The Code establishes a regime for the regulation of covered pipelines in Australia.

9 The Code has its origins in the *Hilmer Report 1993*, which recognises that competition policy should include a limited prices oversight mechanism (in addition to regulatory reform) to prevent instances of “monopoly pricing” which will promote a competitive market: *Hilmer* at Part 12, pages 309, 329.

³ *Envestra Limited v Essential Services Commission of South Australia (No 2)* [2007] SADC 90, per the Court at [37]; *Australian Competition & Consumer Commission v Australian Competition Tribunal (No 2)* [2006] FCAFC 127, per the Court at [7]; *House v The King* (1936) 55 CLR 499 (*House*), per Dixon, Evatt and McTiernan JJ at 505.

⁴ *East Australia Pipeline Pty Ltd v ACCC* [2007] HCA 44; 223 CLR 299 (*EAPL*) per Gummow and Hayne JJ at [79]-[80]; *Application by Epic Energy South Australia Pty Ltd* [2003] ACompT 5 (*Epic 2003*) per the Tribunal, Cooper J presiding, at [11] [2004] ATPR 41-977 at 48,442; *House* per Dixon, Evatt and McTiernan JJ at 505.

⁵ *EAPL* per Gummow and Hayne JJ at [79]-[80]; *Application by Epic Energy South Australia Pty Ltd* [2002] ACompT 4 (*Epic 2002*), per the Tribunal, Cooper J presiding at [30]; *Epic 2003* per the Tribunal, Cooper J presiding, at [11]; *House* per Dixon, Evatt and McTiernan JJ at 505.

⁶ *Epic 2002*, per the Tribunal, Cooper J presiding at [30].

- 10 The Code reflects the Hilmer approach in the Introduction to the Code and ss 8.1 and 2.24 of the Code, which seek to prevent the abuse of monopoly power and balance the conflicting interests between Service Providers and Users of Covered Pipelines.
- 11 GGT sought but failed to have coverage of the GGP revoked in 2004. The Minister for Energy's Decision was based on him being satisfied that access or increased access to Services provided by means of the Pipeline would promote competition in another market.⁷ The Minister was satisfied that GGT does not face effective competition in any relevant market, the commercial incentives will not constrain pricing to the competitive level (that which is based on long run economic costs), and that GGT would have the ability and incentive to engage in monopoly pricing in the absence of access regulation.

SCOPE OF SUBMISSIONS

- 12 BHPB reserves the right to supplement these submissions once it has had access to all of the relevant materials specified in section 39(5) of the GPA Law. It addresses below only its contentions that the Regulator:
- (a) has failed to allocate costs across Services properly in setting the Reference Tariff; and
 - (b) has failed to 'true up' the Reference Tariff to take account of the higher Reference Tariff that applied during the Delayed Start Period.

ALLOCATION OF COSTS OF SERVICES

- 13 This issue concerns the Regulator's decision to:
- (a) calculate the Reference Tariff on the basis that the capital costs, operating costs and Capacity of *only* the covered part of the GGP (**Covered GGP**) should be brought to account in determining the Total Revenue; and
 - (b) determine that the Services to be provided using *only* the Covered GGP (i.e. the Reference Service) should be used to derive a Reference Tariff for the GGP.⁸

⁷ Decision on Coverage, 2 July 2004 p 3.

⁸ Final Decision para 59.

- 14 The effect of these decisions is that the whole of the cost of assets that are used jointly to provide the Reference Service and Additional Services would be recovered from only Users of the Reference Service.
- 15 BHPB's submission is that the Reference Tariff should have been determined by reference to Total Revenue, which should have been calculated by reference to the cost of providing all Services. Those costs include the capital and non capital costs of the New Compressors and all or part of the Additional Services.
- 16 The objectives of the Code are, relevantly, to prevent abuse of monopoly power, promote a competitive market for natural gas and provide rights of access on terms that are fair and reasonable: Code Introduction (b), (c) & (d), s 2.24 and s 8.1. In construing the Code consideration should be given to its Introduction to confirm meaning or determine meaning where a provision is ambiguous or obscure or its ordinary meaning leads to a manifestly absurd or unreasonable result: section: 10.5 of the Code. An interpretation that best meets the objectives of the Code is to be preferred to one which fails to meet those objectives.⁹
- 17 Having regard to those objectives, the Code should have been construed by the Regulator so that the costs of providing Services are allocated effectively across all Services which use covered infrastructure. That construction is necessary to ensure that:
- (a) GGT is not able to leverage off the original capital base of the Covered Pipeline (which on its interpretation is to be fully paid by Users of Reference Services) to earn monopoly profits from new Users charged the same or higher effective price, when GGT need only recoup the incremental costs of the Expansions of Capacity;¹⁰

⁹ *Re D Ken Michael AM; Ex Parte Epic Energy (WA) Nominees Pty Ltd & Anor* (2002) ATPR 41-886 at [130]-[131] per Parker J, Malcom CJ and Anderson J concurring; *Project Blue Sky Inc & Ors v Australian Broadcasting Authority* (1998) 194 CLR 355 (**Project Blue Sky**) at [71] & [78] per McHugh, Gummow, Kirby and Hayne JJ. No word is to be considered superfluous or insignificant if by any other construction it can be made useful and pertinent: *Project Blue Sky* at [71]; *Visy Paper Pty Ltd v ACCC* (2003) 216 CLR 1 at 24 [70]-[78] per Kirby J and *News Ltd v Australian Rugby Football League Ltd* (1996) 58 FCR 447 at 533-534 per Burchett J; s 15AA of the *Acts Interpretation Act 1901* which provides that a construction which promotes the purpose or object of the relevant Act is to be preferred to a construction which would not.

¹⁰ We note that in the NERA report annexed to the GGT's Response to Final Decision, it is acknowledged that the prices charged to new Users are in excess of the prevailing Reference Tariff despite the Reference Tariff being currently calculated to recover the full joint costs: Economic Impact of Proposed Expansion Policy, NERA, 4 June 2010, page 7.

- (b) all Users of the Covered Pipeline share those costs, rather than Users of the Reference Service paying a higher Reference Tariff and so subsidising Users of the Expansions of Capacity (as the Regulator found in its Draft Decision at [190]);
 - (c) the operation of the Covered Pipeline is economically efficient: section 2.24(d) of the Code; and
 - (d) the Reference Tariff and Reference Tariff Policy replicate the outcome in a competitive market and do not distort investment decisions in Pipeline transportation systems or in upstream and downstream industries: section 8.1(b)&(d) of the Code.
- 18 The Reference Tariff should provide GGT the opportunity to recover the efficient costs of delivering the Reference Service over the expected life of the assets used in delivering that Service: section 8.1(a) of the Code. The Reference Service is the receipt of Gas at the Inlet Point, the transmission of Gas to, and the delivery of Gas at, agreed Outlet Points: Access Arrangement clause 4.1(b) and clause 4 of the General Terms and Conditions. Sales of Additional Services provide an avenue to recover a share of the cost of the assets that jointly provide Reference Services and Additional Services. If the contribution of sales of Additional Services to the recovery of costs that are shared between Reference Services and Additional Services is ignored when setting Reference Tariffs, it follows that the Reference Tariffs will enable materially more than the efficient cost of delivering the Reference Service to be recovered over the expected life of the relevant assets.
- 19 The Regulator was required in determining the Reference Tariff and Reference Tariff Policy to be satisfied:
- (a) that the revenue to be generated from all Services (**Total Revenue**) was established consistently with section 8 of the Code: section 8.2(a) of the Code; and
 - (b) to the extent that the Covered Pipeline is used to provide a number of Services, that the portion of Total Revenue that the Reference Tariff was designed to recover was calculated consistently with section 8 of the Code: section 8.2(b) of the Code.

- 20 Total Revenue should be calculated pursuant to section 8.4 of the Code according to the Cost of Service methodology to equal “the cost of providing all Services”, to be calculated on the basis of:
- (a) a return (**Rate of Return**) on the value of the capital assets that form the Covered Pipeline or are otherwise used to provide Services (**Capital Base**);
 - (b) depreciation on the Capital Base (**Depreciation**); and
 - (c) the operating, maintenance and other non-capital costs incurred in providing all Services (**Non-Capital Costs**).
- 21 “Services” relevantly means services “provided by means of a Covered Pipeline”, including (without limitation) haulage services, the right to interconnect and “services ancillary to the provision of such services”: section 10.8 of the Code. Haulage services are the point to point services for the transportation of gas from inlet to outlet specified in the Access Arrangement.¹¹
- 22 The Covered Pipeline is the system of pipes for transporting natural gas from point to point between Yarraloola and Kalgoorlie and any tanks, reservoirs, machinery or equipment directly attached to the system of pipes: section 2 of the GPA Law, section 10.8 of, and Schedule A (at p 9(iii)) to, the Code. In other words, the Covered Pipeline is the physical asset by means of which Services, including all or part of the Additional Services, are delivered.
- 23 The definition of Service(s) is broad and inclusive.¹² The inclusion of ancillary services means that services which are not strictly or wholly provided “by means of a Covered Pipeline” are included within the definition of Service(s).¹³ Moreover, the natural and ordinary meaning of the provision of services “by means of a Covered Pipeline” encompasses the supply or furnishing of services in a wider sense to encompass the control of the operation of the pipeline system to enable gas to enter, be transmitted or hauled through the pipes, and to exit.¹⁴

¹¹ Haulage service is appropriately defined on a point to point basis rather than by reference to the market(s) which it serves: *Duke Eastern Gas Pipeline Pty Ltd* (2001) ATPR 41-821 162 FLR 1 (**Duke**) at [70] per the Tribunal Hely J, Dr MJ Messenger and MM Starrs.

¹² *Duke* at [68].

¹³ *Alinta Asset management Pty Ltd v Essential Services Commission (Alinta)* [2008] VSCA 273 per Dodds-Streton JA at [141], Ashley JA concurring at [4]-[5].

¹⁴ *Alinta* per Dodds-Streton at [188], Ashley JA concurring t [4]-[5].

- 24 In BHPB’s submission, “service(s) provided by means of a Covered Pipeline” includes all services which are provided ‘using’¹⁵, or ‘by the use of’¹⁶ or ‘by the agency or instrumentality of’¹⁷ or ‘in consequence of, by reason of, owing to’¹⁸ the Covered Pipeline, and by definition ‘Services’ also include all other services ancillary to such services. ‘By means of’ does not mean ‘*only* by means of’ or ‘using *only*’ or ‘by reason *only* of’ the Covered Pipeline.
- 25 The Covered Pipeline is required in order to provide the Additional Services. All or part of those services can only be provided using it (with the New Compressors), and they are accordingly ‘Services’ within the meaning of the Code.
- 26 Alternatively, the relevant Additional Services are services ancillary to the provision of services provided by means of the Covered Pipeline, and are accordingly also ‘Services’.
- 27 As all or part of the Additional Services fall within the meaning of Services, the capital and non-capital costs of constructing, acquiring, developing, operating and maintaining them must fall within the meaning of “cost of providing all Services” in section 8.4 of the Code. Those costs must accordingly be used to calculate the Total Revenue under that section and the Total Revenue so calculated must be used to determine the Reference Tariff.
- 28 Moreover, pursuant to section 8.43 of the Code, the Reference Tariff should be designed so that a particular User’s share of the portion of Total Revenue to be recovered from sales of the Reference Service is consistent with section 8.38 of the Code.
- 29 The portion of the Total Revenue that the Reference Tariff should be designed to recover should, pursuant to section 8.38 of the Code, include:
- (a) all of the Total Revenue that reflects costs directly attributable to the Reference Service; and
 - (b) “a share of the Total Revenue that reflects costs incurred (including capital costs) that are attributable to providing the Reference Service jointly with other

¹⁵ Cf *Alinta* at [253]-[254] per Hansen AJA.

¹⁶ *The Macquarie Dictionary* 5th Edition 2009.

¹⁷ *Hughes v Munro* (1909) 9 CLR 289.

¹⁸ *The New Shorter Oxford Dictionary*.

Services, with this share to be determined in accordance with a methodology that meets the objectives in section 8.1 and is otherwise fair and reasonable.”

- 30 The Regulator was accordingly required to share the Total Revenue (costs) across all Services where attributable to providing the Reference Service jointly with other Services.
- 31 This approach was identified as the correct approach by the Productivity Commission in its 2004 Review of the Gas Access Regime, pages 240-241 and fig 7.1 of which are extracted below.

Building block approach and reference tariffs

The Gas Access Regime is a form of cost-based price regulation using what is known as the ‘building block’ approach. In particular, a target is calculated for *expected* total revenue by building up the cost base from its individual components. This requires, among other things, forecasts of future capital expenditure, operating costs and demand. The expected total revenue target is then used to set regulated prices — termed reference tariffs — for individual reference services (services specified in an access arrangement with an associated reference tariff) (figure 7.1).

Each reference tariff generally has to be set so as to recover the costs expected to be incurred in providing the relevant reference service, as reflected in the composition of target revenue (s.8.38). A portion of target revenue might be attributable to services that are not reference services and so do not have an associated reference tariff. Hence, joint costs — including the large portion attributable to capital — have to be allocated between regulated and unregulated services. The Australian Pipeline Industry Association (APIA) argued that taking the additional step of allocating costs between different reference services was undesirable:

... limiting cost allocation requirements under the Gas Code to the issue of cost allocation between the regulated and unregulated business would be a significant step in limiting the impact of regulator imposed information requirements on the day to day operations of the service provider. (sub. DR100, p. 57)

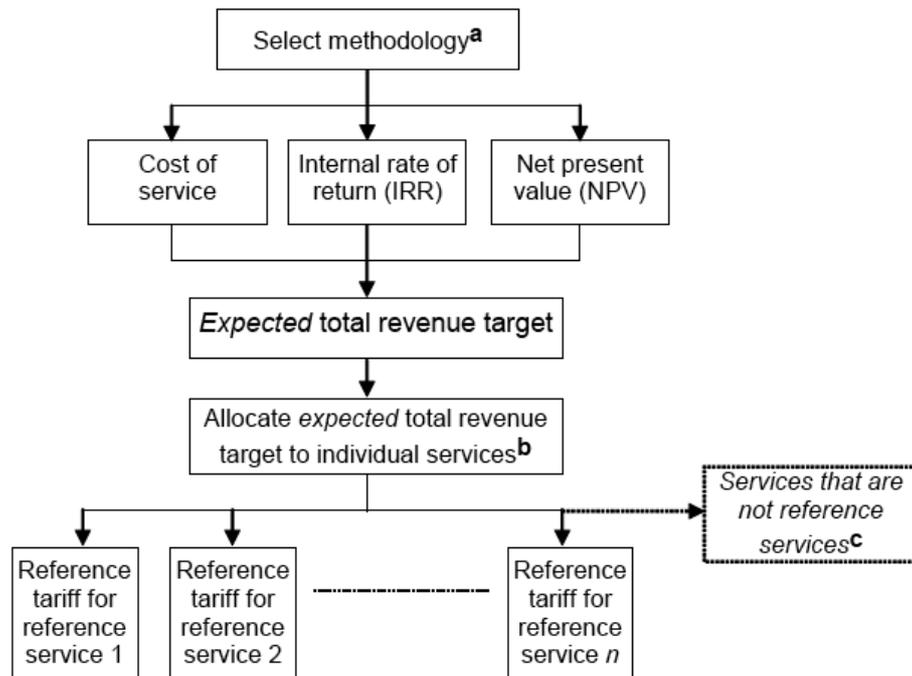
Reference tariffs are intended to be a reference point against which service providers and users can negotiate market-based outcomes:

The reference tariff serves as a benchmark price at which a prospective user is entitled to gain access to services and applies only to the reference service as defined in the access arrangement. ... the [Gas] Code explicitly preserves the right of service

providers and users to enter into negotiated contractual arrangements. Similarly, tariffs can be negotiated if the service required by the user is different to the reference service. (ACCC 2002a, p. 21)

However, as noted in chapter 3, the Gas Access Regime's building block approach has tended to inhibit commercial negotiations.

Figure 7.1 Determination of reference tariffs



^a Methods other than the three shown in the diagram can be used, but only if the resulting total revenue target can be expressed in terms of one of the three methods. ^b The portion of total revenue that a reference tariff recovers for a particular service should generally be attributable to the costs of providing that service (including costs incurred jointly with other services) (s.8.38). ^c Part of the revenue target might be attributable to services that are not specified in the access arrangement with an associated reference tariff.

Source: Gas Code.

- 32 Set out in Annexure A to this submission is a flow chart identifying the process required to be undertaken by the Regulator under the Code in setting the Reference Tariff.
- 33 In its Final Decision, the Regulator accordingly erred in:
- (a) apparently, although not expressly, construing 'Service' to be limited to the Reference Service the subject of the Access Arrangement (Final Decision [57]-[60]);

- (b) deciding that it was confined to considering only the price and terms of access required for the Covered Pipeline without regard to the GGP as a whole (Final Decision [57] & [60]); and
 - (c) as a result, not having regard to the capital costs, operating costs and Capacity of the New Compressors and all or part of the Additional Services in determining the Total Revenue.
- 34 The Regulator accordingly erred in having regard to an irrelevant consideration in setting the Reference Tariff, namely GGT's submissions in relation to the consequences of its election. In doing so, the Regulator misunderstood and misapplied the Code. Whatever the true meaning and effect of GGT's election and its consequences, they are irrelevant to the meaning of "Service(s)".
- 35 BHPB accordingly submits that the exercise of the Regulator's discretion was incorrect and unreasonable as the Regulator:
- (a) did not determine the Reference Tariff by reference to applicable criteria contained in the Code applied to the matters which were before the Regulator before the decision under review was made;
 - (b) acted upon a wrong principle in misconstruing the Code and in particular the definition of "Service(s)";
 - (c) allowed irrelevant matters to affect it in reversing its Draft Decision based on GGT's submissions; and
 - (d) did not take into account matters properly found to be material considerations in its Draft Decision, in particular the relevant costs of the New Compressors and Additional Services.
- 36 In BHPB's submission the Regulator erred in calculating the Reference Tariff on the assumption that the whole of the cost of the shared assets should be recovered through Reference Tariffs, irrespective of the fact that those assets are also used to serve customers who are not on Reference Tariffs (namely those customers that are using the so-called 'uncovered capacity').

- 37 The Regulator's Further Final Decision model and Draft Decision model (which included volume and cost information for non covered load) permit the following different allocations between Reference and non-reference Services to be tested:
- (a) Reservations – where the shared costs are allocated based upon the relative capacity that is reserved by the Reference and non-reference Services;
 - (b) Reservation * Distance – where the shared costs are allocated based upon the relative size (between reference and non-reference) of the product of the capacity reservation and distance of the pipeline that is used. This allocator allows for the fact that different users may use different space in a given length of the pipe, as well as different lengths of the pipe; and
 - (c) Weighted average of Reservation and Reservation * Distance – a combination of the previous two allocators. The motivation for this allocator is that pipeline charges are based upon both reservation and reservation * distance (the weighting that the Regulator has applied for tariff setting are the natural means of weighing these two dimensions of use).
- 38 BHPB submits that the third method of allocation (Weighted average of Reservation and Reservation * Distance) is most appropriate in this case. This is on the basis that, the method of allocation seeks to allocate costs between the Reference and non-reference Services explicitly on the basis of each Service's relative use of the shared assets. Furthermore, this measure of relative use is the same as that used by the Regulator in determining the current Reference Tariff (the weights applied for reservation and reservation * distance are the weights used for the Reference Tariff) and hence is the same measure of relative use that is used to allocate the Capital Costs between Users of the Reference Service (the section 8.42 allocation). As such, it has been endorsed already by the Regulator as the relevant measure.
- 39 In order to calculate the correct allocation it is necessary to specify which assets are shared and the extent to which they are deemed to be shared. BHPB submits that the appropriate assumption for present purposes is that the pipeline, main line valve and scraper stations, receipt and delivery point facilities, SCADA and communications, cathodic protection, maintenance bases and depots are shared assets. The model does not share compressor costs. In calculations that are presented in these submissions, all of the non capital costs that the Regulator used to calculate the Reference Tariff have

been assumed (implicitly) to have been incurred solely for the provision of Reference Services. BHPB has not been able to ascertain at this stage whether this assumption is reasonable. To the extent that this assumption is unreasonable, then the Reference Tariff calculations presented herein would overstate the correct Reference Tariff and so further reduction would be required.

40 Attached as Annexure B to this submission is a spreadsheet setting out various calculations and input data from the Regulator's models to calculate the correct Reference Tariff which is consistent with the process identified in Annexure A. The calculations that are presented in this spreadsheet take account of the fact that the former Reference Tariff continued to apply prior to 20 August 2010, and that an excessive Reference Tariff (for the reasons presented in this ground) continued to apply thereafter, with the assumption that a new (correct) Reference Tariff would apply from 1 July 2011. In addition, a tariff calculation is presented (step 7 in Annexure B) which replicates the Regulator's calculation, whereby each component of the Reference Tariff is set to recover a target proportion of the Total Revenue that is allocated to Reference Services. This calculation shows that if the Regulator's method was precisely replicated, then the "reservation", "reservation * distance" and "throughput * distance" components to the Reference Tariff would be 22.10%, 21.08% and 19.31% lower than the components of the Regulator's Reference Tariff, respectively.¹⁹

41 The table below sets out the results for each of the three allocation methods discussed above, expressed for simplicity in the first instance as a common reduction of each of the components of the Regulator's Reference Tariff. For each allocation, three assumptions are adopted about the time of commencement of the correct Reference Tariff – namely (1) that the correct Reference Tariff commenced on 1 January 2010 (first column of results); (2) that the correct Reference Tariff commenced from 20 August 2010 and account is taken of the actual tariff prior to that time (second column of results); and (3) that the correct Reference Tariff commences from 1 July 2011 and account is taken of the actual tariff prior to that time (third column of results). Price reductions compared to the reference tariffs the Regulator determined on different assumptions as to Reference Tariff Commencement Date, are set out below.

¹⁹ For the purposes of the Annexure B spreadsheet, BHPB has assumed that the costs of the New Compressors are included within Total Revenue. However, this does not have a bearing on the final determination of the Reference Tariff.

Type of allocation	Reference Tariff	Tariff is applied from 1 January 2010	Scenario 2 - Tariff is applied from 20 August 2010	Scenario 3 - Tariff is applied from 1 July 2011
Reservation	Reservation component	-17.89%	-23.84%	-31.09%
	Reservation * Distance component	-17.89%	-23.06%	-30.03%
	Throughput component	-17.89%	-21.70%	-28.27%
Reservation *Distance	Reservation component	-11.15%	-15.87%	-20.70%
	Reservation * Distance component	-11.15%	-15.11%	-19.68%
	Throughput component	-11.15%	-13.74%	-17.90%
Weighted average of Reservation and Reservation * Distance	Reservation component	-12.06%	-16.95%	-22.10%
	Reservation * Distance component	-12.06%	-16.19%	-21.08%
	Throughput component	-12.06%	-14.82%	-19.31%

42 Thus, under the allocator BHPB submits is most appropriate, the allocation of shared costs to non reference services would result in a reduction against the Regulator's Reference Tariff of 12.06%, before any correction has been made for the fact that this tariff did not commence on 1 January 2010 as the Regulator's calculations assume.

43 As set out above, the Regulator's model applies the allocation methodologies described above to indicate the reduction to the Reference Tariff required at three time frames (1 January 2010, 20 August 2010 and 1 July 2011 on the assumption that the Reference Tariffs are re-calculated to apply from this date). The issue of when tariffs commence

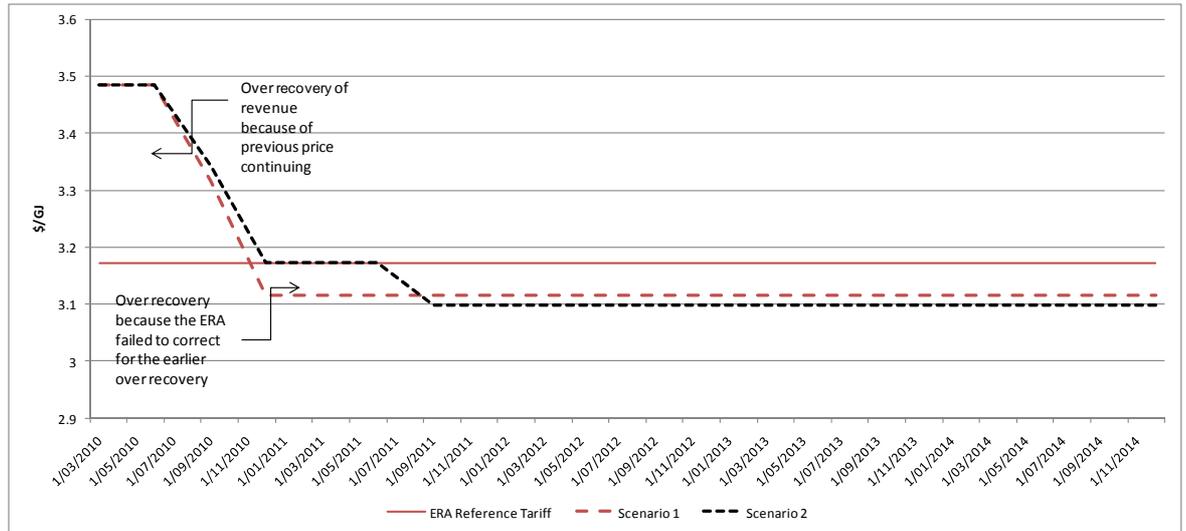
(which is addressed below) is more significant once the allocation error is also corrected because the over-recovery prior to the new tariffs commencing is much larger.

MODELLING ERROR - TRUE UP

- 44 In the Further Final Decision issued on 5 August 2010, the Regulator used a financial model which assumed a commencement date for the 2010 Access Arrangement of 1 January 2010, for the purposes of determining the approved Total Revenue and the Reference Tariff.
- 45 The model did not contain any ‘true up’ mechanism (**True-up Error**) to make allowance for the actual commencement date of 20 August 2010, and fact that in the period 1 January to 20 August 2010 (**Delayed Start Period**), the Reference Tariff charged by GGT was the (higher) Reference Tariff imposed under the 2005 Access Arrangement.
- 46 A true up mechanism is required to avoid over or under recovery flowing from delays in the regulatory system. Such an approach is common and is required in this case to address the reality of over recovery by GGT. Thus for example in 2008 the Victorian Essential Services Commission adjusted the applicable tariffs for late commencement.²⁰
- 47 In the Further Final Decision the Regulator understated the Reference Tariff revenue that would be earned in 2010 and accordingly overstated the Reference Tariff required to equate (in present value terms) the Reference Tariff revenue with the cost of Service.
- 48 Based on the information in the Regulator’s Further Final Decision model, BHPB has recalculated the Reference Tariff assuming the start date of 20 August 2010 and that the previous prices applied prior to that time. On that basis the Regulator should have calculated a Reference Tariff 1.81% lower than it set.
- 49 Alternatively and based on the same data before the Regulator, if the Board was to determine a new Reference Tariff commencing on 1 July 2011, the incorrect Reference Tariff would have applied from 20 August 2010 to 30 June 2011. On that basis BHPB has calculated that the Board would need to reduce the Reference Tariff by 2.36% from

²⁰ Gas Access Arrangement Review 2008-2012, Essential Services Commission Final Decision 7 March 2008 at paras 1.9 on p 15 and 12.17 on p 566.

1 July 2011. A graphical representation of the alternatives under different timing assumptions is set out below.



50 In its application, GGT seek to preserve the benefit of the late effective date and also seek to have 20 August operate as the date from which their proposed amendments take effect. BHPB reserves its position pending consideration of GGT’s submissions on its application, but may in the alternative to these submissions submit that the effective date should have been 1 January 2010 in accordance with the model, and then recover the amounts overpaid from GGT.

RELIEF

51 In summary, BHPB seeks orders that:

- (a) the Final Decision and Further Final Decision be varied immediately to correct the errors identified above; or
- (b) in the alternative that the Board draft and approve a revised Access Arrangement to correct those errors;

and in either case that the Board recalculate the Reference Tariff to:

- (c) allocate costs to non-reference services as set out in paragraphs 38-44 above; and
- (d) true up for over recovery by GGT as set out in paragraphs 47-51 above.

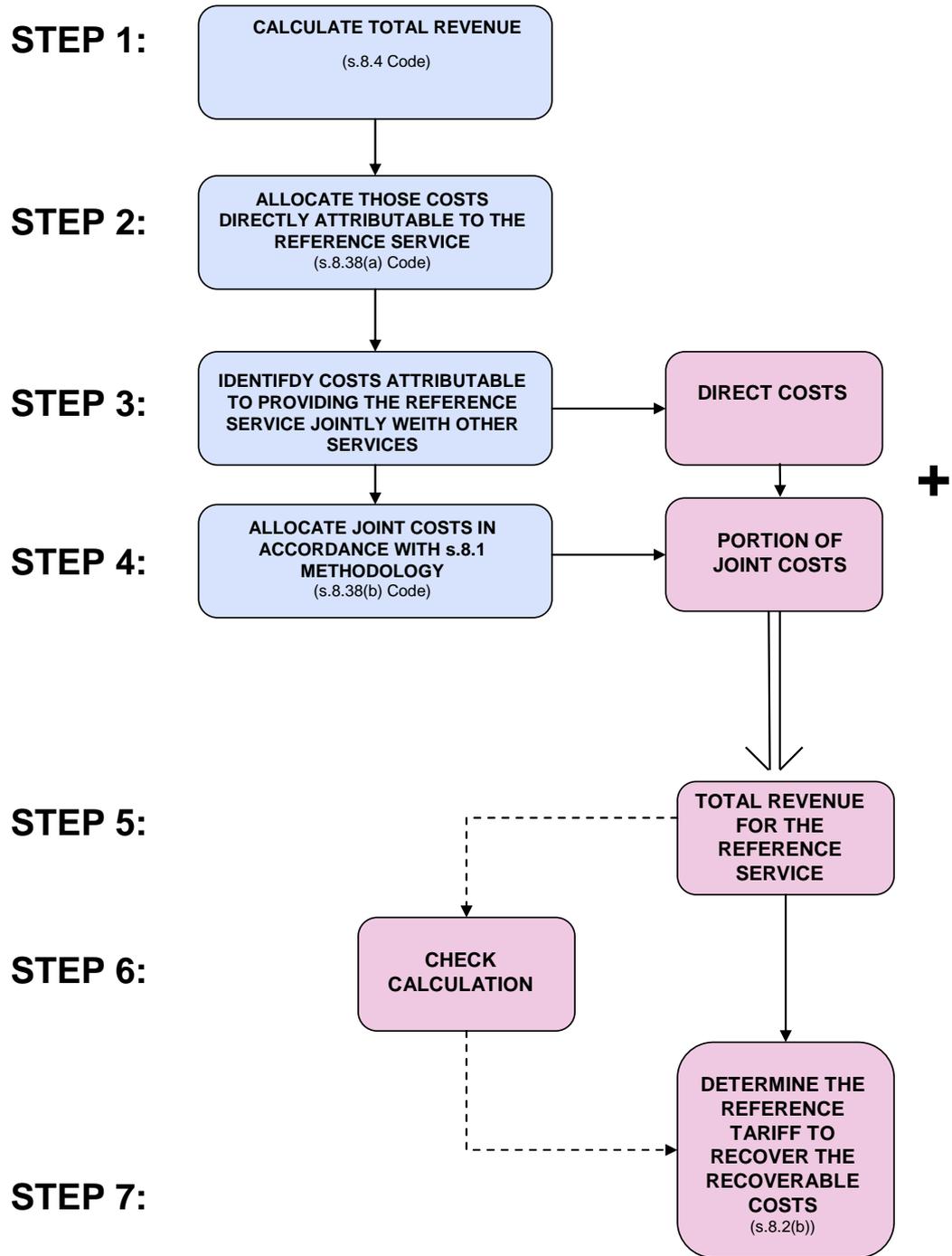
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8 March 2011

ANNEXURE A



ANNEXURE B

(See “Gas Code Reference Tariff Calculation.xlsx” worksheet - attached as a separate document)