31 October 2023

financial reporting guideline for light regulation pipeline services - Allgas Energy Gas Distribution Network

basis of preparation

Contents

1 introduction

In October 2019 the Australian Energy Regulator (**AER**) issued the Financial Reporting Guideline for light regulation services (the Guideline) in accordance with rule 36F of the National Gas Rules (**NGR**).

Under rule 36B (1)(c) and (d) of the NGR, service providers for light regulation services are required to publish specific information, including financial information and weighted average price information. Financial and weighted average price information is intended to assist prospective users in assessing prices being offered by the service provider.

Chapter 9 of the AER Guideline requires the reporting entity to prepare a separate basis of preparation document. This Basis of Preparation should be read in conjunction with the Guideline and the Financial Reporting Guideline for Light Regulation Services Explanatory Statement.

The Guideline require reporting in the following distinct categories:

1. Statement of pipeline revenue and expenses;
2. Statement of pipeline assets – applying a Regulatory Asset Base (**RAB**) roll forward approach;
3. where required, a Recovered Capital Method (**RCM**) approach; and
4. Weighted average price information or alternate presentation of pricing information.

The Guideline states that service providers are required to comply with the Australian Accounting Standards (**AAS**) except where the Guideline provides a methodology that is not consistent with the AAS.

The Guideline creates a new special purpose financial reporting framework, which differs in significant ways from the statutory reporting framework defined by AAS. It is important to note that the information produced under the light regulation Guideline will not in all circumstances reconcile to the majority of financial information prepared by the Service Provider under AAS.

This Basis of Preparation document applies to the Allgas Energy Gas Distribution Network (**Allgas**) whose service provider is Allgas Energy Pty Limited (**Allgas Energy**).

1.1 pipeline-specific information

The Allgas Energy Gas Distribution Network is owned by Allgas Energy Pty Limited whose parent company is GDI (EII) Pty Ltd (**GDI**). The Allgas Energy Gas Distribution Network extends from Brisbane, south of the river, to the northern tip of New South Wales, with separate networks in Toowoomba and Oakey. The network includes some small extensions in Northern NSW (Northern Rivers). As at 30 June 2023, in total, the network includes 3,984 kilometres of distribution mains supplying approximately 121,000 gas users.

The shareholders of GDI are: Energy Investment Two P/L (Marubeni, 40%); SAS Trustee Corporation (40%); and APA Infrastructure Limited (20%). GDI (EII) Pty Limited is not a subsidiary of any one of its shareholders.

APA (**network operator**) operates and maintains the Allgas Energy Gas Distribution Network on behalf of GDI.

The network operator has prepared and lodged this information on behalf of the Service Provider and GDI.

1.2 rounding

Totals in the templates provided may not add due to rounding.

1.3 requirement to publish financial information

The financial reporting under light regulation is an annual reporting requirement for GDI's light regulation pipeline due and published on 31 October 2023.

1.4 assurance requirement

Based on discussions with the AER, the following assurance requirements are expected in the following Worksheet:

Worksheet	Worksheet name	Assurance:
Worksheet 1	Pipeline Information	No assurance
Worksheet 1.1	Financial Summary	No assurance
Worksheet 2	Revenues and Expenses	Audit
Worksheet 2.1	Revenue by Service	No assurance
Worksheet 2.2	Revenue contributions	No assurance
Worksheet 2.3	Indirect revenue	No assurance
Worksheet 2.4	Shared costs	No assurance
Worksheet 3	Statement of pipeline assets	Audit
Worksheet 3.1	Pipeline asset useful life	No assurance
Worksheet 3.2	Shared supporting assets	No assurance
Worksheet 4	Recovered capital	Review
Worksheet 4.1	Pipelines Capex	No assurance
Worksheet 5	WAP	Review
Worksheet 5.1	Exempt WAP Services	No assurance
Worksheet 5.2	Alternate price information	No assurance
Worksheet 6	Notes	Audit

Certain worksheets subject to an assurance requirement listed above present information that is greater than seven years from the date of the initial regulatory year's submission. This is presented in the template but is not subject to audit or review.

GDI will maintain records as follows:

- All base financial records will be extracted from the network operator's financial systems;
- GDI's statutory financial statements and associated accounting records will form the basis of all reporting requirements;
- Analytical templates and work papers prepared for regulatory reporting;
- All records will be kept for at least seven years from date of initial regulatory years submission; and for the subsequent regulatory years, for at least seven years from the date of the respective submission; and
- All records will be available to independent auditors, and the AER.

1.5 no requirement to report an RCM value for Allgas

In accordance with the Guideline, where a Regulatory Asset Base (RAB) value has not been established through an access arrangement, service providers are required to determine a pipeline asset value based on a recovered capital method (**RCM value**) and disclose their calculation of this value in worksheet 4 of the financial reporting template.

As Allgas has a RAB value previously established as a result of being covered and subject to a full access arrangement in accordance with the NGR, the service provider is not required to report an RCM value. Worksheet 4 is therefore not applicable for Allgas.

2 financial summary

The financial performance summary highlights the historical achieved revenues and the theoretical revenues that would be achieved under a building block approach.

The opening asset values reported are from the first year since the RAB was last established.

For Allgas, the opening regulated asset base reflects historical regulatory determinations.

2.1 nominal WACC

In this reporting framework as applicable to Allgas, the Weighted Average Cost of Capital (WACC) is used in 2 areas:

- In Table 1.1.1 Financial Summary; and
- As the half-year capitalised return allowance in the Roll Forward Model to reflect a return on capex undertaken in the reporting year.

A separate WACC must be calculated for each reporting year, according to the WACC hierarchy specified in Box 6.1 of the Guideline.

In summary, the WACC hierarchy provides for the applied WACC to be calculated in the following order of priority (further referenced as Levels):

1. Where the light regulation asset was under full regulation in part of a given year for which an estimated WACC is required, the WACC from the pipeline's ACCC/AER final decision applicable to that given year is adopted.
2. Where there was an ACCC or AER WACC instrument, guideline, or statement of regulatory intent (**WACC Instrument**) in place that would have been applied at the time this WACC Instrument is adopted, to the extent possible, as it would have been applied at the time.
3. The estimated WACC taken from the most recent previous ACCC/AER final decision that covers the same year and the same type of gas asset (i.e. transmission or distribution).
4. The estimated WACC taken from the most recent previous ACCC/AER final decision that covers the same year and different type of gas asset.
5. The estimated WACC based on the first available ACCC/AER final gas transmission or distribution decision from a later year.

In all cases, any WACC calculated is to reflect an "on the day" cost of debt rather than any elements of a rolling average cost of debt that may be reflected in the relevant determination.

Moreover, the calculations of cost of equity and cost of debt are to be updated to reflect the last 20 business days' financial market data for any relevant market parameters applied (e.g. the risk-free-rate, Bloomberg BVAL curve, etc.)

For information on how the WACC hierarchy is applied, please refer to Appendix 1.

3 pipeline financial information

3.1 sources of information

The network operator uses an enterprise resource planning (**ERP**) system, Oracle, as the financial reporting system which comprises a number of modules for managing the recording, processing and reporting of all business transactions from initiation through to payment. These modules include General Ledger, Projects, Fixed Assets, Payables, Receivables and Cash management. Oracle is the primary source of financial information. This system is the underlying source of financial information disclosed in the GDI audited financial statements and the Allgas regulatory accounts. The statutory financial statements are prepared in accordance with the requirements of AAS and other authoritative pronouncements of the Australian Accounting Standards Board (**AASB**) and also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Other financial information is sourced from the Roll Forward Material. Roll Forward Material is defined in the AER's Guideline as, "a suite of guidance materials, published by the AER from time to time, setting out how a service provider is to roll forward the asset base of a covered gas pipeline, such as guidelines, final decisions, handbooks and models."

Financial information extracted from the Oracle financial system and Roll Forward Material underpins the reported *Statement of Pipeline Revenue and Expenses* and *Statement of Pipeline Assets* for the following categories:

- **Revenue:** Revenue recognition complies with the revenue recognition principles prepared in accordance with the requirements of Australian Accounting Standards.
- **Operating direct costs:** Allgas' statutory operating cost categories are in line with the categories identified in the section 3.1.1.2 of the Guideline. Depreciation expense is determined in accordance with the Roll Forward Model used to calculate the pipeline's Regulated Asset Base (refer section 3.3.2.1 in this Basis of preparation).
- **Assets:** Fixed asset opening cost base is driven by the regulatory determination. Annual capital expenditure additions are consistent with statutory financial reporting requirements. For the purpose of the regulatory determination in 2010, pipeline assets were recognised on the basis "as incurred". Allgas has continued to use this approach to capitalise pipeline assets.

GDI has for these reporting purposes allocated a fair proportion of corporate expenditure to each asset in GDI's portfolio based on a revenue allocation method. Refer to Section 3.3.2.2 of this basis of preparation for further details.

3.2 general methodology and principles

Methodologies used for the preparation of the *Statement of Pipeline Revenue and Expenses* and *Statement of Pipeline Assets* are broadly consistent with the methods used in the preparation of the GDI statutory financial accounts and the Allgas regulatory accounts except for revenue categorisation, operating and shared corporate expenditure, shared support assets and depreciation expense.

Financial information for each pipeline subject to light regulation services has been derived from the relevant Service Provider's Trial Balance which forms part of the Allgas *Statutory Financial Statements*, where appropriate. The *Statement of Pipeline Assets* includes all pipeline assets connected with the asset base of light regulation pipeline which is consistent with the Guideline.

There are instances where the reporting of light regulation pipelines does not align with legal entity reporting due to Guideline requirements. The financial information provided is then supported by the Allgas management reporting, regulatory accounts or determinations. The information in these instances has been further verified through underlying regulatory determinations, customer contracts, customer correspondence, third party operating agreements, direct costs and detailed reviews of invoices and asset registers as relevant.

The *Statement of Pipeline Revenue and Expenses* and *Statement of Pipeline Assets* has been audited by Allgas' external auditor, Deloitte Touche Tohmatsu, in accordance with the Australian Auditing Standards.

3.3 statement of pipeline revenue and expenses

Revenue is reported in worksheet 2 and 2.1 of the financial reporting template and is reported by service category as set out in the financial reporting template. The service provider is compliant with revenue recognition principles consistent with the AAS.

3.3.1 *revenue*

In accordance with the AAS, revenue is recognised at an amount that reflects the consideration to which Allgas expects to be entitled in exchange for the provision of services to a customer (the **performance obligations**) under a contract. Allgas recognises revenue when control of a product or service is transferred to the customer. Amounts disclosed as revenue are net of duties and taxes paid. Given the nature of Allgas services there is no significant right of return or warranty provided. Direct revenue is derived from gas distribution services.

Revenue from contracts with customers may either be identified as separate performance obligations or a series of distinct performance obligations that are substantially the same, have the same pattern of transfer and are therefore treated as a single performance obligation that is satisfied over time. The amount billed corresponds directly to the value of the performance to date.

Consistent with the AER-approved Allgas access arrangement, customer contributions for new connections are treated as revenue, with the related costs capitalised as part of the regulatory asset base.

3.3.1.1 related party transactions

There are no related party transactions because the service provider does not provide services to customers who are related parties as defined under the Guideline, in a manner consistent with the *Corporations Act 2001*. No shared cost was paid to a related party.

3.3.2 *costs*

All costs (operating and capital) are captured in the network operator's financial reporting system through cost centre and project reporting. The cost centre and project reporting provides details on the activity type of the costs, reflecting categories of capital, operating & maintenance activities and services.

Allgas has attributed costs directly to projects, activities and services where possible and appropriate.

The key cost allocation principles adopted are as follows:

- costs are not allocated more than once;
- costs cannot be treated as a directly attributed cost and other attributable cost;
- costs are allocated on a causal basis, in instances where direct attribution is not possible.

When assessing Allgas operating and capital costs, the majority of its costs fall within two categories:

- **directly attributable costs** to the pipeline service provider: Expenses that are clearly associated with a specific pipeline asset. Direct costs are coded to the asset or to a project relating to the asset, through creation of a purchase order at the time of purchase or direct employees charging their time to the asset or project, using an hourly rate derived from employee payroll costs.

  Examples of such costs include the pipeline and materials expenses directly attributed to repair and maintenance, the distribution network and the employees who are solely dedicated in providing field services to the light regulation pipeline.

- **other directly attributable costs**: Other directly attributable expenses are costs directly attributable to the assets incurred by Allgas. In order to give a true reflection of the cost of running an asset, it is necessary to allocate a portion of GDI's additional distribution costs to the asset. GDI's costs are reviewed periodically to determine the extent to which the business unit's function has a bearing on the assets.

Other expenditure subject to allocation are GDI shared corporate expenditure which is allocated based on GDI's revenue approach. Further information is provided in section 3.3.2.2.

Operating costs includes an allowance for debt raising costs, calculated by multiplying the average value of the regulatory asset base by an AER-approved debt raising cost percentage drawn from a relevant regulatory determination.

3.3.2.1 depreciation expense

Depreciation expense is determined in accordance with the regulatory depreciation methodology as set out in the Roll Forward Material as required in the Guideline. Roll Forward Material is defined in the AER's Guideline as, "a suite of guidance materials, published by the AER from time to time, setting out how a service provider is to roll forward the asset base of a covered gas pipeline, such as guidelines, final decisions, handbooks and models."

In May 2022 the AER published a new Roll Forward Model for Gas Transmission Service Providers. The service provider utilised this Model to calculate depreciation expense.

For further information on the calculation of depreciation expense using the Roll Forward Model, please refer to the AER's document called final decision "Gas transmission and distribution network service providers, Roll forward model (version 1)" released in April 2020, available from www.aer.gov.au.

3.3.2.2 shared corporate expenditure

GDI incurs corporate expenditure, which is shared amongst the assets in its group. GDI corporate operating expenditure has been allocated based on distribution/non-distribution activities based on the revenue each asset generates.

3.3.2.3 debt raising costs

Debt raising costs as presented in the Statement of Pipeline Revenue and Expenses has been calculated by applying the debt raising cost of 0.095% to the average Regulated Asset Base at the beginning of the year to the permitted proportion of 60% for debt funding. The debt raising cost of 0.095% and the proportion of 60% for debt funding was approved by the Australian Energy Regulator in its May 2022 Final Decision on the access arrangement for the Roma Brisbane Pipeline. The appropriate debt raising cost rate has been drawn from those decisions referenced for WACC purposes as discussed in Appendix 1. Debt raising will be included as part of the operating expenditure reported for light regulated purposes as the concept forms part of the revenue "building block".

The cost is recorded as part of the tab "2.4 Shared costs" which flows into table 2.1.

3.4 statement of pipeline assets

Service providers are required to provide a statement of pipeline assets for the pipeline at worksheet 3 of the financial reporting template. The statement of pipeline assets provides an overview of the assets utilised in the pipeline operations.

The Depreciation and Regulatory Asset Base calculations in worksheet 3 is determined in accordance with the Roll Forward Model.

The light regulation reporting has complied with the AAS and regulatory guidelines; however it should be noted that the Guideline prohibits the inclusion of liabilities in the Statement of Pipeline Assets but allows depreciation to be reported.

3.4.1 *asset capitalisation principles*

Consistent with section 3.1 above, all capital expenditure is captured in the Oracle financial reporting system through cost centre and project reporting. Annual capital expenditure additions are consistent with statutory financial reporting requirements. For the purpose of the regulatory determination in 2010, pipeline assets were recognised on the basis "as incurred". Allgas has continued to use this approach to capitalise pipeline assets.

Once it has been determined that it is appropriate to capitalise the costs, they have been attributed directly to the pipeline.

The asset values in the *Statement of Pipeline Assets* have used the Roll Forward Model to determine accumulated depreciation. The asset values represent historical/acquired cost, plus capital expenditure, indexation (CPI escalation refer section 3.5.3 in this basis of preparation), less disposals and less depreciation.

The asset lives used are consistent throughout a pipeline lifetime. Accordingly, where a pipeline has previously had a RAB established, Allgas has continued to use the economic lives set at the time when the pipeline was under full regulation. Should the asset lives have changed throughout a pipelines lifetime, Allgas has maintained net present value neutrality to ensure that asset is depreciated only once.

No revaluations of the asset base have been included in the Statement of Pipeline Assets. Asset values has been determined in accordance with the Roll Forward Material and the Guideline.

Construction, acquisition, major maintenance and asset replacement costs are capitalised in accordance with *AASB 116 Property Plant and Equipment (AASB 116)*.

Consistent with *AASB 116*, the cost of major inspections has been added onto the carrying value of the pipeline asset in the capitalised maintenance line of the reporting template where applicable. Costs of previous major inspections are simultaneously derecognised.

The following costs associated with routine maintenance and repairs are expensed as incurred:

- administration and general overhead costs;
- labour and consumables; and
- staff training costs.

3.4.2 *depreciation principles*

Depreciation principles set out the basis on which pipeline assets are depreciated. Depreciation has been calculated consistently based on the asset lives principles in section 3.2.3 and 3.2.5 of the Guideline as well as rule 89 of the NGR (depreciation criteria). Assets are depreciated based on asset lives set out in worksheet 3.1.

For the purposes of preparing the statement of pipeline revenues and expenses, the depreciation expense has been determined in accordance with the Roll Forward Model.

Unless otherwise allowed in the Roll Forward Material for the statement of pipeline revenue and expenses and the calculation of the RAB value, depreciation is straight line depreciation consistent with the method prescribed under the AAS. The depreciation calculated is the regulatory depreciation (based on the Regulatory Asset Base). Actual depreciation has been reflected in the template, not forecast depreciation.

The asset value for each year was reduced by the depreciation expense as determined above (noting that the asset value has also been adjusted for indexation, capital expenditure, capital contributions and disposals).

The useful life of the asset and the reason for selecting this useful life is disclosed in worksheet 3.1 of the financial reporting template. These are consistent with asset life principles in Section 3.2.3 of the Guideline and rule 89 of the NGR. For other depreciable pipeline asset classes and for shared supporting assets, Allgas has applied depreciation principles in line with statutory reporting, which is in accordance with the AAS.

Acquisition date detailed as "Various" in table 3.3.1 as assets were acquired over various periods which represents the various range of dates in the Fixed Asset Register.

As the asset categories per the post tax revenue model (**PTRM**) do not align to the asset categories required to be disclosed as part of the light regulation template, the useful lives disclosed in table 3.1.1 are the weighted average useful lives per the access arrangement. This will vary year on year as the weighted average useful lives changes.

Due to the operation of the RFM Nominal Capex an inclusion of a half-year WACC is reported in table 3.1.

3.4.3 *disposals*

Disposals are recorded as proceeds received when an asset is disposed. Disposal in table 3.1 are not equal to cost – it represents the nominal proceeds received.

Allgas has continued to apply the regulatory financial capital maintenance principle which treats disposals as a “return of capital”. In essence, regulatory financial capital maintenance principles provide that once capital investment has been approved for inclusion in the Regulatory Asset Base, the business is allowed to earn a return on that capital until such time as the capital is returned to it either through depreciation reflected in approved tariffs or through cash proceeds received on disposal of an asset.

It should be noted that table 1.1.1 has heading inconsistencies in regards to disposals. Despite headings requesting Disposal $(at cost), the total amounts are presented in $ millions.

The disposals heading in table 1.1.1 has been amended to reflect the nominal proceed amounts in line with other parts of the reporting template.

3.4.4 *shared support assets*

During APA ownership of Allgas until 2011, Allgas received attributed corporate expenditure and shared support assets allocated on a revenue basis. Shared supporting assets of $2,884, recorded in Table 3.1 Pipeline assets, reflects the remaining balance of shared supporting assets allocated to Allgas, whilst owned by APA.

As GDI does not have any shared support assets, under the ownership of GDI, Allgas has not reported any shared support assets.

3.4.5 *shared leased assets*

GDI does not have any leased assets hence Allgas reports no shared leased assets.

3.5 establishing the opening RAB value

Prior to becoming subject to light regulation in August 2016, Allgas was subject to full regulation and had an AER-approved access arrangement in place from 2011-2016.

In accordance with the Guideline, the opening RAB value has been established as that last determined by the AER in its latest access arrangement Final Decision.

3.5.1 *rolling forward the RAB value*

The NGR sets out rules for the roll forward of the RAB value for a covered pipeline. In order to provide interpretation and further guidance the AER has published Roll Forward Material on how service providers of full and light regulation pipelines are to roll forward the pipeline's RAB value.

The Roll Forward Material is applicable to service providers of light regulation pipelines for the purposes of determining the RAB value in accordance with this Guideline.

The Roll forward of the RAB value is to be based on the principles set out in the NGR, in particular rule 77(2). Each year from the year for which the RAB was first established, the RAB value is to be rolled forward as follows:

- Opening RAB value (as determined in accordance with Section 4.1 for the first year, then being equal to the closing RAB value for the previous year thereafter);
- Plus capital expenditure;
- Plus any amounts added to the capital base as a result of:
  - Capital contributions as described in rule 82 of the NGR;
  - Speculative capital expenditure as described in rule 84 of the NGR;
  - Re use of redundant assets as described in rule 86 of the NGR;
- Plus any amounts determined in accordance with rule 77(2)(ca.) in respect of extensions;
- Less depreciation calculated in accordance with Section 3.2.5 of the Guideline;

- Less redundant assets as described in rule 85 of the NGR;
- Less the value of pipeline assets disposed of during the year, noting that net disposals are to be recorded, meaning that the costs of realisation are to be subtracted from the proceeds from disposals.

The Roll Forward Material provides further guidance on the method in which, above elements are to be determined.

The models and calculations used in determining the RAB value are to be published along with the financial reporting template in line with the requirement in section 4.2 of the Guideline.

3.5.2 *indexation*

In accordance with rule 89 of the NGR, the AER permits indexation to be applied to the RAB value. The Roll Forward Material details how indexation is to be applied to the RAB value, and indexation has been applied in accordance with the Roll Forward Model.

3.5.3 *CPI escalations used*

Indexation is to be applied to the RAB value based on CPI Weighted Average of Eight All Capital Cities published by the Australian Bureau of Statistics. The RAB value has been calculated using a CPI March quarter index, which is consistent with Allgas' last Access Arrangement.

4 pricing information

Tariffs for Allgas are derived by applying CPI escalation to the tariffs last approved by the AER under the access arrangement.

Effective 1 November 2020, Allgas entered into renewed contracts with all its shippers reflecting a 5% discount from the then-published tariffs, and a reduction in annual escalation to CPI less 0.5%.

4.1 alternative presentation of pricing information

The guideline allows for an alternative presentation of pricing information. Where the service provider's actual pricing is already presented on the service provider's website, as in Allgas' case, the service provider may use the blank template (worksheet 5.2 of the financial reporting template) to set out its pricing information, in lieu of the format for presenting weighted average price information in worksheet 5.1 of the financial reporting template. Allgas has inserted worksheet 5.2 with the published tariffs, showing tariffs in effect from 1 July 2022. Per interpretation of the Guideline, this alternate reporting has not been reviewed.

A Appendix 1 - WACC Hierarchy

A.1 applying the WACC hierarchy

1. **Where the light regulation pipeline was under full regulation in part of a given year for which an estimated WACC is required, the WACC from the pipeline's ACCC/AER final decision applicable to that given year is to be used.**

A full regulation determination was in effect for the Allgas network for the period from 1 July 2011 to the commencement of light regulation in August 2016[1] as follows:

Pipeline	Allgas Distribution Network
Date of Final Determination	17 June 2011
Cost of Equity	10.20%
Cost of Debt[2]	9.77%
WACC	9.94%
Date Light Regulation Commenced	August 2016

2. **Where there was an ACCC or AER WACC instrument, guideline, or statement of regulatory intent ("WACC Instrument") in place that would have been applied at the time this WACC Instrument is to be applied, to the extent possible, as it would have been applied at the time. The applicable guidelines are the 2013 AER Rate of Return Guideline and the 2018 binding Rate of Return Instrument.**

2013 AER rate of Return Guideline

The 2013 Rate of Return Guideline was issued in December 2013. In accordance with the Light Regulation Guideline, it will apply for the 2014-15 fiscal year reporting periods and subsequent years until the 2018 Rate of Return Instrument is applicable for the reporting period from 2019-2020 onwards. The AER December 2013 Rate of Return Guideline specifies:

- the weighting formula, applying a gearing ratio of 0.6; (p9)
- the use of the Sharpe-Lintner CAPM (**SLCAPM**) as the foundation model for determining the cost of equity; (p13)
- the risk free rate is estimated as the yield on 10-year Commonwealth Government Securities, measured over a period of 20 business days over a period as close as practicably possible to the commencement of the regulatory control period;[3] (p15);

[1] National Competition Council, Application by Allgas Energy Pty Ltd for Light Regulation of the Allgas Gas Distribution Network, Final decision 28 April 2015. Light regulation became effective 60 business days following the date of the NCC Final Decision.
[2] Per decision of the Australian Competition Tribunal in Application by APT Allgas Energy Limited (No 2) [2012] ACompT 5.
[3] Under the Light Regulation Guideline, the risk free rate is to be observed over the last 20 business days of the year preceding that for which the cost of equity is to be determined.

- an equity beta of 0.7 (p15);
- the Market Risk Premium (**MRP**) will be a point estimate based on the AER's regulatory judgement (p16); and
- if the starting point determined by the application of the foundation model is too high or too low, "the point estimate will be changed by an amount informed by the other information (using the AER's regulatory judgement)."
- "the allowed return on debt using a trailing average portfolio approach following the completion of a transitional arrangement period" (p19) (Note that the Light Regulation Guideline requires an "on the day" cost of debt to be determined);
- The return on debt is to be estimated "Using the published yields from an independent third party data service provider" (p21);
- "Using a credit rating of BBB+" (p21);
- "Using a term to maturity of debt of 10 years" (p21);
- The 2013 Rate of Return Guideline goes on (pp21-23) to specify the criteria under which an averaging period is to be established. However the Light Regulation Guideline specifies that the averaging period is to be the last 20 business days of the year preceding that for which the cost of debt is to be determined.

The 2013 Rate of Return Guideline (**RoR Guideline**) relies on the AER's judgement in both determining the MRP to apply in the SLCAPM and then adjusting the outturn cost of equity. In applying the 2013 RoR Guideline, Allgas has adopted the AER's determination of the MRP from relevant contemporaneous regulatory decisions, which are specified below.

Relating to the cost of debt, a review of AER determinations has revealed a range of approaches, including relying on various methods to extrapolate 7-year bond data to estimate 10-year yields.

For the purposes of reporting under the Light Regulation Guideline, we have assumed that the AER applied its 2013 RoR Guideline in all decisions issued while that Guideline was in effect. Allgas have therefore adopted the cost of equity and cost of debt specified in those decisions, as adjusted for changes in the risk free rate for the last 20 business days of the year.

The approach applied to updating the cost of debt for changes in the risk free rate is discussed below.

The AER's 2013 RoR Guideline introduced the move to a 10-year rolling average cost of debt, with a transition period commencing from the start of the business's next regulatory determination. However, the Financial Reporting Guideline for Light Regulation Pipelines requires an on-the-day cost of debt to be applied.

For the years in which the 2013 RoR Guideline was in effect, Allgas has drawn cost of debt information from the first year of a new regulatory determination. This means that these businesses will be just embarking on the transitional journey, so reference to these determinations will reflect the on-the-day cost of debt.

Where a referenced determination applies for two reporting years, Allgas has back-calculated the on-the-day cost of debt applied to the second year from the public AER cost of debt update.

AER 2018 Rate of Return Instrument

The 2018 Rate of Return Instrument was issued in December 2018. In accordance with the Light Regulation Guideline, it will apply for the 2019-20 fiscal year and subsequent years until a new Instrument is promulgated.

The AER 2018 binding rate of return instrument specifies:

- the weighting formula, applying a gearing ratio of 0.6; (para 3(d))
- that the cost of equity is to be calculated using the Sharpe-Lintner Capital Asset Pricing Model (para 4) using:
    - A beta value of 0.6 (para 4(b));
    - A Market Risk Premium of 6.1 per cent (para 4(c));
- the risk free rate of return is to be calculated as a simple average of the daily yields to maturity of Commonwealth government securities, converted into an effective annual rate (para 5);
- the criteria under which the risk free rate averaging period is to be nominated (para 8). However, the Light Regulation Guideline specifies that the risk free rate is to be observed over the last 20 business days of the year preceding that for which the cost of equity is to be determined.
- the criteria under which a separate averaging period is to be nominated by the service provider for the purposes of calculating the return on debt (Paras 23 and 24). However the Light Regulation Guideline specifies that the averaging period is to be the last 20 business days of the year preceding that for which the cost of debt is to be determined.
- the value of imputation credits is set at a value of 0.585 (para 27)

Under the 2018 binding rate of return instrument, the relevant WACC values applicable to the 2019-20 to 2021-22 regulatory years would be calculated as follows:

Cost of equity:	**2019-20**	**2020-21**	**2021-22**
Risk free rate (June 2019, June 2020)	1.3860%	0.9245%	3.78375%
Beta	0.6	0.6	0.6
Market Risk Premium	6.1%	6.1%	6.1%
Cost of equity	5.0460%	4.5845%	7.4438%

On-the-day cost of debt[4]	4.2644%	2.8510%	2.9226%
Gearing ratio	60%	60%	60%
Tax rate	30%	30%	30%
Value of imputation credits (Gamma)	58.5%	58.5%	58.5%
Nominal Vanilla WACC	4.5770%	3.5444%	4.7311%

AER 2022 Rate of Return Instrument

The 2022 Rate of Return Instrument was issued in February 2023. In accordance with the Light Regulation Guideline, it will apply for the 2022-23 fiscal year and subsequent years until a new Instrument is promulgated.

The AER 2022 binding rate of return instrument specifies:

- the weighting formula, applying a gearing ratio of 0.6; (para 3(d))
- that the cost of equity is to be calculated using the Sharpe-Lintner Capital Asset Pricing Model (para 4) using:
  - A beta value of 0.6 (para 4(b));
  - A Market Risk Premium of 6.2 per cent (para 4(c));
- the risk free rate of return is to be calculated as a simple average of the daily yields to maturity of Commonwealth government securities, converted into an effective annual rate (para 5);
- the criteria under which the risk free rate averaging period is to be nominated (para 8). However, the Light Regulation Guideline specifies that the risk free rate is to be observed over the last 20 business days of the year preceding that for which the cost of equity is to be determined.
- the criteria under which a separate averaging period is to be nominated by the service provider for the purposes of calculating the return on debt (Paras 23 and 24). However the Light Regulation Guideline specifies that the averaging period is to be the last 20 business days of the year preceding that for which the cost of debt is to be determined.
- the value of imputation credits is set at a value of 0.585 (para 27)

Under the 2022 binding rate of return instrument, the relevant WACC values applicable to the 2022-23 regulatory year would be calculated as follows:

Cost of equity:	**2022-23**
Risk free rate	3.9325%
Beta	0.6
Market Risk Premium	6.2%

[4] As a proxy to applying the detailed procedure in the 2018 Rate of Return Instrument, Allgas has applied the annual return on debt estimates for 2019-20 and 2020-21 for Roma Brisbane Pipeline and Amadeus Gas Pipelines, as advised by letter from AER to APA dated 22 May 2019, 21 May 2020 and 21 April 2021, respectively.

Cost of equity	7.6525%
On-the-day cost of debt[5]	**3.9999%**
Gearing ratio	60%
Tax rate	30%
Value of imputation credits (Gamma)	57.0%
Nominal Vanilla WACC	5.4609%

3. **The estimated WACC is to be taken from the most recent previous ACCC/AER final decision that covers the same year and the same type of gas asset (i.e. transmission or distribution).**

For the purposes of applying Level 3 of the hierarchy, and for determining the relevant WACC parameters to assist in applying the 2013 Rate of Return Guideline in hierarchy Level 2 above, the following AER/ACC determinations are referenced:

Year ended June	Determination	Cost of Equity	Cost of Debt	WACC	Gamma
2019	AusNet Services 2018-22	7.30%	5.04%	5.94%	40%
2018 2017	Australian Gas Networks (SA) 2016-21	7.10%	5.51%	6.14%	40%

4. **The estimated WACC is to be taken from the most recent previous ACCC/AER final decision that covers the same year and different type of gas asset**

Relevant gas distribution determinations are available to satisfy hierarchy Level 3 for all periods required; it will not be necessary to rely on any AER/ACCC gas transmission determinations.

Level 4 of the hierarchy will not apply.

5. **The estimated WACC is to be based on the first available ACCC/AER final gas transmission or distribution decision from a later year.**

Relevant gas distribution determinations are available to satisfy hierarchy Level 3 for all periods required. Level 5 of the hierarchy will not apply.

A.2 summary

In practice, the WACC hierarchy will be applied differently to different pipelines, depending on the date and duration of their last full regulation determination, the date each became subject to light regulation, the presence of an ACCC/AER Rate of Return Guideline or Instrument, etc. This is summarised below for Allgas: [6]

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[5] As a proxy to applying the detailed procedure in the 2022 Rate of Return Instrument, Allgas has applied the annual return on debt estimate for 2022-23, for the Amadeus Gas Pipeline, as advised by letter from AER to APA dated 4 April 2022.

[6] Entries marked as "2, 3" indicate that the 2013 Rate of Return Guideline is to be applied (hierarchy level 2) but that the application will need to reference contemporaneous regulatory determinations for other distribution networks (hierarchy level 3) to assist in its application, as discussed above.

Fiscal year ended June	Allgas (refer to section A Appendix for details of number references below).
2023	2
2022	2
2021	2
2020	2
2019	2, 3
2018	2, 3
2017	2, 3
2016	1
2015	1
2014	1
2013	1
2012	1

A.3 updating the reported WACC

The Guideline requires any observed WACC values to be updated to reflect the risk free rate as observed over the last 20 trading days of the fiscal year prior to that for which the WACC is to be applied. The costs of equity and debt, and the WACC reported above reflect the risk free rate observed over an averaging period specified by the pipeline and agreed by the AER.

Allgas has adjusted the Final Decision cost of equity, cost of debt and WACC for movements in the risk free rate between that specified in the Final Decision and the average of the yields on 10 year Commonwealth of Australian securities[7] calculated over the last 20 trading days of the year prior to the WACC being applied. This approach is demonstrated for the adjusted Vanilla WACC values below:

Year ended June	Determination	Determination Risk Free Rate	RBA Risk Free Rate Last 20 trading days	Movement in Risk Free Rate	Reported Vanilla WACC	Adjusted Vanilla WACC
2023	2022 Rate of Return Instrument		3.93250%			5.4609%
2022	2018 Rate of Return Instrument		3.78375%			4.7311%
2021	2018 Rate of Return Instrument		0.9245%			3.5444%
2020	2018 Rate of Return Instrument		1.3860%			4.5770%

[7] Referring to the Reserve Bank of Australia data series FCMYGBAG10D and FCMYGBAG10 in files f02D and f02hist respectively.

2019	AusNet Vic 2818-22	2.730%	2.697%	-0.0330%	5.94%	5.9092%
2018	AGN SA 2016-21AA	2.570%	2.408%	-0.1618%	5.90%	5.7415%
2017	AGN SA 2016-21AA	2.570%	2.109%	-0.4613%	6.14%	5.6836%

A.4 tax liabilities in Table 1.1.1

The Australian regulatory framework provides for a “vanilla” Weighted Average Cost of Capital (**Vanilla WACC**) consisting of an after-tax return on equity and a pre-tax return on debt. This reflects the fact that equity earnings are taxable but the return on debt (ie, interest expense) is deductible for tax purposes. As the allowed return on equity is an after-tax return, the regulatory building blocks must include a tax allowance.

The net tax liability is therefore the amount of revenue that must be allowed such that, when tax is levied on the total taxable income, the remaining after-tax amount is equal to the allowed return on equity. As this requires a revenue allowance to be provided for the payment of tax, on which tax must be paid, there ensues a “tax on tax” multiplier effect calculated at a rate of t/(1-t). For $100 of after tax income to be earned, allowed taxable income must be [$100+$100 x (30%/(1-30%))] $142.86, the tax on which is ($142.86 x 30%) $42.86, leaving after-tax revenue of $100.00.

In an Australian regulatory context, this is further affected by the application of imputation credits by a factor representing the estimated value of imputation credits, known as gamma (γ). The tax-on-tax multiplier is then calculated as t/(1-(1-γ)t).

The tax calculation is also impacted by the difference between the regulatory depreciation included in the revenue cost stack and the tax depreciation calculated in the AER’s Roll Forward Model.

More specifically, the net tax liability has been calculated as shown in the following example. This tax calculation supports table 1.1.1. ($000):

Opening capital base	$426,958	
Less: capital contributions	$0.433	
Less: disposals	$0.013	
Net opening capital base	$426,511	
Proportion deemed funded by equity	40%	
Capital base deemed funded by equity	$170,605	
After tax rate of return on equity	10.2%	
After tax return on equity		$17,402
Timing differences:		
Add: Regulatory depreciation[8]	$4,286	
Less: Regulatory tax depreciation	-$14,608	
Net timing differences		-$10,323
Regulatory taxable income		$7,079
Tax allowance:		
Statutory tax rate (t)	30%	
Value of imputation credits (γ)	0.25	
Effective tax rate [t/(1 – (1–γ) t)]	38.71%	
Tax allowance	$2,740	
Less: Value of imputation credits	-$0.685	
Net tax liabilities		$2,055
Regulatory taxable income		$9,134
Proof:		
Taxable income		$9,134
Less: tax at 30% statutory tax rate		-$2,740
Value of imputation credits		$0.685
After tax income		$7,079
Add: Net timing differences		$10,323
After tax return on equity		$17,402

[8] Note that this is impacted by the indexation of the regulatory asset base.