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INFRASTRUCTURE PARTNERSHIPS AUSTRALIA'S SUBMISSION TO THE COUNCIL OF AUSTRALIAN GOVERNMENTS ENERGY COUNCIL ON THE REGULATION OF GAS PIPELINES

October 2016

About Infrastructure Partnerships Australia

Infrastructure Partnerships Australia (IPA) is an independent think tank and the peak industry body for Australia's infrastructure sector. IPA is a membership based organisation drawing together the public and private sectors in a genuine partnership to debate the policy reforms and priority projects that will build Australia for the challenges ahead.

IPA is committed to promoting genuine, cohesive and cooperative partnerships between Australia's governments and the infrastructure industry and educating stakeholders and the community about the economic and social benefits of major infrastructure projects and reforms.

IPA unites the key decision makers from across Australia's governments and private sector. This diverse range of skills and experiences ensures strong balance in our advocacy and a focus on getting Australia's infrastructure frameworks right - irrespective of commercial or political considerations.

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Introduction

The Council of Australian Governments (COAG) Energy Council (comprised of state, territory and Federal energy ministers) has resolved to examine the current test for the regulation of gas pipelines as part of a comprehensive Gas Market Reform Package. The regulatory framework for access to gas pipelines exists under the National Gas Law (NGL) and National Gas Rules (NGR), with access regulation only applying to pipelines that are 'covered'.

Currently, a pipeline becomes 'covered' by access regulation when a party applies to the National Competition Council (NCC) to have the coverage status of the pipeline changed. The NCC examines the application for coverage against four 'coverage criteria' which must be met for a pipeline to be covered. The decision on whether to declare a pipeline 'covered' is then made by the relevant Minister based on the recommendation of the NCC.

The COAG Energy Council's *Consultation Paper*[1] discusses the existing 'coverage criteria' in the context of recent findings from the Australian Competition and Consumer Commission (ACCC). In particular, the *Consultation Paper* calls for submissions on the effectiveness of the current coverage test and the ACCC's recommendation to replace the coverage test with a new market power test.

Scope of this paper

Infrastructure Partnerships Australia (IPA) is pleased to respond with this submission to the COAG Energy Council.

As Australia's peak infrastructure body, representing public and private infrastructure owners and operators, of all types, we are keen to contribute to this review process, as the results will no doubt carry large implications for confidence in regulatory frameworks across not only gas transmission, but all infrastructure sectors.

Our submission covers the broad themes outlined in the COAG Energy Council's *Consultation Paper* but noting the relatively brief period for responses, we have not answered each question in sequence. Rather, our submission addresses the *Consultation Paper* in totality – and focuses on key questions of relevance.

Recommendation

We recommend that the COAG Energy Council rejects the ACCC's proposal to replace the current coverage test with a market power test. Furthermore, we recommend that consistency is maintained in the 'coverage criteria' which apply to gas pipelines and the criteria that apply to all significant infrastructure, under the National Access Regime (NAR).

Our key points

We submit that an appropriate and predictable regulatory framework is critical to maintain investment in gas pipelines. Significantly, investment in gas pipelines and the availability and flexibility of routes to market for upstream gas producers is a critical aspect of addressing the divergence between domestic gas supply and demand.

[1] Council of Australian Governments Energy Council, Consultation Paper, 4 October 2016, http://www.coagenergycouncil.gov.au/publications/examination-current-test-regulation-gas-pipelines-consultation-paper

If regulatory settings for the gas pipeline sector pose a significant risk to investment, there will be a dampening effect on investment in both the pipeline sector and, in turn, the upstream gas production sector. We submit that reduced investment will result in less competition in both the gas production and transmission sectors, resulting in adverse market outcomes across the entire gas supply chain and for gas consumers.

Acknowledging the relationship between the regulation of gas pipelines and the broader gas supply chain we submit that the ACCC's proposal to replace the current coverage test with a market power test would have a detrimental impact on the achievement of the National Gas Objective (NGO) which seeks to:

"Promote efficient investment in, and efficient operation and use of, natural gas services for the long-term interests of consumers of natural gas with respect to price, quality, safety reliability and security of supply of natural gas."

We submit that the ACCC's proposed criteria would expand the potential coverage of the regulatory framework that applies to gas pipelines, putting pipelines at risk of heavy handed regulation and increasing regulatory risk due to uncertainty associated with the application of the criteria.

Further we find that the ACCC's inquiry incorrectly emphasises the rate of return on incremental investments - rates of return which, when viewed in the context of a pipeline's entire asset base, we submit are likely to be comparable with the returns on other forms of infrastructure. This is particularly true given the enhanced risk profile of these investments and the fact that they make up only a small proportion of a pipeline's asset base.

Additionally, we would like to highlight that gas transmission charges account for only 8 per cent of retail gas prices based on national averages and 10 per cent of industrial prices in the east coast gas market[2] and that transmission charges are not responsible for the recent surge in gas prices.

As the peak industry body for the infrastructure sector, representing both public and private stakeholders across major infrastructure, we are concerned that the ACCC's recommendations would result in significant inconsistency between the coverage criteria applying to gas transmission pipelines and the criteria applying to all significant infrastructure under the NAR.

We note the importance of ensuring consistency in the regulatory frameworks across industries is recognised in the overall objectives of the NAR under section 44AA of the Competition and Consumer Act (CCA). The CCA states a clear objective to provide a framework and guiding principles that encourage a consistent approach to access regulation in each industry.[3]

Overview of ACCC position

In its April 2016 report, the ACCC stated that gas transmission pipeline owners are engaging in monopoly pricing behaviour, citing the following evidence:

- rates of return assumed by pipeline owners for incremental investments over the past three years exceeded the Australian Energy Regulator's benchmark return on equity by between 1.4 and 20 times;

[2] *Oakley Greenwood (2016). Gas Price Trends Review. Report prepared for the Department of Industry, Innovation and Science.*
[3] *Competition and Consumer Act 2010* – Sect 44AA.

- ‘as available’ and ‘interruptible’ charges and forward haul charges for some pipelines are two to five times higher than would be the case under regulation;
- one pipeline operator has estimated it is earning 70 per cent more revenue than would be the case under regulation; and
- one pipeline owner is attempting to maintain a rate of return that is 1.5 times higher than would be the case under regulation, despite facing declining volumes.

The ACCC stated that the regulatory arrangements under the National Gas Law (NGL) and National Gas Rules (NGR) are not an effective constraint on the behaviour of pipeline owners because they do not address the type of market failures that have been observed in the market for the provision of gas transmission services. The ACCC contends that, while not necessarily having a detrimental effect on downstream competition, the monopoly pricing behaviour of pipeline owners is giving rise to economic inefficiencies.

Furthermore, the ACCC also considers the existing regulatory framework to be ineffective at preventing the exercise of market power even where pipeline owners are subject to regulation.

Review of the ACCC’s supporting evidence

We submit that it is not appropriate for the ACCC to draw conclusions on the pricing behaviour of an infrastructure provider based on the rates of return earned on incremental investments. The commercial opportunities and risk profiles pipeline owners face when investing in these expansions are significantly different to those applying across the entire asset base. In addition, these investments typically account for a very small component (approximately 5 per cent) of the entire asset base.

A similar argument applies in relation to the ACCC’s analysis of ‘as available’ and ‘interruptible’ service charges. These charges differ significantly from the services typically provided by pipeline owners and account for a very small proportion of total revenues derived from gas transmission pipelines on the east coast.[4] The ACCC’s findings shed little light on the pricing behaviour of transmission pipeline owners.

It is true that delivered gas prices in the east coast market have risen significantly in recent years, driven primarily by growth in the global LNG market and the construction of new export facilities in Queensland. From 2006 to 2015, retail gas prices have increased in real terms by 23 per cent in Victoria, 45 per cent in New South Wales and 39 per cent in Queensland.[5] In addition, industrial gas prices in the east coast gas market have increased by 66 per cent[6] in real terms between 2002 and 2015.[7]

However, the ACCC’s contention that monopoly pricing behaviour by transmission pipeline owners has significantly contributed to these higher prices is incorrect. Transmission charges account for

[4] For example, for the Dampier to Bunbury Natural Gas Pipeline, it is estimated that these revenues account for less than 1 per cent of total revenues.
[5] Oakley Greenwood (2016). Gas Price Trends Review. Report prepared for the Department of Industry, Innovation and Science.
[6] This includes the impact of the carbon tax.
[7] Oakley Greenwood (2016).

only 8 per cent of retail gas prices based on national averages and 10 per cent of industrial prices in the east coast gas market.[8] In addition, Oakley Greenwood found that gas transmission charges have only increased by around 5 per cent and 4 per cent in real terms for retail and industrial users respectively between 2006 and 2015.[9]

We recommend that any of the ACCC's findings on the returns of particular pipeline owners or of particular investments needs to be viewed through this lens. The increase in demand for gas transmission services in Eastern Australia has mirrored the dramatic growth in production; relatively sudden and significant increases in throughput unaccompanied by price rises can be expected to result in larger than expected returns to pipeline owners. However, such an outcome does not equate with monopoly pricing – it simply reflects one outcome of many that were possible at the time the pipeline investment was undertaken. It does not mean that widespread re-regulation of the sector is warranted, especially if proposed reforms to the Competition and Consumer Act (discussed below) are reflected in the NGL.

The ACCC report acknowledged the positive investment outcomes that have been achieved in the gas transmission pipeline sector that has enabled the provision of the necessary transmission capacity to enable gas to be transported to market. The ACCC also noted that pipeline operators have responded well to the shifting demands of market participants, offering more flexible services and undertaking major capital investments resulting in more dynamic pipeline flows and a greater degree of pipeline interconnection.[10]

However, the ACCC did not examine whether such dynamism would have emerged in the heavy handed regulatory environment it recommended. Similarly, the ACCC did not examine the impact of its recommendations on future incentives to invest in gas transmission capacity – the focus of regulators and governments must be on creating a policy and regulatory environment that is conducive to investment in all segments of the gas supply chain, so that there is the necessary investment in both upstream gas production and processing and in pipeline capacity.

With rising demand and tightening supply, availability and flexibility in transmission pipeline capacity, and thus investment in the gas transmission pipeline sector will be critical to ensuring that future domestic gas demand is met. The potential impact of heavier handed regulation on these outcomes is discussed further below.

ACCC's proposed regulatory test

In light of its findings that the current regulatory framework is ineffective, the ACCC has proposed alternative coverage criteria to be applied to gas transmission pipelines. The ACCC's proposed test is a radical departure from previous coverage tests as it seeks to replace the existing regulatory framework under the NGL with a test comprised of three criteria. In accordance with the proposed test, a transmission pipeline would become subject to regulation if:

- it has substantial market power;
- it is likely that the pipeline will continue to have substantial market power in the medium term; and

[8] Oakley Greenwood (2016).
[9] Oakley Greenwood (2016).
[10] ACCC (2016). Inquiry into the east coast gas market, p 8.

- the coverage of the pipeline will or is likely to contribute to the achievement of the National Gas Objective (NGO).

Comparison to the NGL coverage criteria

The criteria that currently applies to the coverage of gas pipelines under the NGL is as follows:

- access (or increased access) to the pipeline would promote a material increase in competition in at least one other market;
- it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the pipeline to which the criteria are being applied;
- access (or increased access) to the pipeline can be provided without undue risk to human health or safety; and
- access (or increased access) to the pipeline would not be contrary to the public interest.

The ACCC's alternative coverage criteria is based on its unsubstantiated view that, due to the structure of the gas market, the existing criteria under the NGL are ineffective at constraining the behaviour of pipeline owners. However, we submit that the current NGL criteria are correctly focused on the impact of coverage on competition in related markets and that regulation be applied where it is in the public interest.

As gas transmission pipelines are not vertically integrated, the ACCC asserts that the declaration of the services provided by pipelines would not increase competition in dependent markets (say, in contrast to pipelines that might be vertically integrated in a dependent market). Significantly, if the ACCC's contention on this issue was correct, then the Australian Competition Tribunal would not have declared the services at the Port of Newcastle (based on the Australian Competition Tribunal's interpretation of criteria (a)), as the Port of Newcastle is not vertically integrated into any dependent market.[11]

Whilst it likely that the relevant criteria in the Competition and Consumer Act is to be amended, egregious pricing by a vertically separated monopoly infrastructure provider will generally have adverse competition impacts on dependent markets (in contrast to the ACCC's assertions). In any event, the proposed amendments will clearly be an effective response to the harm the ACCC asserts is occurring.

Shift away from focus on competition

The ACCC's criteria effectively propose that a pipeline be regulated if it holds non-transitory and substantial market power and its coverage will contribute to the achievement of the NGO. The NGO is to promote efficient investment in, and efficient operation and use of, natural gas services for the long-term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.

[11] Application by Glencore Coal Pty Ltd [2016] Australian Competition Tribunal 6.

Thus, the ACCC's proposed criteria represents a change in focus from the impact of coverage on competition with a dramatic lowering of the threshold and a corresponding loss of clarity from the current test.

It is widely accepted that competitive markets deliver efficient outcomes and maximise consumer welfare. Indeed, the promotion of competition to enhance the welfare of Australian consumers is the objective of the CCA, under which the ACCC operates. It should be the overriding objective of any regulatory regime, including the NGL, to promote efficient outcomes, by ensuring that regulatory settings promote outcomes consistent with competitive markets.

The key role played by competition in assessing the appropriate level of regulatory intervention is demonstrated by its inclusion in the criteria under which proposals to increase regulatory coverage are assessed. The impact of coverage on competition is a criterion under both the current NGL and the NAR under Part IIIA of the Competition and Consumer Act. The NCC has previously drawn parallels in relation to the coverage criteria for pipelines under the NGL and to the declaration criteria under Part IIIA, the first of which is that coverage must result in a material increase in competition.[12] Prolonged excessive pricing that does not attract a competitive response will normally significantly reduce competitive opportunities in upstream and downstream markets, as it will reduce the competitiveness of gas relative to other fuels (downstream) and provide a disincentive to the exploration and development of gas fields upstream.

This can be seen in the linkage between the gas transmission sector and upstream investment in gas production and processing. Gas producers are heavily reliant on pipeline infrastructure to be able to transport gas to either export facilities or domestic customers and, as the ACCC points out, the inability to market gas will inevitably affect gas exploration and market development opportunities. Indeed, if the regulatory settings in the transmission pipeline sector pose a significant risk to transmission investment, they will have a dampening effect on investment in both the pipeline sector and, in turn, the upstream gas production sector. This will result in less competition in both the gas production and transmission sectors, resulting in adverse market outcomes across the entire gas supply chain.

Similar dynamics exist in relation to the impact of competition in downstream markets, such as the use of gas by major industrial facilities. The viability of these facilities is contingent upon the ability to secure an affordable supply of gas (or alternative energy source). This is largely contingent on both the necessary quantities of gas being produced and the ability of gas suppliers to transport gas to customers via transmission pipelines at a competitive price. A lack of investment in pipeline capacity due to inappropriate regulatory settings and the flow-on impacts on gas production (see above) will prevent industrial users from accessing the necessary gas at a competitive price, resulting in a reduction in competition and adverse outcomes in these downstream markets.

Impact of ACCC's criteria on investment incentives

The ACCC's proposed criteria would expand the potential coverage of the regulatory framework applying to gas transmission pipelines, including increasing the risk of pipelines becoming subject to heavy handed regulation, in addition to increasing the degree of uncertainty associated with its application.

[12] National Competition Council (2013). Gas Guide – A guide to the functions and the powers of the National Competition Council under the National Gas Law.

Gas transmission pipeline owners have undertaken significant investment in pipeline capacity totalling approximately $30 billion over the past 15 years.[13] This investment has led to an increase in basin-to-basin competition and assisted in the development of gas trading hubs. The clarity and certainty provided by the NGL regulatory framework, in addition to bilateral negotiation and contracts, has been an important component of the environment that has facilitated these investments.

As discussed above, with demand increasing and gas supply tightening, the continued supply of gas into the domestic market in the medium to long term will be largely contingent upon continued investment in transmission pipeline capacity. The ACCC's proposed criteria represent a threat to this continued investment. By shifting the focus of the regulatory test from facilitating competitive market outcomes to targeting all pipeline owners with non-transitory market power (itself a very subjective test), in addition to the introduction of other highly subjective criteria (i.e. the extent to which coverage will contribute to the achievement of the NGO), the ACCC's proposed criteria would significantly increase the regulatory risk to which new pipeline investments would be exposed, dampening investment incentives in the sector.

The existence of substantial market power is not an appropriate threshold for the application of economic regulation. Despite extensive enquiry, the ACCC did not produce credible evidence that the existing threshold, or a modified threshold (such as that contemplated in proposed reforms to the Competition and Consumer Act) was ineffective at meeting legitimate policy objectives in the gas transmission sector. In addition to the clear market evidence, as acknowledged by the ACCC, of gas pipeline owners responding to market circumstances in a manner as would be expected under workable competition, there is also clear evidence of competition in the provision of new transmission pipeline capacity.

As such, the ACCC's proposed test confuses the situation that faces would-be pipeline developers before and after an investment has occurred. Before an investment, the investment opportunity is contestable – there is competition for the market opportunity. Assessing the environment post investment is according to entirely different circumstances to those that prevailed at the time the investment occurred. Accordingly, applying the ACCC's proposed test will invariably have a chilling effect on investment and the responsiveness of the pipeline industry to investment opportunities.

There is also significant regulatory risk associated with the qualitative and subjective assessment that would be conducted by the ACCC in assessing the third of its proposed coverage criteria – that coverage contribute to the achievement of the NGO. It is entirely possible (but not acknowledged by the ACCC) that were this criterion to have been applied over the past 15 years, several of the significant investments in pipeline capacity that have contributed to the development of the east coast gas market would not have been undertaken due to the regulatory risks involved.

The QSN Link in the South West Queensland Pipeline (SWQP) is an example of a pipeline investment that benefited from low regulatory risk. Constructed in 2008 at a cost of $140 million, the QSN Link is a 182km extension to the SWQP that has become a crucial link in the East Coast Gas Grid, enabling gas to flow to the Moomba gas supply hub and to the Adelaide and Sydney markets. The initial SWQP (constructed in 1996) was subject to access regulation by the ACCC under the Gas Code. However, a Queensland Government derogation precluded the ACCC from reviewing reference tariffs associated with the pipeline until 2016, with reference tariffs being approved by the

[13] APA Group – ASX Announcement: APA notes the release of the ACCC's East Coast Gas Report, 22 April 2016.

Queensland Minister. There is considerable doubt as to whether this critical investment would have proceeded in a riskier regulatory environment. The SWQP is not a covered pipeline under the NGL.[14]

The deferral or cancellation of investments in transmission pipeline capacity such as the QSN Link due to increased regulatory risk over the past 15 years would have resulted in an even more pronounced supply-demand imbalance in the domestic gas market. This is the risk currently facing the industry, particularly given the need for new investment in all segments of the gas supply chain if future domestic gas demand is to be met.

The potential significance of regulatory risks in relation to the viability of gas pipeline investments was previously noted by the Productivity Commission in its 2015 research paper on 'Examining Barriers to More Efficient Gas Markets':[15]

> …it is clear that access regulation can affect investment incentives. If pipeline owners are uncertain about how regulation would be applied (as discussed above) and if there are risks associated with the arrangements for determining regulated prices to expansions, the risks from investing in pipeline infrastructure could be compounded. These risks could increase investors' hurdle rate of return for making investments in spare capacity beyond the expected return, inhibiting investment. Also, if regulated rates of return are not expected to fully compensate investors for the risks incurred, investments may not proceed.

In addition to having a dampening impact on investment, regulatory frameworks, if too light-handed, can also result in an inefficiently high level of investment being undertaken. However, it is widely recognised, including by the Productivity Commission,[16] that the risk profile is asymmetric, with the potential adverse impacts of the dampening effect of overly heavy handed regulation on investment exceeding the risk of over-investment.

The Productivity Commission has previously stated the following in relation to the dampening effect of access regulation on investment incentives in the gas pipeline sector:[17]

> Investors in regulated pipelines will proceed only with projects that deliver the relatively low expected rate of return allowed by a regulator if those projects are also low risk. A distortion thus arises because some risky projects, which have the potential to generate economy-wide benefits, do not proceed as early as they might have otherwise.

As noted above, the conditions for investment, including regulatory settings, in the transmission pipeline sector have significant implications for market outcomes in the upstream gas production sector. Given the current supply-demand imbalance and projected growth in gas demand, there is a need for significant investment in gas production and processing.

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[14] 'QLD: South West Queensland Pipeline'; Australian Energy Market Commission; See: http://www.aemc.gov.au/Energy-Rules/National-gas-rules/Gas-scheme-register/QLD-Ballera-to-Wallumbilla; DOA: 20 September 2016.

[15] Productivity Commission (2015). Examining Barriers to More Efficient Gas Markets. Research Paper, p 115.

[16] Productivity Commission (2013). National Access Regime. Inquiry Report No 66, p 259-60.

[17] Productivity Commission (2004). Review of the Gas Access Regime. Inquiry Report No 31, p 107.

Investment in additional transmission pipeline capacity, while important to achieving efficient outcomes in the east coast gas market, is not a substitute for investment in additional gas production. This is demonstrated by the fact that, despite the worsening supply-demand balance in the domestic gas market, there have been no observed bottlenecks in gas transmission pipelines, with the flexibility and availability of pipeline capacity having actually increased in recent years.

Upstream investment is critical if the continued divergence between domestic gas supply and demand is to be addressed. A Gas Market Model developed by the Department of Industry, Innovation and Science indicates that based on available proved and probable gas reserves, there is a surplus of gas available[18] to the domestic market.[19]

However, it is important to note that adequacy of overall reserves does not necessarily imply that the investment necessary to produce the volume of gas required to meet demand will be undertaken. The need for investment is highlighted by the 2016 Gas Statement of Opportunities (GSOO) Report, which projects under its 'medium' or 'most likely' scenario that proved and probable gas reserves will start to deplete from 2019 and that in order to maintain adequate gas supply from 2019 to 2035 considerable development of gas reserves will be necessary.[20]

The realisation of the necessary level of investment in gas production is contingent upon a range of factors, one of which is the availability of transmission pipeline capacity. Gas producers cannot be expected to invest unless they can be confident that the necessary level of transmission pipeline capacity will be available for them to be able to transport their gas to market.

The importance of creating a policy and regulatory environment conducive to investment in transmission pipeline capacity is demonstrated by the fact that proved and probable gas reserves in the southern states are insufficient to meet demand over the long term, with customers to be reliant upon either the development of contingent resources or the importation of gas (via transmission pipelines) from other jurisdictions (e.g. Queensland or Northern Territory).[21]

Subjecting transmission pipelines to more heavy handed and uncertain regulation under the ACCC's proposed criteria will put this investment in gas production at risk, as gas producers will lose confidence in the ability of the transmission pipeline sector to deliver the necessary transmission capacity for producers to get gas to market. Investments in pipeline capacity will invariably be delayed (less responsive), distorted (less spare capacity) or diminished (due to financing difficulties) under regulation relative to the current environment, imposing costs on end users of gas.

Inconsistency with NAR criteria

The application of the ACCC's proposed criteria would result in significant inconsistency between the coverage criteria applying to gas transmission pipelines and the criteria applying to all significant infrastructure under the NAR. As previously discussed, the criteria that currently applies to gas transmission pipelines under the NGL are very similar to the NAR criteria.

The importance of ensuring consistency in the regulatory arrangements that apply to significant infrastructure across industries is recognised in one of the two overall objectives of the NAR under section 44AA of the CCA, which is to provide a framework and guiding principles to encourage a

[18] It is important to note the model has been built on the assumption that no additional trains are to be developed at the Gladstone LNG export terminal.
[19] Department of Industry, Innovation and Science (2015). Gas Market Report 2015.
[20] Australian Energy Market Operator (2016). 2016 Gas Statement of Opportunities.
[21] Department of Industry, Innovation and Science (2015).

consistent approach to access regulation in each industry.[22] In addition, the implementation of a simpler and consistent national approach to the economic regulation of significant infrastructure was a key objective of the CIRA.[23]

The ACCC has previously noted the important role that the access criteria under the NAR provides in terms of providing the framework for the regulation of infrastructure across all sectors of the economy:[24]

> The ACCC considers that Part IIIA has been, and continues to be, successful in promoting a consistent approach to access issues across the economy. This is the case even though Governments have legislated for industry-specific access regimes in a range of industries such as electricity, gas, telecommunications and post. While there are clearly differences between the specifics of each of these access regimes, Part IIIA is the umbrella or template. The principles in these industry-specific regimes are drawn from the more general access provision of Part IIIA. Part IIIA therefore promotes a level of consistency in economic regulation across sectors. It follows that the ACCC applies a broadly consistent approach to regulatory issues across the economy.

The ACCC's proposal to implement a set of criteria to apply to the regulation of gas transmission pipelines that differ significantly from the NAR criteria is inconsistent with its stated position. The ACCC has also recognised the importance to maintaining consistency in terms of the regulation of access to infrastructure across sectors in incentivising efficient investment:[25]

> The ability of an integrated, multi-sectoral regulator to provide coordinated regulation and to deliver consistency across sectors is of particular importance to promoting efficient investment incentives. Given that all industries compete for investment capital, inconsistent approaches to issues such as the valuation of capital could lead to inefficient investment patterns.

Comparison to proposed declaration criteria under the NAR

Based on the recommendations contained in the Harper Review Final Report and the Federal Government's response, the proposed declaration criteria to apply under the NAR under Part IIIA of the CCA are as follows:[26]

(a) that access (or increased access) to the service would promote a material increase in competition in at least one market other than the market for the service, with the comparison based on competition with and without access on reasonable terms and conditions through declaration;

(b) that the facility that is used (or will be used) to provide the service could meet the total foreseeable demand in the market at the least cost;

[22] *Competition and Consumer Act 2010* – Sect 44AA.
[23] Competition and Infrastructure Reform Agreement, 10 February 2006.
[24] Australian Competition & Consumer Commission (2013). Productivity Commission Review of the National Access Regime – ACCC Submission to Issues Paper, p 22.
[25] Australian Competition & Consumer Commission (2013), p 125.
[26] The criteria relating to the service not being declared if it is subject to a certified access regime remains as a threshold to the application of this test.

(c) that the facility is of national significance having regard to the size of the facility; the importance of the facility to constitutional trade or commerce; or the importance of the facility to the national economy;

(d) that the declaration of access would promote the public interest.

Importantly, the NAR criteria, unlike those proposed by the ACCC, do not explicitly focus on whether the infrastructure provider holds significant market power. Whether an infrastructure provider holds significant market power, even if non-transitory, is not sufficient justification for access regulation. Rather, the appropriate test is whether the relevant facility is a natural monopoly, that the declaration of the services provided by it will promote an increase in competition and subsequently efficiency gains in upstream or downstream markets, and the declaration would promote the public interest. To the extent that reform of the declaration test in the NGL is required, aligning it with the declaration threshold test in the CCA would achieve the legitimate policy objective and achieve consistency in access regulation.

There is a strong case for the access declaration criteria to be aligned across industries. Unless there are issues that are unique to gas pipelines that warrant different treatment, the declaration criteria against which all nationally significant infrastructure are assessed should be aligned. Applying a different coverage test to gas transmission pipelines will increase the regulatory risk associated with investment in this infrastructure compared to other forms of infrastructure, potentially distorting investment decisions and reducing economic welfare. In the absence of industry specific anomalies, the criteria set out in the Exposure Draft should therefore apply to all infrastructure, including gas pipelines under the NGL.

Conclusion

We hope that you have found IPA's submission a useful contribution to the examination of the current test for the regulation of gas pipelines and we look forward to engaging further with the COAG Energy Council as the review process unfolds.