INFORMATION MEMORANDUM

PROPOSED AMENDMENT TO THE NATIONAL THIRD PARTY ACCESS CODE FOR NATURAL GAS PIPELINE SYSTEMS

NATIONAL GAS PIPELINES ADVISORY COMMITTEE

1 February 2001

Table of Contents

TABLE OF CONTENTS 2

1. INTRODUCTION 4

2. REGULATORY OVERLAP AND BACKGROUND TO APIA PROPOSAL 6

2.1. Introduction 6

2.2. The Trade Practices Act and Code access regimes 6
Key differences between regimes *7*

2.3. Regulatory overlap 7

2.4. Regulatory certainty 8

2.5. Background on the Darwin-Moomba pipeline and the proposed amendment 9
Proposed Amendment *11*
Stated purpose of proposed Code change *11*

2.6. Reviews of Part IIIA and the Code 12
Productivity Commission review of Part IIIA *12*
Independent Code review *12*
Impact of timing of reviews on APIA's proposal *13*

3. TREATMENT OF PROSPECTIVE PIPELINES UNDER THE CODE 14

3.1. Overview 14

3.2. Code issues identified by APIA 14

3.3. Analysis of identified Code issues 16
i. Definition/use of the terms 'Pipeline' and 'prospective Pipeline' *16*
ii. Use of the terms 'Service Provider' and 'Prospective Service Provider' *18*
iii. Actual capital cost not known in advance *19*
iv. Access request before a Pipeline is in service *20*
v. Information *21*
vi. Limits on the duration of an Access Arrangement *22*
vii. Certainty on tariffs across periods *23*
viii. Scope for market-based tariffs *24*
ix. Delays *26*
x. Prescription, flexibility and regulatory discretion *26*

3.4. Conclusions on greenfields Pipeline issues 27

4. PROPOSED AMENDMENT TO THE CODE 29

4.1. Overview 29

4.2. Option A - APIA Proposal 29
Why the amendment may be desirable *30*
Possible disadvantages *31*

4.3. Option B – 'No coverage' alternative 31

4.4. Option C – Greenfields Pipelines amendments pending major reviews 33

4.5. Option D – No immediate change 34

5. REQUEST FOR PUBLIC COMMENTS 35

ATTACHMENT A — CODE BACKGROUND 36

1. The Natural Gas Pipelines Access Agreement 36

2. What the Code Provides 36
Coverage *37*
Access Arrangements *37*
Reference Tariff Principles *38*
Negotiation *38*
Dispute Resolution *38*
Ring fencing *38*

3. How the Code is given legal effect 39

4. How the Code is amended 40

ATTACHMENT B: STAKEHOLDERS' PRELIMINARY VIEWS 41

Western Australian Office of Energy 41

Australian Gas Association (AGA) 42

Australian Competition and Consumer Commission (ACCC) 43
Australian Competition and Consumer Commission approach to Part IIIA Access Undertakings in respect of Natural Gas Pipelines *43*
Timeframes for considering an access arrangement compared to an access undertaking *44*

1. Introduction

On 7 November 1997, the Commonwealth and each of the States and Territories agreed upon a National Third Party Access Code for Natural Gas Pipeline Systems (the Code). The Code was intended to establish a uniform national framework regulating third party access to natural gas Pipelines. Each of the States and Territories has passed legislation applying the Gas Pipelines Access Law, including the Code as Schedule 2, as a law of that State or Territory.

The Commonwealth, States and Territories have established the National Gas Pipelines Advisory Committee (NGPAC). The members of NGPAC include an independent chair and representatives of the Commonwealth and each of the States and Territories, together with industry and regulator representatives. One of NGPAC's functions is to make recommendations to Commonwealth, State and Territory Ministers on amendments to the Code. The relevant Ministers may, following receipt of a recommendation from NGPAC, amend the Code by agreement between them.

NGPAC is currently considering recommending to relevant Ministers that an amendment be made to the Code.

The amendment being considered has been put forward by the Australian Pipelines Industry Association (APIA), initiated by Epic Energy in the context of its proposed new gas transmission pipeline between Darwin and Moomba. The APIA proposal seeks to amend the Code in order to remove - on an interim basis pending the outcome of forthcoming reviews - the possibility of 'regulatory overlap'. That is, the dual regulation of a new pipeline under both the Code and Part IIIA of the *Trade Practices Act 1974* (TPA).

Neither APIA nor Epic Energy have categorically expressed the view that new pipeline developments cannot be built under the Code. However, APIA claims that all proponents currently involved in projects that must contemplate the Code and its alternatives have expressed major concerns with the Code as it stands.

APIA suggests that there are a number of problems and uncertainties with the Code, both in its application to prospective Pipelines, and its ability to accommodate particular terms of access that new Pipeline developers may wish to put forward. APIA believes that these problems lead to a lack of 'regulatory certainty' for greenfields projects, which is likely to discourage investment in new Pipeline infrastructure that could become covered by the Code. For those reasons, Epic Energy wishes to offer the ACCC an access undertaking under the TPA rather than an Access Arrangement under the Code. APIA is seeking this Code change urgently to accommodate Epic Energy's development timeframe, which requires regulatory certainty by 30 June 2001.

NGPAC has not reached a overall view in relation to the APIA proposal. Individual members of NGPAC has a range of views on whether, and to what extent, the issues raised by APIA represent substantial problems or uncertainties with the Code. Individual members do not necessarily accept the argument that there is a lack of

'regulatory certainty' under the Code, or that the level of 'regulatory certainty' in making an Access Arrangement under the Code is greater than that for undertaking under section 44ZZA of the TPA. NGPAC is of the view that APIA has raised some important issues that will need to be carefully considered to assess the extent to which modifications to the Code may be desirable. NGPAC welcomes any input from public consultation on these issues.

This Information Memorandum sets out:

- an outline of how regulatory overlap may arise and the background to the APIA proposal (section 2);
- the underlying problems and uncertainties identified by APIA in relation to the Code's treatment of 'greenfields' Pipelines and comments by NGPAC on each of these issues (section 3);
- the possible amendments to the Code NGPAC is considering, explaining why such amendments may be desirable and any possible disadvantages (section 4);
- a request for public comments on the issues raised and the possible amendments being considered (section 5); and
- a description of the Code, how it is given legal effect and how it can be amended (Attachment A);
- preliminary comments received by NGPAC from some members prior to the development of this information memorandum (Attachment B).

A copy of the original APIA proposal is available on the NGPAC website (http://www.coderegistrar.sa.gov.au). The APIA proposal described in this information memorandum is somewhat different from the original proposal (see section 4.2).

Written comments on the possible amendments, or any queries in relation to this Information Memorandum, should be directed to:

The Executive Officer
National Gas Pipelines Advisory Committee
Level 13, Wakefield House
30 Wakefield Street
ADELAIDE SA 5000
Fax: (08) 8226 5866
Email: temp.ngpac@saugov.sa.gov.au

Respondents should, if possible, supply a copy of their submission in electronic form (Word 6 or 7), as well as a printed version. The electronic form can be forwarded to the Executive Officer's above e-mail address.

Written comments should be received by Friday 23 February at 5.00pm (Adelaide time). All written comments will be treated as public documents and will be made available to interested parties on payment of an administration fee.

2. Regulatory overlap and background to APIA proposal

2.1. Introduction

NGPAC is currently considering recommending to Ministers an amendment to the Code proposed by APIA that NGPAC considers to be significant. As required by section 9.2(a) of the Code, this Information Memorandum sets out the significant amendment being considered and includes statements of why the amendment may be desirable. Background information on the Code is provided in Attachment A.

The APIA proposal is intended to remove the possibility of 'regulatory overlap' between two of the access regimes that may apply to prospective gas Pipelines, as described in this section. APIA is of the view that the Code regime cannot provide Prospective Service Providers with sufficient 'regulatory certainty' to commit to, or obtain the funding to proceed with, substantial greenfields Pipeline projects. The meaning of 'regulatory certainty' is discussed in section 2.4.

The proposed amendment is only intended to apply to new Pipeline projects for a limited time, in view of pending reviews of both access regimes that are expected to address both the regulatory overlap issue and the potential problems for greenfields Pipelines under the Code (see discussion in section 3).

2.2. The Trade Practices Act and Code access regimes

Overview

Part IIIA of the TPA was enacted to discharge the Commonwealth's obligation under Clause 6 of the Competition Principles Agreement signed in April 1995 (CPA). Part IIIA is intended to facilitate access by potential users to services provided by means of significant essential facilities, such as gas Pipelines. Relevantly, Part IIIA includes provisions:

- recognising State and Territory access regimes (such as the Code) for particular services, and providing a framework for them to be certified as "effective" access regimes under section 44ZZN; and
- establishing a mechanism for Service Providers and potential Service Providers to give access undertakings to the ACCC, which may include the terms on which they will provide access to the service (section 44ZZA).

Access regimes and access undertakings are not expressed in the TPA to be mutually exclusive. Accordingly, a Service Provider may offer, and the ACCC may accept, an undertaking in relation to a service that is, or could be, the subject of an access regime. In considering whether to accept a proposed access undertaking, however, the ACCC must have regard to specified matters, including whether access to the service is already the subject of an access regime. In this respect the ACCC has commented in its booklet "Access Undertakings" (September 1999) as follows:

> Part IIIA does not explicitly state that certification of an access regime as effective also excludes the operation of an undertaking. On this basis it is open to the Commission to consider and accept an undertaking from an access provider, even where the relevant access regime has been recognised as being effective.
>
> However, the Commission is not willing to accept undertakings where an effective regime is in place unless there are strong reasons for doing so.

NGPAC notes here that, to date, the Code has only been certified as effective in respect of South Australia, the ACT and Western Australia, although applications for certification have been made in respect of New South Wales, Victoria and Queensland.

Part IIIA of the TPA therefore provides gas Pipeline Service Providers with the option of offering an access undertaking to the ACCC. They may choose this option whether or not the Pipeline is covered by the Code. The ACCC must then decide whether to accept the undertaking, having regard to the criteria in section 44ZZA of the TPA. An assessment of the Code's applicability to the Pipeline will be a relevant factor in that decision.

Key differences between regimes

The key difference between the regimes is that section 44ZZA of the TPA is, on the face of it, less prescriptive in relation to the content of an access undertaking than the Code in relation to an Access Arrangement.

Section 44ZZA prescribes only that a proposed undertaking must specify an expiry date, and gives examples of other things that might be included. Section 3 of the Code, on the other hand, prescribes a number of elements that must be included in an Access Arrangement and section 8 contains particular requirements for Reference Tariffs.

The matters that the relevant regulator must consider in deciding whether to accept an access undertaking or Access Arrangement are also slightly different. The Code includes (in section 2.24) matters of specific relevance to gas Pipelines, while section 44ZZA is necessarily more general.

In practice, however, the application of section 44ZZA of the TPA and the Code may produce similar outcomes in terms of the content of an access undertaking or Access Arrangement. The ACCC has recommended that owners or operators should provide sound reasons should they wish to depart from the principles reflected in the Code.

2.3. Regulatory overlap

Given that access to a service may be regulated under either an applicable access regime or an access undertaking, the potential for regulatory overlap arises, that is, can that service be regulated simultaneously by both methods? For example, a new gas Pipeline is a facility that can be regulated by an undertaking under Part IIIA. The same Pipeline may also become covered under the Code as outlined in section 2.2 of

this Information Memorandum, on the application of any person. The Code would then require the Service Provider to submit an Access Arrangement in respect of the Pipeline, irrespective of the Service Provider's choice to offer an access undertaking.

Accordingly, a Service Provider may be bound both by the terms of its access undertaking to the ACCC and by the terms of an applicable access regime such as the Code (possibly with different regulators, although the ACCC is also the relevant regulator under the Code for gas transmission Pipelines except in Western Australia). The ACCC has recognised this issue in its "Access Undertakings" booklet:

> If the Commission accepts an undertaking where there is an existing access regime, a possible outcome is regulatory overlap. Areas such as dispute resolution, for example, may be covered by more than one regulator. The Commission will take this into account when assessing undertakings, with the objective of maintaining a consistent and coordinated approach to regulatory activities between the Commonwealth, State and Territory regulators.

Section 109 of the Commonwealth Constitution is relevant to the issue of regulatory overlap. Section 109 states that:

> When a law of a State is inconsistent with a law of the Commonwealth, the latter shall prevail, and the former shall, to the extent of the inconsistency, be invalid.

Section 109 could be applied to give priority to an access undertaking under the TPA (a Commonwealth Act) over the Code, which is applied by State and Territory laws, in two situations:

- where there is a necessary inconsistency because the Commonwealth act intended to "cover the field" of access regulation to the exclusion of State access regimes; or
- where it is impossible (not just impractical) to comply with the terms of both regimes.

As section 44ZZA contemplates that an access regime and an access undertaking may coexist, the TPA apparently did not intend to "cover the field". Consequently, the two mechanisms may coexist, to the extent that is possible to comply with both. This overlap may produce undesirable results, for example:

- unnecessary duplication where a Service Provider must submit an Access Arrangement when an undertaking is already in place;
- the possibility of different maximum tariffs applying under the two regimes (because the Service Provider could theoretically comply with both by charging no more than the lower amount); and
- the possibility of dual dispute resolution procedures and appeal paths under the TPA and the Code.

2.4. Regulatory certainty

APIA and Epic Energy use the term 'regulatory certainty', in the context of a greenfields Pipeline, to mean that a Prospective Service Provider is able to ascertain, in advance of the decision to invest, the tariffs (or maximum tariffs) and other key terms and conditions that a regulator will apply for access seekers. This is required as foundation customer contracts typically have 'most favoured nation' clauses that

provide for a foundation customers price not to be more than the price for a subsequent user. The Prospective Service Provider also requires certainty that the regulator will not revise the tariffs, terms and conditions outside of the range or the circumstances that may be specifed for in the initial Access Arrangement or undertaking for a minimum fixed period. This period is sometimes called the investment horizon and is the period over which a degree of commercial and regulatory certainty is required in relation to the future cash flows in order to be able to commit to, and obtain finance for, the initial investment. The investment horizon is typically linked to the period of the foundation customer contracts. In APIA's view, developers and their financiers generally need regulatory certainty over the investment horizon before they can commit to construction of a major Pipeline.

Epic Energy believes it can obtain greater regulatory certainty for the DMP by drafting and offering to the ACCC an access undertaking under section 44ZZA rather than submitting a voluntary Access Arrangement under section 2.3 of the Code.

2.5. Background on the Darwin-Moomba pipeline and the proposed amendment

Epic Energy is proposing to develop a new natural gas transmission pipeline from Darwin to Moomba in South Australia (the DMP). The new 2,200km 'Timor pipeline' would involve an investment by Epic Energy of up to A$1.5 billion, and would transmit gas initially from the Bayu-Undan field in the Zone of Cooperation and subsequently other fields in the region in the Timor Sea to gas markets in the Eastern and Southern States of Australia. A description of the project is provided in Box 1 below.

Box 1 Overview of the Proposed Darwin to Moomba Pipeline

Epic Energy is seeking to build, own and operate a large diameter high pressure natural gas pipeline between Darwin and the Moomba gas hub in South Australia. If the project goes ahead, the new pipeline would be the longest high-pressure large-diameter pipeline in Australia.

Epic Energy anticipates that the new pipeline would be characterised by:

- a 20-24 inch diameter;
- an initial capacity of 100 PJ/a (300 TJ/d);
- a fully compressed capacity of 200 PJ/a (600 TJ/d);
- a maximum operating pressure of 2,000+ psi;
- 7 compressor stations; and
- laterals to Gove (Nabalco), and potentially to Mt. Isa and Ballera.

In terms of the commercial aspects of the project, and its potential economic and environmental effects, Epic Energy claims that the project would:

- involve an initial capital investment of approximately A$1-1.5 billion;
- generate around 1,600 jobs during construction, and 20 full-time jobs once operational;
- provide gas-on-gas competition based on the world class Timor Sea reserves;
- expand security of supply in Australian gas markets;
- enhance greenhouse gas benefits through use of gas as a fuel source (eg displaces oil burning by Nabalco at Gove); and
- provide a royalty stream to East Timor.

Epic Energy and Phillips Petroleum Company of Australia ("Phillips") have been working together to develop the market in South Eastern Australia for gas produced by Phillips and the transmission of that gas through the DMP.

A significant proportion of the pipeline's capacity would be contracted with foundation customers, which would underpin the financing of the project. Epic Energy claims that the prices in these contracts reflect market prices as they would be negotiated between commercial entities of equal bargaining power.

Epic Energy advises that the initial capacity of the pipeline may not exceed the initial contracted capacity, however, the intention is that it will be configured in such a way as to provide for more efficient expansion of capacity subsequently. Such a configuration would be more expensive than a pipeline optimised for the initial contracted capacity but would have the advantage of lower incremental expansion costs.

Epic Energy proposes to bear the risk that a market for this potential spare capacity will fail to materialise. Also Epic Energy will take the construction risk that it can contract the capacity at a cost that will provide the expected return. The Reference Tariff applying in the access regime would apply to any spare capacity. Epic Energy claims that, given its market and construction risks, it requires certainty of the Reference Tariff for the full investment period (likely to be about 20 years). In particular, without this certainty, there is a concern that foundation customer contracts may have 'most favoured nation' clauses under which the foundation contract price could fall to a potentially lower Reference Tariff. Epic Energy submits that unless greater regulatory certainty can be achieved in advance in relation to third party tariffs, terms and conditions, then it would have no alternative but to reduce the size of the pipeline to cater for foundation volumes only if it constructs the pipeline at all.

Epic Energy is seeking a quick decision from NGPAC on the basis that timing issues are critical in two areas.

First, Epic Energy claims that Phillips' have an arrangement with a construction firm (Multiplex) that includes an option in relation to a sizing of the offshore pipeline, and that this option expires on 30 June 2001. According to Epic Energy, Phillips claims the proposal for the construction of the off-shore pipeline is an essential component in the competitiveness of this gas delivery chain, and there is no guarantee that it would be offered beyond 30 June 2001. The final sizing of the offshore pipeline is dependent on the sizing of the on-shore pipeline. Epic Energy claims that it must urgently progress and secure formal customer commitments on key commercial terms and regulatory certainty before Epic Energy can commit to Phillips in a manner that will enable Phillips to exercise the off-shore pipeline option prior to June 30, 2001.

Second, Epic Energy's potential customers have expressed a strong interest for new gas supplies to be delivered by 2004. In order for Epic Energy to meet this market demand, it believes that regulatory certainty must be achieved no later than June 30, 2001.

Proposed Amendment

The proposed amendment to the Code considered in this Information Memorandum is sought by APIA, against the background of Epic Energy's proposed construction of the DMP. Epic Energy wishes to offer an access undertaking to the ACCC under Part IIIA in respect of the DMP and wishes to avoid regulatory overlap by amending the Code such that it will not be required to submit an Access Arrangement under the Code for the period of the undertaking. In short, the APIA proposal argues that:

- the detailed provisions of the Code are aimed more at existing Pipelines than prospective or 'greenfields' Pipelines;
- the Code provisions relating to Access Arrangements and Access Arrangement Information cannot be effectively applied to prospective Pipelines;
- in particular, the Code provisions are too inflexible and prescriptive to accommodate the proposed DMP in areas such as the setting of reference tariffs; and
- as a result, Epic Energy cannot obtain sufficient regulatory certainty to proceed with the DMP under a Code Access Arrangement.

In view of the proposed major reviews of Part IIIA and the Code, APIA's proposed amendment focuses on providing an interim solution to the problems of regulatory overlap by clarifying that, if and for so long as a Service Provider has an access undertaking in force, it would not be required to submit an Access Arrangement or Access Arrangement Information under the Code. APIA believes that this amendment would allow progress on the DMP (and similar projects) to continue in the medium term while any problems with the Code are addressed at or before the proposed major review.

Stated purpose of proposed Code change

In a paper to NGPAC dated 20 November 2000, APIA brought forward Epic Energy's Code change proposal. APIA states that the purpose of the proposed amendment is:

> to allow Service Providers of new Pipelines to achieve the necessary level of regulatory certainty prior to the Pipeline being built, to remove doubt about the application of the Code to "prospective Pipelines" and to ensure the desired outcome through a straightforward amendment to the Code.

NGPAC has developed a number of alternatives to APIA's proposal, that may, to a greater or lesser degree, provide regulatory certainty in relation to prospective pipelines. These alternatives are also considered in this paper.

2.6. Reviews of Part IIIA and the Code

Productivity Commission review of Part IIIA

On 10 October 2000, the Assistant Treasurer announced a review by the Productivity Commission of Part IIIA of the TPA and Clause 6 of the CPA, to report within 12 months. The review will expressly not reconsider existing or pending undertakings or certifications of effective access regimes. The scope of the review will include (among other matters) consideration of:
- the objectives of Part IIIA;
- any alternative means to achieve the objectives of Part IIIA, including non-legislative approaches;
- the benefits, costs and overall effects of Part IIIA and any identified alternatives, including the impact of Part IIIA on investment in infrastructure;
- the need to promote consistency between regulatory regimes and efficient regulatory administration through improved coordination to eliminate unnecessary duplication; and
- mechanisms to improve Part IIIA processes for achieving third party access to significant infrastructure facilities, including increased flexibility and certainty and reduced complexity, costs and time.

The Productivity Commission's review will be a consultative process, resulting in recommendations to Government. The Assistant Treasurer indicated that Government intends to consider the recommendations and consult as appropriate, as soon as possible after receiving the Productivity Commission's report. Further details of the review, including an issues paper and indicative timetable, are available on the Productivity Commission's website at: http://www.pc.gov.au/inquiry/access/index.html.

Independent Code review

On 16 October 2000, the Federal Treasurer and the Minister for Industry, Science and Resources announced the Government's in-principle support for an independent review of the operation of the Code. The Ministers agreed that a review would be appropriate following completion of the regulators' final decisions on the first round of Access Arrangements and the outcome of the Productivity Commission's review of Part IIIA.

The announcement was made in response to infrastructure industry concerns over the impact of recent regulatory decisions on future investment in natural gas Pipelines. On this basis, it is likely that the review will consider whether the provisions of the Code are appropriate for prospective Pipelines. The Ministers noted, however, that NGPAC has an established procedure for the consideration of specific Code changes and encouraged the industry to make full use of this process.

The Commonwealth, State and Territory governments are currently considering a range of issues concerning the structure, scope, timing and *modus operandi* of the independent review. An agreement between governments on these details is anticipated to be reached early in 2001. At this stage, the review of the Code is expected to commence in the second half of 2001 and is expected to take 12 months to complete.

Impact of timing of reviews on APIA's proposal

In its paper to NGPAC dated 20 November 2000, Epic Energy states that:

> Timing pressures in relation to the project are such that Epic Energy has a very short period of time in which to obtain regulatory certainty for the access regime to apply for the DMP. That period does not allow it to wait for any of the broader reviews of the Code to resolve these uncertainties.

As noted in section 3.1, Epic Energy believes that if the DMP access regime cannot be finalised quickly, the opportunity to develop the DMP, or to develop it efficiently, is likely to be lost. Specifically, Epic Energy says that commercial issues for the gas supplier (Phillips) and market demand indications mean that it needs to achieve regulatory certainty for the DMP by 30 June 2001.

3. Treatment of prospective Pipelines under the Code

3.1. Overview

A major argument underlying APIA's proposed amendment is that the existing Code is inadequate to provide regulatory certainty for greenfields Pipeline development, and that it has acted as an impediment to new Pipeline investment. This section sets out and analyses a number of issues raised by APIA as problems or uncertainties of the Code in this respect. This section also raises a number of questions on which interested parties may wish to comment.

NGPAC notes that the APIA proposal does not seek to address these problems or uncertainties at this point through Code changes, given its view that such changes could not be achieved within Epic Energy's timeframe. APIA has indicated that these issues will continue to be explored with a view to bringing forward additional Code change proposals and/or as input to a major review of the Code. In commenting on these issues, interested parties should be aware that, even if every issue could be resolved to APIA's satisfaction within this timeframe, Epic Energy would still be entitled to choose the access undertaking route for the DMP, and in fact have indicated that they would do so.

3.2. Code issues identified by APIA

Comments have been made in a number of gas pipeline industry forums, in particular at a number of workshops, meetings and conferences organised by APIA, concerning problems with the Code in relation to greenfields Pipelines. The most detailed list of these issues to date is provided in APIA's proposal to NGPAC. A number of additional issues have been raised by APIA in subsequent discussions with NGPAC.

It should be noted that NGPAC has not reached an overall view in relation to these perceived problems and uncertainties. Individual members of NGPAC have a range of views on whether, and to what degree, the following may be problems or uncertainties in the Code. However, NGPAC notes that APIA raises a number of significant issues that will need to be carefully considered to assess the extent to which modifications to the Code may be desirable.

APIA has identified the following problems or uncertainties in the Code in relation to the development of greenfields Pipelines.

i. **Definition/use of the terms 'Pipeline' and 'prospective Pipeline'** — APIA notes that it is not clear whether a prospective Pipeline can be a covered Pipeline for the purposes of the Code given the inconsistency in the Code between the definition of 'Pipeline' and the references to prospective Pipelines in sections 1.20 and 2.3 of the Code.

ii. **Use of terms 'Service Provider' and 'Prospective Service Provider'** — APIA notes that to the extent that any sections of the Code (other than sections 2.4 to 2.27, which are specifically referred to in section 2.3) refer to a 'Service Provider', they do not include a reference to a 'Prospective Service Provider'.

iii. **Actual capital cost not known in advance** — Section 8.12 provides that the 'initial Capital Base' is the actual capital cost of those assets at the time they first enter service. APIA claims that it is absurd to attempt to apply section 8.12 when the capital expenditure has not been incurred and when a commitment has not yet been made to the construction of the Pipeline.

iv. **Access request before Pipeline in service** — If an Access Arrangement was approved under the Code prior to any commitment to build the Pipeline, then APIA asks how the Prospective Service Provider would deal with an access request received prior to the Pipeline being built, in particular where it may never actually get built?

v. **Information** — What would be required to be included in any Access Arrangement Information ("AAI") submitted for a prospective Pipeline? APIA notes that the effect of sections 2.6 and 2.7 is to require all the information specified in Attachment A to the Code to be included in the AAI, the Prospective Service Provider would be faced with the problem that most of that information would not be known or available at the time the proposed AAI would need to be submitted. APIA also notes that this raises the question of whether such information or approach is appropriate for a prospective Pipeline.

vi. **Limits on the duration of an Access Arrangement** — APIA notes that there is uncertainty regarding whether the discretion afforded to the regulator under the Code can support a duration for an Access Arrangement Period that matches the investment horizon for a greenfields pipeline development, which is typically around 15 to 20 years, without any re-openers.

vii. **Certainty on tariffs across periods** — If a number of Access Arrangement Periods are to be required over the investment horizon, APIA claims that there are serious limitations regarding the use of Fixed Principles to establish regulatory certainty for tariff structures and methodologies over the period.

viii. **Scope for market-based tariffs** — APIA notes that there is uncertainty regarding whether the Code can adequately support an approach to developing tariffs that is based on the market price arising from negotiations with foundation customers, as opposed to a cost-based approach.

ix. **Delays** — The experience to date has shown that a significant period elapses between the date proposed Access Arrangements are submitted and the date final approval is granted. No Access Arrangement has been approved in less than 12 months time, many taking 20 months. APIA makes no observation as to the "fault" for this, but notes that much time is spent by all parties concerned in dealing with the detail and application of the Code in the prescriptive provisions such as section 8.

x. **Prescription, flexibility and regulatory discretion** — APIA has made a number of comments on these issues as follows. While the intent behind the Code was probably to provide a non prescriptive system, similar to that under Part IIIA of the TPA, the inclusion of a number of sections, such as sections 3 and 8, which include very prescriptive provisions has served to confuse the effect of the Code. APIA notes that, by the attention paid to the prescriptive provisions of the Code in decisions of regulators, there is a perception that the Code will be applied in an inflexible and prescriptive manner. APIA is of the view that given the problems of application to prospective Pipelines raised above this is a cause for serious concern, and hence uncertainty, as to how the Code will in fact be applied by regulators in this case. APIA notes that this aspect is reinforced by the regulators apparent concerns about creating precedents.

3.3. Analysis of identified Code issues

Each of the above issues raised by APIA is addressed below in turn. In many cases these are matters of interpretation of the Code. NGPAC notes that section 7 of the Appendix to the Gas Pipelines Access Law is relevant in relation to the general interpretation of the Code. Section 7 states that the interpretation that will best achieve the purpose or object of the Law is to be preferred to any other interpretation.

i. Definition/use of the terms 'Pipeline' and 'prospective Pipeline'

Legal advice obtained by Epic Energy and attached to the APIA proposal addressed the issue of whether a 'paper Pipeline' (ie a prospective Pipeline that may not yet be under construction or even have been committed to) could be covered, as follows:

> "…a Pipeline may become covered in one of four ways. For the purpose of this advice, only two ways are relevant, namely:
>
> (a) if any person applies to have the Pipeline covered under section 1.3 of the Code and the specified criteria in respect of Coverage are satisfied; or
> (b) if the Relevant Regulator accepts an Access Arrangement proposed by a Service Provider (or Proposed Service Provider) pursuant to section 2.3 of the Code.

Section 1.3 of the Code provides that any person may make an application to the NCC requesting that a particular Pipeline be covered.

"Pipeline" is defined in section 10.8 of Schedule 2 as having "the meaning given in the Gas Pipelines Access Law" ("Law").

Section 2 of Schedule 1 of the Law defines "Pipeline" to mean:
"a pipe, or system of pipes, or part of a pipe, or system of pipes, for transporting natural gas, and any tanks, reservoirs machinery or equipment directly attached to the pipe, or system of pipes, but does not include –

(a) unless paragraph (b) applies, anything upstream of a prescribed exit flange on a Pipeline conveying natural gas from a prescribed gas processing plant; or
(b) if a connection point upstream of an exit flange on such a Pipeline is prescribed, anything upstream of that point; or
(c) a gathering system operated as part of an upstream producing operation; or
(d) any tanks, reservoirs, machinery or equipment used to remove or add components to or change natural gas (other than odourisation facilities) such as a gas processing plant; or
(e) anything downstream of the connection point to a consumer."

Based on the above definition of Pipeline, it [the definition] does not on its terms apply to a "paper Pipeline". This is because it is defined in a tangible sense (ie, it refers to physical pipes).

This interpretation is supported by sections 1.22 and 1.23 of the Code which provide that a Prospective Service Provider (ie, a person who seeks or may seek to become a Service Provider) may seek an opinion from the NCC as to whether a proposed Pipeline would meet the criteria for Coverage in section 1.9 of the Code. The express use of the word "proposed" in this context clearly suggests that elsewhere, where Pipeline is used on its own, Pipeline has its physical/tangible meaning.

Also, the section states that while the NCC may provide an opinion in response to such a request, that opinion does not bind the NCC in relation to any subsequent application for Coverage of the Pipeline. Again, this supports the conclusion that Coverage pursuant to section 1.3 of the Code can only be sought in respect of a physical/tangible Pipeline.

In short, in our view, a person could not apply under section 1.3 of the Code for the Pipeline to be Covered if it was merely a "paper Pipeline". However, as soon as the definition of Pipeline became satisfied (ie, because some or all or the Pipeline had been constructed), a person could apply to have the Pipeline Covered.

However, in theory it is possible for a Service Provider (or a Prospective Service Provider) to obtain Coverage for a "paper Pipeline" in accordance with sections 2.3 and 1.20 of the Code. Section 2.3 of the Code expressly refers to a Prospective Service Provider in respect of a proposed Pipeline submitting a proposed Access Arrangement to the Regulator for approval. Section 1.20 of the Code deems a Pipeline which is subject to an Access Arrangement submitted under section 2.3 of the Code to be Covered from the date that the Access Arrangement becomes effective."

NGPAC agrees that a prospective Pipeline is covered under section 1.20 of the Code if a Prospective Service Provider volunteers an Access Arrangement under section 2.3 of the Code and the Relevant Regulator approves that Access Arrangement. This was the clear intention when the Code was drafted.

APIA's proposal also notes, however, that even if a 'paper Pipeline' can be covered some problems remain in applying the Code to a prospective Pipeline, as numerous Code provisions (and in particular in section 8) use the term 'Pipeline' but do not use the term 'prospective Pipeline'. Similarly, the proposal notes that the Code uses the term 'Covered Pipeline', but that the term does not apply in relation to a paper Pipeline until an Access Arrangement is approved. APIA suggests that this casts doubt on whether section 8 of the Code can be applied to a 'paper Pipeline'.

NGPAC agrees that there is some inconsistency in the definition and/or use of the terms 'Pipeline' and 'prospective Pipeline', which may lead to ambiguity in applying parts of the Code to prospective Pipelines. However, NGPAC believes that, if any ambiguity exists, it would be relatively easy to remove through a simple Code amendment. For example, section 2.3 of the Code could be amended to provide that in relevant sections of the Code the term 'Pipeline' includes a 'prospective Pipeline' that is the subject of a proposed Access Arrangement under section 2.3. This change would not affect the voluntary nature of an Access Arrangement submitted by a Service Provider in regard to a Prospective Pipeline under this section.

- Does the use of the term 'Pipeline' and 'prospective Pipeline' in the Code mean that some sections of the Code (eg Section 8) cannot apply to paper pipelines?
- If so, could this be fixed by a simple Code change to section 2.3?

ii. Use of the terms 'Service Provider' and 'Prospective Service Provider'

Similarly, the APIA proposal noted that to the extent that any sections of the Code (other than sections 2.4 to 2.27, which are specifically referred to in section 2.3) refer to a 'Service Provider', they do not include a reference to a 'Prospective Service Provider'.

NGPAC also notes that the Code defines a 'Service Provider' by reference to the Gas Pipelines Access Law definition, ie, "in relation to a Pipeline or proposed Pipeline … the person who is, or is to be, the owner or operator …". NGPAC agrees, however, that the separate reference to Prospective Service Providers in section 2.3 of the Code may cause interpretation problems where the term 'Service Provider' is used in some other sections of the Code. However, NGPAC believes that any such problem would be relatively easy to resolve through a simple Code amendment. For example, section 2.3 of the Code could be amended to provide that in the relevant sections of the Code that the term 'Service Provider' includes a 'Prospective Service Provider'.

- Does the use of the terms 'Service Provider' and 'prospective Service Provider' in the Code mean that some sections of the Code (eg Section 8) cannot apply to paper pipelines?
- If so, could this be fixed by a simple Code change to section 2.3?

iii. Actual capital cost not known in advance

The relevant section of the Code is section 8.12:

> 8.12 When a Reference Tariff is first proposed for a Reference Service provided by a covered Pipeline that has come into existence after the commencement of the Code, the initial Capital Base is, subject to section 8.13, the actual capital cost of those assets at the time they first enter service. A new Pipeline does not need to pass the tests described in section 8.16.

The APIA proposal suggests that the Code was drafted for physical Pipelines and argues it is absurd to attempt to apply section 8.12 to an Access Arrangement for a prospective Pipeline when the actual capital expenditure has not been incurred and when a commitment may not even have been made on the construction of the Pipeline.

NGPAC acknowledges a possible interpretation of section 8.12 is that a fixed number for the term "actual capital cost" must be known in order for an Access Arrangement to be approved. However, NGPAC is of the view that a better interpretation of the Code (consistent with its original intention) is that while capital costs cannot be estimated, there are a number of potential approaches under which an Access Arrangement could be approved for a prospective Pipeline without needing to know the actual capital cost of the Pipeline in advance.

NGPAC notes that, in determining the initial Capital Base for a prospective Pipeline, the "actual capital costs" could be interpreted to be an ascertainable value rather than a specific number fixed in advance. The actual capital cost of a prospective Pipeline would not be known in advance of construction and commissioning, however, it would be highly likely to fall within a fairly limited and knowable range, in particular given the ability to estimate most of the costs fairly accurately. The necessary analysis by the regulator and the public consultation processes could be performed on this basis and an Access Arrangement could be approved. The actual capital cost could be determined *ex post* through some pre-defined audit process, and automatically flow through pre-defined formulae to the Reference Tariffs. In simple terms, the actual capital costs are whatever they turn out to be. This view can be supported by the definition of a "Tariff", which means the criteria that determine the Charge, not necessarily the actual figures themselves.

Some pipeline developers contest this view, suggesting that the actual capital cost of a prospective pipeline is not accurately known in advance of construction and a range of factors and risks will influence the final capital cost. APIA notes the following:

- The capital cost can be influenced by a range of variables (eg delays in securing planning and other approvals, on-site labour issues, unexpected weather delays, the need to resolve pipeline integrity issues post-construction), most of which add to the ultimate cost of the pipeline.
- The developer carries this construction risk, and while contractual arrangements, (eg with construction contractors) can be used to ameliorate some of these construction risks, final resolution of such issues can often take considerable time and with very uncertain outcomes, especially if there are disputes regarding the interpretation of contractual arrangements.
- The regulator could, in theory, derive an estimate of the likely actual capital cost, however, regulatory bodies have no practical knowledge of, or experience in, determining such complex "construction risk" issues. Any suggestion that matters relating to the initial capital cost could be resolved through "pre-defined formulae" to the Reference Tariff is highly simplistic and would do nothing to alleviate regulatory uncertainty.

NGPAC notes that an alternative would be to define the initial Access Arrangement Period as ending when the Pipeline comes into service (or to provide for a trigger for a review that has the same effect). A review could then be conducted but with the key parameters of the Reference Tariff Policy of the initial Access Arrangement protected from being re-opened by the Regulator through being identified as Fixed Principles under section 8.47 of the Code. One limitation of this approach is that fixed principles are confined to elements of the Reference Tariff Policy and cannot extend to things other than the Reference Tariff Policy (such as for example the duration of the second AA period, trading and queuing policies, etc). Aspects of this approach are further discussed under issue vii. below.

NGPAC has yet to form a view on whether an approved Access Arrangement including such approaches could potentially provide foundation shippers and debt and equity providers with sufficient regulatory certainty prior to the construction of (or to the commitment to the construction of) a prospective Pipeline to negotiate appropriate commercial arrangements.

- Can section 8.12 be applied to prospective Pipelines before the actual capital cost is known?
- Is it necessary or desirable to amend the Code to provide more explicitly for the types of arrangements described above? For example, specific provisions could be included in the Code enabling a Regulator to approve an Access Arrangement for a prospective Pipeline that constituted a range of binding principles along with a specific mechanism for applying these principles to determine Reference Tariffs after construction and commissioning.
- How complex would such amendments be and what implications would this have for the timing of the DMP?

iv. Access request before a Pipeline is in service

APIA has questioned how, if an Access Arrangement is approved under the Code prior to any commitment to build the Pipeline, the Prospective Service Provider would deal with an access request received prior to the Pipeline being built, in particular where it may never actually be built.

NGPAC notes that, while it is impossible for a Service Provider to physically provide access prior to a Pipeline coming into operation, it may be that a Prospective User wishes to make contractual arrangements in advance for such services. If an Access Arrangement is in place, the Prospective User may seek access in the future to services and could initiate dispute resolution proceedings in an attempt to enforce access under the Code.

NGPAC notes that the Access Arrangement could potentially define a range of conditions in relation to access to future Services that may include a queuing policy or risk-sharing mechanisms regarding the final tariff, and may define the point at which these Services become available (eg. after financial closure or when the Services become physically available). Otherwise, it would be difficult to see how an arbitrator could sensibly make a decision on access under the Code. Of course, the option of negotiation between the parties is open at any point and such a Prospective User may also have the option of becoming a foundation customer.

NGPAC notes that issue (iv), by itself, does not appear to warrant an urgent change to the Code, however, if other greenfields issues were being addressed through amendments to the Code then it would be sensible to also address this issue at the same time.

Does this issue warrant clarification through a Code change? If so, should it be progressed urgently or await the major review?

v. Information

The APIA proposal queries the content of any AAI submitted for a prospective Pipeline, and whether such information or approach is appropriate for a prospective Pipeline.

NGPAC notes that Service Providers of existing pipelines that are covered must provide a range of forecast information in an AAI. In this sense the requirements are not different to those for prospective Pipelines. However, it is acknowledged that the degree of confidence or certainty attached to the forecasts may be different between different pipelines depending on their characteristics, market environment and stage of development.

NGPAC also notes that there has been significant debate in the industry regarding the precise effect of sections 2.6 and 2.7 of the Code. The contrary view to that expressed by APIA in the proposal is that only the categories of information in Attachment A to the Code are required in an AAI, and the specific listed items are only illustrative. It may be that information is limited in some cases to reasonable

forecasts, within some range, of future financial or operational information. Ultimately, the content of an AAI is largely at the discretion of the Regulator.

NGPAC notes that the whole area of information provision by Service Providers, including through the AAI, was highly contentious during the development of the Code and has been identified by a number of stakeholders as an important area for attention in the proposed major review of the Code.

- Is it likely that a Regulator would interpret the Code in a manner that requires a Service Provider to provide information in relation to a prospective Pipeline that is unreasonable or impossible to comply with?
- Do the AAI requirements in relation to prospective Pipelines warrant clarification through a Code change? If so, should it be progressed urgently or await the major review?

vi. Limits on the duration of an Access Arrangement

The APIA proposal suggests that prospective Service Providers for new pipelines need fixed Reference Tariffs during the investment period (in Epic Energy's case, about 15 to 20 years) without any re-openers, and that there is uncertainty whether the discretion afforded the Regulator under the Code supports this.

NGPAC notes that under sections 3.18 and 3.19 of the Code, an Access Arrangement may be of any length, and is not limited to five years. If an Access Arrangement of more than five years is proposed, however, the regulator must consider whether the Access Arrangement should provide for within-period review mechanisms. This is a matter for the regulator's discretion.

Some stakeholders have noted that given the above parameters that a regulator must consider, in practice, regulators may be reluctant to approve longer periods. In response to this, the ACCC noted that a 10 year period was approved in relation to the Central West pipeline. However, other stakeholders noted that the issue does not appear to have been tested under the Code to date in relation to a ‘paper Pipeline’ (Central West was not a ‘paper Pipeline’). IPART noted that a 15-20 year period is possible under the Code but what is uncertain is whether sufficient justification could be provided for the Regulator to approve such a period. IPART also notes that there is no regulatory certainty that such a period would be granted under the section 44ZZA route without a similar justification.

- Does the current Code provide sufficient flexibility on the duration of an initial Access Arrangement Period for a prospective Pipeline?
- Do the parameters that a regulator must consider restrict, in practice, the likelihood that regulator will exercise the discretion to approve a longer period? Is more explicit guidance required to achieve regulatory certainty?
- Is a Code change warranted? If so, should it be progressed urgently or await the major review?

vii. Certainty on tariffs across periods

Notwithstanding the discussion above, if the regulator decides that an Access Arrangement should be reviewed every five years (or at intervals that are shorter than the Service Provider's investment horizon), the Access Arrangement may specify that some elements of the Reference Tariff Policy are "Fixed Principles". Under section 8.47 of the Code, Fixed Principles cannot be changed for a specified period (extending over one or more Access Arrangement reviews) without the agreement of the Service Provider.

NGPAC notes that subject to the potential problems in applying section 8.12 (discussed above), a Fixed Principle might state that a Reference Tariff is to be calculated in a certain way, for example by defining the detailed methodology to be applied. As such, Fixed Principles could potentially provide a high degree of certainty in relation to tariff structures or methodologies over time. However, NGPAC also note that the use of Fixed Principles is subject to some important limitations as outlined below.

The Reference Tariff itself cannot be a Fixed Principle. Fixed Principles are restricted to "structural elements" of a Reference Tariff Policy. Structural elements are principles or methodologies used to calculate a Reference Tariff, excluding "market variable elements". For example, a depreciation schedule, a financing structure or a rate of return margin may be structural elements, but not actual values which may vary with market conditions, such as sales figures, indices, interest rates, capital and operating costs.

In considering what elements may be Fixed Principles in an Access Arrangement, the Regulator will need to consider the respective interests of the Service Provider and Prospective Users.

Elements other than the Reference Tariff Policy cannot be Fixed Principles. So while the tariff methodology might be fixed, the non-tariff dimensions of the services to be provided under these tariffs could potentially change (eg Services Policy, Queuing Policy, Trading Policy, Extension/Expansions Policy).

- Are the provisions relating to Fixed Principles sufficient to provide regulatory certainty for tariffs across Access Arrangement periods?
- Is the inability to be able to make non-tariff elements Fixed Principles likely to be a problem in practice?
- Is a Code change warranted? If so, should it be progressed urgently or await the major review?

viii. Scope for market-based tariffs

APIA notes that some pipeline developers have stated a clear preference for offering third party access tariffs that are based on the market price arising from negotiations with foundation customers and that there is uncertainty regarding whether the Code can adequately support such an approach.

Epic Energy has indicated that its current intention is that the tariffs for the DMP would ultimately be set by the market. The prices negotiated with foundation customers would set the price path for the service to be offered by Epic Energy on the DMP. This will be reinforced by the expected requirements of the foundation customers that their tariffs should follow any downward movement of tariffs offered to third parties. Epic Energy notes that the outcome represents the result of an interactive process undertaken by informed buyers and sellers to "discover" the price at which investment will be commercially feasible for all parties.

Epic Energy argues that the task of the regulator under such an approach should be to satisfy itself that the outcome represents the result of an "arms length" bone-fide commercial negotiation process, rather than to apply the formulae-based models used under the Code as the basis for assessment.

Epic Energy argues that the market-based tariffs will be negotiated in a competitive market between parties of broadly equivalent bargaining power. In support of this Epic Energy notes that:

- The gas that will be transported through the DMP will be competing with gas from existing or prospective gas sources/pipelines (including gas from Cooper Basin producers at Moomba in respect of the South Australian market; and gas from Cooper Basin producers at Moomba and BHP/Esso at Longford in respect of the Victorian and NSW Markets) as well as with alternative forms of energy.
- In practice, the pricing of tariffs for major new pipelines is never "mandated" by the developer, and in many cases the buyers of pipeline services will have market power equivalent or greater than that of the developer.
- In some cases, the gas transported through the DMP will be competing with energy sources in other locations in Australia or overseas to attract 'footloose' energy-intensive businesses.

Epic Energy claims that this approach is consistent with the approach envisaged in the Hilmer reforms and through Part IIIA of the Trade Practices Act. However, Epic Energy believes that this approach is unlikely to be able to be accommodated under the existing Code.

NGPAC notes that the option of market-based tariffs is clearly available under the Code if it complies with the competitive tendering provisions in sections 3.21 to 3.36 of the Code. This option is unlikely to suit a pipeline developer that has managed to identify and secure an opportunity to develop a pipeline through its own entrepreneurial efforts or that has secured some kind of exclusive arrangements to provide key services, either with gas producers or with gas shippers or both.

NGPAC understands that Epic Energy and Phillips have been working together to develop the market in South Eastern Australia for gas produced by Phillips and the transmission of that gas through the DMP.

NGPAC notes that the Code as currently drafted does not appear to allow for pure market-based pricing in the absence of transparent competitive tendering. For example, if the regulator were presented with a tariff for approval along with information on the negotiation process, it would be difficult to show how the tariff complied with the requirements of the Code, in particular section 8.

NGPAC notes that a less pure form of market-based pricing could potentially be accommodated under the Code but this would depend on the degree to which the market-based tariff could be justified in terms of the requirements of the Code, and in particular section 8. In one sense, the requirements of section 8 could be seen as simply providing a framework to assist the regulator in making judgements on whether the market-based tariff is consistent with the price that might be charged by an efficient new entrant.

IPART notes that one interpretation of the Code is that there is scope to implement market-based tariffs by adopting a depreciation schedule to support such prices. This can be reconciled to efficient costs as required by the Code. In these circumstances a normal rate of return, taking into account the specific risks involved, could be achieved over the lifetime of the pipeline. The Central West pipeline is cited as an example of this approach.

The ACCC has indicated (in Attachment B) that, regardless of the pricing methodology chosen, it will require reference tariffs to be “based on the efficient cost of providing reference services.” Further, “prices should converge towards efficient costs over time”. These matters mean that proponents of access undertakings must provide adequate information enabling the ACCC and third parties to assess these issues. Amongst other things, “the Service Provider must explain the basis for setting access prices”, and “the access undertaking should also include a policy describing the principles that were used to determine the reference tariffs”.

- Does the Code adequately support a market-based tariff approach, other than as part of a transparent competitive tender?
- Are regulators well equipped to make the commercial judgements necessary to approve a tariff developed under a market-based approach?
- Is a Code change warranted? If so, should it be progressed urgently or await the major review?

ix. Delays

NGPAC notes that there have clearly been significant delays in reaching decisions under the Code. The reasons for these delays include the more complex and precedent setting nature of initial decisions, the level of experience of regulators, resources constraints within regulatory bodies, delays in specifying and collecting information from Service Providers and in considering whether the information should be publicly released and delays arising from related Coverage or Revocation of Coverage decisions. There is no evidence that similar delays would not have been experienced under the section 44ZZA undertaking route.

The ACCC has observed (see Attachment B) that there is significant similarity between the processes it must follow in respect of Access Arrangements and access undertakings. Both require a public consultation process and the ACCC will consider similar frameworks in its assessment. On this basis, the time period under each approach could be expected to be similar.

NGPAC is not aware of any simple amendment to the Code that will resolve this issue in the shorter term. In the longer term, decision-making time-frames are generally expected to reduce as regulators and industry gain experience, as issues narrow in subsequent reviews and as precedents are established. Again, the timeliness of decision-making processes under the Code has been identified as an issue that warrants consideration at the proposed major review of the Code.

- Are potential delays more likely under the Code compared to section 44ZZA route?

x. Prescription, flexibility and regulatory discretion

APIA claims that, while the intent behind the Code was probably to provide a non-prescriptive system similar to that under Part IIIA of the TPA, the inclusion of a number of sections, such as sections 3 and 8, which include very prescriptive provisions has served to confuse the effect of the Code. APIA argues that as a result of the attention paid to the prescriptive provisions of the Code in decisions of regulators there is a perception amongst pipeline developers that the Code will be applied in an inflexible and prescriptive manner. APIA points out that, given the problems of application to prospective Pipelines referred to above, this is a cause for serious concern, and hence uncertainty, as to how the Code will in fact be applied by regulators in this case. APIA notes that this aspect is reinforced by the regulators' apparent concerns about creating precedents.

An alternative view from some stakeholders is that the level of prescription in section 8 of the Code coupled with the number of decisions made by regulators (and other material published by regulators) should provide increased certainty for a Prospective Service Provider regarding the likely tariff to be approved under the Code in

comparison to the Section 44ZZA route, where the requirements are less prescriptive and where there are few relevant decisions.

NGPAC notes that APIA's comments on the perceptions of pipeline developers regarding the inflexible application of the Code by regulators mainly relate to broader issues on the overall design of the Code and ongoing issues concerning regulatory practice. There do not appear to be any simple amendments to the Code to address Epic's concerns, and in any case there is no clear consensus on these issues amongst stakeholders. Many of these issues have been identified as issues to be considered as part of the proposed major review of the Code.

The ACCC (see Attachment B) considers that the Code reflects worthwhile principles that are likely to be relevant to any consideration of an access undertaking. Therefore, the ACCC recommends that owners/operators should provide sound reasons should they wish to depart from the principles reflected in the Code.

NGPAC notes that the ACCC appears likely to undertake a substantially similar approach in considering a section 44ZZA undertaking to that provided for an Access Arrangement under the Code. As such, the above issues appear likely to apply to a similar extent regardless of which of these routes a Prospective Service Provider chooses to take. However, in some cases the regulators under the two different routes will not always be the same body, such as in relation to distribution pipelines in all jurisdictions and transmission pipelines in WA.

- Are the perceptions of pipeline developers regarding the level of prescription, flexibility and regulatory discretion best dealt with in a major review?

3.4. Conclusions on greenfields Pipeline issues

NGPAC notes that the Code was clearly intended to be able to support Access Arrangements from prospective Pipelines. It was also anticipated that a range of technical refinements would probably be necessary in the early years of the Code and that the Code would also evolve over time. The uncertainties and problems discussed above appear to fall into three main categories:

- **Simpler or no amendments** — issues concerning technical deficiencies in the drafting of the Code with respect to greenfields that could be addressed by relatively simple Code changes (eg issues i., ii. and iv above) or issues that arguably require do not require amendments (eg issues iv. and v.).

- **More complex amendments** — issues concerning potential technical deficiencies or uncertainties that are somewhat more complex than those in the first category but that may be desirable to address by prior to the major review (eg issues iii., vi. and vii.).

- **Broader issues suited to the major review** — third, broader issues concerning the overall design and application of the Code that are probably better dealt with as part of the proposed major review of the Code (eg issues viii., ix. and x.). While some of these issues may represent problems or uncertainties for Pipeline developers, it is not clear that these problems or uncertainties would be substantially different under the section 44ZZA route.

NGPAC notes that, with broad support, it is likely that the relevant amendments in the first category could be progressed in a similar time-frame as would be required to progress APIA's proposed amendment.

NGPAC notes the issues in category two could be further assessed and a Code change progressed if this was thought desirable, and that it was likely that these issues could be addressed prior to the major review but not in the same time-frame as APIA's proposed amendment.

The above list of issues is not exhaustive. It may well be that there are technical deficiencies, uncertainties or broader issues beyond those identified by APIA. While no other specific greenfields Pipeline issues have been brought to the attention of NGPAC, some interested parties have indicated that they will be bringing forward Code change requests in relation to a number of issues. A more comprehensive analysis of greenfields Pipeline issues would be required to determine whether other changes to the Code would be desirable.

On the other hand, some stakeholders (eg WA in Attachment B) are of the view while the Code could be improved, it is important not to overstate the potential problems and that a prospective Pipeline could potentially be progressed under the existing Code.

Nothwithstanding the above, Epic Energy has indicated that, even if all the potential problems identified in relation to the existing Code could be addressed in its desired time-frame, it would still choose the 44ZZA route in relation to the DMP.

- Does the Code as currently drafted represent an impediment to new pipeline development?
- Can the Code provide sufficient regulatory certainty for paper pipelines to proceed under a voluntary Access Arrangement?
- Should the issues in the first two categories above be further assessed and any desirable amendments progressed prior to the major review of the Code?
- Should the broader issues in the third category above be further assessed and any desirable amendments progressed prior to the major review of the Code?

4. Proposed amendment to the Code

4.1. Overview

NGPAC is considering whether to recommend to Ministers that the Code be amended to clarify the issue of regulatory overlap in relation to prospective Pipelines, either as proposed by APIA (Option A) or an alternative Option B. Two further options are also discussed – to amend the Code to address the technical issues and uncertainties raised in section 4 of this Information Memorandum (Option C) or to do nothing in the short term (Option D). Each option is set out below, including why it may be desirable and any possible disadvantages.

4.2. Option A - APIA Proposal

Proposed drafting

APIA's original proposal to NGPAC (available on the NGPAC website) was refined after discussion with NGPAC and an amended proposal is set out below. The amended APIA proposal supports the inclusion of a new section 2.3A immediately after section 2.3 of the Code as follows:

> "If an access undertaking has been accepted under section 44ZZA of the Trade Practices Act 1974 within the two year period commencing 28 November 2000 and no Access Arrangement has been submitted and approved under this section 2, in respect of the whole or any part of:
> (a) a Covered Pipeline; or
> (b) a Pipeline or proposed Pipeline that is not Covered,
> and that Pipeline was not physically in existence on 28 November 2000 then, for so long as that undertaking is in operation:
> (c) that undertaking is taken to be an Access Arrangement and applicable Access Arrangement Information submitted and approved under this section 2 for the whole or the relevant part (as the case may be) of the Pipeline, notwithstanding that the undertaking may not include the elements in section 3 or comply with the requirements of section 8; and
> (d) if the Pipeline or proposed Pipeline is not Covered, and to the extent the context permits, the term "Covered Pipeline in sections 4, 5, 6, 7 and 10 (inclusive) includes the Pipeline or proposed Pipeline."

and insert the following new paragraph (aa) after section 2.2(a):

> "(aa) within 90 days after the expiry of an applicable access undertaking if section 2.3A applies in respect of the Pipeline; or"

The amended APIA proposal addresses two unintended effects of the original drafting proposed by APIA:

1. The original drafting did not deem the access undertaking to be an Access Arrangement for the purposes of the other Code provisions that APIA contemplates would apply to new Pipelines (assuming they become covered). Some of these provisions may be difficult to apply in the absence of an Access Arrangement. For example:

- Section 5.1 of the Code requires Service Providers to establish and maintain an information package that includes the Access Arrangement and Access Arrangement Information;
- Section 5.9 requires Service Providers to maintain a public register of Pipeline, capacity, including "Spare Capacity", which is defined by reference to an Access Arrangement;
- Section 6.1 effectively provides that a Prospective User or Service Provider cannot use the Code dispute resolution procedure unless there is an Access Arrangement in respect of the relevant Pipeline. The arbitrator of a dispute must apply the Access Arrangement provisions; and
- Section 7.2 dealing with associate contracts refers to a "Reference Tariff", which is defined by reference to an Access Arrangement.

2. Although the original drafting did not preclude the relevant Pipeline from becoming covered under the Code while the access undertaking is in operation, it did not address what happens when the undertaking expires. Under the amended proposal, section 2.2 of the Code provides for appropriate time limits within which an Access Arrangement must be submitted.

WA raised an additional concern about potentially overlapping processes between the Code and the TPA and proposed that an additional provision be added to the APIA proposal to address this issue. While the following amendment was not proposed by APIA and while NGPAC has not formed a view, APIA and NGPAC agreed that for the purposes of public consultation it would be useful to include this possible amendment in the Information Memorandum.

Insert the following after the first sentence of section 7.19:

> "In considering an application for an extension to a time period under section 2.2(a), the Relevant Regulator may have regard to (without limitation) whether an access undertaking has been offered under section 44ZZA of the Trade Practices Act 1974 in respect of the relevant Pipeline and the status of the consideration process in respect of that access undertaking."

Why the amendment may be desirable

APIA's objective is to remove any uncertainty created by regulatory overlap by making it clear that if an access undertaking is accepted under Part IIIA, the obligation to file an Access Arrangement, and therefore the application of a second access regime, is removed for the duration of the undertaking. APIA has stated to NGPAC that the proposed amendment has the following benefits:

- it gives the Prospective Service Provider a choice whether to seek approval of an access undertaking under Part IIIA or an Access Arrangement under the Code;
- it does not preclude the Pipeline from becoming "covered" under the Code once the Pipeline is constructed;
- once the access undertaking expires or is withdrawn (if the Pipeline is still a covered Pipeline), the Service Provider is automatically obliged to file a proposed Access Arrangement;

- the other provisions of the Code (except sections 3 and 8) will still apply, eg provisions dealing with ring fencing, associate contracts and provision of information; and
- it has a limited life, as it only applies to Pipelines constructed after 28 November 2000 and access undertakings approved before 28 November 2002.

Option A is intended to be a temporary solution. APIA recognises that the wider reviews of Part IIIA of the TPA and of the Code may result in legislative or Code changes that remove the possibility of regulatory overlap and/or resolve any uncertainty relating to prospective Pipelines. Therefore, the proposed amendment is specifically directed at the Code provisions relating to the submission of Access Arrangements. This has the advantage of being a minimal change and preserving the application of other Code provisions to prospective Pipelines (if covered under the Code).

Possible disadvantages

Some possible disadvantages or unintended effects of Option A have been identified, as set out below.

1. An access undertaking may not contain all the information that the Code envisages in an Access Arrangement, so the risk remains that some Code provisions could not be effectively applied.

2. Some stakeholders have expressed concern that the proposal involves a risk that future major gas Pipeline developers would seek to have coverage by the Code of their assets revoked, and that future major gas Pipeline developers would seek to use the same Part IIIA route. This risk is mitigated by the application of the proposed clause to new Pipelines for which an undertaking is approved in the next two years. NGPAC recognises, however, that any such Pipelines would be not be fully regulated under the Code for a substantial period of time. This would be contrary to the objective of a uniform access regime for gas Pipelines.
3. NGPAC has received submissions noting that the proposal may develop a schism between the regulation of transmission and distribution Pipelines. Although the Part IIIA route is theoretically open to distributors, most new distribution Pipelines in the near future are likely to be extensions of existing covered Pipelines and hence generally not able to use the proposed new Code provision.

4.3. Option B – 'No coverage' alternative

Proposed drafting

Insert the following new section 1.42 immediately after section 1.41:

Access Undertaking under Trade Practices Act

1.42 Notwithstanding anything to the contrary elsewhere in the Code, a Pipeline or any part of a Pipeline may not become Covered if:

(a) that Pipeline was not in existence on 28 November 2000; and

(b) an access undertaking has been accepted under section 44ZZA of the Trade Practices Act 1974 in respect of the whole or the relevant part (as the case may be) of that Pipeline within the two year period commencing 28 November 2000 and that undertaking remains in operation.

This section 1.42 does not prevent the making of an application, recommendation or decision on Coverage of the relevant Pipeline under this section 1 but any decision on Coverage may not have effect until the date on which the relevant undertaking ceases to have effect.

The concern raised by WA under Option A in relation to potentially overlapping regulatory processes between the Code and the TPA could also apply in relation to Option B. NGPAC has not formed a view on this issue but agreed that for the purposes of public consultation it would be useful to include this in Information Memorandum the following possible drafting to address this issue.

Insert the following new section 1.43 immediately after the proposed new section 1.42:

1.43 Notwithstanding anything to the contrary elsewhere in the Code, the NCC or the Relevant Minister may, in their absolute discretion, not proceed to consider, or take any other step in relation to, an application for Coverage of a Pipeline or any part of a Pipeline if:

(a) that Pipeline was not in existence on 28 November 2000; and

(b) an access undertaking has been offered by the Service Provider under section 44ZZA of the Trade Practices Act 1974 in respect of the whole or the relevant part (as the case may be) of that Pipeline within the two year period commencing 28 November 2000 and that offer has not been withdrawn and has not been the subject of a final decision or determination by ACCC under that section.

Why the amendment may be desirable

The effect of Option B would be to provide that new Pipelines cannot become "covered" under the Code if and to the extent that an access undertaking under Part IIIA is in force. This may avoid, in part, possible disadvantage 1 under Option A in that the undertaking will be a free standing instrument that does not rely on the Code to apply important access provisions other than those that would otherwise be covered in an Access Arrangement (eg ring fencing, associate contracts and provision of information). That is, it may offer a simpler approach.

Possible disadvantages

Option B, however, does not necessarily address the principal thrust of possible disadvantage 1 on whether an undertaking under Part IIIA will actually include all the elements required in an Access Arrangement under the Code or provided for in the Code itself. In addition, Option B does not address possible disadvantages 2 and 3 of Option A. It would result in the relevant new Pipelines being regulated wholly outside of the Code while an access undertaking is in force. NGPAC notes, however, that areas such as ring fencing, associate contracts and provision of

information could be regulated under the access undertaking if the ACCC considered it appropriate to do so.

4.4. Option C – Greenfields Pipelines amendments pending major reviews

Proposed amendments

Option C consists of:

- In the short to medium term, progressing any desirable amendments identified under section 4 that could improve the Code's application to greenfields Pipelines prior to the major review of the Code;
- In the medium term, addressing the issue of regulatory overlap and the broader issues regarding regulatory certainty for greenfields Pipelines as part of the major review of the Code, taking into account the outcomes from the Part IIIA review.

NGPAC notes that the issue of whether the section 44ZZA route should remain as an option for pipeline developers can only be addressed by the Commonwealth Government as it would require a change to the TPA.

No specific drafting for this option has been put forward at this stage.

Why the amendments may be desirable

The objective of making the initial amendments is to give Pipeline developers the option, in the short term, of proposing an Access Arrangement for a 'paper Pipeline' under the Code with a degree of regulatory certainty that is, arguably, not significantly lower than would be available under an access undertaking.

The potential for regulatory overlap only arises for Pipeline developers that choose the access undertaking route where the Code is also available. If the Code (possibly with some desirable amendments that could be progressed in the short to medium term) can provide reasonable regulatory certainty for such Pipelines, it could be argued that regulatory overlap is more appropriately addressed by the legislation.

In the medium term, following the review of Part IIIA of the TPA, the Commonwealth could give consideration to removing any scope for regulatory overlap by closing off the option of a section 44ZZA access undertaking for prospective Pipelines that could be covered by the Code. Also in the medium term, during the proposed major review of the Code (or earlier through the NGPAC process) further amendments to the Code in relation to greenfields Pipelines could be considered.

Possible disadvantages

NGPAC acknowledges that even the shorter term Code changes may not be able to be progressed in time to meet the DMP timeframe proposed by Epic Energy. In any event, Epic Energy's view is that even if the shorter term Code changes could be made in time, it would still prefer to submit an access undertaking for the DMP.

Consequently, Epic Energy would still be faced with the problem of regulatory overlap. If the potential for regulatory overlap is not removed quickly, then APIA claims that the DMP and other potential new Pipelines may either not proceed at all, or proceed on a scale that would not allow third party access for several years.

4.5. Option D – No immediate change

Why this option may be desirable

Option D involves no changes to the Code under the present Code change proposal. This would leave the regulatory overlap issue to be considered in the context of the review of Part IIIA of the TPA, where it arises. The application of the Code to greenfields Pipelines involves some complex issues and may have wider policy implications. These may be better debated in a full Code review. Short-term 'fixes' may complicate these issues.

Possible disadvantages

Option D would not solve Epic Energy's problem. If the potential for regulatory overlap is not removed quickly, then APIA claims that the DMP and other potential new Pipelines may either not proceed at all, or proceed on a scale that would not allow third party access for several years.

5. Request for Public Comments

NGPAC is seeking public comments on the proposed amendment to the Code. In addition to seeking any general comments on the proposed amendment options, NGPAC is seeking public comments on the following specific issues.

- Are the reasons provided by APIA for urgently progressing this potential amendment reasonable?
- Could regulatory overlap cause problems for prospective Pipelines and deter or delay infrastructure investment that would otherwise go ahead?
- Is it appropriate for the Code to attempt to remove the potential for regulatory overlap?
- Does the APIA proposed amendment (option A) achieve its stated objectives? Are there any alternatives that could better achieve those objectives?
- Which option or options best meet the objectives of the Code?

Attachment A — Code Background

1. The Natural Gas Pipelines Access Agreement

On 7 November 1997, the Commonwealth and each of the States and Territories signed the Natural Gas Pipelines Access Agreement (the Inter Governmental Agreement). The objective of the Inter Governmental Agreement was to establish a uniform national framework for third party access to natural gas pipelines that:

- facilitated the development and operation of a national market for natural gas;
- prevented abuse of monopoly power;
- promoted a competitive market for natural gas in which customers could choose suppliers, including producers, retailers and traders;
- provided rights of access to natural gas pipelines on conditions that were fair and reasonable for both Service Providers and users; and
- provided for resolution of disputes.

Under the Inter Governmental Agreement, the Commonwealth, States and Territories agreed upon the Code, which was intended to establish the proposed uniform national framework for third party access to natural gas pipelines. The parties also agreed upon a legislative scheme to give legal effect to the Code (described in Section 2.3 below).

The Inter Governmental Agreement also established NGPAC. NGPAC's members are:

- an independent Chair (Mr Greg Harvey);
- the Code Registrar;
- one representative of each of the Commonwealth and each State and Territory;
- one representative of each of:
  - Australian Gas Association;
  - Australian Petroleum Production & Exploration Association;
  - Australian Pipeline Industry Association;
  - Business Council of Australia (Energy Working Group); and
- two representatives of State and Territory independent regulators and one representative of the Australian Competition & Consumer Commission (ACCC).

The National Competition Commission (NCC) participates as an observer and adviser. Only the Commonwealth, State and Territory representatives are entitled to a vote at NGPAC meetings.

One of NGPAC's functions is to make recommendations to Commonwealth, State and Territory Ministers on amendments to the Code. The Code may be amended by agreement between the Commonwealth, State and Territory Ministers.

2. What the Code Provides

The key provisions of the Code are summarised below.

Coverage

The Code applies to Pipelines used for transporting natural gas (Pipelines). The Code applies to both gas transmission Pipelines and gas distribution networks but does not apply to upstream facilities.

The operative provisions of the Code apply only to Pipelines that are "covered" by the Code. A Pipeline may become covered in a number of ways.

- Certain Pipelines, which are listed in a Schedule to the Code, are covered automatically. The Schedule to the Code lists all major Pipelines in Australia.
- A Pipeline may be declared to be "covered", on a case by case basis, by a relevant Minister (after having received a recommendation from the National Competition Council) if the Pipeline satisfies certain criteria for coverage.
- The owner or operator of a Pipeline may volunteer to have the Pipeline covered.
- A Pipeline will also become covered if a competitive tender process conducted under section 3 of the Code is used to select the Service Provider for a new Pipeline.

The coverage of a Pipeline may be revoked by a relevant Minister (after having received a recommendation from the National Competition Council) if the Minister is satisfied that the criteria for coverage are not satisfied.

Access Arrangements

The owner or operator of a covered Pipeline (a Service Provider) must establish an "Access Arrangement" to the satisfaction of the relevant regulator for that covered Pipeline. An Access Arrangement is a statement of the policies and the basic terms and conditions that will apply to third party access to a covered Pipeline. The relevant regulator is the ACCC in the case of transmission Pipelines (except in Western Australia where there is an independent State regulator) and there will be an independent State or Territory regulator in the case of distribution Pipelines (except in the Northern Territory where the ACCC is the regulator).

As a minimum, an Access Arrangement must include:

- a description of the services provided by means of the covered Pipeline (a Services Policy);
- a statement of the "Reference Tariffs" that a Service Provider will charge for certain defined services provided by the covered Pipeline (Reference Services) and a statement of the principles that were used to determine the Reference Tariff (a Reference Tariff Policy);
- the Terms and Conditions on which the Service Provider will supply each Reference Service;
- a Capacity Management Policy;
- a policy on the trading of Pipeline capacity (a Trading Policy);
- a Queuing Policy, which defines the priority that Prospective Users will have to negotiate for spare capacity;
- an Extensions/Expansions Policy; and
- a Review Date.

A Service Provider and a person seeking access are free to agree to terms and conditions that differ from those contained in the Access Arrangement (except where it affects the interests of other users or potential users under the Queuing Policy). If a dispute about access arises, however, and is referred to the relevant regulator for arbitration (see below), the regulator must, amongst other things, apply the provisions of the Access Arrangement in resolving the dispute.

Reference Tariff Principles

The Code sets out principles with which Reference Tariffs and the Reference Tariff Policy contained in an Access Arrangement must comply. The overarching requirement is that when Reference Tariffs are determined and reviewed, they should be based on the efficient cost (or anticipated efficient cost) of providing the Reference Services. Within these parameters, the Reference Tariff Principles are designed to provide a high degree of flexibility so that the Reference Tariffs and Reference Tariff Policy can be designed to meet the specific needs of each Pipeline.

Negotiation

The Code includes a number of provisions designed to facilitate negotiation between a Service Provider and a person seeking access. In particular, Service Providers for covered Pipelines are required to:

- establish, and provide to bona fide access seekers, an information package containing general information on the terms and conditions of access and explaining how to make a specific access request;
- respond within 30 days of a specific request for access; and
- establish and maintain a public register of spare and developable capacity.

Dispute Resolution

The Code establishes a mechanism whereby disputes between a Service Provider and access seekers in respect of covered Pipelines can be submitted to the relevant regulator for binding arbitration (or, in Western Australia, to a separate statutory body, the Gas Disputes Arbitrator). The regulator's decision may deal with any matter relating to access. For example, the decision may require the Service Provider to offer to enter into a contract to provide a service to the access seeker at a specified tariff and on specified terms and conditions.

In resolving an access dispute the regulator must, amongst other things, apply the provisions of the Access Arrangement. If the sole subject of a dispute is what tariff should apply to a Reference Service, the regulator must make a determination requiring the Reference Service to be provided at the Reference Tariff.

Ring fencing

The Code includes a number of provisions designed to ensure the separation of activities in non-contestable markets (the ownership and operation of a covered

Pipeline) from activities in contestable upstream and downstream gas markets (for example, retailing of gas) (a *Related Business*). In particular:

- a Service Provider must not conduct a Related Business (as a consequence a vertically integrated Service Provider will need to transfer its upstream or downstream activities to another company, for example, a subsidiary);
- any contract between a Service Provider and an "associate" for a service may be entered into only if approved by the relevant regulator;
- Service Providers must maintain separate accounts for activities that are the subject of an Access Arrangement;
- confidential information provided to a Service Provider by a user of a covered Pipeline, or obtained by a Service Provider which might reasonably be expected to affect materially the commercial interests of a user, must be kept confidential and not disclosed, for example, to an associate of the Service Provider who competes with the user; and
- marketing staff of a Service Provider must not work for an associate that takes part in a Related Business and marketing staff of an associate that takes part in a Related Business must not work for the Service Provider.

3. How the Code is given legal effect

The Code has been given legal effect through an 'application of laws' scheme with South Australia acting as the lead legislator.

In 1997, in accordance with the Inter Governmental Agreement, the State of South Australia passed the *Gas Pipelines Access (South Australia) Act*. That Act applied the "Gas Pipelines Access Law" comprising Schedule 1 (Third Party Access to Natural Gas Pipelines) and Schedule 2 (the Code), as laws of South Australia. Schedule 1 contains various provisions necessary to give the Code legal effect (for example, it deals with such things as how the Code may be amended, the procedures to apply in the arbitration of access disputes and the consequences for a breach of the Code and it provides for administrative appeals from decisions of various bodies made under the Code).

Each other State and Territory (other than Western Australia) has passed its own *Gas Pipelines Access (name of State/Territory) Act*, which applies the Gas Pipelines Access Law, including the Code, as set out in the schedules to the South Australian Act (and amended from time to time), as laws of their State or Territory.

Western Australia has enacted the *Gas Pipelines Access (Western Australia) Act 1998*, which has essentially identical effect to the *Gas Pipelines Access (South Australia) Act 1997*. That Act applies the Gas Pipelines Access Law, including the Code (as set out in Schedules to the Western Australian Act and as amended from time to time) as laws of Western Australia.

The *Gas Pipelines Access (Commonwealth) Act 1998* completes the coverage of the access regime by ensuring, among other things, that it applies in offshore waters. It also permits the use of certain Commonwealth bodies in the operation of the Code.

4. How the Code is amended

The Code may be amended by agreement between the relevant Ministers of the Commonwealth, States and Territories. Subject to certain limitations specified in the Gas Pipelines Access Law, the Code can be amended by agreement between Ministers without the need for an amending Act to be passed by the State of South Australia or any other State or Territory.

Section 6(1) of Schedule 1 provides:

> "6(1) If the relevant Ministers of the scheme participants have received advice in accordance with any relevant provisions of the Code relating to amendment of the Code, the relevant Ministers may, by agreement in accordance with this Law, amend the Code to make provision for or with respect to any matter relevant to the subject matter of the Code as set out in Schedule 2 to the *Gas Pipelines Access (South Australia) Act 1997* of South Australia, as enacted."

Sections 9.1 and 9.2 of the Code provide:

> "9.1 This Code may be amended by agreement between the Relevant Ministers of the Scheme Participants in accordance with the Gas Pipelines Access Law if, not earlier than eight weeks prior to the agreement, the NGPAC has provided a report to all Relevant Ministers of the Scheme Participants in accordance with section 9.2 which:
> (a) makes a recommendation in relation to an amendment to the Code;
> (b) sets out reasons for that recommendation; and
> (c) sets out a summary of the views of any member of the NGPAC who does not agree with the recommendation.
>
> 9.2 A report by the NGPAC for the purposes of section 9.1(a) must state whether the NGPAC considers the amendment it recommends to be significant or not significant. If the amendment is considered to be significant, the report must confirm that the recommendation is made following a public consultation process under which the NGPAC has:
> (a) prepared an information memorandum setting out the amendment being considered and a statement of why such amendment may be desirable;
> (b) published a notice in a national daily newspaper which at least:
> (i) stated that the NGPAC was considering recommending an amendment to the Code;
> (ii) stated how copies of the information memorandum could be obtained; and
> (iii) requested submissions by a specified date, being a date not less than 21 days after the date of the notice; and considered any submissions received within the time period specified in the notice."

Attachment B: Stakeholders' preliminary views

Western Australian Office of Energy

Note: The following comments from the Western Australian Office of Energy was received by NGPAC prior to the development of this Information Meomorandum.

The relevant provisions of section 44ZZA of Part IIIA of the Trade Practices Act (TPA) existed at the time the Commonwealth legislation implementing the Code was drafted. However, due to perceived difficulties with progressing a successful amendment, the TPA was not amended to avoid the duplicate application of the two regimes to pipelines which fall within the definition of the Gas Pipelines Access Law. The current necessity to amend the Code to remove for a specific short period that duplication is a product of the hesitation to amend the TPA at that time. It is clear that under the circumstances it may not be under review by the Productivity Commission and may therefore be subject to such amendment in due course.

Western Australia is of the view that a subsequent amendment to the Part IIIA to remove the ability of Service Providers to give undertakings to the ACCC in relation to pipelines that are covered by the definition in the Gas Pipeline Access Law is desirable. This view stems from the history of the Code of development. As you will recall, the Code was developed and agreed following extensive consultation with industry. Until evidence to the contrary is provided, Western Australia is confident that the regime applied through the Gas Pipelines Access Law, including the Code, has achieved a balance between the interests of the Service Providers and users of pipeline services. The regime also has a strong focus on transparency of regulation.

While section 44ZZA may be able to achieve similar outcomes to those produced under the Code, the relevant TPA provisions are yet to be fully tested. In addition, as pointed out by the Productivity Commission in its recent Issues Paper on the National Access Regime, the regimes are not identical. For example, the ACCC's interpretation of the public interest, in assessing a proposed undertaking under Part IIIA, makes it potentially broader than the tests applying to certification and declaration applications (Issues Paper, October 2000)

Various sections of the Code were intentionally designed to provide for the specific requirements of greenfield pipeline developments, such as the Goldfield Gas Pipeline project which was being developed at that time. So far no convincing argument has been put forward by industry identifying inherent deficiencies of the Code in respect. Subject to industry providing, during the forthcoming review of the Code, evidence that such deficiencies exist the Code may need to be amended accordingly. However, at present WA is not convinced that the Code does not adequately cater for new pipeline developments.

In the interim WA recognises the need to transitionally address the threat of "double jeopardy" in the case of the Darwin to Moomba pipeline, that is, it recognises the possibility of that pipeline having an accepted undertaking under section 44ZZA of the TPA and a subsequent application for coverage under the Code. An amendment to the Code, limited in scope and time, appears to provide an appropriate temporary resolution to this situation. The amendment will remove the obligation on a Service Provider to submit an Access Arrangement under the Code, where a pipeline becomes covered under section 1 of the Code subsequently to an access undertaking being accepted to the ACCC under the TPA and remaining current in respect to services of that pipeline.

WA considers that a number of Code sections, such as those containing the ring-fencing obligations, should still apply to the relevant Service Provider from the date an access undertaking is accepted under section 44ZZA of the TPA. Following some additional deliberations, WA considers that most practical way of achieving this is that each relevant access undertaking approved by the ACCC is deemed to be "an approved Access Arrangement" for the purposes of the Code as if that access undertaking was submitted as a voluntary Access Arrangement under section 2.24 of the Code. The amendment being contemplated should, in WA's view, be drafted to have this effect.

The amendment will have a sunset clause whereby its operation will be discontinued 2 years after 28 November 2000. This in the view of WA, will provide sufficient time for the relevant reviews and/or amendments of 44ZZA of the TPA and the Code. The new pipelines that have undertakings accepted within the 2 year period, and thus are relieved from lodging Access Arrangements under the existing terms of the Code, will need to revert to an Access Arrangement under these terms after of the expiry of the applicable undertaking ie after 15 or 20 years.

Western Australia's concerns at the amendment potentially developing a schism between the treatment of transmission and distribution pipelines under the Code is noted.

Australian Gas Association (AGA)

Network operators are very concerned at the lack of certainty provided to greenfield projects under the National Gas Code. The key issue is the Code requirement that Access Arrangement periods be constrained to five years (assuming no trigger mechanisms) whereas funding and investor requirements for major projects have horizons closer to twenty years. Longer periods between regulatory resets would provide greater certainty and are supported by both pipeline and distribution asset owners.

Pipeline owners have responded to this uncertainty by proposing a Code change that would enable greenfield developments to be regulated directly under Part IIIA of the Trade Practices Act rather than through the processes contained in the Code. This approach would enable the period of the access undertaking to be consistent with funding and investment requirements. While there are many limitations in the

structure and application of the Code that the industry is keen to see addressed, the proposed code change raises wider issues relating to regulation of the gas industry. The key policy issue is the extent to which there should be consistency between regulatory regimes applying to pipeline and distribution assets throughout Australia.

Network operators are cognisant of the substantial benefits of basin on basin competition and the role that significant new pipeline projects can play in facilitating competitively priced gas being delivered into South Eastern Australia.

However, the proposed change involves a risk that owners of transmission assets would seek to have coverage by the Code of their assets revoked, and that future major gas pipeline developers would seek to use the same Part IIIA route. This could conceivably create the perverse outcome (in terms of the Code's original intention) of fewer gas transmission pipelines operating fully under the Code, whilst the distribution sector remained broadly covered.

Network operators are also concerned about ad hoc Code changes being made to accommodate particular projects. It is the preferred view of distribution businesses that the issue of the treatment of greenfield developments should be addressed within the Third Party Access Code by any necessary changes.

AGA would support any process to ensure necessary Code changes be expedited to facilitate Epic Energy's current proposal. This would provide an opportunity for all of the issues involved to be considered for inclusion as a Code amendment that better addresses the needs of all regulated businesses.

Broadly, there seems to be a case for asset owners (both transmission pipelines and distribution networks) to be permitted, at their election, to treat major extensions and/or expansions as part of existing facilities (and therefore subject to nominally five year regulatory lives) or as new facilities for which longer (say 15 to 20 year lives, again at the election of the asset owners) would apply.

Australian Competition and Consumer Commission (ACCC)

Australian Competition and Consumer Commission approach to Part IIIA Access Undertakings in respect of Natural Gas Pipelines

The NGPAC secretariat has requested the Australian Competition and Consumer Commission ("ACCC") to provide it with an indication of the approach that the ACCC would be likely to take should it be given an access undertaking to assess under Part IIIA of the *Trade Practices Act 1974* ("TPA"). The ACCC is somewhat limited in the comments that it can make on this subject since individual undertakings must be assessed on their merits in the context of the particular circumstances relevant to the application. However, the ACCC is able to make some general comments on the overall approach that it is likely to adopt.

In the first instance, the ACCC must clearly assess the application against the criteria set out in Part IIIA. In order to provide more specific guidance to parties that may be considering lodging an access undertaking, the ACCC published a guide to access

undertakings in September 1999. These guidelines describe procedures for assessment and lodgement; the main factors that the ACCC will take into account in applying the legislative criteria; and the elements that an owner/operator of a facility should include.

While it is the case that the legislative criteria must take precedence over the ACCC's published guidelines, the guidelines nevertheless describe the ACCC's considered view on how an access undertaking should be approached. As such, while the ACCC will ensure that it gives adequate consideration to the merits of each particular case, owners/operators should provide sound reasons should they wish to depart from the approach foreshadowed in the guidelines.

The ACCC has indicated in the guidelines that, absent special circumstances warranting a departure from the guidelines, whatever pricing methodology is chosen, it will require reference tariffs to be "based on the efficient cost of providing reference services." Further, "prices should converge towards efficient costs over time". These matters mean that proponents of access undertaking must provide adequate information enabling the ACCC and third parties to assess these issues. Amongst other things, "the Service Provider must explain the basis for setting access prices", and "the access undertaking should also include a policy describing the principles that were used to determine the reference tariffs".

Further, in respect of natural gas pipelines the ACCC observes that an industry access code has been developed: The National Third Party Access Code for Natural Gas Pipelines. As this Code has been specifically designed to address access to natural gas pipelines, and has been certified by the Minister as an effective access regime in a number of jurisdictions, the ACCC considers that the Code reflects worthwhile principles that are likely to be relevant to any consideration of an access undertaking. Therefore, the ACCC recommends that owners/operators should provide sound reasons should they wish to depart from the principles reflected in the Code.

Timeframes for considering an access arrangement compared to an access undertaking

The NGPAC secretariat has also requested the ACCC to provide comments on the timeframes that might apply to the assessment of an access arrangement compared to an access undertaking.

Once again the assessment timeframe will depend substantially on the individual circumstances relevant to each application. It has been the ACCC's experience in the past that the timeframe required to assess an application depends critically on the Service Provider and the time it takes to provide the ACCC with the necessary information to assess the application. Assessment timeframes can also vary substantially where the Service Provider amends its application in response to reactions from the ACCC and/or interested parties.

The ACCC observes that there is significant similarity between the processes that it must follow in respect of access arrangements and access undertakings. Both mechanisms require the ACCC to undertake a public consultation process and as noted above the ACCC will consider similar frameworks in assessing the application. Thus in broad terms there would seem to be few inherent reasons why one mechanism would require more time to assess than the other.