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TRANSCRIPT
OF PROCEEDINGS

PRODUCTIVITY COMMISSION

INQUIRY INTO REVIEW OF THE NATIONAL ACCESS REGIME

MR G.R. BANKS, Chairman
MR J.H. COSGROVE, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT PERTH ON MONDAY, 18 JUNE 2001, AT 9.04 AM

Continued from 14/6/01 in Brisbane

MR BANKS: Good morning, ladies and gentlemen. Welcome to our hearings here in Perth for the Productivity Commission's inquiry into the national access regime. My name is Gary Banks - I'm chairman of the Productivity Commission - and I'm with my fellow commissioner John Cosgrove. The purpose of the hearings is to give those with interest in these issues an opportunity to present submissions in response to the commission's position paper which was released at the end of March.

I've noted previously, and we said in our report, that we released that draft, that position paper, earlier than we normally would have in order to align it more closely with two other draft reports that we'd released bearing on the same issues - one to do with the Price Surveillance Act and the other to do with telecommunications competition regulation. Since then we've also been given an inquiry into airport pricing which, again, raises overlapping issues. I've also noted that we've been quite fortunate in the quality of the submissions that we've received, and it continues here again in Perth today. It's been very helpful to us in preparing that position paper in the time we had available and will be very useful in going from there till final report.

Today will be the last day of hearings on this position paper. We'll then be giving further consideration to the points raised. People have an opportunity to make further submissions, if they wish, in response to what they hear during the hearings, although we'd like to have all submissions in by the end of the month, if possible - at the end of June. We're intending to get our final report to the government in September, again to align it with our final report for the telecommunications inquiry. I note for the record that, while we like to conduct the hearings as informally as possible, we do keep a transcript. We make that transcript available. It should appear on our Web site hopefully without too much delay, but certainly very soon after we get it back from the court reporter service.

I might also note that the Productivity Commission Act requires people to be truthful in their remarks. We don't have any formal oath-taking. However, you'll be relieved to know written submissions are also available on our Web site; in fact, all submissions can be found there. They are the only introductory remarks I'd like to make. I'd now like to welcome the Chamber of Commerce and Industry of Western Australia. Could you please give your names and positions.

MS CUSWORTH: My name is Nicky Cusworth and I'm chief economist with the Chamber of Commerce and Industry of WA.

MR BANKS: Thank you.

MR SASHEGYI: I'm Bill Sashegyi, manager, industry and resources from the Chamber.

MR BANKS: Thank you very much. Thanks for being the first cab off the rank here today and for the submission which you sent us prior to our releasing the

position paper. As we discussed, perhaps you might like to raise whatever points you like, both drawing on your earlier submission but also in response to our position paper, and then we'll ask you some questions.

MS CUSWORTH: Yes. Given that we've already made a written submission, I'll be fairly brief, just bringing you up to speed with some of the developments in WA since we made that written submission, of which the most obvious is that there has been a change of government and that, therefore, there has been to a certain degree a change in the policy environment affecting the industries most likely to be covered by access issues. In particular, the incoming administration has a policy that it will introduce a greater degree of competition into the electricity market by separating generation and transmission. We don't yet have detail of how that policy is likely to operate, but it is a major change in terms of the government's direction compared to the previous administration which had argued that the electricity utility should be maintained as a vertically integrated monopoly.

I will cover fairly briefly, I hope, some of the key points which we made in our submission which we would like to perhaps highlight to the commission. The first is that we regard access regulation essentially as being (a) not an issue which can be considered entirely in and of itself - that it's actually part of the broader regulatory environment, and access issues have to be considered in that context and also that in many respects the need for access regulation indicates that you have a third-best solution in terms of the market structure.

So it's our view that access issues are most likely to arise in instances where there is a vertically integrated monopoly which has the potential to face competition in parts of its market but not otherwise, otherwise you have either what is essentially a straightforward monopoly problem whereby a major infrastructure owner might have the opportunity and the incentive to charge an inefficient price for access to the infrastructure but would not have any particular incentive not to permit access to that infrastructure, or you can have a situation which under competition principles perhaps could be resolved by breaking up a vertically integrated monopoly.

So we regard really access infrastructure as being indicative of the fact that there are perhaps other problems within that market which potentially at least could be addressed more effectively by other mechanisms. The second key point we would like to make is in regard to how regulation can be conducted, and the issues paper asked the question of whether access regulation should be in the form of a national regime or an industry-specific arrangement or some combination of the two. We have a strong preference for an arrangement which has not hitherto been introduced in WA but which some other states have, which is that there should be a cross-industry regulator but that it should be state based rather than being nationally based.

We argue that for a number of reasons. The first is that it is administratively efficient because many of the issues and expertise which is required in operating a

regulatory environment are common across different industries. It reduces risk of capture, which is an issue which I think was seen in some instances being a real concern for us here in WA, and it allows a degree of consistency and intellectual rigour in the application of policy processes which you tend not to get with an industry-specific regulator.

We would prefer that it be stated based rather than federally based, partly because that is where the regulatory regimes tend to be determined and so it's appropriate merely for the sake of convenience, but also because we have had some concerns under the competition policy process that its emphasis on uniformity nationally has actually, in some cases, tended to work to the detriment of competition. In particular we would see that the capacity for states vary to a certain degree in the way in which they apply regulation and for the whole process of competitive federalism to take place, are actually undermined to some extent by the competition policy model which was proposed by Hilmer. We also would argue that on the basis of subsidiarity; that it's appropriate that regulatory regimes, by and large, are determined in the context of the populations who are affected by those regulations.

One of the difficulties that we have also with the way in which the current regulations are determined is that, in a sense, it actually started off down the wrong track by asking the question of what infrastructure is essential rather than focusing on what we believe should be the key determinant of whether or not regulation is appropriate which is what is a characteristic of the market, and that in itself I think introduces potentially a number of concerns with central access issues, which is that the normal processes of judging regulatory efficiency - which is whether the benefits are exceeding the cost - tend to be, to a certain extent, overridden by considerations of whether or not the asset is in fact what could be deemed to be essential.

I think as well we are developing, as competition policy has become more mature, and in particular in WA and in other regimes privatisation processes have now become quite established. There are some key issues arising as to the appropriate regulation of new versus established assets. In particular we have the concern that what would be an appropriate rate of return on an established asset in an established market, which typically under current arrangements might well be a privatised asset, are not necessarily appropriate for new projects, major infrastructure projects which, by definition, almost will be far more risky than the purchase of an established and ongoing operation.

The major risks, which we've identified with large projects in WA, might include market risk, it might include network risk, construction risk, technological risk and sovereign risk, all of which can be greater for a newly established project, than for an ongoing one. We would be keen to see that any access regime adequately took cognisance of the fact that different degrees of risk would necessitate different rates of return.

MR SASHEGYI: It's probably just useful to give you a few extra points about things that have been happening in Western Australia as of the current time. The first is that Nicky has obviously talked about the reform of the structure of the electricity market in Western Australia. There is an electricity reform steering group that has been put in place, or should be announced shortly by the state government and, importantly, full open access in 2005 is what has been announced for electricity but obviously there is no detail about how that will be achieved and what regime will be in place to oversee that.

There is also a gas market steering group that is in the process of being established by the state government to oversee the full, open access by the middle of 2002 for gas, down to the household level. Again, we haven't seen the make-up of that yet, or the full terms of reference, but that should be made available to us shortly and no doubt you'll be getting that information yourself from the WA government, the Office of Energy.

We made a point in our submission about the time taken to get decisions out of the regulatory process and while I don't think people in Western Australia would have a concern about the way in which OffGAR has been going through its determinations, in terms of just technically how it has been doing it, but certainly when it comes to the time taken to get a resolution we still have not seen a draft of the decision from OffGAR on the Dampier to Bunbury natural gas pipeline, and we have seen a draft for the Goldfields gas transmission pipeline, but no final decision. In our paper we state that it's reasonable to expect that the access arrangement will not be in place - this is for the DBGNP - for two to two and a half years after Epic commenced work on it. No doubt the people from Epic will be dwelling on that as well.

The other issues, obviously the areas of the risk issues to do with new pipeline construction and the potential for the open access regime, if there isn't an appropriate account taken of the risks involved in new gas pipelines and being considered by a reference group that the chamber has established, to consider gas pipeline regulation. It's early days for us but we will, over the next few months, be starting discussions with OffGAR on that. One of the reasons for the delay was really awaiting some of the final decisions, or at least draft decision in the case of DBGNP, from OffGAR before we commenced those discussions. We have a few comments - I have a few issues to target from your tier 1 proposals, but perhaps we can wait to see if you have any questions first.

MR BANKS: All right, a couple of things I thought of in relation to the points you made. Firstly, you've expressed a strong preference for a cross-industry regulator, state based. You don't have that in WA. As you say, some of the jurisdictions do. How do you see that evolving? Have there been any moves in that direction?

MS CUSWORTH: Not that we're aware of. It's something which we have consistently lobbied both the new administration in WA and the previous

administration for. There has been some indication that they're sympathetic to that view, but as far as I'm aware that hasn't been (indistinct)

MR SASHEGYI: For example, there has been delay in appointing a rail regulator, just to see how that might fit in to a more broadly based regulator, and the announced changes in the cabinet portfolios in Western Australia would be conducive to the establishment of a broadly based economic regulator. But again the details are not forthcoming as yet, as would be reasonable with a relatively new government.

MR BANKS: You talk about the problems of uniformity, and I have some sympathy with those views and, indeed, you talk about competitive federalism and how that can be a positive force. You also mention subsidiarity as a reason for going for this model. To what extent do you think that reflects WA's particular position relative to, say, the eastern states which are more interconnected?

MS CUSWORTH: That would obviously be more of a concern for us in WA. Energy would be an obvious example, where you have supposedly a national energy regime which of course can't include WA for practical reasons. We are conscious of the fact that in many respects we are physically likely to remain separate and, I suppose from a WA perspective, that means we are particularly nervous of any national regime which would not necessarily be addressing what is really a national market; that the design of any regulation might be understandably slanted towards the needs and the interests of the eastern states.

MR COSGROVE: Even in the case of rail?

MS CUSWORTH: Rail lesser. It depends on whether or not there is a genuinely national market or a national consideration. As we said in our submission, where you do have an industry which has national dimensions, then a national regulator may well be the most appropriate way to go. It's not necessarily that one size fits all; we're not saying that in every instance there should be only state based regulation.

MR COSGROVE: You also mentioned in your remarks about regulators; that a single regulator across a range of industries could have the benefit of avoiding capture. There are various forms of capture, of course, and some people might still see a risk of a different type of capture, say, in the interests of users or consumers. I was wondering, therefore, whether you have any thoughts about the principles or criteria which might be utilised to provide guidance to such a regulator as you have advocated. I don't know whether this gets back to the remarks that your colleague was planning to make on some of our proposals about tier 1 criteria. You've got an objects clause that we proposed. We've also put forward proposals for changing the criteria relating to declaration in particular. Do you have any thoughts on those?

MR SASHEGYI: I wasn't going to talk about the impact on a single broadly based regulator.

MS CUSWORTH: You're talking more specifically about the pricing objectives in your proposal?

MR COSGROVE: Yes, those sorts of things, but also perhaps the question of coverage essentially. Would a single industry based regulator be more or less likely to apply declaration in the absence of clear principles which might constrain it from doing so?

MS CUSWORTH: It's not an issue, I think, that we've given any great consideration to. It's an interesting question, though, and I would perhaps be prepared to forward some written comments to you before the end of the month.

MR COSGROVE: Thank you.

MR BANKS: We might let you get on with any reaction to the position paper and then perhaps come back to any gaps or any follow-up questions.

MR SASHEGYI: I certainly wasn't going to go into a lot of detail, but certainly the inclusion of the objects clause in Part IIIA relating to the efficient use of and investment in essential infrastructure facilities, certainly the investment in issue is important in terms of the new pipeline construction and, as I said, although we haven't gone through the full processes, we'll need to go through in the Chamber. It certainly would seem to me to go some way towards addressing the concern of the gas pipeline industry regarding new pipeline construction and whether there would be consideration of a reasonable rate of return in terms of the case of a new pipeline or risky pipelines. So certainly I thought that was very important.

In terms of the pricing principles in Part IIIA to facilitate speedier resolution of access disputes, well, just in terms of getting a speedier resolution of the access regimes - and I thought that may have some impact on the time it takes to get decisions through OffGAR and the like and, again, that would address one of the key concerns that's been raised with us. The other one I want to touch on was the issue about provision for service providers to lodge undertakings after services have been declared. This could avoid time-consuming bilateral negotiations between a service provider and a series of access seekers. Really, all I wanted to obviously note is the application by Normandy Mining for declaration of the South-West interconnector system for Western Power which is currently going through process, and that could well be a case study in terms of what might be the outcome and, secondly, what might different access seekers have to do.

I would hope that if the South-West interconnector system is declared, that there is some easier way of arriving at some new set of access conditions, rather than individually access seekers having to go through a separate negotiation process. We were interested to see your thoughts - ultimately anyway - about that process and that case study.

MR BANKS: You mean specifically in relation to this Normandy - - -

MR SASHEGYI: Yes. I'm certainly interested to see what might, under the current situation, be the process that might result if the South-West interconnector system is declared and what ways that might be able to be made more efficient for access seekers in the future.

MR BANKS: Generally, you're supporting this notion that there should be provision for an undertaking to occur post-declaration?

MR SASHEGYI: Certainly supporting the need to find an easier way than have people have to individually have negotiations, bilateral negotiations.

MR BANKS: Right, okay. Any other comments?

MR SASHEGYI: No, that's it.

MR BANKS: Thanks for that. Coming back to one point that was emphasised, and that is in relation to the question of new investment and the difference between existing and new. You've seen the key to that in some respects as being an appropriate rate of return. I'm just wondering if you had any reactions to the access holiday-type approach that the commission had ventured in the position paper?

MS CUSWORTH: It's one way in which those concerns might be accommodated. I don't think we have a preference for one model as opposed to another. So long as the issue is adequately addressed, an access holiday is certainly one way in which it could be, yes.

MR BANKS: I guess one of the issues that has been pressed upon us is this need ex ante for greater certainty or less uncertainty, and the question of what the rate of return might be, I suppose - you know, over time, I guess it could reassure people that an adequate rate of return will be applied, but I don't think it would address some of the concerns that have been put to us about an ex ante position still - being concerned that there will be truncation of returns and so on.

MS CUSWORTH: Yes.

MR BANKS: We've talked in our position paper about the likelihood of many new investments to the extent that they're contestable in some broad sense, actually not having great scope ex ante for rent and, indeed, in some respects probably ex ante taking placing once the returns become normal and therefore whether you might simply want to exclude such contestable investments from the regime altogether and then think about - really the only investments that you would include would be ones where there was a lack of contestability either because the incumbent was in a position to influence the timing or whatever.

MS CUSWORTH: Yes, I think that's a very interesting and useful approach, especially given the fact that we're looking here only specifically at the issue of access and that you would presumably have in place in any event some degree of control for monopoly power in the event that you're creating a monopoly. So given that it's exclusively an access issue, I would have thought that that's a useful model to follow, that contestability ought to be one of the criteria which will, given that access, need not be declared.

MR SASHEGYI: But it does depend on what you mean by contestability. In the case of say the Goldfields gas transmission pipeline, when it was first conceived it had to be sold to the major gas consumers in the northern goldfields, in the goldfields. They would have gone through a process of determining who they thought was the best gas pipeline owner and canvassed bids broadly. They would have gone through a process of tendering out the gas pipeline construction, so for that point in time certainly the gas pipeline was put in place in a very contestable environment.

But 10 years down the track, that is no longer - well, certainly the contestability of the competitiveness of that pipeline and those rates can no longer be guaranteed, and again you make that point yourself, anyway. You say the issue isn't whether the access holiday type of concept is reasonable. The question is more about how long it would apply, and the only comment perhaps to make there as an obvious one is that the riskier the investment, the shorter the payback period, and the less risky the investment the lesser difference there would be between sort of a steady state ongoing operational rate of return and the rate of return that the company might have been operating on when it established its pipeline.

MR BANKS: We've also had a number of other suggestions put to us, and I'd actually appreciate it if you had the time to have a look at some of those and give us any comments later. NECG, Network Economics Consulting Group, in their submission on the position paper looked at a number of what they called safe harbour mechanisms but all directed at providing greater certainty up-front to investors, and some of the submissions today, I think including by the Western Australian government, look at processes equivalent to say authorisation, where again rulings could be made, whether binding or not, in relation to the provisions that apply, all intended really to get more certainty up-front before the assets are actually sunk, therefore reducing significantly the risk - the sorts of risk that you identify in relation to these facilities.

MS CUSWORTH: Yes, we'll be happy to make a further submission on that as well.

MR BANKS: Good. Thank you.

MR COSGROVE: You referred in your submission and again today to the slowness of the OffGAR process. Are there any particular design features of the way

OffGAR operates that result in that, or is it simply that it's dealing with some complex matters of detail that take time to work through, and I wondered whether you or any of your members that you know of have contrasted what's happening here with the otherwise in Australia use of ACCC as the gas transmission pipeline regulator, and whether one is seemingly performing better than the other?

MR SASHEGYI: We haven't done any of the contrasts so we aren't able to advise you of what the difference is. There are obviously complex issues to be resolved and they are time-consuming. But one contributing factor of course is the openness of the process, but that is what has been applauded by the industry in general, and certainly no-one can fault the openness of the OffGAR process, and anybody who wishes to make a comment is able to do so. So that speeding up the process is a good objective but not of course if it resulted in less open process.

MR COSGROVE: So are lengthy periods allowed for submissions to be presented or consultation of a public nature to take place?

MR SASHEGYI: Typically there is - I wouldn't say lengthy but I presume that perhaps the WA government might be able to tell you exactly what the period of time is. I haven't got it with me at the moment. One of the problems I think is the continual extensions; that there is a time frame announced at the outset and then there will be a whole series of extensions to the process, from what we can gather, with good reason. But certainly that would be very frustrating, and again I've no doubt Epic will be able to address those questions that you've raised when they take the stand. They are nodding, so they'll have the answers.

MR BANKS: Getting back to the question of your preferred governance arrangements in terms of a single state based regulator and so on, we've had some discussion through the hearings in response to the tier 2 proposals in here about perhaps having a single regulator, and also the question of what role there should be for ministers, and I'll just give you the opportunity, if there's any comment again from a WA perspective on either of those things, but perhaps particularly the question of the role of ministers in this process of access and ultimately having a say as to whether access should proceed or not.

MS CUSWORTH: Simply to make again the observation which I think we made in our submission, which is that however good on paper your regulatory apparatus appears to be, there will always, I suppose, to an extent be a political dimension to some of the more important decisions which are being made. I cannot see that there would ever be a regulatory arrangement which could completely bypass the political process, nor perhaps either would it necessarily be desirable. The key question is do you have, in terms of your regulatory structures, a process which is clearly focused and which is transparent in order that the political dimension is introduced in an appropriate manner so that it's properly informed.

I think if you have ill-specified objectives for the regulator, or if you have an

overly-clinical process, you could come up with some optimal outcomes, but you can't, I don't think, completely bypass the political dimension in regulation. It might be theoretically desirable in an ideal world but I've never seen any instance, anywhere around the world, where that's happened.

MR BANKS: There are people actually who have said, even theoretically, that the role of ministers is quite important because of the matters of inherently political judgment to be made about things like significance, and indeed the public interest dimensions on that. I guess in the interests of trying to find more expeditious ways through - and you've talked about some of the delays that can incur - we've been trying hard to find different areas where that could be achieved. We're obviously reviewing all of those in the light of the feedback we've got, but you see pragmatic, obviously, as well as in-principle reasons for that.

MS CUSWORTH: Yes. I can't see that there would be a politician who would completely abandon the capacity to affect these outcomes. I would not, however - and I might be misleading you - want to imply, for example, that the political process could short-cut the regulatory process while we have frustrations about the time in which some of these decisions are made. We would not want to see the capacity for political override to be one way in which that's addressed. We would say that the regulatory consideration process has to be gone through as a precursor to the final political decision, and not a short cut.

MR COSGROVE: I suppose there's a bit of an issue, perhaps a tension, between recommendations made by a body such as NCC - National Competition Council - and the subsequent reactions of a state minister, where it's possible that some of the broader interests which the National Competition Council might have been addressing are lost once the issue is resolved at the ministerial level. You would still, though, see that as appropriate?

MS CUSWORTH: Yes, and I recognise that there are difficulties in that process for exactly the reasons that you identify. The national dimension can be and quite often is lost when decisions get bounced back to the states but that's inevitable in a federal system. I can't see that there is a model which will ever completely resolve that kind of an issue. You do have, I suppose, with the current political structure, the final penalty which is threatened against inappropriate state behaviour, which is that the Commonwealth payments will be withdrawn. That is a constraining factor on inappropriate political responses but that tension is going to exist, whatever regulatory arrangement you put in place. I can't see that there's a way around it.

MR SASHEGYI: A practical example, not so much in terms of declaration but in terms of the certification process, was the negotiations that took place between the WA government and the NCC on the certification for the rail system rail access in WA. If you were to quiz the NCC later on today, I'm sure they would tell you the discussion was quite a robust process. There was very robust debate but the outcome at the moment appears to be a very reasonable one in terms of the desire for the state

government to sell the Westrail freight operation as a single entity, because they wanted to get a reasonable return for the sale and yet protect people wishing to send the freight along Westrail rail, an open access regime. That was the concept of selling the Westrail freight company as a holding company with two subsidiary companies. There were various options that were put forward in the sale process but essentially it was to separate the main east-west link from the above-rail operator part of the Westrail freight.

Of course the proof will be seen in the future in terms of the satisfaction or otherwise of the people seeking to have access to that network, but at the moment it certainly seems to be a reasonable outcome and the NCC would have been certifying the regime except for the fact that the interrelationship - which again gets back to the interface between national interests and state interests - the fact that the agreement for the NRTC and other state based regimes hadn't been finalised. They didn't want to certify the West Australian system in advance of those other arrangements being put in place.

But apart from that, I gather it was given a tick, so it certainly is possible to work your way through the state versus national interests under the current regime.

MR COSGROVE: Ultimately you'd have the declaration application as a possible further mechanism.

MR BANKS: The only other point I was going to seek clarification on really was that you'd drawn attention to the particular problems of vertically-integrated facilities, but I'd just like you to clarify perhaps your view in relation to, say, vertically-separated facilities that still have strong natural monopoly power. You weren't saying that they were not a policy issue?

MS CUSWORTH: The point I was trying to make there was that in the event that you've got a monopoly, your issues are less to do with access than to do with pricing. In other words, it's only where you have a vertically-integrated entity with monopoly power in parts of the market but not others that the entity would have an incentive to deny access to a second user if it was profitable to do so. So I can't envisage any market in which that would happen. I can certainly see that there would be problems with a monopolist in terms of pricing, but denying a profitable business proposition seems to me only likely to happen where you're using a monopoly power in one part of a market to prevent competition in another part.

MR BANKS: Yes. I guess we argued in here that at the end of the day it often comes down to terms and conditions because in a vertically-integrated facility there may be terms and conditions that would satisfy them in terms of allowing access but that would still be a very inefficient outcome.

MS CUSWORTH: Yes.

MR BANKS: While we accept the point you make we have actually seen the

national access regime as covering both vertically-integrated and vertically-separated facilities. Do you have any problems with that?

MS CUSWORTH: Only to the extent - and it might be perhaps just a technical distinction, but it's our view that you are looking primarily to price issue rather than access issue when you're talking about a non-integrated monopoly.

MR BANKS: That's true, and then the question is what is the best mechanism for dealing with that. That's why I spoke earlier about our need to consider these issues in a coordinated way in relation to the PSA inquiry as well as this one, because some had advocated that as a route for dealing with it.

MS CUSWORTH: And it comes back as well to the point we made in our submission that you can't really see access as being an issue separate from other forms of regulation.

MR BANKS: Good, thank you.

MR COSGROVE: You mentioned in your submission - at least in this state you seem as an extraordinarily complex set of overlapping acts which impede access in the gas sector. Do you think that the gas code in particular deals adequately with new investments as distinct from existing pipelines? Is that an issue that has arisen here?

MR SASHEGYI: The main area of concern really is in technical and safety regulations and that's where a lot of that has come from. Concerns have been expressed in the gas market about that and also most recently again with some proposed technical and safety regulations for the electricity market to be in place to oversee the more competitive electricity market that is expected to develop into the future. There are other areas but certainly that's where the greatest concern has been raised.

MR BANKS: All right. We don't have any other questions. Thank you very much for appearing. Any other final comments?

MS CUSWORTH: No, just thank you for the opportunity to present and we will be forwarding a brief submission covering the points which we've already outlined.

MR BANKS: Thanks very much for that. We'll just break for a few minutes, please.

MR BANKS: Ladies and gentlemen, we'll recommence. Our next participant is Epic Energy. Welcome to the hearings. Could I ask you, please to give your name and position with the company.

MR WILLIAMS: David Williams. I'm the general manager, corporate services and strategy development at Epic Energy.

MR BANKS: Thank you. Thanks very much for participating today. We also had a useful meeting with you, I think, in the first round prior to preparing our position paper, so I'll hand over to you to make whatever remarks you'd like.

MR WILLIAMS: Thanks very much, Mr Chairman. Epic unfortunately didn't file a submission but that was probably more due to fighting regulatory battles and not having the time to focus on it, so I do thank the commission for the opportunity to make a submission today.

As one who spends an inordinate amount of time struggling with the shackles of operating a business in a heavily regulated environment, one of the most gladdening moments of the year was the declaration by the tribunal that "regulation is a second-best option to competition". What must be of serious concern to us all is that the tribunal had to make this decision at all. This meant that not only had the body charged with overseeing national competition policy failed to observe a fundamental premise of its existence, but that a senior cabinet minister had also endorsed the view that economic theory took precedence over the workings of the market. I refer, of course, to the decision by the Australian Competition Tribunal overturning the coverage determination under the National Gas Access Code of the eastern gas pipeline, a pipeline that until very recently some protagonists insisted was "built under the code".

I intend today to outline the effect of heavy-handed and intrusive regulation on significant, often foreign, investment in the gas pipeline industry, and ask that you consider what I have to say against the question, is this in the public interest and the best interests of Australia.

The first area I'd like to touch on is regulatory overlap. When Epic Energy came to the realisation that the development of its vision of bringing Timor Sea gas to south-eastern Australia was likely to become a reality, it started ordering the major risk areas it would need to address in going forward with the project. It is disappointing to record that for a $1 billion to $1.5 billion major piece of infrastructure for Australia, equal top with market risk was regulatory risk. It is of grave concern that investment decisions as significant as this turn on what theoreticians believe is an appropriate level of return and degree of intrusion by outsiders. As we go through this presentation you will come to realise how significant an impact that has been, potentially with a major impact for Australia.

Epic Energy was faced with working out how to remove or minimise to an acceptable level the regulatory risk associated with constructing a new pipeline. It is interesting to note that the other parts of the value chain for gas, other than distribution networks, are not subject to regulation - not the production of gas nor the sale of gas. You can squeeze the value chain in the middle but it will not come out; it will simply transfer up to the producers or down to the sellers who benefit. Little wonder they are the most vocal in these debates and are generally focused solely on tariffs.

In dealing with the regulatory risk, Epic Energy started from the premise that the Darwin to Moomba pipeline would be regulated, that being the clear indication given by national regulators at that time. This was an unsatisfactory situation, given Epic Energy knew that the tariff and terms and conditions for the Darwin to Moomba pipeline would be determined by the market and there was no scope for Epic Energy to arbitrarily set the tariff or terms and conditions. The traditional cost of service approach of regulators with regular reopeners and hence limited certainty as applied by regulators using the code, plus the inordinate length of time taken by regulators to reach their decision, were clearly unacceptable.

Epic Energy looked to the other avenues available. A far more flexible route appeared to be open to it, namely an approved access undertaking under Part IIIA of the Trade Practices Act. This was a legal right it could elect, being very much consistent with the structure of Part IIIA which is the overarching structure for access regulation in Australia. However, there was a risk of regulatory overlap associated with that approach. I refer to the chance that although that undertaking is extant, a pipeline could become covered under the code and an access arrangement required to be submitted under that regime. If that pipeline were in Western Australia it would be regulated not only by two regimes but also by two regulators.

Epic Energy, through its industry association, the Australian Pipeline Industry Association (APIA), endeavoured to have that overlap removed with a relatively simple amendment to the code. That was submitted in November last year to the "owners" of the code, the Natural Gas Pipelines Advisory Committee (NGPAC). To be fair to NGPAC, it did move far more quickly on the proposal than it had done ever before. However, due to a certain degree of paranoia amongst some of the members of NGPAC, it is not possible for me to talk openly about the deliberations of that body. Needless to say, that amendment now sits on the shelf.

The effect of this prevarication, along with the intransigence of the national regulator, means that I am not in a position to advise our board that it is possible to obtain the necessary regulatory certainty for the investment. To proceed with this project in a way which has the most efficient configuration to meet the long-term future needs of this country - that is, with any level of spare capacity - would, in addition to construction risk, commercial risk and land issues such a project faces, attract significant regulatory risk which could severely impact on the expected returns in the future.

While it may be said with the GP decision the Darwin to Moomba pipeline will not be a covered pipeline and hence not subject to regulation, with what degree of certainty can that be said and for what period? The decision itself said it was focused on the present time and things may change over time. In addition, the decision is based on an interpretation of certain words in the code and Part IIIA, some of which are notoriously difficult to set hard and fast rules as to their meaning. While the decision is a good start in the right direction, it is not the end of the path that needs to be trod. In itself it does not provide the necessary degree of certainty as to non-regulation significant new infrastructure projects require.

The next area I'd like to refer to is the length of access arrangement approvals. Recently the ACCC set something of a record for Epic Energy. It released a draft decision within 10 months of our submission of an access arrangement. I refer there to the Bellara to Wallumbilla pipeline. Mind you, that was an access arrangement which had the tariff setting derogated. The Moomba to Adelaide pipeline access arrangement was filed in April 1999 - over two years ago - and the final decision is still some time away.

In Western Australia we have waited 18 months for a draft determination of an access arrangement for a pipeline that was built in this state 17 years ago and we are still waiting. In that time we have already contributed to OffGAR's costs plus our own external costs of over $2 million and, at the same time, the impact of the delay has let to a loss of potential revenue of over $20 million. In the Goldfields gas pipeline draft decision, the regulator has already acknowledged that it will fail to abide by the code itself and set a revision submission date nine months prior to the revision's commencement date, instead of the six contemplated under the code.

When we set out at the start of the year advising the ACCC that we were keen to invest up to one and a half billion dollars in developing a significant piece of infrastructure for Australia during which around 1200 construction workers would be engaged, but that we needed some early regulatory determinations to assist us to be in a position to have that project approved to proceed by around 30 June this year, we were presented with a number of insurmountable hurdles. In fact we asked again, given the strong statements made by the Australian Competition Tribunal in the Eastern Gas Pipelines decision, but again we were advised that they had no interest in trying to explore expediting the process, completely ignoring how the real world market operates. The pipeline will be built, but built in a way that means that the regulator becomes irrelevant during the initial investment period. However, there still remains a dark shadow, to which I will return a little later.

The next area that I'd like to touch on is the cost of regulation. The administrative costs of regulation to industry are fairly well understood. However, the perception by the Productivity Commission that much of the cost would be otherwise expended in the course of negotiation is not necessarily the case. Often industry is faced with regulatory scrutiny of negotiated outcomes and therefore pays

additional costs for regulation. It would be of benefit to industry if the regulator were to adopt an approach where negotiated outcomes were simply accepted as having met a particular threshold. This is a further reflection of the view that regulation should only occur in circumstances of demonstrated market failure.

In Western Australia gas pipeline owners pay all standing and service charges for the gas access regulator which, although it regulates a specific industry regime, is still part of the national access regime. Whilst the benefit of this arrangement is that there is minimal impact on state funds, as Western Australia has opted to have its own regulator (OffGAR) rather than the ACCC, gas consumers pay a "stealth tax" in the form of higher charges for delivered gas. Alternatively, those charges have to be absorbed by the service provider and adds another squeeze on margins. The way that OffGAR is funded has been a serious concern to many in the gas pipeline industry since its inception. Pipeliners feel aggrieved that whilst they fund all activities of the regulator, they have no influence of the timing of regulatory decisions, nor the consultants engaged on their filing, who they pay for, nor the methodology and costs associated with the decision-making process. Whilst it is proper for the regulator to remain independent, it is not right that the regulator should have no accountability for the way in which costs are accrued.

Epic Energy faced the interesting phenomenon last year when the Western Australian government chose to run a spurious argument based on the confidentiality deed to suppress major parts of Epic Energy's case put to the regulator, an approach which the minister later said he did not endorse. In order to try to break the deadlock the regulator engaged a QC. At the end of the day Epic Energy believes it was proven right, but who had to pay the cost of the QC? Epic Energy. Not surprisingly it left a somewhat bitter taste in our mouth. The question of who might pay costs associated with litigation is also unresolved. There is a view that proper transparent public funding of the regulator will lead to more accountability and more efficient use of resources than the current method.

The next area is resets. The question we would pose is: why is it so essential that the regulator insists on not only access arrangement of no more than five to 10 years in length for greenfield pipelines and five years for established pipelines, but also triggers to unwind the arrangement in the event that some external force may alter some parameters of that arrangement? Whatever happened to providing a degree of certainty for all parties? Does the regulator understand that this period does not reflect the investment horizon? No investor will contribute a significant sum of money unless some assurance can be offered that he will get an acceptable return for the life of the investment.

If you have a risk that rules will change part-way through the investment horizon, but you cannot say exactly how, this can only act as a deterrent to investors. Why should regulator risk threaten return on a new investment? There are more than enough risks already faced by proponents of new pipelines. The Productivity Commission has given weight to Professor King's suggestion of access holidays. If

the concept is broadly acceptable, as it seems to be, then at the very least the present regulators should be prepared to approve access arrangements for 20 years or so, without reopeners.

Coming back to the rate of return, much has been made of the generous returns offered in Australia compared to the US and UK. Whether that is true or not, there are no grounds for a simple or straight comparison. Australia is a very undeveloped market with a relatively recent regulatory history. Its overall economy is quite different from those countries. An example is the reference in the EGP decision to US legislation enacted in the 1890s. The bottom line is: what is the point at which it is attractive to foreign investors to bring capital in, or indeed to encourage domestic investors to leave capital in Australia? Epic Energy's owners comprise both of these categories of investors and both are equally vocal about their concerns in this area.

Asset valuation - a very brief word on asset valuation. There are a host of ways of in which an asset value can be determined and, as with many aspects of economic theory, some of these are hotly contested as to their merits. As far as we are concerned, it is again difficult to encourage investment when the regulator requires the actual capital cost to determine the reference tariff for a greenfields pipeline when investment decisions must be made years in advance of the construction commencing and regulatory decisions are required prior to the time of making such decision.

A further troubling feature of recent decisions of regulators is the apparent move to clawing back returns from the past. The moves to date have been in the guise of clawing back deferred tax liabilities when adopting a post-tax WACC approach, as seen in the draft decision of the ACCC for the Moomba to Adelaide pipeline. It is but a small step to say, "Well, we think that the returns you have obtained during the non-regulated period are higher than we would have allowed, so we will regard that excess return to be a return of capital and not a return on capital" and hence the capital base is reduced. Again the spectre of this gives pipeline investors little comfort for the future.

Overly consumer bias - a comment you will have heard many times is the concern about the regulator's overtly consumer bias.

Many times I've had said to me by regulatory staff, "We know what is good for the consumers. They do not." I continue to be incredulous about such statements given that the consumers of gas transmission pipelines are not mums and dads but are significant companies such as AGL, Santos, Origin and the like. It would be hard to find more sophisticated customers, and it is amazing that the regulator's officers would have better knowledge and ability than them to run their businesses.

To provide an illustration of the uneven bias, let us take a look at the Moomba to Adelaide pipeline. When the proposed access arrangement for the Moomba to Adelaide pipeline was filed, it was filed for the maximum regulatory period of

five years. In a sense it was nonsensical to make this filing as the Moomba to Adelaide pipeline was fully contracted through and beyond that period and would not be impacted by any tariff determination by the regulator. However, as required, an access arrangement was filed.

It was then interesting to see the draft decision issued by the ACCC which penalised Epic Energy on the rate of return as it had no risk during the regulatory period as it was fully contracted and had no spare capacity. However, it was then the double standard that was applied when Epic Energy was told that it needed to bring in other services and modify terms as the access arrangement would be used to negotiate access contracts far beyond the contracted period. That really being the purpose of the access arrangement - hang on, why are we then judged for a return on a narrow period but then judged on other matters for a longer period? There needs to be a better balance of interests.

Another example is the so-called light-handed regulation intent of the code. Service providers have come under an increasing narrow and pedantic scrutiny by regulators which has led to time consuming and over-complicating work being done on access arrangements. An illustration is again with the Moomba to Adelaide pipeline where, would you believe, we were told how to redraft our precedents of documents clause, and I refer to amendment A3.29. There seems to be a view that as the pipelines are regulated, then by controlling and squeezing them, the regulators are able to control the end prices paid by consumers. This is simply not the case. In fact it may well be a myth that those who have everything to gain from that being believed perpetuate. I invite the commission to dig a little deeper in this area and see whether in fact the reduction of tariffs on gas pipeline systems has in fact flowed through to the end consumer.

Accountability - one of the major issues at the heart of this is the lack of accountability that regulators have. There is simply no ability to have checked what the regulators are doing. Service providers are left with no ability to have the work of regulators checked. The omission of a right of merit review is a serious omission and flaw in this area of regulation. It is somewhat unusual in this day and age for an area of administrative law not to have an ability to have a regulator's decision reviewed on the merits. A good example of how this could be done is the well-tested system adopted in Australia's industrial relations system. The need for such a review is imperative given the impact that such regulation has on the viability of the pipeline businesses; businesses which have significant dollars invested in the ground, yet their fate is presided over by academic theoreticians. This is an area where we would encourage the commission to also look into.

I would like to come back to greenfields development. There are strong arguments that support the view that new pipelines should not be covered at all. This includes the contestability of new pipelines prior to construction. Look at the various proposals that have been announced in relation to the Victorian-South Australian pipeline. Also new pipelines are likely to offer competition in the form of competing

supply, competing basis or competing energy sources. It was heartening to see the Australian Competition Tribunal recognise this.

There is a more fundamental argument that harks back to the coverage test for pipelines under the code. It is patently not in the interests of a non-vertically integrated business to block access to its pipelines. The question is therefore how can regulated access make a pipeline more competitive than the market. We recently asked the chairman of the ACCC to assist in hastening any determination on a potential filing bias on the Darwin to Moomba pipeline - this was in relation to the access undertaking route - by testing the concept of the market derived tariff, particularly in the light of the eastern gas pipeline decision and its reference to regulation being a second-best outcome to the market.

Our proposal was the possibility of having the merits of a market derived access arrangement versus a cost-of-service approach examined in a public process ahead of any formal filing of the undertaking. The reply we received:

> The commission has reservations with the approach owing to the abstract nature of the concept put forward by Epic. The commission does not consider that it would be appropriate to form a judgment on the concept of market derived terms in the absence of detailed services of the pipeline. It is not possible to assess whether market-derived terms have been determined by competitive pressures or the exercise of market power without examining the specific circumstances.

We were simply asking the chairman to have the ACCC determine whether market results should be favoured over theory, something the policy makers continually insist is the nature of Australian regulatory regime. An answer to this question would have enabled us to shape our approach in reaching a determination on how best to construct the Darwin to Moomba pipeline.

I would just like briefly to refer to the Australian Taxation Office prospective ruling on effective life. Industry has been expressing its concern recently over the possibility of an immediate application of a ruling by the Australian Taxation Office to extend the depreciation of pipelines from 20 to 50 years. That this remains a real possibility is of serious concern to the industry and will have a direct impact in dampening pipeline investment. Whilst I recognise this does not directly relate to a review of Part IIIA, you are the Productivity Commission and must be interested in the potential impact.

Taken together with a dead-handed regulation it is becoming increasingly difficult to make the required returns from building and operating gas pipelines. We at Epic Energy, undoubtedly alongside others, are reviewing our commitment to this industry and must consider turning to non-regulated activities instead in order to generate the required returns.

The impact of regulation investment. I will finish now with our answer to your $64,000 question. How does Part 111A and its associated industry access regimes impact on investment? We are a pipeline company. We want to build and operate the best pipelines in the country, pipelines that earn us a decent return, yes, but also to promote development as that, to us, equals a bigger market. It leads to innovation and efficiency and ultimately shapes Australia to be able to compete worldwide across the energy sector.

At the moment what are we faced with? Building pipelines to purpose, underwriting them so there is no spare capacity. That includes enhancements of existing pipelines. How many pipelines have been developed and built under the access regimes? How many enhancements with spare capacity have been made? That's not announcements or speculation but actual pipes in the ground. Who has or is spending the money? How and when?

The recent eastern gas pipeline decision gave us hope that there was a will in this country to promote infrastructure and reward risk, that it came from a review tribunal comprising a blend of skills and interest and was vigorously opposed by the regulators - and I refer you for example to comments made by the ACCC in its draft decision on the Bellara to Wallumbilla pipeline - should be of great concern to us all. The current regime is too bureaucratic, too theorist and, for that matter, too centred in Canberra, which is hardly the seat of industry, to understand the needs of regional Australia and to have an understanding of the need to break the shackles and step in only when there is proven market failure.

The market must take primacy over economic theory. We therefore welcome the recent COAG initiative which considers amongst its priority issues identifying any impediments to the full realisation of the benefits of energy market reform, examining regulatory approaches that effectively balance incentives for new supply investment, demand responses and benefits to consumers, and identifying means of encouraging the wider penetration of natural gas, including increased upstream gas competition, value-adding processes for natural gas and potential other users, such as distributor generation, because it is an abundant, domestically-available, and clean energy resource. I thank the commission for the time and would be happy to answer any questions.

MR BANKS: Thank you very much for that. My colleague and I have some questions which occurred to us as you have been speaking. One of the earlier points you made was the proposition that you put to NGPAC in relation to changes to the code to remove this sort of overlap problem that you were concerned about in getting some certainty for this investment. Could you just elaborate a little bit on what you were proposing there.

MR WILLIAMS: The proposal was aimed at at least removing the overlap in a short-term period, recognising, as always, that the code needed a fundamental review, particularly in the area of greenfields. There are a lot of differences in

opinions and I respect those differences but, primarily, we were faced with the situation that if we had gone down the access undertaking route and obtained an approved undertaking under Part IIIA, that once the pipeline was built it was then open for someone to apply for that pipeline to be covered and, if it was determined to be a covered pipeline then we would immediately - or within 90 days - be obligated to file a proposed access arrangement under the code.

Once that has gone through its processes, you have an agreed access arrangement under the code and an approved access undertaking under Part IIIA, so you would have two access regimes applying: one, you would have the confusion about which was to apply and, secondly, you had the difficulty or the potentiality that what you had made your investment decision on could be white-anted or depreciated by what ultimately became approved as an access arrangement under the code.

So Epic, through the APIA, proposed an amendment to the code that said if you had an approved access undertaking you did not need to file an access arrangement while that approved undertaking was in existence - while it remained approved. We put a couple of changes to that and that came out of discussions with various jurisdictions. One was to put a sunset clause on it because, quite rightly, the fear was that if you make an amendment no-one will ever come back and sort it out. It really was only intended to be a temporary fix as far as greenfields was concerned, so we put a two-year sunset clause on that provision - if you hadn't had an access undertaking approved within the two years then there was no guarantee that that provision would apply to you after that.

The second variation to that was that it would only apply to pipelines not already built, and that was to negate a fear that existing pipelines would move holus bolus away from out under the code to under an undertaking route under Part IIIA, and that again wasn't the intention. It was intended to deal with greenfields pipelines. As I said, to be fair to NGPAC, they really did work extremely diligently on it and moved it through at an extraordinary pace, of which Epic particularly was most appreciative, but the actual amendment that came out - that was recommended - had a further variation on it and that variation was that if you had an approved access undertaking under Part IIIA then you would automatically be a covered pipeline under the code for the duration of the code.

At the time I was faced by commercial expediency and, at the time, Epic believed that the Darwin to Moomba pipeline would be a covered pipeline, given the nature of the decisions and the pronouncements at that time. While it didn't agree with the automatic coverage in principle, because it seemed to fly in the face of even the principles in Part IIIA, let alone the code, it was driven by commercial expediency and I couldn't say that there was going to be any benefit to me in opposing that because we believed we would be covered at that time.

Once of course the eastern gas pipeline decision came down, which gave a pretty strong indication that - on the view of the tribunal - it was likely that the

Darwin to Moomba pipeline wouldn't be regarded as being a covered pipeline, clearly we could no longer support that proposition and, unfortunately, that amendment now has gone into limbo. Be that as it may, that is not to say that we won't continue to push for that because I think we still see a place for removing that regulatory overlap, despite the way, potentially, it is likely the pipeline will now be configured. Hence it removes the need for that regulatory certainty.

MR COSGROVE: The gas code is intended effectively to operate under Part IIIA.

MR WILLIAMS: Correct.

MR COSGROVE: Why is it then that an approved undertaking under Part IIIA is not regarded as acceptable for gas code purposes?

MR WILLIAMS: I think you would have to ask some other people that. That's exactly our point, and I should perhaps explain why Epic looked at going down the undertaking route in the circumstances. The reason it did that is that, as I explained before, the Darwin to Moomba pipeline is very much a product of the market. The existing market has said, "We'll pay this particular price. We know what we can buy it from our existing suppliers or other suppliers, so if you are prepared to sell us your gas on these terms and conditions and this price, we'll buy it." Philips, who has the gas, says, "Well, it's our gas. We want this amount for the gas." What falls out is the tariff

and, in a sense, the terms and conditions as well for the gas transmission pipeline. So we don't have an ability to lift it up. Obviously we could drop it down if we wanted to but we don't have the ability to lift it up. We therefore have to look at what is the product of that as to whether it's still a viable project or not.

So given the way that the regulators to date had applied the code - and I should hasten to add that it's an approach that Epic doesn't agree with, and particularly I personally don't agree with. I believe in actual fact the code as drafted was intended to be a flexible document. It does contain some detail but the detail was more as an illustration or to provide some assistance to the regulator, it's not intended to be a prescriptive document, but the way it has been applied by regulators to date has been in a very prescriptive manner to say basically say what is set out in the code is what we have to apply.

When I contrasted that with the provisions in Part IIIA for the undertaking, which had four or five very simple principles, it seemed to me that if there was a will, as far as the regulator was concerned, the better was down the undertaking route because he wasn't caught by the legislation specifically saying these prescriptive terms, he had a piece of legislation that said, "Well, you only have to satisfy these principles. You have to balance up these principles, so therefore you really can go on whatever path you want, be that a market-derived path or what have you."

Having said that, I knew that - I was still staring at the wall - it was not going to be any easy task, but at least I was providing myself a better situation than I was under the code. The reason I say I was still staring at the wall was that the ACCC's published guidelines and its preferred approach was to still apply the code as the code, giving an example of what were appropriate principles it should look at in balancing those broader principles under Part IIIA of the access undertakings.

That is a comment in relation to something that the Productivity Commission has referred to about perhaps having greater specification of pricing principles in Part IIIA for the undertaking route. I think the difficulty with that is that unfortunately regulators will grab hold of those too much - and understandably. I don't necessarily criticise the regulators. It's perhaps a frustration I have, but clearly we'll be looking for guidance and for more prescription - if you contain too much prescription then it takes away from the flexibility that was intended, and the code and its application by regulators to date is a very, very good example of that.

We are faced with the situation, and we've been faced with it, where the regulators - or the regulator, in the case of Darwin to Moomba - is used to the code and believes the code sets a good example, and has great difficulty in moving away from that code to something that, for Darwin to Moomba, which is a product of the market, we believe should just be a very simple tick and, "Good on you. Get on with the business and get investing that money. That's going to be great for Australia. There is no need for us to interfere because the market is in control of you at the moment."

As a postscript to that I should emphasise that Epic, throughout that process of putting the code change through NGPAC, was at pains to say that we accept that ultimately we would be a regulated pipeline, be that even if there was interbasin competition, which is likely to be the case as you develop that infrastructure, once you've got a captured market, once you've got someone having their first contract, when they then want to go on to their next contract they are in a sense captured, although where you've got interbasin competition it's not necessarily the case. Maybe that is a time for regulation. So we don't fear regulation but we just find it a stultifying influence as far as new investment is concerned.

MR COSGROVE: Who is the regulator in respect of the Darwin-Moomba line?

MR WILLIAMS: ACCC. It's only if you've got a pipeline purely in Western Australia that it will be OffGAR - in gas transmission pipelines.

MR COSGROVE: So you have the same regulator applying different rules under Part IIIA and the gas code in respect of transmission lines.

MR WILLIAMS: That would be the case, as of course it could be for distribution systems if they were to do an access undertaking, But it is and it isn't. I take the view that if you look very closely at the code, the code isn't prescriptive, it is

fundamentally about and was only ever, I believe, ever intended to be about setting a broad framework in which a broad line in the sand would be set to provide a reference point for prospective users and service providers to negotiate, so that you weren't operating in a vacuum; that there would be at least some guidance to both the parties negotiating and ultimately an arbitrator, if an arbitrator was required. It wasn't intended to lead to a very prescriptive set of provisions like the US model, where things are very detailed and very prescriptive as to the different services. That wasn't the intent of the Australian system. So in a sense I don't see any disjunct between the access undertaking route and the code route.

MR BANKS: You said that your assessment of the prospects of coverage of the Darwin to Moomba pipeline changed following the Duke decision. Could you just explain why you saw that?

MR WILLIAMS: I suppose it was more in what had come out, and maybe it was also a jaundiced view about the regulators industry, if I can put it that way. It was particularly with the pronouncements that had been made to date by the NCC on the eastern gas pipeline and also in a sense the arguments put by the ACCC, even though it wasn't as such directly regulating that area. It seemed that, even though a pipeline or two pipelines might service the same end market, because they didn't service the same market along the way they were therefore a natural monopoly in the simple fact that you had a pipeline in there and, unless you had the situation where you had a pipeline side by side, it was never going to not satisfy the tests of a covered pipeline.

Then when the pronouncement from the tribunal came out that it was really looking far broader than that and it was looking at, "What impact will it have on the market? Will regulation add something that's not already going to be there?" and that it's pretty obvious to us as investors in infrastructure and developers of new projects - it's always been patently obvious to us that we are always in a competitive environment, particularly with a new investment. You're either competing with existing suppliers of energy, be they gas or be they other forms of energy,

or you're actually competing to come up with a viable cost for a new project, so a project that's not even in existence, and therefore you're always operating under competitive pressures, and the regulatory environment is going to do nothing to that than what the market will, and again we're talking about gas transmission pipelines which are operating with sophisticated users, and again it's not so much the mums and dads that are dealing with it.

So with Darwin to Moomba, by bringing the Timor Sea gas down, and the gas from the Timor Sea Basin, it's competing with gas suppliers who are already and will continue to be in the Cooper Basin and produced by the Moomba producers, but also competing with the gas coming out of Longford through the eastern gas pipeline, so that we're immediately subject to competitive pressures in order to sell the capacity in a pipeline. No-one has committed to us, and they'll only commit to us if they think they're going to get a good deal.

I remember having a comment made to me at one stage, "Well, you need to be checked on in case you're ripping off the end user." My comment to that is, well, if we are ripping them off, and I can guarantee you we're not - we wouldn't be - but if we were, then they're already getting ripped off a hell of a lot more than we are because they're already existing purchasers of gas from the market. So isn't it better that they're ripped off less than they're already getting ripped off, if that's your view of the world. That's the market, the competitive tensions. So when we looked at that and we looked at - well, yes, we are an absolute product of competition in much the same way, although slightly different positioning physically of the pipelines, but in much the same way as the eastern gas pipelines. Then under a number of the tests that were put up by the tribunal and a number of the comments made by the tribunal, at least at this stage Darwin to Moomba would not be a covered pipeline.

MR BANKS: From what you're saying, it related more to the way they assess competition rather than the natural monopoly component per se. Is that what reassured you?

MR WILLIAMS: I think that's right. It's the recognition of the fact that in order for you to get the sales then you are in a competitive environment, so regulation is going to add nothing in that case. It's interesting when you actually take it out of that environment where you're dealing specifically with inter-basin competition, to other environments where you're actually dealing with new projects or existing projects that might like to switch energy sources, where you might be the sole pipeline, if you put it in, that can supply, and it's obviously not as clear-cut as the Darwin to Moomba situation, but because you've got to compete and get the price right for that project for something that it doesn't already have access to, then it doesn't matter if you get a good return. It's still got to be a good result because the project is not going to go down that path and contract with you, or use that form of energy unless it's an appropriate price for the project.

MR BANKS: How would you see the potential revocation of the Moomba to Sydney pipeline as factoring into all of this in terms of the essential contestability in the market or the competitive conditions in the market?

MR WILLIAMS: I suppose we would certainly watch it with interest but just as an observation it would seem a bit odd if you've got one pipeline that's regulated and another one that's not and they're competing for the same market. One would assume that the prices of the tariffs, the future contracts on the Moomba to Sydney pipeline, will have to be competitive in meeting the tariffs of eastern gas pipeline. The other interesting observation that I don't think is often made, although I did refer to it in the comments I made earlier, is that that's fine, you can squeeze down the costs of transport along the way, but at the end of the day are you going to make any difference to the delivered gas price, because what the market is interested in is the delivered gas, and the market will set the price of delivered gas. So that's great, you can screw down as much as you like the tariff that a pipeline operator will get, but I'll

bet my bottom dollar that it won't make any difference to the end tariff.

MR BANKS: So you're saying there's monopoly power in other elements of the chain which will appropriate the rents.

MR WILLIAMS: Absolutely, and at the moment all that is being regulated, all that is being squeezed, as I said, is the middle.

MR BANKS: So where do you see that monopoly power residing, upstream or downstream?

MR WILLIAMS: It can reside in both places. It will depend on the particular market. Sometimes it may well be upstream, sometimes it may well be downstream, and that will vary from market to market, but don't necessarily think that the panacea and the means of control, of ensuring that the end price is right, is to simply squeeze the pipelines in the middle.

MR BANKS: But isn't in a sense what you're saying the squeezing or the provision of access itself attempting to address the competitive conditions in the downstream market?

MR WILLIAMS: Well, it is, in the sense of where you've demonstrated that you're not playing the game as you should be playing it, that you need to have regulation. Regulation, after all, is about policing someone that is exercising their monopoly power in one situation or is not playing according to the rules of the market to come out with an efficient result. Now, I'm not sure that we've seen that, and I'm not sure that's been demonstrated that that has been the case in the past, but largely most of the pipelines that have become regulated were operated and owned by the state governments before that. Maybe it's a sad indictment on the state governments that they believed in selling them, that perhaps in the way that they had operated them there needed to be regulation, because that's the only experience that was there in existence at the time.

But certainly in the case where you've got a healthy market and you look at our situation, because we're a pure pipeline, our interest is to get as much gas flowing through our pipeline as is possible. That's the game we're in. It's no interest of ours to constrain people putting gas through our pipelines; quite the opposite.

MR BANKS: We talked about impacts on investment and you talked about it at the end, but you also I think may have referred to it earlier on, where you talked about - and I think you were talking about again the Darwin to Moomba pipeline, that it would, I think to quote you, "be built in a way such that the regulation would be irrelevant in the early period". Would you care just to elaborate on that.

MR WILLIAMS: Yes. Clearly entering into a project with such significant investment as a billion to a billion and a half - clearly, like any infrastructure project,

we'll be looking for some underwriting as far as contracts are concerned, but we also have a vision about what the demand will be over a 10-year horizon, and we typically look at projects over a 20-year horizon. Typically you're talking about as significant sums as that, and when you take the view about how the market is likely to develop, you realise that, as I say, over 20 years you'd expect that the flow through the pipeline to be much greater than what the initial capacity is that it would be contracted for, particularly when you're dealing with pipelines of this size. It is far more efficient and far more cost-efficient and far more efficient in the set-up if you build that pipeline initially with spare capacity - build the capacity now that you know you're going to have taken up.

You've obviously got to balance the market risk and the sunk costs now with later on, but largely, if you've got an expanding market, it is going to be more efficient to build that pipeline with greater capacity. Therefore, you're going to be able to provide it on a cheaper basis and a more efficient basis to consumers once it comes along. As soon as you have spare capacity, you've got an opening for the regulator to step in and have some say in what's going to happen. Unfortunately, when you initially contract at the start the initial shipper is clearly not going to be wanting to be out of the market - he's the one that's making the initial investment as such that's going to make the project go so he's clearly going to be interested in a favoured nations clause. Therefore you know that if the regulator steps in later on and determines that the capacity should be at a price lower than what you might have contracted for at the beginning and you get someone who comes along and contracts, forces you to sell the capacity at that price, immediately you've got flow-on to the initial shipper.

That's particularly feasible with the Darwin to Moomba pipeline. Given its length it requires compression, so with a 2200-kilometre pipeline you couldn't build a free-flow pipe from Darwin to Moomba or the Moomba area. It has to have some compression, which therefore means that you can design it to meet specifically the initial capacity that's contracted for. So it will be built without spare capacity. That therefore means that when someone else comes along later on and says, "I'd like some capacity," then we'll have to have a look at it as to what the enhancement of the pipeline will be to match that requirement, because again if there's the spectre of the regulator interfering we won't build it with spare capacity.

I can cite to you two current examples of that practice. Both of those are our own. One is the Dampier to Bunbury natural gas pipeline where the recent stage 3A enhancement- a $120 million enhancement - was constructed; no spare capacity. The other is the Moomba to Adelaide pipeline, the stage 2 looping, which is a much lesser investment, but again no spare capacity was built. Investors are not going to build spare capacity when they know they're going to get a pre-tax real return of 6.7, as is in the draft decision of the Moomba to Adelaide pipeline.

Similarly, you can manage that. The problem is that the incremental costs of the expansion then are going to be much higher, so that someone coming along (1) is

not going to have the spare capacity readily available. That means they're going to have to come and talk to us at an early stage in their project or at an early stage of their negotiations to ensure that they can negotiate additional capacity in sufficient time which gives us the ability to build it, and it will of course get built in a far less efficient means.

MR BANKS: Is there any concern that this could open you up to the provisions in IIIA whereby the ACCC could require additional capacity to be provided? This is a point that we addressed in the position paper and, indeed, questioned whether that provision should apply as opposed to provision for interconnection.

MR WILLIAMS: There's a similar sort of provision in the code as well. It's a little bit more detailed and I suppose we sit a little more comfortably with that provision. At the end of the day, you can take a horse to water but you can't make him drink, and the fact of the matter is you can turn around and say, "You will build that capacity," but if the returns are not such that means that the funding is available - and that's not just funding from the owners; that's also funding from the banks, financing from the banks; we're not talking about small sums of money to enhance - you can't force someone to do in a practical sense something that is just not feasible to do.

We will always build, if it's commercially viable, and the fact of the matter is we don't believe that we'll ever need a regulator to tell us to build, because if someone is coming along and genuinely wants the capacity, we'll do whatever we can to make sure that they get that capacity because our business is flowing as much gas as possible through our pipelines. There is no demonstration of existing owners, or certainly of Epic and other owners that I'm aware of, acting in a monopolistic way that's to the detriment of potential users.

MR COSGROVE: You were critical at the beginning of your remarks today about the decisions taken by a regulatory body and a minister which led to the need to go to the tribunal on the EGP case. Do you have any general views about the role of ministers in these processes or access?

MR WILLIAMS: Yes. It's interesting, because we're also stuck in the middle indirectly of another one that's going at the moment, and that's the Queensland access legislation. You may well be aware of that, where Queensland enacted its legislation with a number of derogations for existing pipelines, the derogations which were specifically contemplated and referred to in the intergovernmental agreement that led to the code happening. The intergovernmental agreement said, "We'll have a code," and in the case of Queensland there are going to be derogations for these pipelines, as of course there were a number of other derogations for other states and a number of other special provisions for other states.

We indirectly are facing the situation where the NCC has recommended that, for all of its own reasons, it should not be determined to be an effective access regime and would therefore pull the whole Queensland regime apart. We've just

recently got a draft decision from the ACCC on the Bellara to Wallumbilla pipeline and, again, that is littered with comments about, "This is not fair." We should be dealing with the tariffs. At this stage the minister has not made a decision.

We understand that the minister is carefully considering all that's been put to him, both as a recommendation from the NCC and from subsequent comments from industry and from the Queensland government. It is for him to determine what should be the policy, because when we're talking about coverage and that sort of thing we are really talking about government policy, and it's my belief that the intent of those provisions was to say, "As to what should really be governed by this, well, it's hard to tell, but we'll put in some rules." At the end of the day it really is up to the government to determine what it should cover, what the government's policy intent is to cover or what the government's policy intent is as to whether that's an appropriate regime or not. So in that sense, when you're dealing with policy issues, the minister very much has a role to play provided that he doesn't act as a rubber stamp.

I think that's the problem that we would argue, or others would argue as well, as far as the minister's action in relation to the use of gas pipelines. And to be fair to him, it was early days and even I admitted myself that I thought that was the way it was going to go, as per the recommendation. But at the end of the day he mustn't be a rubber stamp, he must make his own decision and must simply look at what he receives from the NCC or whomever as just part of the advice that he takes into consideration. I would take the view that the ministers do have a role to play in this area of determining policy issue coverage.

MR COSGROVE: Coverage, yes.

MR BANKS: Okay, thank you. The only other question I was going to ask you was that we've had some discussion with others in your industry in relation to access holidays and provisions that would give greater certainty ex ante at the time when greater certainty is really needed. You know, as you were saying earlier, you saw the regulatory risk as being right up there with the market risk as sort of major considerations. A critical issue in relation to access holidays is what the period of holiday would be. Would you like to make any comment on that?

What we put forward in the position paper was I guess the provision of whatever you like to call it, a safe harbour or access holiday whereby certain new investments would be excluded from the purview of the regime for a particular period; not forever, because that could set up some perverse incentives in terms of the initial investment decision - but for a period. The question then is: what should that period be? Some have said to us if it's too short it misses the point because you don't need it so much in the early days when you're making losses and you really need it to when you're in a position to be able to make up some of that ground further down the track. Would you have any comment to offer on that?

MR WILLIAMS: Certainly. Obviously the illustration of the Darwin to Moomba pipeline is a classic but we believe at least in the initial phase you do; it would be helped enormously if there was a moratorium on access regulation for a period of time. I've talked about our investment horizon generally as 20 years. The contracts that customers are talking about are in the order of 15 to 20 years. Yes, that could well vary from pipeline to pipeline, but at the end of the day I suppose - and this almost comes back to the earlier question about the minister's role - at the end of the day the need for infrastructure investment, the need for infrastructure development can play a very important role; a very important part of a country or state's economy.

It may be that therefore is an area where it should come back to the minister to consider taking into account the relevant feature or the relevant issues, the relevant pressures facing a particular pipeline proposal. What is important is that must be known with a high degree of certainty at a very early stage in a project. Projects don't happen overnight; projects have a number of pieces of the jigsaw that have to all come together and all come together at the right time. One of those important ones at the moment - because it fundamentally affects the economics of a project - is are you going to be regulated or not? If you are not going to be regulated, for what period of time?

One way of looking at it is that you could look at it almost as a two-stage process. You could look at providing that moratorium for the initial investment horizon, the initial investment period of what is seen to be reasonable for it. Again, that might vary from project to project, but you then leave it open so that at the end of that period you still need to determine whether it's appropriate that regulation should apply. So you shouldn't have automatic coverage at the end of the moratorium, or even during it. It should be left alone and then look at the test of: how has the market developed at that time?

But you certainly need, with significant infrastructure investment, a reasonable period of time to provide the incentive. Again, I suppose it's almost supply and demand, isn't it? It's that unknown question of how long - I can't give you the answer - do investors need before they become jaundiced and don't invest, or invest in a particular way? It's going to vary, I would suggest, certainly on the amount of investment, but also the nature of the market and how the market is likely to play out, perhaps how much speculation have you taken, how much is secure because it's an underwritten contract? The obvious thing is that if it is an underwritten contract that is 15 to 20 years. Okay, the time to look at it is when that contract needs to be renewed and knowing that it will be able to be renewed in the aura of regulation if it's required.

MR BANKS: Typically, when you say an "underwritten contract," regulation aside, what proportion of capacity would you seek to underwrite up-front?

MR WILLIAMS: As much as possible. Again, it will depend upon your view of the market and how strongly you take the view of whether the market will

materialise, how vibrant do you think the economy is that you're going into, how likely is it that that market will come to your investment and not to someone else's investment. So it is a function of market risk as to how much you build in there. That's why it is difficult. I mean, let's say you had no prospect of a competing pipeline or a competing basin, but you're speculating on getting into a new area and that it is going to grow, or you might take the view that in 20 years' time it will be double, so you might be prepared to build a pipeline that has 25 to 50 per cent spare capacity.

On the other hand, if you're going into an area that is highly competitive and you know you'll get the first part of it but there's no guarantees of whether you'll get the next part, you've got to balance what is going to be the cost of increasing the pipeline to meet that future demand: will that make me competitive, or do I actually need to make a bit more of an investment now and take a bit of a punt, because I know that's going to put me on a better footing to compete with those other sources?

In saying that, there also can be ways in which you set up a pipeline at the beginning, that it could produce the same capacity but you could set it up with a lower capital investment, which will mean it's got a much higher incremental cost later on, or you can invest it with a higher degree of capital investment at the start - still with the same initial capacity but then has a lower incremental cost down the track.

MR BANKS: Okay.

MR COSGROVE: The other main policy question associated with these holiday and moratorium ideas is which projects would be eligible? We've been thinking about the notion of contestability as perhaps the useful criterion in that context. Do you have any thoughts on that point?

MR WILLIAMS: At the end of the day any new project for a gas transmission pipeline is in a contestable environment.

MR COSGROVE: Even if an incumbent pipeline operator is expanding its own network?

MR WILLIAMS: Sorry, yes. I just was dealing at the moment with new pipelines. I'll come back onto the expansion side of it, which is a little more complicated and I accept some of the comments you might talk about there. But in the case of a new pipeline you're necessarily either going into a new area, and therefore you're competing with existing energy forms or you're competing to get the economics right to make a new project happen, or you're operating into a market where there are already suppliers and therefore you're immediately into a contestable environment. I would take the view that in the case of a new pipeline you're always in a contestable environment and therefore it's a non-issue.

MR COSGROVE: Perhaps the regulator should be required to show why it would be otherwise; that it should be covered.

MR WILLIAMS: Yes, that's true. I fail to see how there could ever be a case that, because right from the outset there are different issues. There might be a situation where a government chooses to - you know, "I want a piece of infrastructure here as a government decision, a social policy decision. I want a piece of infrastructure." That's where the competitive tendering provisions come in, because that's going to ensure that the government gets the best price. But when it's a private industry initiative, obviously they're competing with the market. They don't have a captured market there. They're trying to create it or they're trying to capture it from someone else, so the pressure is there. It's a different environment and clearly competitive tendering is not going to work.

If you'd relied on competitive tendering, the germ of the idea that came out of Epic - and then by working with Philips, which led to the Timor Sea project - would never have happened. That's not something that has come out of competitive tendering. It has come out of two different people having an idea and testing the market and finding the market is receptive. It's a different situation if a government decides as a matter of social policy it should have a piece of infrastructure, and there you've got the competitive tendering which covers it.

The expansion extension is an interesting element and I have to be honest and say that it's not 100 per cent the same as a new pipeline because there can be situations as part of more expansion where you've got an existing customer whose business is growing and who started that basis that he's getting gas through his pipeline, that therefore might need to be able to get that further expansion, provided that it is economic for the pipeline producer to do it. A lot of the situations are of course where you've actually got new business coming, and an expansion to meet new businesses again is subject to that same competitive or contestability situation. You're either competing to make the economics of the project work, or you're competing with that new project having another fuel source. In the case of power generation in Western Australia you're competing against distillate or coal, so you're competing to try to beat the energy forms in order to be able to supply to new generators or existing generators.

MR COSGROVE: Just one last question. You raised some rhetorical questions, I think, about how many new pipelines have been built since the gas code arrangements were put in place. In doing so I took you to be meaning very few. There is a submission which we've received from BHP, which paints a somewhat different picture. If you have a chance to look at it and give us any comments on the material in that submission, that would be interesting.

MR WILLIAMS: Yes, I'm well aware of the comment and I suppose I might have missed out a specific word but that's where my comments were quite deliberate about pipelines being developed and built under the code. In actual fact the prime

reference that they refer to is the eastern gas pipeline and, as you're aware, it is not a covered pipeline. It was a pipeline that the current owner and operator, Duke, who constructed the pipeline, were at pains right from the outset to say it wasn't a covered pipeline and eventually were proven right. So you can't say that that was a pipeline developed and built under the code; quite the opposite.

Central west, yes, was built ultimately under the code. It's a much smaller pipeline, much smaller investment, but I can't think of any others. There's a lot in the press. We talk about this. We've said in the press, "We're going to build Darwin to Moomba," but I've also said today that's where we're heading and we've always said from the outset, provided we can get regulatory certainty; or provided it can be structured in such a way it doesn't have regulatory exposure. If you look deep down in the other announcements you'll find much the same.

MR BANKS: All right, thank you very much for that. If you can get back to us with any further thoughts, we would appreciate it. Thank you very much for your time today.

MR WILLIAMS: Thank you.

MR BANKS: We'll just break for a moment.

MR BANKS: Our next participant this morning is Tap Oil Ltd. Welcome to the hearings. Could I ask you, please, to give your name and position with the company.

MR UNDERWOOD: Paul Underwood, chief executive officer and managing director of Tap Oil Ltd.

MR BANKS: Thanks for attending today, and also for the submission that we've received. We've got a few questions for you on that submission but we will give you the opportunity to make the main points.

MR UNDERWOOD: Thanks. Today I did intend to be accompanied by commercial manager and in-house counsel Michael Dagostino. He was called overseas and he has been the one dealing with most of the detail on this so we don't have a written submission for today. As I was just saying, I do consider myself to be somewhat of a unique commentator on this whole process, and I will make today's submission somewhat general in nature but deal with some specific material that was raised this morning, and also a WA focus.

Why I say I have somewhat of a unique exposure to this process: going right back to 1989 I was at the mercy of the owner of a pipeline in Queensland where my company paid 20 cents a barrel to transport oil less than it cost to truck it. Let's face it, the whole genesis of this national access pipeline code goes back to an issue in Queensland where access was frustrated and it was thought that the ACCC legislation wouldn't deal with it and this whole process four years ago was born out of that. It was a federal issue to solve an issue in Queensland.

What I would say is WA ain't Queensland and Australia ain't the USA, and I think the process is flawed because of that philosophy. What I would say is that we now have a blanket solution for the country which probably has solved the Queensland issue or, if it hasn't, probably will. But I step back from it and say, "Well, what has changed?" I might add that I'm on the council of APIA; I'm chairman of the fiscal committee, so I do follow this intimately.

What has changed since this came along? From a small company's perspective nothing has changed. There has been a lot of paperwork, a lot of time, and for a company our size it's almost debilitating just trying to keep up with it. I'm not saying it's a bad thing but I think there are a number of strategic initiatives that we have got wrong. What we are experiencing is ongoing extensions. The process seems to be unbearably sluggish and I guess for a company our size to be able to follow what is happening on a month-to-month basis is very, very difficult; it takes a lot of resources. I think I am repeating myself there.

To talk of a WA focus, you can characterise the Western Australian gas market as being very thin and narrow; that is, it has few suppliers and few customers. It has few big suppliers and a few big customers, and a plethora of smaller ones. The

market is around 750 terajoules a day, and 550 of that is exempt at the supplier end. It's exempt because of a technicality I still can't grasp. It has also delivered up to us a deregulation timetable which I would say is entirely politically and treasury-driven convenient, and I am talking about the domestic market. Companies like us would have loved to have been selling into that market for a long time, and we can't get there until 2002.

If you step back from that, what are the barriers to entry for a company like us getting there in 2002 when finally we get the green flag to go there. The barriers into entry are you've got an established company that has been operating for 20 years. It has got new ownership and they have got another two years to get their pencil as sharp as they possibly can, and then we've got to come in with a fresh page and try and penetrate that market. We still don't know what the rules are to even consider how we penetrate that market, and this comes back to the commentary I make about how sluggish the process has been. We don't know what the game rules are to get there and it's only a year away. It's almost an impossible ask. So I look at the big picture and say, "What has it delivered to us?" Well, we've got one of our biggest competitors able to go after our markets and we can't get after their markets for another year still. We've got one of the biggest suppliers of gas in the state exempt on a technicality.

I take serious objection to the comments made in the last presentation in respect of there is monopoly at the supplier's end. Gas markets in Western Australia over the last four years have been quite volatile, and there has been a lot of downward pressure on price. It is commented by many that the price has come down by 30 per cent and it aggravates me that government are taking the credit for that decrease in price because of this legislation and because of other initiatives they've made. It has happened for no other reason - no other reason than there has been competition in the supply end of gas. The tariffs haven't moved. The tariffs are static. The only demonstrable monopoly in the supply of gas to Western Australia is in the pipeline end. So the previous commentator's fact that there are monopolies at the suppliers' end and the transporters are getting squeezed is just not a fact.

I suppose I would add to that, that let's delve into what that means in terms of who's in the supply chain of energy to Western Australia. In our business, in the upstream supply business, we've got a range of risks that pipeline owners and builders would not be able to contemplate. We've got to get the acreage in the first place, which is a competitive process. We operate in an offshore environment. It's a hostile environment; more cyclones than anywhere else in Australia. We've then got to go and explore for it and find it. We have all of those risks. If we're lucky enough to find it, then we're a player in this market.

We've then got to develop it. We've got to get hundreds of tonnes of steel out to the ocean, build it and maintain it. Once we build it and get it out there we don't know whether it is going to work. Sometimes they don't. We have then got to win markets and, as I have just described, we're trying to go after markets where the

playing ground is not level because of what I would argue is convenient political process - convenient political decisions - and what I am specifically referring to there is the sales timetable for Alinta gas into the domestic market The tariff for delivered gas into south-west markets is one-third of the delivery price, so it's unreasonable to say that the tariff and the transport and the pipeline owners are the ones that are copping this in the neck. It's just not true.

Then I move on to the other element of this, which is really the previous commentary - and, make no mistake, I have no axe to grind with Epic. I in fact am very sympathetic to a lot of the comments that they made but we do need to set the record straight here to get the entire gas market into perspective. Epic got wound into the gas markets in Western Australia certainly out of what I would say is government/treasury driven policy. They bought a monopoly and, in my opinion, they paid for a monopoly. They have mentioned it is causing them a lot of grief and I am sympathetic to that - I think it is causing them a lot of grief - but, quite frankly, if we were to step back from this and say, "How are we going to get cheap energy to Western Australia?" the answer is not, "Sell an asset as a monopoly, price it as a monopoly, and then try and beat them up over regulatory policy."

The answer is to encourage someone else to come along and build another one and then let them go head to head in the commercial environment where they can work their tariffs out amongst themselves and the cheaper one will get the load. We have a situation now where there are severe barriers to entry in Western Australia. I can't comment on the eastern states because I haven't got enough time to look after what we've got, but the barriers to entry to get an alternate transporter of gas on the main arteries in Western Australia are significant and I suspect will never be overcome. Epic made the comment in the last presentation that they are enhancing at capacity, not in advance of capacity, which means that no-one will ever be able to get around them.

If someone has a load, let's say a start-up load for a new build, Epic will always be - and it doesn't matter whether it's Epic. I don't mean to pick on Epic. It could be XYZ company, I don't care who owns it - in this case it is Epic that owns it. But they're always going to just loop and compress another hundred kilometres, and they'll do that for a hundred million bucks versus a billion dollars to build a new one. Now, it will be a big decision for anyone to go and build a new pipeline, and in my opinion it will never happen.

The barriers to entry at the domestic level I think are equally robust. How is someone like Tap Oil or the Harriet joint venture going to get past 20 years' experience, an existing billing system, an existing customer base? It's a bit like Telstra and One.Tel. It's going to be inordinately difficult. I think the likelihood of twinning the DBNG pipeline is about one per cent. What has happened with that particular event is that the whole issue I think has been highly politicised rather than strategised. The sale of the DBNG was to deliver funds to the WA Treasury, and to me that is a wrong initiative for something as important as energy supply to a

country. I think the competition payments by the federal government to seduce the state governments to take on their mandates is also an unhealthy situation. It comes back to public interest versus political outcomes, dollars to Treasury.

I think I'd then make an overall statement that Australia seems to be obsessed with process and regulation, and this is consistent with what Epic was saying, rather than incentivising investment. The way to achieve a cheap product - and it doesn't matter whether you're talking about airline products, telephone products or energy - it to get competition into the market, and that is we need to widen and deepen the market. What Epic have just told us is that they're reconsidering their investments in Australia. They're saying it's too hard. They're saying the regulatory risk is a disincentive of proportions where they're thinking about going elsewhere, and I agree with that.

In Australia we should start concentrating on how we encourage investment because it's a circular argument. If you can get someone to build another pipeline, the tariff will come down, there will be more customers build new projects off the end of it, and the whole process will be circular. If we make the investment experience a good experience in Australia, rather than putting people through the wringer, clearly like Epic has been, then they won't come back and put more dollars here.

In my submission we addressed ring fencing. The ring fencing that was proposed in the legislation I just do not understand for a second. I think it's entirely naive to think that if you transfer an asset out of one entity into another with the same owners that you're going to have any different investment decisions, any different strategies. The owners are the owners, and all you're doing is causing everyone a lot of tax problems, a lot of administrative problems and it's not going to change any outcomes at all.

In summary, in WA we are exposed to the national access code. In my view, the world hasn't changed. We still have monopolies. It's a 99 per cent chance we'll have monopolies into the future. We've got more paperwork, more regulation to deal with, and energy prices have only come down because the suppliers have been going head to head - no other reason. Western Australia is not the east coast. We don't have a connected gas market. We have specific dynamics in the Western Australian market. West Australia is the biggest state with the biggest delivery problems and the smallest market. The United States templates that everyone seems to be obsessed with going after is also dealing with an entirely different market dynamic.

I also agree with the comments with respect to accelerated depreciation. This is another classic example of us disincentivising investment in this country. What I would add here is that I don't think it's good enough for Australia just to be as competitive as the next country. Ireland worked this out recently. Ireland, until a few years ago, was the basket case of Europe. They realised that their tax fiscal regimes weren't competitive, that they were the same as everyone else's and no-one

went there. They fixed that, and now it's the fastest growing economy in Europe. It's not good enough for Australia to sit back and say, "Well, we're as good as the US on regulations and fiscal regimes," because we ain't the US, and the sooner we realise that, the more likely we will be of growing our industry.

I guess in summary I would say that we need to stop being obsessed with regulation and process, and we need to consider how we encourage more investment to deliver the competitive outcomes that will inevitably come with more investment. That's all I've got to say.

MR BANKS: Good. Thank you. Perhaps just to clarify it for us, where you talked about the biggest supplier to the market being exempt on a technicality, is this where you're talking about the North West Shelf gas situation? Could you just elaborate a little bit on that, please.

MR UNDERWOOD: Sure. The North West Shelf joint venture source their gas from the Rankine platform system, and they take it to the Burrup Peninsula as raw unprocessed gas. 550 terajoules a day of that goes into the domestic market. Because the gas is not processed offshore, under the code it is defined as gas that is exempt from the code. In our situation we process the gas on an island offshore and send it onshore as processed gas, and hence ours can be captured under the code, North West Shelf's can never be.

And I'd point out that until my joint venture got involved in the market, gas prices didn't move. We're the only people that brought competition to the market, and yet the supplier that's been there as a price giver for 15 years is exempt. Now, to me it's just a classic example of how a national blanket solution is just perversely almost humorous in the West Australian scenario. But that was it, and we made applications under that, pointing it out to the legislators, but people wanted to treat it like a big sausage machine, they didn't want to differentiate in the legislation, and it didn't happen and that's the outcome.

MR BANKS: Is your concern about the gas code more to do with the fact that it's what you describe as a one-size-fits-all, a sort of a national regime, or are you against having any access regime at all in relation to gas transportation in WA?

MR UNDERWOOD: In WA the answer is no. Let me amplify my answer. We didn't have a problem in WA, but the problem which will become more and more important is - one issue - that the two main artery pipelines are monopolies. That's the WA problem in a nutshell. Other than that, we don't have a problem. So I would argue that really the answer to all of this would have been what - perversely so - now seems to be being contemplated in terms of the Darwin to Moomba pipeline, to differentiate that event and treat it exclusively. Now, I'm not up to speed with what's happening there, but that's the sense I get. That just makes a mockery of this national blanket straightaway again. To me the answer would have been to deal with Queensland and see what happened elsewhere. In summary, I don't think we needed

this legislation at all.

MR BANKS: You say the only thing about the situation in WA is the two main arteries are monopolies. So how do you deal with that?

MR UNDERWOOD: Well, they should have been dealt with under the ACCC or the Trade Practices Act.

MR BANKS: Under Part IV?

MR UNDERWOOD: My lawyer is not here so - forgive me - I'm not sure what part, but Queensland was dealt with with this legislation because there was commentary out of Canberra that the TPA couldn't deal with the Queensland problem, and now we've got a list and, quite frankly, with respect, I think there's a lot of really smart people with totally the right mind-set trying to get the right solution, trying to make this thing work, but with respect I just think it's a dog's breakfast. You know, we're now trying to make this national blanket work, and I'm not seeing it work.

MR BANKS: You are both a producer and a pipeline owner.

MR UNDERWOOD: Yes.

MR BANKS: You have an interest in both. From which perspective do you see it being most problematic?

MR UNDERWOOD: Well, the fact that my pipeline is going to be included under an access code I think is just obscene, and I say that from an economic point of view. I pointed out the risks to you that we have to overcome to get our gas to market, if we can find a market. To go through all of that and then someone come in and tell me that we're going to take a seven per cent return is unbelievable, and to me, in our original submissions and all the way along, suppliers' pipelines should never have been in this. Where the issue is is the main artery pipelines.

Like I say, one third of the delivered price of gas in WA is transport - not my transport, my company's transport. They get that in the gas price. We sell gas at CS1, which is the entry point to the DBNG, so really the issue is that the artery pipelines are a monopoly. They're the ones that needed to be dealt with. The rest of it is - well, imagine how we feel. We're captured under the code, and 550 of a 750 terajoule a day market is exempt. It's of Monty Python proportions, really.

MR COSGROVE: When you referred to your lack of knowledge of the rules of the game, what are those rules that you would like to see put in place?

MR UNDERWOOD: You'll have to help me more with that question.

MR COSGROVE: Well, I'm not sure that I can. I wondered whether you were referring to the arrangements under which Alinta gas is to be sold or - - -

MR UNDERWOOD: Of the domestic market, yes. I understand the question now. We don't know what the cost of access to the reticulation system will be, so how can we build a business model on trying to capture market share if we don't know what those rules are. We've got one year to go and we're starting a business from scratch against a company that's been in it 20 years, just been recapitalised and has got an American owner who's been doing it for 40 years in the United States, and we're going to have to start from scratch to go head to head with them, and yet we're a year away from 2002 domestic market deregulation and we for our business model don't know what the rules are to access that market. We don't know what the tariff is going to be, we don't know how we get into the system. The determination hasn't been made - was my understanding.

MR COSGROVE: So you need some sort of access arrangement in that part of the market, if I'm understanding you correctly.

MR UNDERWOOD: Yes. Well, Alinta owns all of the reticulation system. It's a bit like Telstra owning all the telephone lines and Optus coming in.

MR COSGROVE: Yes.

MR UNDERWOOD: Now, for us to be able to go to anyone in this room and say, "Look, we'd like to sell gas for your hot water system," we need to build a business model for that. We don't know what the rules for accessing that market are going to be, we don't know what the tariff is going to be, we don't know how much we can put in - all of that, because basically Alinta have a monopoly on it right now, and the part that really upsets me about that is that that's a market we can't go near and yet it is a very lucrative market. There is more return in the domestic market in terms of dollar back per gigajoule of gas by a quantum of four or five hundred per cent on what we get from our market, which we can't access, and yet Alinta have been given full access to all of our customers from day one. And yet there's this, "You can't go there until we're ready. We need another couple of years to get ready so that we can really humble you," and that's not competition, it's misguided and - - -

MR COSGROVE: So don't you have an interest in adequate access arrangements in that, I assume, distribution part of the market?

MR UNDERWOOD: Well, we do, we do, and I think it should have been dealt with under - I mean, the big picture - I don't understand how it couldn't have been dealt with - - -

MR COSGROVE: Isn't that covered under the gas code?

MR UNDERWOOD: The domestic reticulation?

MR COSGROVE: Yes.

MR UNDERWOOD: Yes. I mean, look, the big picture is, I would have thought this could have been dealt with on a case-by-case basis, as Queensland should have, but now we've got this national blanket there are anomalies in it, and how are you going to deal with all of those different localised issues. That's what everyone is struggling with. To me, yes, I think it's appropriately pointed out that what is relevant in the WA context is the two main monopoly artery pipelines and access to the domestic reticulation. We've been kicked out of contracts with one because the government said, "No, that's Alinta's. You can't have access to that lateral," so we've had to tear up the contract and Alinta just rolls straight in there. I can give you more detail than that but - I can't, but - - -

MR COSGROVE: Do you have any right of appeal against those sorts of decisions under the gas code?

MR UNDERWOOD: The code's the code. The minister's directive is the minister's directive.

MR COSGROVE: That's true also in terms of the national regime, as we've seen in the case of the eastern gas pipeline. A ministerial decision on the basis of an NCC recommendation was overturned by the competition tribunal. Is that not an avenue available under the gas code also?

MR UNDERWOOD: I guess it probably got to a point of futility. I mean, the past government had an agenda, which was to maximise the exit price from some government assets, and they did a very good job of that. If you're going to get in the road of a government agenda for the sake or four or five terajoules a day, you're a fool - I'm talking about myself.

MR COSGROVE: So what's your view of the role of ministers in the process?

MR UNDERWOOD: Contrary to the previous presentation, I think it's just fraught with danger when you get ministers with political agendas impacting on matters of national strategy towards the supply of energy. This is one of the most important things this country has got to confront, and we've seen political decisions - because someone's electorate is screaming doesn't mean to say it's good for national strategy.

MR COSGROVE: And in the case of your operations as a gas producer, would you again be happy to leave the question of coverage in the hands of a regulator as distinct from a government minister?

MR UNDERWOOD: Look, I suppose my perhaps naive view of the world is that what we're dealing with here is matters of energy supply to a nation on a 50-year time scale. That deserves a national strategy government department to come up

with the right answers. If you look at the way we're going about it, we've got 12 different government departments going in 12 different directions with 12 different agendas, and at the end of the day we're going to end up with a camel when we wanted a horse.

MR BANKS: Or several camels, because weren't you saying that you actually preferred a case-by-case, jurisdiction-by-jurisdiction approach to this matter?

MR UNDERWOOD: I think I would admit that that is a parochial comment because I don't know what's happening on the other side of Australia. I do know what's happening here, and it's just demonstrably clumsy, clunky and not delivering the answers that it was intended to do. But I suppose what I'm saying is let's view this as a country, intelligently and when something gets too hard, don't just throw a blanket across the whole country. I think we're a bit smarter than that, but that's what we've done, and the blanket doesn't work. We all know, base case, the blanket doesn't work, and we're all trying to find ways of - say, "Well, we'll tear the blanket away from that corner of the country and we'll put something different in there." Well, if that was what we were going to do, why didn't we do that in the first place?

MR BANKS: Is a big part of your concern the way in which this blanket, as you call it, is sort of catching or covering new investments that are high risk? We talked earlier about them generally being inherently contestable in the pipeline area. Is that your concern, that really it's picking up facilities that shouldn't be picked up?

MR UNDERWOOD: Yes. The fact that we've got to go and jump over all of those risks that I listed out for you and then at five minutes to midnight another company comes along and says, "Well, thanks for building all that and, by the way, we'd like to have access to your pipeline," when in two years' time, three years' time, we might find another gas field that we want to get down but can't, because our own gas pipeline is full of someone else's gas - - -

MR BANKS: Yes.

MR UNDERWOOD: When you explore the upstream particular dynamics of this, it becomes ridiculous, and if you have a look behind this legislation in terms of its practical application to upstream businesses, as we've put in our submission, it is demonstrably silly, but I support that in the main arterial pipelines because they are monopolies.

MR BANKS: Yes. So in a sense there's not a great difference between us in that we argue in the position paper that it should apply where market power is a problem and it shouldn't apply where it's not, and you're making the same point from your perspective.

MR UNDERWOOD: Yes, I think that's a fair conclusion.

MR BANKS: All right, thank you very much for that. We appreciate it. You indicated, I think, that you may have had other material that you were going to send to us, but is that correct or not?

MR UNDERWOOD: No, we didn't get a submission prepared.

MR BANKS: All right. Can we treat this as your submission then?

MR UNDERWOOD: You can do.

MR BANKS: Okay. Thank you very much.

MR UNDERWOOD: Pleasure.

MR BANKS: We'll break now, and we're going to resume at 2 o'clock.

(Luncheon adjournment)

MR BANKS: Our next participants are from the WA government. Welcome to the hearings. Please, could you give your names and the capacities in which you are here today.

MS NOLAN: Thank you, Gary. My name is Anne Nolan. I'm the executive director of the WA Treasury.

MR CROOKE: I am Matthew Crooke, the acting assistant director of utilities, policy branch, in WA Treasury.

MR FARRANT: I'm Les Farrant. I'm the coordinator of energy in WA and head of the Office of Energy.

MR BANKS: Thank you very much. We really appreciate you participating in these hearings. We've also received a submission from you on the position paper and thank you also for the earlier submission you provided in the first part of the process which we found very helpful. So, as discussed, perhaps I will let you provide an overview of your main comments and then we can find some areas to talk about.

MS NOLAN: Thank you, Gary. We're here on behalf of the WA government but in our own capacity from the various agencies from which we have coordinated a whole of government response to your issues papers and the submissions that we have forwarded to you, sir. We're here as Treasury and Office of Energy representatives and I believe that would be consistent with the WA government's position.

MR BANKS: Thank you for that.

MS NOLAN: So thank you again for the opportunity to provide some input into this review. We welcome the opportunity and we think it's a very opportune time to review the access arrangements as they apply. We believe they are genuinely very important to the Western Australian economy in terms of ensuring that we have the very effective access arrangements and we have the right sorts of processes that surround those. As you would appreciate, the Western Australian economy is very much an export orientated economy and international competitiveness is essential to the ongoing success and standard of living of all Western Australians.

So we certainly believe in the role that access arrangements have to play in our economy and the opportunity for some finetuning in those arrangements is very much welcomed, and we do believe it is in the environment of finetuning rather than wholesale change to those arrangements, as you would have seen from our submission and our rejoinder submission. As we've mentioned, we believe that this was an ideal opportunity to clarify the application of the access arrangements, perhaps look at some of the linkages between the alternative paths available to the participants in terms of both those seeking access and those who are the owners of the infrastructure themselves; obviously an environment where we are trying to ensure continued investment certainty and removal of uncertainty always goes a long

way to making for better arrangements.

Finally, there is very much that difficult balancing act that goes on in any regulatory environment to ensure both the interests of the infrastructure, potential new people in the industry are given a sort of balanced approach - sorry, I will say that again - that we look at the balancing of their relative interest in such arrangements. So that balancing of interest is always the interesting one. How things turn out obviously depends on people's different perspectives but we do think that is the very essential nature of these access arrangements.

So just clarifying what Treasury's role is, by obvious implication we're not an owner of major utility and certainly we're not in terms of an independent regulator - our involvement is more from the policy front, as is the Office of Energy's. So our interest is very much policy perspective, in terms of ensuring there are the right sorts of frameworks for access arrangements operating in Western Australia. I will probably also commence by noting that our government is a new government and has made a number of statements with respect to the regulatory environment in terms of the potential to establish an independent economic regulator and we would see that independent regulator having responsibility in the electricity, gas, rail and water industries, and obviously - well, not obviously but would include regulating for third party access in those industries, particularly electricity, gas and rail services.

So that in terms of the potential future direction for the bureaucratic environment which we all see ourselves in - this government also came to power on the desire to look at the electricity industry from a fresh perspective and to appoint an independent electricity reform taskforce, and some of the roles of that taskforce will be to look at the reform and regulation of the industry, the electricity industry, including potential for structural reform of Western Power, wholesale market design issues as well as looking at potentially an industry code. So that gives you an idea of where some of the current thinking is happening in the WA government.

But more specifically, turning to the access arrangements themselves, there are a couple of key points that I would like to draw out that I think are important to the Western Australian government. One of those is the importance of clause 6 in terms of the general principles for access regulation. We believe that they're a fundamental part of the environment that has seen the development of access regimes in Australia and we believe there's a fundamental role, continuing role, for clause 6. The second part of that is the question of the continuing role of the states and territories in access regulation. We believe that constitutionally the responsibility for industry regulation lies with the states and access is obviously an integral part of industry regulation, and therefore the role of the states we don't think can be dismissed lightly, in terms of access arrangements or regulatory arrangements in general.

I also believe this was a fundamental aspect of the intergovernmental agreement that saw the establishment of access regimes in competition policy principles more generally. So I think that role of the state then - as it pertains to the role of ministers - can't be dismissed lightly and needs to be given a lot of consideration and thought. I think in keeping with that we would see the primacy of

the industry specific regulation and access regimes as enacted by parliaments as having a fundamental role to play into the future and we will address that in a little bit more detail later through Matthew.

I would again emphasise that this role of the state in access arrangements we believe is fundamental. Particularly they have a number of advantages, we believe, over more generic arrangements and we will come back to those in more detail but thank you for the opportunity to make some general introductory statements and I will leave it at that.

MR BANKS: Good, thank you. Would you like to make any further comment now, any of you, or should we - - -

MR CROOKE: Yes, I had some comments in order to summarise the submissions for you and just to point to what we saw as the major issues.

MR BANKS: All right, I think that might be a good way to proceed, yes.

MR CROOKE: So that shouldn't take too long.

MR BANKS: No, that's fine, go ahead.

MR CROOKE: Thank you, chairman. As Anne just mentioned, we believe that the access framework is generally sound but there are inevitably some improvements that could be made to it and I think the commission has done an excellent job in identifying what those might be and so I think it's fair enough to say we are generally in favour of the proposals which, I think, are a fintetuning of the current framework but we're sort of less agreeable to some of the philosophical changes in approach to access regulation and what you might call the higher level framework issues.

Most notably, as Anne outlined before, we actually see clause 6 as being the origin of access regulation. It basically refers to state and territory regimes in clause 6.2 and I think refers to the Commonwealth's access regime enacted under Part IIIA as its own sort of entity and it always saw the continuing role of industry specific or, if you like, state based regulation alongside the administrative path to access that Part IIIA provides. We see the possibility of clarifying clause 6, perhaps strengthening that sort of framework role, but are not terribly attracted by proposals to make Part IIIA somehow the model for national access regulation. Rather we would see Part IIIA as being one part of the national access regime.

Our first submission, which I will only skip through fairly quickly because it's obviously on the public record, noted the importance of access regulation to the Western Australian economy. It, I guess, asserted a primacy for industry-specific regimes and that's something which, I think, has also been picked up on by a number of other participants and the Network Economics Consulting Group, the CCI of WA, I think the Australian Gas Association and South Australia and New South Wales governments all seem to take that view that there is something about industry-specific access regimes that is desirable in terms of the increased clarity and

prescription, and that's also a view which we would agree with.

That said, we see it as desirable to limit the spread of access regulation. It is not something that's designed to be used in all situations and fundamentally I think the approach taken in the position paper has got that right but, in terms of state based or industry-specific regimes, the accountability rests with the parliament or ministers as in what situations access should be a mechanism. Where it applies as a regulatory tool, we believe that independence in regulation is important and so the actual application of the rules is a separable question. The balancing of interests that Anne referred to before is something that seems by its design to require a degree of discretion on the part of the regulator but we're in favour of, I guess, tightening some of the criteria which are applied in that environment. We don't see there being any sort of fundamental problems with the criteria as they stand. It's more when you get down to the pricing principles and that sort of thing - irregularity, balancing of interests.

The first submission focused on the national gas access code and Western Australia's rail access regime as a working model, if you like, of our experience with access regulation. For the rail access regime we noted some difficulties in gaining certification for the rail access regime because there were some obvious issues there as to how uniform the arrangements might be when they are ultimately crossing state borders and that led to a suggestion that interim certification could be a possible means of dealing with that uncertainty. I just note that again because it doesn't appear to have made its way into a recommendation by the commission, although I understand the position paper looked upon it with some favour.

In terms of gas, and that's where I think we've got the most experience, we really view the gas code as a good working model of access regulation. It's been referred to by a number of other participants as providing a pretty good basis for looking at this whole question of access and I believe that it is a very good model for demonstrating how industry-specific access regimes can work, how they can bring on all the participants in an inclusive fashion in the design of an access regime and hopefully promote a better working model.

The key suggestions in our first submission, and I must admit it wasn't terribly focused - at that time in the process it was a bit hard to grapple with all of the issues - but it called for greater recognition for industry-specific regimes within the national access regime. It suggested that perhaps a single body might be appropriate at the Commonwealth level rather than suggesting a single access regulator for all access regimes and it argued in favour of maintaining ministerial responsibilities. That's something I will pick up on again shortly.

So moving to our second submission which was in response to the Productivity Commission's position paper, the focus of our second submission was more on those issues with which we had some concerns. We considered the position paper to be an extremely positive addition to the debate and really helped us focus our minds on what's left to have a look at. To boil it down, I think the key areas that we perhaps have some disagreement with the approach taken in the position paper is all about

what should Part IIIA be in the context of the national access regime as opposed to what can clause 6 do further clarify the situations in which you might move along with various paths to access and, if you like, rank those in order of some form of hierarchy such that you might have the industry-specific regime sitting at the top because of the fact that they have been legislated by parliaments, the fact that they are more prescriptive and have their own processes and basically moving down the various other parts - but I will outline that a little later.

I don't believe that the national access regime should be bound by Part IIIA because the circumstances in which of the various paths is meant to apply can be quite different and looking at the industry's specific regimes as one example, then I think we need to cater for some differences. They need to be much more focused whereas the administrative path to access via Part IIIA needs to be perhaps designed more broadly as both a threat to move to those more specific regimes and as a last resort for gaining access when nothing else has worked.

I would also perhaps suggest that there are certain policy synergies between regulating access and regulating industries - and made that point before. Basically the states have a role in access because they have a role in regulating industries. We see the two as being very complementary and basically the electricity reform process that was outlined before is sort of a working model of that, if you like - the need to consider these issues at the same time.

On the role of ministers, Western Australia supported retaining the role of ministers because this allows a separation of two important questions - firstly what the law applies to and, as I mentioned before, we believe that either parliament or ministers - if that's how the legislation is designed - have a role in determining situations in which the law may apply and that is quite separate from the question of how the law applies, which is, as I outlined before, a job for an independent regulator.

It is consistent with the other roles of government or ministers in determining how industries are regulated; for example, in determining access thresholds or contestability timetables or design of markets and provisions governing market conduct and those sorts of things. I see the coverage question as one that needs to be assigned to ministers because of their accountabilities and the regulatory issue obviously needs to be removed from political influences. I would also perhaps suggest that there might be, although I am no specialist in this area, some administrative law reasons for maintaining that sort of separation, in keeping the roles separate and in not having regulators determine the situations in which they will regulate.

I also believe - and a second submission I think suggested this - perhaps it might have been something we are silent on, but symmetrical appeal mechanisms are also appropriate. I think there is a suggestion that basically you could remove the right of appeal in certain circumstances, such as where a minister decides in favour of declaration that may not be in accordance with due process of natural justice.

That said, we would, where ministerial decision-making is retained in the national access regime, support stronger time frames for decision-making in that part of the process to determine coverage, but we wouldn't see the merit in automatic declaration - perhaps because that could lead to some difficulties down the track for failure to engage in due process and subsequent possibility of appeal. The position paper also made a recommendation regarding the certification of Commonwealth access regimes. Our submission saw that as perhaps inconsistent with the practice applying in the states and territories, where certification is a voluntary step and suggested a possible alternative where perhaps the Commonwealth might consider not ruling out declaration within its industry-specific regimes were it not to actually test that question of effectiveness.

The implications of mandatory certification might need to be considered as well. Without exploring it too far it appeared that it might lead to uncertainty having some impact over the legal applicability of a regime even after that has been passed by a parliament. Requiring the Commonwealth to have its regime certified might in fact sort of lead to some difficulties in applying the regime during that period.

I think it is fair to say that the focus of the second submission though was more about setting out what we saw as a possible hierarchy of paths to access and that this might be something that a revised competition principles agreement could set out in a little more detail and each jurisdiction would reflect this sort of framework in the relevant statutes. I think noting that Part IIIA has interactions with other regimes is only looking at half of the picture and, if that was the basis upon which the suggestion arose - that Part IIIA could somehow form a model for the rest - I think we need to look a little further and consider in fact what clause 6 has done in establishing the regime. When I use the term "hierarchy" it is in quite a loose sense because it really depends on the perspective from which you view each alternative; for example, while we would see perhaps declaration as being the last resort it has an influence throughout the entire regime by encouraging the enactment of compliant industry-specific regimes.

I would also suggest that there is a need to exercise a degree of caution when considering claims that it is appropriate to somehow make consistent or uniform the principles that apply in each case; for example, there is a suggestion that the same principles might be applied for declaration, for undertakings and for certification, and I understood that to mean so that they might all only apply in the same situations. I would in fact suggest that it is necessary to differentiate the situations in which part might apply with declaration being the broadest possible application, although the hardest test to meet, such that it is a more general regime capable of applying to a number of different circumstances with general pricing principles, but which can only be used as a last resort, and applying to those core services that have been identified as worthy of being regulated in that way - namely, natural monopolies - and distinguishing that against the industry-specific regimes which might well be much more prescriptive in terms of policy objectives and pricing principles and matters to which a regulator might have regard in making determinations.

Just to quickly run through that possible hierarchy that we saw: the certified

industry-specific regimes sit at the top of that. The basis for our saying that is clause 6(2), which says that the Commonwealth regime is not intended to replace the state or territory regimes; also, because of the way that the regime is currently designed, whereby certification rules out other paths to access, we see that as fairly sort of strong evidence of the primacy of industry-specific regimes, whether they be Commonwealth or state regimes, and the need to rule out other paths to access where they have in fact been legislated by parliaments. These regimes would require robust coverage and revocation procedures, and that is where the focus ought to be. We have argued previously that ministers have a role in that regard.

Sitting under that, and recognising that the certification process is a voluntary one, we would see non-certified industry-specific regimes as having a place. Basically that would recognise that it may not always be cost-effective or necessary to formally apply for certification, although a parliament may decide that access regulation is warranted. If a competing application such as a declaration or undertaking is received, then a process needs to commence to question the effectiveness of that regime. This would provide protection from deficient regimes, because the alternative paths are left open until that question of effectiveness is resolved in the positive.

Underneath that we would see access undertakings and industry access codes under Part IIIA as having their place. The voluntary nature and the greater detail associated with these regimes makes them preferable to declaration. We consider that they are perhaps better able to deal with the multipoint nature of many network services as opposed to a declaration. We also believe quite strongly that they need to be ruled out as alternative undertakings ought to be ruled out if there is an effective industry-specific regime in place to cover the services or facilities in question.

We argued in our submissions for an amendment to Part IIIA to foreclose that possibility. We note that the position paper takes a contrary view and suggests that in fact industry-specific regimes ought to be amended. While that might be possible I think the practicalities are such that, say, if we take the gas code as an example versus Part IIIA, securing an amendment to Part IIIA would be a simpler process and a more certain outcome. Given if there were some conflict between state and Commonwealth legislation, the Commonwealth legislation should prevail.

Finally, that leaves the declaration or the threat of declaration at the bottom of the hierarchy, but it flows through as an influence over the whole regime. As an administrative path to access it provides an important discipline on the design of the above arrangements, and we generally agreed with the proposition that although it sits at that point you might at a later stage be able to move up the hierarchy and therefore, for example, to an undertaking once the service has been declared. I think I have probably gone on for long enough on those issues, but will give Les the opportunity to make some comments if he would like.

MR BANKS: Good, thank you.

MR FARRANT: The introduction said that the Office of Energy was in the policy

area, and indeed it is, but it is also in the practitioner area of this business of access regulation and infrastructure regulation generally. I have been involved with the evolution of the gas code, the interaction with industry about the code and the amendments thereto, and currently expecting to run the electricity reform task force in the state to determine exactly what structural changes ought to happen in electricity and exactly what regulatory environment ought to be set up - also currently effectively a pseudo-regulator for electricity access in this state, where we have a regime under law which is not an effective access regime - never been submitted for that test, but which is the state's current position while it owns the Electricity Corporation.

While that may change, given the flagging of an independent economic regulator for this state fully intended to regulate electricity access, there are no rules yet for how that will happen. One of the tasks for the electricity reform task force here will be to devise those rules, and we would like to do that in the context of whatever the commission's view of life is that the state can live with as a result.

There was also mention earlier in the day of gas deregulation being scheduled for July 2002 in this state - that's full retail contestability. Another element of practitioner here - is that we are organising a steering group with players in the industry to devise the mechanisms to reach full retail contestability at that date, which is a considerable challenge. With that background, I'm happy for the other panellists to take questions or discuss issues.

MR BANKS: Good. Okay, thank you very much. You have covered a fair bit of ground and we will probably backtrack a bit and just explore some of the points with you. I guess it might be appropriate for me to just mention again that in preparing this report we tried to advance things quite a bit in terms of the timing, because we had an inquiry into telecommunications competition regulation which had a three-month head start on us, so we saw a great advantage in synchronising the draft reports for the two inquiries, even though we were three months behind. That led to producing a position paper rather than a draft report. It also led us to provide two tiers of proposals I guess, the second tier being the ones that we recognised were perhaps more substantial in terms of their impacts on the regime, and it was unclear to us whether, on balance, the benefits would be worth the costs or indeed, you know, what the costs might be.

Therefore we're very grateful to you for the submission, because I think it helps us assess in particular a number of the tier 2 recommendations, although there's a couple of tier 1 recommendations that you comment on as well. So I just thought I would put it in that context. But perhaps coming back to your general point that taken over the tier 1 and tier 2 you say, I think on the first page of your submission, that a number of the related proposals would, and I quote you:

> ... fundamentally alter the design of the national access regime and its associated checks and balances.

We can go through and explore some of that. You then give four points there,

under that, to illustrate that. I just wonder whether I might invite you to think about how you might rank those points that you've made. I mean, one picks up the objects clause, a second one talks about moving the principles into Part III as in clause 6, and you obviously think that's very important, the question of ministerial decision-making, and the fourth one is the single regulator.

I should say that where we talked about the single regulator in our position paper we were thinking of that for the purposes of IIIA rather than for the purposes of all the regimes, so we weren't envisaging that a single regulator would suddenly assume responsibility for the industry-based regimes necessarily as well, but you were aware - - -

MS NOLAN: Thank you for that clarification. We thought that could be misinterpreted and hence our - - -

MR BANKS: Right. It has been interpreted that way by others so I thought I had better just clarify that. But if we come back to that point, I don't know whether you would like to make any comments on that in terms of the weighting that you attach to some of those components.

MR CROOKE: Yes, thanks, chairman. We actually probably couldn't do that because we've really approached this on a bit more of a wholesome basis. They all seem to be related in terms of, I guess, shifting the balance away from the Commonwealth and state and territories agreement under clause 6 to enact regimes that complied with a certain set of principles and I guess some of the points might be subsidiary to that, but, yes, they were generally sort of framework questions that we considered were of equal merit.

MR BANKS: Okay.

MS NOLAN: They're not alternatives or a ranking scenario. We saw it as part of a whole that looked at how you would actually go about designing the national access regime and its various parts.

MR BANKS: Yes. I think in terms of your point about the hierarchy - I mean I wondered whether our suggestions for the objects clause in relation to Part III would have been problematic for you.

MR CROOKE: In the sense only that Part IIIA was somehow going to become a framework for the rest of the other access regimes. Something like that, in our view, might perhaps be more appropriately addressed through clause 6, although Part IIIA may well have its own objects clause. That's I think a matter for the Commonwealth, but our view is that Part IIIA is that last resort path to access, and so perhaps the objects clause could reflect that, whereas the object of clause 6 I think is to promote consistency, as opposed to uniformity, across access regimes when enacted by parliaments.

MR COSGROVE: You seem to have drawn the conclusion that we plan Part IIIA

as - I will use your word here - a binding framework for the industry-specific regimes. I'm not quite sure that's quite what we had in mind. It was more a question of laying out a general set of guidelines which industry-specific regimes should have regard to and not deviate from unless there are circumstances which make deviation sensible, in which case an industry-specific regime might have some features which are not part of the IIIA framework. Does that piece of information cause any adjustment of your view of the objects clause role?

MR CROOKE: In part, because that's putting up the interpretation that was meant. Perhaps again it's a question of the location of that sort of framework currently that's contained within clause 6 that was negotiated by all involved. Perhaps there's a degree of sensitivity in moving those sorts of framework questions within a Commonwealth statute.

MR BANKS: Just on the question, aside from what's driving what, in terms of the objects clause itself did you have any views or would you like to venture any views as individuals on the way we framed that objects clause? I will give you a page number.

MS NOLAN: I was going to say we would probably have to go back and refresh our memory on that.

MR BANKS: So you're point was more about its location and what role it would have rather than the specifics of how we caste it.

MS NOLAN: And its relationship to clause 6. What role would you see for clause 6 in that sort of environment I think would be a pertinent point to think about as well. I know it's not my point to ask you questions here, but I mean if that was to preclude the existence of clause 6, or they would be seen as sitting side by side, I think there is some issue there that we would probably need to explore.

MR BANKS: Yes, certainly that's an area where our own thinking is perhaps going to advance between the position paper and the final in terms of what's sufficiently important, that it would need to be imported into clause 6 as opposed to letting IIIA do the work. I guess you're arguing to us quite strongly that we perhaps neglected the important role in our federation of clause 6 as the sort of cement that's binding all this together.

MS NOLAN: That may be just a question of your degree of emphasis, or was it a message that was being sent as well, I think was what we were raising, that there's a need to think of it from both perspectives rather than just focusing on the Part IIIA.

MR COSGROVE: In practice what would be the difference between the present arrangement with IIIA and clause 6 separate and the movement of clause 6 principles into Part IIIA? I mean, you would still have capacity for state industry-specific regimes to be established, whether certified or not. Does it boil down essentially to this question of states, or your state at least, wanting to be able to have some degree of control over the content of clause 6?

MS NOLAN: I will make a few general comments, and Matt might want to. I don't think it's a question of the states wanting to control it for the sake of controlling it. I think that sometimes in the intergovernmental arena it's just like a bit of parochialism - you know, states wanting to have their say - but as we see it there is a role for the state in industry regulation or utilities regulation and you can't split that off from access regulation. They go together so closely. So therefore we do see a role for the state and we think it's quite an important role, particularly with respect to intrastate.

We appreciate the difficulties that are involved with respect to interstate, and we would probably have some comments to make about the clause 6 principles in that regard in terms of the detail. As we say it clause 6 was about providing an element of consistency across jurisdictions as well, and that consistency, as Matt said, without uniformity we think was a valuable part of clause 6 and became a basis for assessment by the NCC for certification and the like. So I think that clause 6 has played a strong role in the development of the overall underpinnings of what access arrangements mean to Australians to date. I think in the role for the state in negotiating all of those it can be underestimated, whereas in Part IIIA they would largely be a federal issue, a Commonwealth issue.

Secondly, the issue becomes what sort of framework would you be looking at, as you said, if you were allowed to have state access regimes within that environment, what sorts of principles would you have underpinning those or can they in fact reflect whatever a jurisdiction likes? I don't think that would necessarily be in the national interest itself - so that would be some of my general comments.

MR CROOKE: Beyond that, I would only sort of add that it would provide a greater sense of ownership, if I can put it in such uncertain terms, but it really derives from the shared responsibilities between Commonwealth and the states for regulating various industries. It just seems to me more appropriate to deal with it in that context and to subsume with a Commonwealth statute.

MR BANKS: Okay, coming back to the actual content of that objects clause, if we just looked at it in isolation now as a kind of intellectual exercise, if you like, what do you think about what we've got there under Part A.? This is on Roman numeral XXV - page 25. We talk about the objective as being to enhance overall economic efficiency by promoting efficient use of an investment in the session for structure services.

MR CROOKE: My view is that is an appropriate addition and it could be a valuable one. It is something that could be included both in clause 6 and Part IIIA.

MR BANKS: Okay, good, thanks for that. There is just really a question here of me not probably understanding the point you were making. It was on the bottom of page 4 under the heading Modified Criteria for Declaration and it's the section where you are talking about countervailing market power. I just wondered whether you could just take us through more - - -

MR CROOKE: Sure - I'll just quickly flick to the - perhaps if you could point me to the - - -

MR BANKS: It's just the bottom of page 4, the very last paragraph.

MR CROOKE: I found that in our submission but I was having reference to one of the proposals in your own executive summary, so that might help me as well, if that's okay.

MR BANKS: Okay.

MR CROOKE: Sorry, I've found it. It's on Roman numeral XXVI.

MR BANKS: Yes.

MR CROOKE: This was responding to the tier 2 recommendation and especially the wording of paragraph C. Reading it literally, there was I guess a concern that it was focusing only on downstream markets and we made a simple point that upstream and downstream may be relevant in containing the ability of the owner of a bottleneck facility to actually exercise their market power.

MS NOLAN: I think it was as simple as that point.

MR CROOKE: Sorry, the bottom of page 4?

MR BANKS: Yes.

MR CROOKE: I might be addressing the bottom of page 5. I'm sorry if I have.

MR BANKS: No - unless we have got different pagination. I think page 4 - there was a section headed Modified Criteria for Declaration in your submission.

MR CROOKE: Yes.

MR BANKS: And then at the bottom you say "an increase in competition in downstream markets".

MR CROOKE: Yes, sorry, there seems to different pagination.

MR BANKS: So if we could find that paragraph - "it could reduce the countervailing market power". You are quoting again of each downstream user - "such that the relative market power of the service provider is increased by a new entry". I just wondered what you were trying to do here. Were you trying to contrive an exception to the rule or something? But surely you might get a perverse outcome from enhancing downstream competition but I just - it might be something you could get back to us on.

MR CROOKE: Yes, I will quickly attempt to explain that but we could possibly get back to you as well. It's not so much trying to point out a potential perversity in that sort of general rule; rather, I think it's suggesting that you need to consider more than perhaps a number of competitors but more the nature of competition in the downstream market and perhaps the ability of individual companies to negotiate a fair deal of their own right. It's a bit of a slippery concept and perhaps something I should have again addressed but - - -

MR BANKS: Well, expressed like that I don't have a problem with what you are saying. It might just be the way you've cast it here. Anyway if you have any further thoughts on that at your leisure later, if you wanted to get back to us on that, that would be helpful.

MR CROOKE: Yes.

MR BANKS: Yes, I was going to ask you also, on the next page - I mean, at the end of that same section, if our pages are corresponding, above the heading to do with inserting price increase that was in Part IIIA, it says that WA is concerned about the proposed nexus between IIIA and criteria for coverage under the industry-specific regimes. You don't believe that a direct link is appropriate. You say:

> While the government accepts the desire to limit the application of IIIA to natural monopolies, there may be cases at which jurisdictions intend multiple competing facilities to be covered such as occurs under the gas code.

I just wondered if you could elaborate on that point.

MR CROOKE: Yes. I think the fact that you have pointed to it suggests that there might be some imprecise wording. I didn't necessarily mean multiple competing facilities to mean sort of two substantial pipelines but it was more a general statement that there might be some broader policy reasons for having access apply in a particular set of circumstances. Looking at the gas code and its application in Western Australia, it definitely does apply where there are ostensibly pipelines running next to each other.

I think the gas code is more capable of dealing with the actuality of that in terms of different standards of gas that the pipelines might carry and more able to address the actual sort of extent of competition that a second pipeline actually brings and considering if one supplies only 5 per cent of the market and the other supplies 95 there are appropriate distinctions to make. Differing quality of gas is another issue that the gas code is more capable of addressing than perhaps a criterion which is sort of more focused on duplication.

MR BANKS: Yes, well, again we envisage there could be some differences and, indeed, our own draft report on telecommunications competition regulation contains some telecommunication-specific dimensions to the declaration criteria, so I think if

that is the point you are making I guess we would agree because, in the case of telecommunications you could have a number of facilities but the big issue is to what extent they are really effectively competing or not, given network externalities and so on.

MR COSGROVE: On that same page, perhaps again a point of clarification under the pricing principles section there, you have as your second point a concern if this proposal was suggesting that existing regimes should be subject to a new round of evaluations against the proposed criteria. I don't think that was our intention, but presumably when an existing access arrangement had come to its conclusion date then new principles would apply. Would that be still a concern to you?

MR FARRANT: I suggest it would be a concern to those people who own the infrastructure. I mean, if they were facing an uncertain future in this - the comments that Epic made this morning would ring very true. I think to change something after you have embarked upon a legislated access regime is a serious activity and it's - -

MR COSGROVE: Yes, although I thought that was more a question of the brevity of the initial period of access agreement. I mean, Epic, as I recall, were saying, "We'd really like something longer than five years in the case of an existing pipeline or 10 years in the case of a new one."

MR FARRANT: John, as I understand it, they are saying, "We'd rather like the prices set for 20 years, not just the regime set."

MR COSGROVE: Yes.

MR FARRANT: If you are also going to change the regime five years into a 20-year life of an asset that would be even more serious.

MR BANKS: Maybe the only other point we would make here is that the pricing principles we envisage here are not so prescriptive. I suspect Epic wouldn't be unhappy with the application of these pricing principles at the conclusion of a regime once that regime expired because I don't think - I mean, they're intended to perhaps give a bit more recognition to the incentives to invest and maintain infrastructure than might otherwise occur.

MR FARRANT: To an extent, to say, "Well, if the regime was more attractive they wouldn't mind it applying?"

MR CROOKE: I guess another point on this issue is perhaps it also needs to be considered in the context of our sort of broader model that we're proposing and while these pricing principles might be okay as far as they go we would perhaps only see them applying in the case of declared services and not in fact influencing those which might apply in other situations, such as under the gas code. There are already processes in place to sort of deal with changing the code and perhaps - I'm not sure whether there is a need yet - there might be a need to revisit the code following the conclusion of this review, but I wouldn't see the principles inserted in Part IIIA as

perhaps impacting on the gas code.

MR BANKS: You don't think they, or some variation of them, could be imported into the code itself, or there is no need for that?

MR CROOKE: Depending on what your restrictions sort of agree in terms of potential changes to clause 6, and I realise I am asserting our model over what has been proposed, but I think that is a separate process to be considered in that gas context.

MR BANKS: Yes. I guess all I am raising there again is just the question - I mean, what we are hearing quite a lot was that there was a need for more guidance, that a lot of the delays and uncertainty and prevarication reflected the lack of guidance, that pricing principles, broad pricing principles, would help establish that, so there is a question about again abstracting from the exact location of these to what extent you may see these as being helpful. I don't know whether you have had an opportunity to actually discuss a view or reaction to the principles as stated, as opposed to the question of whether they should be in clause 6 or not.

MR CROOKE: Generally I think we did make the remark in the second submission that in that broader context they actually seemed fine.

MR BANKS: I think I did see that somewhere. I have just lost it.

MR COSGROVE: The last paragraph of that section.

MR BANKS: Okay, yes.

MS NOLAN: There's no particular concerns with the actual proposed pricing principles.

MR BANKS: That is useful feedback anyway, apart from what we know is your main point in relation to it.

MR FARRANT: Mr Chairman, to the extent that those principles are already reflected in the gas code then just putting them in Part IIIA is not necessarily going to change anything in the gas code at all, so it is a question of what do you intend to make different in that set of principles from that which is already legislated for for this particular aspect of the gas industry.

MR BANKS: Yes.

MR FARRANT: It may help in future situations - as I have already anticipated, WA is going to be working on electricity code for this state, as it is somewhat disconnected from the rest of the country's grid, and as a consequence those principles are probably going to be enshrined in that in any event, but if they are in Part IIIA then it really doesn't make a great deal of difference to the process.

MR BANKS: No, other than - I perhaps make the observation that my colleague and I take a very long-term view in these things and you yourselves have said that you see to some extent when things are in play that IIIA can have an effect in terms of - it is the default mechanism, and so I suspect that at times when the industry codes are being reviewed that that would be a consideration, so it's indirect but - therefore we felt that we should try to make IIIA as good as we can make it, in our mind anyway, with the thought of that sort of dynamic influence over time. We have probably seen it more as driving things or described it more as driving things than you're happy with but, ultimately, you see it also as having an influence in a more indirect way.

MS NOLAN: Yes, we would support that comment.

MR BANKS: Okay. You've got a brief section there on the role of ministers - you've talked more about it. It has been one of the areas on which a number of participants have had difficulties. You mentioned there that you see merit, however, in adopting the alternative set of proposals, distinct from the time frames and information requirements. What about the proposal also for a deemed acceptance where those time frames are not complied with or not met, rather than currently it just lapses as a deemed failure or rejection.

MR CROOKE: I briefly touched on that before and perhaps wasn't too precise in what I was saying. If I can just quickly address even the first part of what you said, the basis for agreeing to the sort of stronger time frames and information requirements was perhaps more a recognition that such responsibilities are potentially on ministers anyway in having to afford natural justice and due consideration when making administrative decisions. So in a sense I guess we can easily accept formalising their responsibilities in that regard.

I make that point because I don't believe you can then move to a situation where, by default basically, a decision is made that impacts upon the property rights of the facility owner, recognising that there's a pretty tricky problem there in terms of trying to set meaningful time frames and what to do if in fact a decision isn't made. I think, having a default decision, that something ought to be declared is perhaps fast-tracking the process a bit too much and might give rise to challenges that basically, "That decision is invalid because you didn't consider the criteria; it simply became declared because you failed to do so." There's potentially a bit of a tricky situation there.

MR BANKS: There is provision for review on the merits in the ACT, which presumably would still apply.

MR CROOKE: Yes, perhaps you could then move to that stage and have the ACT consider the matter afresh where a minister had failed to make a decision, rather than saying that, yes, declaration is the case. It's only a small distinction.

MR COSGROVE: I guess that's already a possibility, isn't it, an access seeker in the event of non-declaration could appeal?

MR CROOKE: Yes.

MR FARRANT: One of the items already mentioned is the amount of information available to the decision-maker in these cases, whether it's a minister or even in the regulatory process where a regulator is involved in decision-making, and any deemed outcome is always endangered to the extent that the information isn't provided in an adequate form at the right time for the decision-maker to exercise his right, or is it requirement to make a decision. In the regulatory case it's easy to see a means to solve that, simply by the regulator then having to declare what information it is that he needs and therefore having his decision put off until such time as he gets the information. It's much more difficult to see you doing that in a ministerial position when you're coming to decisions like declarations.

So I think we just need to take on board that any deemed outcome in this needs to be thought about in terms of the information circumstances. If we can figure out a convenient way for information to be dealt with in that then deemed outcomes are easier to accommodate or to stomach, really, because they're a bit - default outcomes in these, where you're talking property rights for individuals, is a serious matter.

MR BANKS: At one point - I think it was you, Matthew - you talked about the gas code as providing a very good model, and it wasn't clear to me to what extent you were speaking of it as a good model in the sense of the government's arrangements being good, involving all the jurisdictions and the way the oversight arrangements work and so on, as opposed to being a good model in all respects, in terms of the substantive provisions. In particular, I perhaps might just invite you to comment on the gas code in relation to new investment because that's something that we've heard quite a lot about in the course of these hearings, including today, where you would have heard Epic Energy talking about the quandary it was in in terms of whether it would seek to take action under IIIA to get something done and proposals that it put forward to make changes to the gas code. Would you like to react to that?

MR CROOKE: Perhaps Les might be better placed than I to do that.

MR BANKS: Good.

MR FARRANT: There are certain provisions in the code for new pipelines, the bidding process which was already referred to earlier - maybe today - as perhaps not being appropriate in some circumstances for new investment, and I think we support that. There are some circumstances in new investment where the bidding arrangement doesn't suit. In this state though we haven't seen an example of the existence of the code being adopted in law here and an effective regime here in stopping pipeline development in the state. Epic itself has expanded its own pipeline in this environment. It's expanding it because it has got some customers to serve and it knows that they're going to be served under the code and so do the customers.

We have already had one pipeline built in the mid-west of this state, which is also going to be a code pipeline under their regime. We will have more pipelines

built in this state. We currently have an announced a proposal to supply gas to Esperance in this state which requires a pipeline extension from Kalgoorlie to Esperance. The builders of that, or the people who are proposing that pipeline, perfectly well understand the code arrangements that are expected to be in place, after all the code applies to the pipeline down as far as Kalgoorlie, and they would have every reason to believe that the code will apply south of there.

So locally, if you like, in WA, we haven't seen that consequence which Epic is holding up with respect to the Darwin to Moomba pipeline, which is their particular immediate concern. This state was prepared to agree an arrangement to amend the code for a short-term provision to enable the Darwin to Moomba pipeline to proceed via an access undertaking under Part IIIA without having the necessity to lodge an access arrangement under the code provided the access undertaking under Part IIIA was deemed to be an access undertaking under the code and therefore didn't create a conflict between those two mechanisms for determining a regulatory regime.

At the moment that proposal has been withdrawn by the Natural Gas Pipeline Advisory Council/Committee largely because of the Australian Competition Tribunal decision, I believe. It has really been withdrawn because the industry now doesn't think it needs that amendment. Therefore, I would say that the code currently can't even be said to be frustrating that outcome with the Darwin to Moomba pipeline, so - I am having difficulty in finding the example. I do think there's a lot of benefit of having the code in its current form with respect to new pipelines, when we think about third parties subsequently wanting to get access to them.

It's one thing for Epic to say it has an inherent problem with foundation customers and the code as it tries to get its investment up. It's quite another to then say, "But when new third parties come along after the pipeline is up we don't need the code," or something relatively equivalent to it, because it's those customers who fundamentally don't have bargaining power. In the first instance the foundation customers have one hell of a lot of bargaining power. In fact to put a sharp point on it, that's Epic's problem. Those foundation customers are wanting the most favoured nation clauses saying, "We think if the code is applied to this then we want the better deal, whichever is better under the code or whatever we negotiate as foundation customers." It's not very constructive for Epic to argue that that isn't exactly commercial negotiation for foundation customers who believe they've got a negotiation capacity.

The pipeline won't be built unless Epic convince foundation customers they don't need a most favoured nation clause if Epic won't invest on any other basis. The code is not stopping that. That's a commercial issue. Hence, at the moment I don't believe there are going to be amendments to the code driven by the Darwin to Moomba pipeline, and nor do I think that it's inappropriate to apply the code to that pipeline for third parties after the pipeline is built.

MR COSGROVE: Yes, although Epic said this morning that the regulatory risk associated with access would prevent them from investing in the additional capacity to enable those people you say have little bargaining power to have access.

MR FARRANT: What regulatory risk is it, because if indeed third parties were to be subject to the code Epic knows precisely what the regulatory regime would be that applied to it in servicing those customers? What they're saying is they don't think the return on incremental investment under the code is what they're in the business of investing for. If they're not, then they shouldn't be in monopoly pipelines.

MR COSGROVE: That was part of it I think, and also a concern about changes in regulation during the course of the lifetime of their investment.

MR FARRANT: I think it was perfectly practical for the National Gas Pipeline Advisory Committee to say, "We aren't going to change the regime. We'll provide that an access undertaking is in fact a deemed undertaking under the code," and the regime would not change.

MR COSGROVE: I'm not quite sure what you mean by "the regime". The application of the regime could presumably change and that was, I thought, their concern.

MR FARRANT: The application, sorry, wouldn't change either. There are some other provisions of the code to deal with ring fencing and so forth, which if Epic were to adopt the - if the amendment which is proposed by the National Gas Pipeline Advisory Committee were to be adopted, it would indeed bring other provisions of the code into play, including ring fencing arrangements. That's set up in the code.

MR COSGROVE: Does the code enable terms and condition of access to be set for a period of, say, 20 or 25 years?

MR FARRANT: It's to be tested. So far the regulators have been prepared to give longer periods, and with the introduction of this idea that new investment in new pipelines needs to be fostered, then the regulator's capacity to set a longer period hasn't yet been examined or tested in that way. I am aware that the ACCC has no problem with contemplating longer periods in these circumstances. That's my understanding. It's the ACCC in this case who would be the regulator either under an access undertaking or under the code, so I think that it's important that it's their view that needs to be assessed in this case.

MR BANKS: Perhaps going from that question of access holidays, I guess the question of getting greater certainty ahead of investments in sunk assets being undertaken is an issue that has been pretty widespread in this inquiry so far. As you know, in the position paper we saw some merit in the notion of an access holiday, particularly in the case of investments that would be inherently contestable and therefore only likely to, in a sort of risk-adjusted sense, anticipate relatively normal profits, at least in an ex ante sense, regardless of what might happen down the track. You've sort of started at that point, but not actually specifically addressed the notion of an access holiday.

You have gone into the question of what is analogous to an authorisation of

any competitor conduct under Part VII of the Trade Practices Act. I just thought I would give you the opportunity to comment on that, whether you saw the approach that we put forward as not being viable and therefore you are putting up this as an alternative, or whether you see this as simply another way of approaching the same issue.

MR CROOKE: Thanks, Mr Chairman. I would suggest that it's probably the latter, that it was, if you like, a bit of creative thinking on our part at the end of it to suggest perhaps alternative ways of doing the same thing, and in doing so hopefully expanding on the concept a little into its component parts. I think the critical question to be asked is perhaps would that be in the public interest. That's how we tend to approach things. If there were that sort of process involved, the question is a relevant one to ask. Giving some degree of protection from an access regime may well be appropriate, but I think it's up to the investor to be making that case. Perhaps it's not important in terms of the means of how that sort of thing is achieved, but that the right questions are asked.

There is also, I think, some parallel between doing it this way, as proposed in the second submission, and even in considering the public interest associated with providing access under the declaration criteria already. I think it was also sort of instructive to separate that question from what might the terms and conditions be that are appropriate to a particular risky venture, the risk-weighted returns if you like. I thought it was helpful to try to separate those two issues, nothing else.

MR FARRANT: Perhaps I would add that an access holiday deals with this issue of the most favoured nation clause to some degree. It simply says, "For foundation customers there is no chance of you getting a code outcome for the period of the access holiday." Hence, I think it's quite favoured by the builders of new pipelines on the concept that it's another way of solving the foundation customer conundrum without actually saying, "We won't ever be code-regulated." However, the gap between the pipeline being in existence and the end of the access holiday continues to expose the parties who aren't the foundation customers, so it's not necessarily an ideal solution to that problem.

MR BANKS: Sorry, say that again - the latter part.

MR FARRANT: It would mean that there would be no access arrangement or no code-regulated outcome for the period of the access holiday for all users of the pipeline, not only the foundation customers, therefore those who come along subsequently take their chances and they then take their chances with a built pipeline where potentially their competitors already have access by a foundation customer basis and they are really vulnerable as a consequence.

MR BANKS: Although at that point the facility could be declared presumably and then they would be in a position of - - -

MR FARRANT: That's like saying, "We'll have an access holiday but we might declare you in the meantime." That won't solve the problem.

MR BANKS: No, what I'm saying is it's not the end of the holiday. At the end of the holiday, by definition, the situation would revert to one in which someone could apply for declaration.

MR FARRANT: I think that would be fine except now we would need to contemplate the extent of the holiday because if it were effective for the sorts of issues which Epic has been quite clear about then you might be talking 15 or 20 years.

MR BANKS: What would be wrong with that?

MR FARRANT: If you think about the development of say the South Australian or New South Wales economy over that period of time and contemplate that a pipeline delivering gas out of the Timor Sea for that period of time for third-party users, that is not foundation customers who would not have access to a potential for either declaration or regulated outcome, I think that's quite serious.

MR BANKS: But is it more serious than not having the pipeline built?

MR FARRANT: It is true that those customers aren't the people who caused the pipeline to be built in the first place necessarily, although the future is always in the mind of the pipeline builder. You know, we're talking about assets here which the ATO thinks at least will last 50 years and certainly the pipeline builder is always driven to put steel in the ground in order to win future customers. Epic will echo that comment from here this morning, so it's their business to grow the market.

MR BANKS: But, see, you could have a situation which, if you had an access holiday, they may be more inclined to provide additional capacity because they would see themselves having more control over the terms and conditions at which that capacity was made available to a third party who may not be a foundation customer. So I wouldn't necessarily see those third parties being ruled out. It's just that they wouldn't be operating in a regulated environment.

MR FARRANT: If the investment were made in extra capacity, and that was a condition of an access holiday, then you have a different set of economic or commercial drivers on the pipeline owner and on those customers. If we, as we have in this state with the construction of the Goldfields gas pipeline, made it quite clear that there was to be extra capacity in the pipeline over and above that of foundation customers, then partly of course from the state's point of view it's public interest in making sure of economic development in the future and like issues and we will probably do that with other pipelines in this state to ensure that there is capacity for the economy to expand but it hasn't happened by the state of infrastructure.

What you are hearing though with respect to the Darwin to Moomba pipeline is that the pipeline won't invest in that. It doesn't mean that there isn't a good reason for the country to want it to be invested in and to give an access holiday without the other side of the equation would leave you vulnerable to exactly the thing that a

regulatory regime has been contemplated for here.

MR BANKS: Yes, well, I guess it's a horse and cart issue. As I say, it may well be that capacity is being restricted as a way of avoiding coverage and, if provision is there to negate coverage, then you wouldn't have that distorted incentive.

MR CROOKE: If I could just add a couple of comments to that, I think the same series of issues can already be addressed by sort of what we have in place. I'm open to suggestions that there's a need to amend the regime to do it but I'll just propose an alternative situation to you. Basically somebody is looking at building a pipeline, it's potentially subject to coverage either via declaration down the track or say subject to the gas code. The code already contemplates proposed pipelines and there would be an ability for that infrastructure builder to come forward and try to secure the regulatory arrangements to apply to that pipeline.

Now, there are questions about the term for which they might run and there are questions about is the return appropriate to compensate for the risk-taking in that. There is probably also capacity to spread the returns across time as well in terms of bringing new capacity into the capital base down the track and having that reserved, if you like, such that it can actually be reclaimed over the life of the asset. So I think, although we can consider it in terms of an access holiday, there are perhaps sufficiently broad arrangements in place to deal with the concept. It just hasn't been done.

MR BANKS: Your suggestion here in terms of the public interest, if it is analogous to the current authorisation provisions under Part VII, essentially there is a presumption of guilt, if I could put it that way, that would trigger this process. I guess our presumption was a presumption of innocence to the extent that these investments were contestable, that there wasn't a problem that needed regulating. That therefore raises a question about to what extent this would create greater certainty or bring about greater investment.

There's also the question of how the public interest itself would be interpreted and of course, I mean, ultimately it's up to the political process to make that interpretation. To me it seemed to have the virtue of at least bringing forward a decision which would obviously reduce uncertainty but bringing it forward in the way that had a lot of things in play that were themselves uncertain. I mean, it's a very useful suggestion and it's one that we will look at along with a number of others that we've got. I don't know whether you want to make any further comment on that.

MR CROOKE: Yes, only a couple. I must say that it wasn't something that we really spent a lot of time in formulating. We were just noting the parallels between potentially asking that question of what would be in the public interest in this circumstance. Generally, there are problems with it. Section 46 is conduct that can't be authorised. In terms of the presumption, I don't think I quite agree with your comments. This would be an optional process for somebody wishing to build new infrastructure. It wouldn't be something that they sort of have to do to protect themselves from - sorry, they could simply leave open the option of declaration

down the track on the basis that they thought, you know, the pipeline wouldn't qualify or the facility wouldn't qualify.

I just see it as more of an option for an investor in clearing the way, if you like, that sought to consider the interests of not just their investing environment but what it does to competition in markets. In terms of the public interest it would depend on who is assessing this issue. There are probably inconsistencies between what we have suggested earlier in terms of ministerial involvement and I think what this purports to in terms of potentially the ACCC considering the issue as it does under Part VII. That is something else that would need to be resolved. But, that said, there is a growing body of cases where the public interest is being considered in terms of the legislation review process, where all sorts of restrictions on competition are sort of given the once over with a balanced drill and also the commission's own approaches in applying the law in other situations under Part IV.

MR BANKS: Currently the commission has the public benefit test which - I mean, it's essentially making judgments - what some might say are inherently political judgments - about public interest there, but so far under IIIA the considerations of public interest are made by say the NCC, but ultimately it is advising the minister, who makes a final call on them, so in terms of your earlier comments - as you say, there is a little bit of attention with the role that you've previously seen for ministers.

MR CROOKE: There is, yes, and it perhaps boils down to that first point when we tried to deconstruct the issue, if you like. There's the concept of coverage or the reverse question of exemption from coverage.

MR BANKS: Okay.

MR COSGROVE: In this area, too, there are some interesting issues concerning the national and the state industry-specific regime structures, I think. You have indicated that you are not keen to have IIIA superimposed as a framework on industry-specific regimes, so if there were to be an access holiday provision available how would that work for a sector or industries - pieces of infrastructure - which are potentially subject to an industry-specific regime? Would you see the holidays being provided case by case with each regime's regulator deciding whether or not to issue such a holiday? More specifically let's say that under IIIA provision was made for an access holiday subject to certain criteria of say 20 years. Would you be relaxed with that situation on the grounds that an industry-specific regime in this state could provide something equivalent? How would those matters work out?

MR FARRANT: If you were going to be covered by any of these regimes you either volunteer or you are declared into it. If the process is one of seeking to be declared for coverage then the decision - in this case by a minister - as to whether you were going to be covered or not could indeed include the holiday provision. He could simply say, "I've considered this and I won't reconsider it for another 10 years" or something or, "On the grounds of public interest it is not appropriate to declare this for coverage now, but I will review it in 10 years" or some provision of that sort.

I think the decision needs to be well and truly up-front rather than allowed to be made by a regulator down the back end of this process. Firstly, you don't want to waste time or money in the issue; secondly, with new investments you want as prompt a decision as you can get because the window for making investment is a commercial one and you don't want to impose something that is going to conflict or confuse that issue, so bringing it right up-front to the decision as to whether it is covered or not might be a way of doing it, and certainly I could conceive of a structure agreed between jurisdictions which would enable ministers to do that, without actually touching the code.

MR COSGROVE: And if it were not agreed - I mean, there would be different incentives in play potentially here. You could have a pipeline investor seeing an opportunity of an access holiday under one regime of a period that was pretty attractive to it, choosing to go for that option rather than, as I thought you would prefer, under an industry-specific regime.

MR FARRANT: Yes. I think if the hierarchy that we have spoken about earlier were recognised in an appropriate way then we might not have the difficulty that you have just alluded to.

MR COSGROVE: With the industry-specific approach driving - - -

MR FARRANT: With the industry-specific - what is it? The effective access regime industry-specific legislated by jurisdiction being the number 1 priority in that, if you like, and therefore access holidays given in that circumstance would be effective.

MR CROOKE: I think if this concept of the access holiday gets a run then quite a few things need to be considered. There will be a question for each of the industry-specific regimes as to whether that approach would be appropriate. I am thinking now of an access holiday basically in terms of a derogation and the possibility that a regime loses its effectiveness by not applying to a particular facility or service that might otherwise be intended to be covered. I mean, having it at the national level, Part IIIA presents one set of problems. I'm not sure that we can fully fathom the possible implications of trying to achieve it at the industry-specific level and I guess I just go back to my comments before about perhaps the problem can be dealt with anyway via questions of coverage under industry-specific regimes and appropriate rates of return, so that's something I think we would need to consider a bit further.

MR FARRANT: To the extent that those regimes also provide review - in this case by the NCC - of coverage matters, or revocation matters in this case, there wouldn't be any particular reason why the NCC should not be involved in decisions about access holidays and providing advice on that in the same way as we have advice provided now for the fundamental decision - coverage or not.

MR COSGROVE: In terms of your hierarchy, although you have seen us as coming at it from different angles, I think there is a lot of common ground here in terms of the pecking order you have got and, at the end of the day, I guess while - as

you say - declaration may be a last resort, in testing the effectiveness of non-certified regimes it is creating a discipline there. You commented earlier - and it is in your submission at the top of my page 8 - that, while we seem to agree with your suggestion - WA's suggestion - that interim certifications be permitted, this doesn't appear to have been translated into a proposal for reform. I guess we may have been under the misapprehension that effectively that scope already existed under current arrangements given the short period of certification, for example, of a New South Wales regime, but that I suspect doesn't satisfy you, and I just thought I would get you to react to that.

MR CROOKE: Yes, just a very short reaction: I think in essence it boils down to perhaps not basing certification on the concept of time necessarily but on a series of conditions, and so perhaps a better word for that would be conditional certification, so that you can then move towards an interstate model, if you like, if it was presented in that context.

MR BANKS: So subject to certain conditions being resolved or incorporated down the track.

MR CROOKE: Yes.

MR COSGROVE: We heard this morning from Epic Energy that the costs of the Office of Gas Access Regulation activities include an element of direct cost recovery from the firms. So I was wondering whether the figure given at the bottom of page 8 of your submission, the 260,000 per access arrangement assessed, excludes those cost recovery elements or not.

MR FARRANT: I think we would have to ask OffGAR for more recent information. It's my understanding it does.

MR COSGROVE: It does include them?

MR FARRANT: It's my understanding it does. However, if OffGAR is around they can answer that question perhaps later.

MR COSGROVE: Yes, that would be interesting to - - -

MS NOLAN: Alternatively we can get back to you with the information.

MR CROOKE: Or Michael might like to address it now, perhaps.

MR COSGROVE: You will have to come to the microphone. We will let you have 15 seconds for starters. If you just perhaps first say your name and then comment on it, thank you.

MR JANSEN: Mike Jansen from the Office of Gas Access Regulation. The costs basically are the direct costs of the Office of Gas Access Regulation incurred in terms of reviewing the access arrangement. It's just an average across all access

arrangements.

MR COSGROVE: Funded from the budget?

MR JANSEN: Funded by the industry. It doesn't include the costs associated with the preparation of access arrangements on behalf of the industry. It's just basically the review costs that OffGAR incurs in reviewing and approving access arrangements.

MR BANKS: Thank you for that.

MR FARRANT: One aspect of that - in WA the legislation enables the regulator to recover these costs from the regulated. It has relevance to the period of time taken by the regulatory action. We are doing well in Western Australia. I don't know whether this means that the ability to recover the costs of regulation helps the process along somewhat in terms of time.

MR BANKS: I think we heard this morning that those who are paying would like more influence over the outcome.

MR FARRANT: Like speed.

MR BANKS: Like every good client. The last thing - I know we've detained you quite a while - you've got some very helpful comments on price monitoring and its relationship with access declaration, and I might just take you to the second-last paragraph of that where in fact you see merits in having something like this. You then go on to talk about how it might work and I thought I might just get you to elaborate. It wasn't entirely clear to me here how you would see it being initiated in the context of, say, an application for declaration at that point, or whether you saw it being initiated without such a trigger - you know, something that a regulator may just decide to do without responding to a formal access request.

MR CROOKE: Once again I have to admit that this wasn't something that we perhaps considered ad nauseam but generally I would have seen it as a process that could be fast-tracked, compared to that of declaration of services for access, for example, but we had the important check in the process of the regulator having to convince the minister that a particular service ought to be subject to this form of monitoring and the accountability lies with the minister. I understand that's generally how things work currently for the Prices Surveillance Act. So it was really just maintaining the minister in that process.

MR BANKS: We have another report, as I indicated earlier, into the Prices Surveillance Act where we have tried to strengthen the basis for even making decisions about monitoring, in that we were hearing - particularly in that inquiry - that it could be quite intrusive and so on, which probably goes a little bit against what you're suggesting here, which would be a more pragmatic, more readily available tool. If you had any comments to make to us in response to what we've said in the PSA report that would be quite helpful I think.

MR CROOKE: Not having really dealt with that particular report in the same level of detail perhaps I would be able to consult with my colleagues who have and get back to you on that.

MR BANKS: Thank you. I suppose from this inquiry's perspective the main thing is how would price monitoring work in the context of the national regime, and I suppose we saw it primarily as an alternative to declaration but probably one that would be decided upon at the point of considering whether declaration would occur or not, so it would be self-selected in that sense.

MR CROOKE: I think what's contained within our second submission is perhaps taking a slightly broader view of the possibility, in that on the face of it it seemed to be a less intrusive form of intervention than actually getting in there to determine the terms and conditions. As far as I'm aware I believe that the process of getting involved and understanding how industries work has been quite helpful to resolving some issues and perhaps petroleum is one example where a period of perhaps even more intrusive regulation led to a better understanding of the industry and the problems that are contained within in.

MR BANKS: I'm sorry that we've kept you here this long. It just shows how interesting your answers are that we keep asking you more. I will just have a quick look to see if there's anything else.

MS NOLAN: Again, if you find other points you would like to raise with us we are more than willing to respond to you in writing or in discussion.

MR BANKS: Thank you very much, again. We appreciate your contribution to the inquiry and we will certainly take you up on that offer if we need to as we are developing our final report. Thank you very much.

MS NOLAN: Thank you for the opportunity today.

MR BANKS: We will just break for a few minutes, please, before our final participant.

MR BANKS: Okay, ladies and gentlemen, we'll resume. Our next participant, and I think our final participant in the hearings, is the National Competition Council. I guess that is appropriate because it will give you the opportunity to have the last word, at least in the hearings. Welcome to the hearings. I will just get you to give your names and positions, please.

MR WILLETT: Ed Willett, executive director, National Competition Council.

MS GROVES: Michelle Groves, director, National Competition Council.

MR BANKS: Thank you very much for participating in these hearings. You have also provided a very hefty submission in the first round and we've seen some preview, I guess, of the points that you want to make in relation to the position paper. I'll give you the opportunity to perhaps give an overview of those points and then we might pick up some for discussions.

MR WILLETT: Okay, thanks for the welcome, Gary. We certainly welcome the opportunity to appear today. I think I would like to start by congratulating the commission on a very good position paper. I think the commission has got on top of what is a very complex area of law and economics very quickly. That stands you in good stead, I think. You've got a draft of our submission and I will turn in a moment to drawing out some salient points from it, rather than providing a summary of it.

I might start by saying that there are a lot of things that are in the position paper that the council supports. We have tried to identify those in the draft submission, but naturally we tend to focus on things that we think need further thought. Many of those things involve refinements or clarifications of the commission's position. We've tried to provide the comments being as constructive and helpful as we can possibly be, recognising how important this review of Part IIIA is. Having said that we certainly haven't hesitated to say things where we think we can contribute on the basis of our experience so far with Part IIIA.

I want to draw out a few themes from what is in the draft submission at this stage. Most of those themes are by way of what I might call dichotomies or distinctions between different things that we think are pretty important. I'll then conclude by saying some things on the proposals in the position paper for amending the criteria for declaration. One of the first distinctions that I think is important is in relation to what the commission has said about access holidays for new investment. We certainly think that there is some merit in thinking about how access holidays might be put in place, but there is an important distinction in our minds between what you might regard as some sort of non-declaration process versus what might be regarded as some sort of qualified undertaking process.

Our thinking in this area is developing as this review goes on and along with others, I think, and there have been some interesting propositions put to the commission in response to the position paper. Basically we see a non-declaration process as some sort of binding ruling that the declaration criteria are unlikely to be

met, and that it's the sort of mirror of the declaration process but with some commitment that that ruling or opinion would have binding effect for a period of time. That is to be compared with what might be regarded as a qualified undertaking of some sort which would be applicable where access regulation is likely to be appropriate.

But in relation to new investment, some certainty is needed by the prospective infrastructure owner in some respects to facilitate that investment. So the proposal for some sort of qualified undertaking would be an undertaking which sets parameters of how access is going to be provided, sets parameters for terms and conditions to provide certainty for the prospective investor. It seems to us that firstly, those two processes are mutually exclusive, they actually serve different roles. Secondly, the use of both of those instruments might be a better approach than the commission's current leaning towards some sort of null undertaking.

The second dichotomy I want to draw out is the distinction between effective access regimes and undertakings. We think these two things are different and they perform different roles. The legislative access regime, particularly by a state or territory, sets the access rules in an industry including institutional arrangements and processes for the determination of terms and conditions for access. That is to be compared with a voluntary undertaking by a particular service provider which actually goes to those terms and conditions of access.

Perhaps the distinction between those two things has been clouded somewhat by the one and only undertaking which has been accepted, which is the NEM undertaking. The reason for this clouding, I think, is that the NEM undertaking is actually a hybrid set of arrangements rather than a pure undertaking. It does have legislative backing by the states and territories, but it also involves an undertaking by way of industry code, and the Trade Practices Act was amended to facilitate the submission of an undertaking by an industry code, so I'm not sure whether the NEM undertaking is a good example of the undertaking approach. Perhaps we need to see how undertakings develop.

But because it is a hybrid arrangement perhaps it does tend to cloud the distinction between legislative access regimes, which might be subject to testing as an effective access regime versus private undertakings. In saying those things we're not suggesting that it's not appropriate to question whether you need both of those instruments. What we are saying is that there is an important distinction to be drawn between those two instruments. The starting point of the commission's analysis is actually identifying what those two instruments are.

The third dichotomy I want to draw out is the difference between access policy and access regulation. I understand this has been the subject of some previous discussion in your hearings. The council's role as we see it under Part IIIA is to advise and design coverage of access regimes. That role basically sets the parameters of access regulation and provides or raises jurisdiction for the regulators. We see this as a policy role quite distinct from the actual regulation of terms and conditions of access, which involves a case-by-case setting of those terms and

conditions of access by a particular service provider.

Again, I think it's important to set up a distinction - this distinction between what is a policy role and what is a regulatory role - because I think it does have implications for what different instruments do and what appropriate institutional arrangements might be,
and I think the commission's draft report on the review of the Prices Surveillance Act has already made some attempts to draw that distinction between policy and regulation. Once that distinction between policy and regulation is established, then it's appropriate to test current arrangements against that distinction to see whether they're appropriate.

I'll conclude by saying some things about the proposed amendments to the criteria for declaration. We have provided some considerable comments on the proposals. I won't go through each of those comments right now, although we can discuss those, if you wish, through questions. But I do want to stress the importance of recognising the value of established precedent on the existing criteria. We have had a few tribunal decisions, Federal Court decisions. They are discussed in the draft submission. Those decisions already provide some certainty on the scope of application of Part IIIA and, broadly, we would say that the current criteria appear to be catching the right sort of things, working away.

Our interpretation of the commission's views on where access regulation should be applied is being reflected in the current interpretation of the criteria, so there's a real question in our mind about whether it is appropriate to be amending the criteria at this stage. Thank you.

MR BANKS: Thanks very much for that. We could go back through the themes that you've enunciated but I suspect we'll trip ourselves up, and it might be better if we perhaps go through the draft submission that you've got and perhaps elaborate on those points where you yourself have elaborated on the themes.

MR WILLETT: Sure.

MR BANKS: The first question I was going to ask is addressed on the first page of your submission where you say that you disagree with the conclusion reached that the current framework has significant deficiencies in terms of the national access regime. Then you say it may be more a disagreement of emphasis than substance, and you also say that we don't have much evidence of fundamental deficiencies.

You've raised the question of access holidays, which I think highlights one - well, some participants have clearly seen that as the significant deficiency in terms of provisions for new investment. The objects clause I think is one that a lot of participants saw as a significant omission. You've made reference to the Trade Practices Act and to what extent that can accommodate or serve the same purpose, and I guess pricing principles was another area that some participants place great store on, and indeed one participant said that it was perhaps the single most important area for improvement in the regime, but I'll just give you the opportunity

to respond to that.

MR WILLETT: Yes, I think I can respond pretty quickly. We certainly see some scope for refinement of Part IIIA but we don't think the architecture of Part IIIA is fundamentally flawed. What that means is, while there's scope for refinements we wouldn't see major changes made to either the architectural, the fundamental elements that we see that make up Part IIIA. The things you mention are all things that we support, but we tend to see them more as refinements. I suspect we probably wouldn't agree that they reflect fundamental deficiencies in the current approach but they are certainly refinements that would provide some clarity on the application of Part IIIA and would be helpful to the operation of Part IIIA.

MR COSGROVE: So your statement on page 11 in section 2.6 that the current mechanisms do not seem to be operating in a way that provides appropriate certainty for infrastructure investors is to be read as a need for finetuning and no more?

MR WILLETT: I guess you can get into semantics about what finetuning is, and I'm not sure how useful that is. Certainly we see the sort of things we have proposed here as sort of development or finetuning rather than fundamental change.

MR COSGROVE: Or, to put it another way, improving that situation for these investors would not require change in the structure of the regime.

MR WILLETT: That's right. There is a question in my mind whether the concerns that are being expressed by infrastructure owners are totally justified, but the fact that they're expressing concerns is an issue in itself and needs to be considered, at least.

MR BANKS: As you know, one of the things we've been trying to get more concrete information on is the impact on investments, and I think it's in the area of gas that we've had quite a lot of information, but a lot of it has been contradictory as well, so we'll spend a little bit of time after these hearings sifting through it all. At the end of the day I think those kinds of anecdotes only get you so far and you do need to come back and think about conceptually how the thing is operating and how it could have an effect, so that's I guess the context in which we've put forward that suggestion.

MR WILLETT: Sure.

MR BANKS: Mentioning the objects clause earlier, my reading of at least your draft position is that you broadly support that notion and, indeed, would see a need for the objects clause to be taken into account in the interpretation and application of the Part IIIA provisions, which was mentioned in the draft on the top of page 5.

MR WILLETT: Yes.

MR BANKS: Would you like to elaborate on that? You're seeing an active role for it rather than a passive one, and I just wanted you to comment on how you would see that best being achieved.

MR WILLETT: Yes. In our first submission and indeed in this draft we recognise that there is an objects clause for the whole Trade Practices Act in section 2, and that appears to be reflecting an efficiency objective which wouldn't be inconsistent at all with the sort of approach that the commission is advocating to Part IIIA. I guess as we've thought about it some more, and particularly in the light of our experience in putting arguments before the tribunal in the Duke matter, there do seem to be some benefits to us to providing a somewhat more comprehensive objects clause specifically for Part IIIA, and picking up on the things that are identified in the first part of your objects clause
would seem to us to be the right sort of things.

The draft submission expands on those somewhat to reflect our understanding of what that objects clause would mean. While I don't think it would make any difference to the way the council has addressed the criteria for declaration or its other roles in Part IIIA to any extent, it would be beneficial, we think, to include that sort of objective and to condition interpretation of the declaration criteria in other Part IIIA roles by that objective. There has been a suggestion by another participant to this inquiry that there would be some benefit in that, and we agree. It wouldn't change what we do, but just ensuring that that's clear would provide some benefit.

MR COSGROVE: Your section on the pricing principles left me somewhat unclear as to whether or not you actually supported the proposal in specific terms which we have in the position paper - proposal 8.1. You agree the principles need to be general and high level. You say on the bottom of page 5:

> Council considers that the existing regimes and arrangements already approved under Part IIIA are consistent with pricing principles.

I again wondered whether you felt you didn't really need this degree of specification or not.

MR WILLETT: I think there is some benefit in providing that sort of guidance up-front. I think that it's probably going to be of more benefit to provide more guidance about arbitration undertakings than trying to establish the pricing principles up-front, because I think setting pricing principles up-front is somewhat problematic in that you would need to be so general that there's a question about how much guidance it's actually providing. So it's beneficial; there's a question about how much benefit it actually provides.

MR COSGROVE: We'll perhaps come later to your alternative or your other suggestion that it would be better to clarify the negotiation and arbitration arrangements. What do you say?

MR WILLETT: There are other suggestions that we have made - and indeed reflected in your proposals - that would actually enable the provision of more information on a case-by-case basis in infrastructure regulation. We think those sorts of proposals would probably provide more benefit than trying to set some

overarching pricing principles to apply generically to all access matters. Inevitably overarching pricing principles are going to be very general. They would need to be. You can't be too prescriptive in your overarching pricing principles.

MR COSGROVE: But in the absence of them individual regulators would retain essentially a considerable degree of discretion in their own decisions on terms and conditions of access.

MR WILLETT: Yes, it's arguable that they would have more discretion now than they would if these pricing principles were applied. I'm not sure that, in actual fact, they exercise more discretion than is reflected in these pricing principles currently.

MR BANKS: One of the contexts in which we saw this was the same as in which we saw the need for an objects clause that talked both about efficient investment and efficiency of use. I guess even high-level guidance through the pricing principles - that incentives for efficient investment were an important part of it - I think we thought would be useful. It may be implicit, but there were a lot of people who were saying it wasn't, and having some explicit recognition of that I guess was the contribution that we thought it made.

MR WILLETT: Again to the extent that those sorts of principles aren't already recognised, it would provide some benefit to ensuring certainty. It just seems to me that those principles are by and large reflected in current practices by regulators.

MR BANKS: In section 2.4 there on the bottom of page 9 you've expressed concern about implications of removing the notion of market from criterion A and substituting with a notion of activity. I guess I just wanted to reassure you that at the end of the day we didn't recommend that or propose it but explored it on the way to somewhere else.

MR WILLETT: It might have been my error in reading but I read that as you leaning towards that sort of position in your canvassing of it.

MR BANKS: No, I think in fact we took account of the points that you have made here in not pursuing it - but anyway, just to clarify that. You go on to talk about vertically-integrated separated providers. You don't, I think, see a need to be explicit about that. I guess I just thought I'd ask you why being explicit would be problematic. I say that with due fear and trepidation because, having talked to quite a few lawyers, things that I thought were quite unexceptional have turned out to be quite complicated and difficult. But anyway, I give you an opportunity to comment.

MR WILLETT: I guess it always raises the question of what you intend by that. Generally there's an understanding in legal interpretation that if something is amended then something different is intended. That can be a bit dangerous if all you're trying to do is confirm what's actually happening, rather than actually change things.

MS GROVES: I think additionally with this - and this is one more of the lawyer

sort of problems and I think it's been highlighted by a couple of other submissions as well - is the difficulty in defining vertically integrated and vertically non-integrated from each other within some sort of definition such that it's got meaning and there aren't gaps between them, because there are concepts of Corporations Law, separate companies. You've got concepts of holding companies, companies that are legally separate but have common ownership,
you have got concepts of vertical integration through contractual arrangements, and it would just seem that getting into having to increase the complexity and the technical definition section of the act is just a question of what would be achieved by that when in fact its silence at the moment seems to be doing exactly what it is that the commission seemed to be supporting.

MR WILLETT: I might add to that that I think it is important to recognise in these things that the quote that appears on the top of page 11 from the Sydney Airports decision - that is the current state of Australian law because the tribunal decision has some authority until it is overturned by a superior court.

MR BANKS: So you would see this as being one of the matters that at least had been settled by the appeals process by the tribunal.

MR WILLETT: That is right.

MR BANKS: Perhaps if we come to the access holidays point again, which was the first of the four themes that you raised, I think the points you have just made are actually quite helpful, and the distinctions you're making there between non-declaration and a qualified undertaking - you would be aware that NECG and some others have put a lot of emphasis on this and looked at different ways of achieving, in their terms, what they describe as a greater investment certainty ex ante, which I think is obviously a useful objective. There are many ways to skin a cat and I guess the different proposals that are being put forward would do it to a greater or lesser extent. They are the things that I suppose we need to look at.

Your qualified undertaking was there you were proposing that essentially it would apply to a facility that is likely or would be covered but it was just bringing forward the point at which the parameters would be set to enable a greater certainty for the investment. Is that the - - -

MR WILLETT: That's right. I think we need to be careful not to set up incentives to broaden the scope of Part IIIA, simply because these instruments are available. What that means, I think, is that it's important to design the instruments to deal with a particular issue; the right instrument for dealing with infrastructure services that wouldn't be likely to meet the criteria, to make it clear that they wouldn't be likely to meet the criteria, and to provide some protection ex ante in that situation. On the other hand, if there are proposed infrastructure services that would be likely to meet the criteria for regulation in some form but nonetheless there is some need and we can recognise there might be some need to determine some parameters of the access arrangements ex ante, then the right approach to dealing with that issue, it seems to us, would be the AusCID and the NECG proposal of a framework undertaking.

MR BANKS: Could that be done under current arrangements?

MR WILLETT: That is an interesting question. I don't see any reason why it couldn't be, at the moment, but I'm not sure we have looked closely at that at this stage.

MS GROVES: The current arrangements certainly technically allow it up-front because an undertaking can be submitted of a service provider for a proposed service, so there isn't that sort of definitional problem up-front. The criteria for undertakings on the face of it look quite general and not necessarily having anything on the face of them that would seem to exclude the possibility of one of these. I suppose the problem has been that there has been very little attempt to test the current mechanisms, either under the more general Part IIIA undertaking route, or even the more specific provisions of, say, the gas code, which has a similar arrangement. A prospective service provider can submit an access arrangement before construction of the pipeline to try and have the regulatory framework determined before they put the pipe in the ground.

Those mechanisms are there but there hasn't be a lot of use of them - or in fact, really, any of them. It is actually for people to say up-front whether they would not provide the answer that they're looking for. A number of service providers have had some doubts about whether or not some of those provisions would be able to assist them. I am assuming they have those doubts based on their own analysis of those provisions but we haven't had one really put up and the regulators say, "No, because of this we can't look at these sorts of things" or, "We can't take these things into account," so it's a bit difficult to say.

MR BANKS: It might be worth, in your final submission, if I can call it that, perhaps exploring that implementation aspect a little bit further.

MR WILLETT: We will do that.

MR BANKS: Both in terms of whether you think the existing arrangements are adequate or what might need to be added to achieve that. In talking about the commission's exploration of an access holiday through an undertaking, which was one mechanism that occurred to us, you say that the council would be concerned if the determination of whether an access holiday would be available is based on an ex ante assessment of profitability of any particular project. I have seen evidence that the ACCC has the same view and, indeed, it is one I sympathise with, about not being seen as a king-maker or a winner-picker in this kind of domain.

I guess what we were exploring in the position paper was perhaps a rule of thumb that might be quite robust in terms of the contestability of investments as a guide to whether a holiday should be provided or not. I think Michelle was probably there during some of that discussion. It is something which we would appreciate any reaction to. We have that discussion mainly - well, the first time probably in some detail - with NECG. It is really just a question of whether, going on from our

position paper, it would be possible to draw a circle around those sorts of investments that wouldn't be contestable.

On our thinking, they tend to come down to investments that would involve the extension or augmentation of facilities by the incumbent; therefore, in a sense, using the position of market power in terms of the timing of such investments to extract some rent through those investments,
in which case the onus would be on the provider to show why an access holiday should be provided. But in all other contexts the onus would be on the regulator to show why such a holiday should not be provided. I don't know whether you've got any immediate reactions to that. In a sense it wouldn't be a case-by-case assessment in that way. However, the notion of contestability would have to be reasonably well defined. I guess that's the area that we're giving some thought to.

MR WILLETT: Indeed. I can see a few dangers with this sort of approach and perhaps I can make a few comments. It seems to me the notion of the ex ante profitability of prospective investment having some influence on whether an access holiday would be granted draws some parallels with some problems with the interpretation of uneconomic development of another facility to provide the service in the declaration criteria. The parallel is drawn because in both cases there's a question about whether inefficient investment of one sort or another should get more favourable treatment in terms of Part IIIA than efficient investment. That involves some quite perverse incentives on investment if that were to turn out to be the case. I think you accept that proposition. I can go into that in more detail if you wish, but I think you accept that - - -

MR BANKS: I'm not sure that I'm with you actually.

MR COSGROVE: No, I'm not.

MR WILLETT: In the Sydney Airport decision the tribunal said that it favoured a social cost-benefit interpretation to the "I think I might develop another facility" criteria. One of the reasons it did that was because of the evidence of Philip Williams in those proceedings, whereby he explained that if that wording was to be interpreted from the point of view of private costs and benefits, there was a risk that inefficient investment that relied on use of a facility might be able to gain access to a facility, whereas more efficient investment - which might be so efficient as to be able to underwrite the construction of another facility - that that investment wouldn't be able to be conducted with the benefit of access arrangements.

The perverse incentive that sets up is that you might actually end up with the inefficient investment having a higher net present value, because it can get access to the existing infrastructure, than the efficient investment. That was one of the problems with taking a private approach to the interpretation of that criteria. Similarly, if you were to have access holidays turning on questions of prospective profitability, it seems to me that it raises those same sorts of considerations; that you're going to provide more favourable treatment under Part IIIA to inefficient investment as opposed to efficient investment.

MR BANKS: Yes.

MR WILLETT: When you start getting towards questions of contestability investment, then you start to get some distortions if, on the one hand you're saying, well, if you're not going to be highly profitable then you're going to get favourable treatment under Part IIIA - more favourable than if you are going to be highly profitable.

MR BANKS: I guess that's why we've avoided, in a way, using profitability as the test, but rather the broader competitive conditions that would determine profitability ex ante. Just as you've talked about the need to think about the structural determinants downstream or exposed, you could think about it ex ante before an investment is made. I guess the logic would be that in many cases an investment would be undertaken at the time that it became profitable to do so, if it was broadly contested and there was more than one player and they didn't have a privileged position from which to make that decision, almost by definition. That might be conceptually wrong but we haven't yet seen any arguments to show that that is wrong.

From that starting point I guess we then go to say, at least ex ante, for those classes of investments we would see benefits in providing them an access holiday because, ex ante, they're the sorts of investments that would be likely to be deterred or stopped by a burden that would actually make them unprofitable. The problem is ex post they may turn out to be quite profitable because they're looking at probabilities and they've got a distribution of expected returns. That may be factored into, then, how long a holiday you would give to such a proposal.

Certainly our approach wasn't requiring the regulator to make judgments about profitability. I agree completely with the point you're making. I suppose the question for us is how robust would such a rule of thumb be, and would it in itself give rise to any perversities. We're having trouble thinking of some but if you can come up with any, now or later, that would be helpful.

MR WILLETT: Let me draw two other distinctions I think might be relevant to you.

MR BANKS: Okay.

MR WILLETT: I hope I'm going to get through these two.

MR BANKS: Right.

MR WILLETT: The first distinction I think is that there might be two reasons at least why a prospective investment might be unprofitable. The first reason might be because the infrastructure owner just isn't going to have any market power. If that's the case, then the binding ruling approach might be the appropriate approach or, if necessary, if it's not clear, then the framework undertaking might be an approach that

could be taken.

Distinguish that situation from a situation where a prospective investment is unprofitable simply because it is inefficient or not as efficient as it might be, and there are opportunities to invest in that infrastructure more efficiently, perhaps by a proposal that comes a little later in time. If that's the case, then an access holiday on the grounds that the prospective investment is unprofitable might be a bit problematic.

The second distinction I was going to draw was the distinction between contestability in the construction and operation of an infrastructure facility - distinguish that on the one hand from the exercise of market power by that infrastructure owner. They're two very different things. You can attain efficient construction and operation through one form of contestability - auctioning the sure right to build infrastructure - without necessarily dealing with the market power problems.

MR BANKS: Yes.

MR WILLETT: Now, the gas code at the moment has a mechanism you're probably familiar with, which deals with both the contestability to enable efficient construction in the operation, as well as the market power issues associated with operation or ownership of that infrastructure facility.

MR COSGROVE: Why wouldn't the auctioning process whittle away the chances of exercising market power? If potential investors can see that there are high returns probably to be had, won't that be reflected in the price they are prepared to pay for constructing the facility?

MR WILLETT: Well, it may be, but all that would do is transfer the rent-seeking opportunity away from the infrastructure owner to whoever conducted the auction process. If we're talking about investment in natural monopoly infrastructure and there are rents to be had through the exercise of market power, then simply because you have a contestable set of arrangements that ensure efficient construction and operation of that facility doesn't mean that you've dealt with the market power issues.

MR BANKS: So, in a sense, I guess you're drawing a distinction between the ownership of the facility and the ability to exercise market power - - -

MR WILLETT: Exactly.

MR BANKS: - - - and the construction and production of the facility which could be contracted out in a way that didn't affect the owner's market power but simply ensured efficient production of the facility.

MR WILLETT: The contracting arrangements might simply transfer the rent-seeking opportunities derivable from the market power to the person conducting the auction, so that in effect they contract out the operation of a monopoly and derive

all the rents themselves.

MR BANKS: Yes, and the distortions remain.

MR WILLETT: That's right.

MR BANKS: That's a useful point that would need to be considered. I thought your middle point still was hinging on this question of profitability rather than looking at the conditions that would determine profitability - well, the appropriate conditions in which your judgment could be made.

MR WILLETT: I think that's right.

MR BANKS: But that's useful, and any further thoughts you had on that we would appreciate, as we will think more about the question of a binding ruling as another way to achieve the same thing. We've been talking a little bit about price monitoring and what role it might have in all of this, and you raised the prospect or the possibility of it - this is on that same page - being used in conjunction with an access holiday. Would you care to comment on that? Would you see the price monitoring being used to trigger action during the holiday period or providing information that would be helpful subsequent to the end of that period?

MR WILLETT: Yes. I guess the way it would work would depend on how you set up the prices monitoring arrangements, but the point that was being made there is that perhaps a mix of these instruments might be an appropriate approach to dealing with an issue at a particular point in time. We can give that some more thought, if you wish, and enhance that point.

MR BANKS: Okay. You may have more on price monitoring later but anything you can say to help us on that would be useful, and again it's one of the areas where we have a degree of overlap between at least three of our inquiries at the moment, all of which are grappling with aspects of that. On the binding rulings, am I right in suggesting that what's really happening here is simply a pull forward of a decision on declaration? I'm just wondering to what extent the regulator would be in a position to make such a ruling without all the information that might have otherwise been available to the regulator.

MR WILLETT: Yes, that's right, there would need to be some conditions set on the binding nature of the ruling, depending on the process that was adopted and the information available. If the binding ruling was made on the basis of misleading information provided by the infrastructure owner, for example, then you'd probably need to qualify the binding nature of the ruling on that ground. What the binding ruling would do is basically two things: one, you're right, it would drag forward the consideration of whether declaration or coverage in an access regime was appropriate, but, secondly, in order to be of use to an infrastructure owner in these circumstances it would also bind the non-application of declaration or coverage for a period of time.

But we do see that even if the information wasn't available to provide that very certain outcome, there might still be some benefit to the infrastructure owner in getting at least some of the parameters of declaration or coverage determined on a preliminary basis, and that would all go to increasing the certainty of the infrastructure owner on the sorts of conditions or circumstances under which regulation would be applied in the future.

MR COSGROVE: It still seems to leave it a bit up in the air so far as the investor is concerned. It may, as you say, advance his understanding of what he might face in the way of regulation but it's not really providing assurance that for a certain period of time there will be, if you like, a moratorium on regulation.

MR WILLETT: In that latter circumstance you're right, but I'm not suggesting that there wouldn't be other circumstances where it would be possible to provide a binding ruling, and if that were possible then it would provide that protection.

MR BANKS: Yes, I guess one area where I could see it declining is where projects were obviously submarginal and required government subsidy or whatever to survive. I imagine that that might be a situation in which such a ruling could apply, and there are some examples you probably could think of where that sort of situation has already occurred.

MR WILLETT: Yes, there's a question I guess where the subsidy goes or where it should go. One case where we had cause to consider that issue is in the proposed access regime for the Tarcoola to Darwin railway, which was the beneficiary of some government support.

During the course of consideration of that access regime the question was raised, "Well, how are public contributions to that infrastructure to be taken into account in the determination of asset valuation rates of return and costs of provision of rail track services?" There was some debate about whether, in effect, the public contribution should go to the track or should go, more broadly, to the incumbent integrated track and train operator. In the end, what that regime does is leaves it to the regulator to determine how those public contributions should be treated in the determination of access terms and conditions within the regime. So it was accepted there's a very real question about how you appropriately treat those sorts of public contributions in those cases.

The examples we've provided where binding rulings might be of use are where it's likely that one or more of the criteria for coverage wouldn't be met. For example, it might be possible to say in an ex ante sense, on the basis of information available, that the prospective infrastructure wouldn't satisfy the natural monopoly test in criterion B, or in other circumstances it might be possible to say that it's unlikely that this particular infrastructure would have market power in the relevant market. If it was possible to say either of those things, then it would be appropriate to grant some sort of binding ruling on future coverage, on the grounds that the criteria would be unlikely to be satisfied.

MR BANKS: I don't know whether this is the appropriate time to raise it, but you've said, for example, that it may be obvious that it doesn't pass criterion B. Would it be fair to say, as some have argued to us, that the Duke decision in a sense is a rather permissive interpretation of the natural monopoly test, and that in fact the sorts of facilities we're looking at - it would be hard to find a situation in which it didn't pass that test, as interpreted in the - - -

MR WILLETT: In terms of gas pipelines?

MR BANKS: Yes.

MR WILLETT: Generally, I think it's fair to say that gas pipelines would satisfy criterion B. There are some circumstances where that wouldn't be the case, and in fact I think we've recently expressed the view that a relatively short pipeline might not satisfy criterion B. But generally gas pipelines involve diminishing costs over relevant range demand and, as a consequence, would satisfy the natural monopoly test. I'm not sure that that's a permissive interpretation. I don't find it terribly surprising that that sort of infrastructure would satisfy that test. That test was designed to single out the sorts of infrastructure that involve decreasing cost or natural monopoly characteristics.

MR BANKS: Again, it comes down to - and I don't intend to have a discussion, because it could take us the rest of the night - the interpretation of natural monopoly technology versus a natural monopoly which is defined in terms of the market, where one provider can supply the market at least cost. You've argued in here, and the Duke decision itself argued, that those things should be looked at separately essentially, by defining the service in a way that means that the natural monopoly is assessed without considering the market at all.

MR WILLETT: Yes. In terms of the Duke decision, it's important to say something by way of background in terms of market analysis, because it's very important to understanding where the tribunal came out, I think. The important aspect is that both expert economists in evidence before the tribunal adopted the US Origin destination market approach to the analysis of gas pipeline services. The two economists differed in what they thought was the relevance of the Origin destination market analysis.

I might explain what the Origin destination market analysis involves. It is looking at the impact of gas pipelines at the point where the pipeline moves gas away from a gas field and looking at the impact of the gas pipeline at points where the pipeline delivers gas. This sort of market analysis for gas pipeline services is adopted by the regulatory authorities in the US, but it's used not to test natural monopoly characteristics. In the US it is simply assumed in this part of the regulation that gas pipelines have natural monopoly characteristics. This analysis is used to test the influence of gas pipelines in dependent markets - in gas sales markets or in the sale of the bundled product of delivered gas.

In the tribunal matter one expert, Geoff Macomb from NERA in the US, said

that, "Well, Origin destination market analysis is totally irrelevant for the consideration of the natural monopoly characteristics of gas pipelines," whereas Henry Ergas - and Geoff Macomb - said that, "You only use that sort of market analysis - it's only relevant for considering whether a gas pipeline has market power in a dependent market," and that's a consideration relevant to criterion A of the coverage criteria in the gas code. Henry Ergas said that's the market analysis you use for both criteria A and B - in other words, not only testing for market power but also testing for natural monopoly characteristics.

I think the tribunal had some difficulty in considering criterion B, the monopoly test, in the light of that sort of market analysis, and as a consequence I think in its consideration of criterion B in relation to the eastern gas pipeline it avoided questions of market. I think the reason for that is fairly clear.

Origin destination market analysis bears little relationship to the actual services provided by a gas pipeline in moving gas from point A to point B. It just doesn't make sense to analyse the market for the transportation service from A to B in the context of a field of rivalry that doesn't encapsulate that service from A to B.

When we proposed the test of natural monopoly that we did and it was accepted by the tribunal, we had this difficulty in mind but we also had in mind that in testing for whether the EGP had decreasing costs over a relevant range demand - we did have in mind the consideration of substitutes to meet that relevant demand, and indeed the tribunal picked up on that approach and did consider the availability of substitute services to meet that relevant range of demand. In fact, it considered at some length whether the interconnect provided substitute services for the EGP such that the availability of those substitute services would undermine the natural monopoly characteristics of the EGP.

So having said all that I think the conclusion is that the tribunal was applying a natural monopoly test too in the consideration of criterion B in relation to the eastern gas pipeline. They did dismiss fairly readily whether the Moomba to Sydney pipeline provided relevant services and some would argue that the tribunal should have actually considered whether those services were substitute services for the services provided by the eastern gas pipeline. They didn't. They said, "Well, they're different services."

One way of looking at that is to simply say, well, what the tribunal has done is recognised that while there might be competition in the supply of the bundled products of delivered gas, which is basically what people are really interested in - they want gas at their door - they recognise that there isn't necessarily head-to-head competition between the Moomba to Sydney pipeline and the eastern gas pipeline, but then of course when you turn to their consideration of criterion A they look at it in terms of the Origin destination market approach and they are considering the influence of both pipelines in the provision of services in the Sydney region.

MR BANKS: As I say, I think we could probably spend a long time exploring that but you've provided useful material to us, I think, for our deliberation, and we may

well at some stage get back to you as our own thinking develops on that.

MR WILLETT: Certainly.

MR BANKS: But would you say, in relation to those matters, that we now have a fairly settled judicial view or are we likely to see surprises?

MR WILLETT: I think the legal and economic principles that are applied to especially criteria A and B for both gas code coverage and declaration are well settled by the two tribunal decisions we've had so far. To the extent that there are difficulties associated with that Origin destination market analysis of gas pipelines, those problems are confined to the analysis of gas pipelines and are not readily transferable to other infrastructure services.

It would be difficult, for example, to say that the right way to analyse, say the provision of airline passenger services, was to compare all flights into Sydney or all flights out of Melbourne, which is basically the parallel to the sorts of analyses that's conducted through the Origin destination market approach. Although it's interesting to note that if I'm in Melbourne and I'm considering a holiday and I have available to me the possibility of a holiday in Brisbane and a holiday in Perth, and the package of flight to Brisbane and flight to Perth and staying in a hotel and doing some other things to have that holiday, those bundled products might indeed be substitutes to me, but that's a very different thing from saying that the flight from Melbourne to Brisbane is a substitute for the flight from Melbourne to Perth.

MR BANKS: You wouldn't be here today if you had gone to Brisbane instead.

MR WILLETT: Indeed. I think the usefulness of that sort of market analysis would merely provide a very good excuse to being late for meetings.

MR BANKS: We deviated from our game plan and probably should backtrack a bit to where we got to. John, did you - - -

MR COSGROVE: No, I was going to move on actually but to a point related to what we've just been discussing, and that's the inclusion in your draft submission, on page 17, of what the tribunal had to say in the Duke case. It's relevant to Gary's question about how settled is the body of law. In that quote you see at first that the tribunal is saying that the notion of promoting competition involves the idea of creating the conditions or environment for improving competition from what it would be otherwise. That seems to be a pretty easy hurdle to jump, yet later on at the very end of that quote the tribunal is saying:

> It is in this sense that the notion of promotion of competition involves a consideration that if the conditions or environment for improving competition are in enhanced then there is a likelihood of increased competition that is not trivial.
>
> So you get in that second statement more towards I think what we were trying

to capture in our proposed amendment of criterion A, something in the nature of likelihood of substantial increase in competition. It seemed to me that just within a single statement by the tribunal one could divine more than one interpretation and one wonders then how clear these legal precedents are really going to be.

MR WILLETT: Yes, I think the important point to note there is that what the tribunal is doing is expressing the test and also expressing a likely outcome from the satisfaction of that test. So in other words the test is focused on impediments to entry or barriers to entry, and they say, "Well, if this test is satisfied what you would expect to see - although you may not necessarily see it - is increased competition that is not trivial."
That is why they use the word "likelihood" because it's very hard to say that something is definitely going to increase competition in a measurable sense. It is for that reason that we have suggested if you are going to apply some sort of substantial increase of competition test, which presumably mirrors the substantial lessening of competition test in Part IV of the act, then you would want to focus on the likelihood of substantial increase test, rather than it would definitely lead to a substantial increase.

MR BANKS: Or "promoting" even I suppose is a less restrictive word than "lead to" - the existing words. It seemed, as we were chatting about this and looking at that test there, that to say opportunities environment for competition will be better than they would without it, doesn't necessarily mean - I don't think that does lead to a presumption of non-triviality, because you could argue that any provision of access will mean that the opportunities environment for competition will be better than they would otherwise have been, almost by definition, because you have allowed access. You are allowing potentially other players to come in who may not have been able to get in before, potentially.

MR WILLETT: I think that is going to depend on the conditions for competition downstream, or upstream, in the dependent market. What we saw in the Duke decision was the tribunal coming to a view that the eastern gas pipeline doesn't have market power in that dependent market and, as a consequence, access wouldn't be said to promote competition in that dependent market. So you are really looking at - in the application of that test - well, what's going on in the dependent market? What are the other sources of competition in that dependent market?

MR BANKS: Just on that, the conclusion in the Duke case that there wasn't market power in the dependent market, how much did that depend on the fact that the Moomba to Sydney substitute service, if you like, was itself covered?

MR WILLETT: That's an interesting question. The tribunal hasn't addressed that specifically or explicitly, I think, in the decision.

MR BANKS: Okay.

MR WILLETT: Certainly in the conduct of the hearing the presumption was the MSP was covered and there was explicit recognition of that during the conduct of the

hearing. But it hasn't translated to any explicit recognition in the decision.

MR BANKS: Okay. It wasn't clear to me, in reading the decision - and it's some time since I read it - whether that may have been a factor that weighed on the tribunal's mind.

MR WILLETT: It's very hard to say because it hasn't found explicit voice in the decision.

MR BANKS: Would it follow from that that things may not be as settled as you were indicating earlier?

MR WILLETT: In terms of?

MR BANKS: Just how the question of competition - how the criteria in A would, for example, be interpreted?

MS GROVES: I think the test is settled. I think its application to the particular factual situation that you will always get on a case-by-case of whether or not a market participant has market power will vary. But that is not to say that the questions asked and the approach taken to that analysis is not settled. We will get different results for different pipelines, or different railways, or whatever sorts of infrastructure we are talking about, depending on the factual circumstances that those market participants find themselves in.

In the Duke case the tribunal found that Duke didn't have market power in the downstream market - the south-east Australian gas sales market. It made no comment on the market power of other participants, and in fact it determined that it didn't think that Duke had market power because of the existence of other large players in that downstream market and the influence they have.

MR BANKS: Okay. You have a number of comments on our tier 2 proposals. Again, I guess we will take these on board in our thinking. I don't want to go through them in great detail here you will be relieved to know. You take us to task a little bit for using the concept of "economically feasible," which you don't think has much parentage. I'd appeal to clause 6, which you hold in high regard in other contexts as a source. But your point may still be right, that it is not all that well tested; indeed, clause 6 has other concepts like "effective competition" which could be problematic legally as well.

MR WILLETT: Yes.

MR BANKS: I wasn't sure of a couple of points where you seem to be implying that the commission had a concentration-type interpretation of competition. One of them is on page 28 where you say, "The notion of insufficient competition appears to encapsulate an approach to measuring competition which is rejected by the tribunal" - in favour of, you know, structural impediments to competition. I guess we didn't see it that way. I don't know whether there is anything you can elaborate on that

would support that point.

MR WILLETT: We'll have a look at that. There is nothing more I can say at this point, I should think.

MR BANKS: Okay.

MR WILLETT: It may have been simply our misunderstanding of what you intended.

MR BANKS: I suppose, again, our thinking in terms of this tier 2 proposal was not that we were getting something that was necessarily so different to the tier 1, the existing declaration criteria, but, rather, given the opportunity to have a clean sheet, how would we structure the intent of the existing arrangements in a way that we thought may have been more satisfactory. It was in that spirit that we put it forward.

MR WILLETT: Sure.

MR BANKS: We do agree - I mean, your bottom line there is I think how much benefit there is to be derived from a change in relation to what is already covered under tier 1, criterion A. You then, on page 29, talk about proposed criteria in D and you raise questions about - I mean, you say there's a question where there is a need to avoid small or negligible increases in efficiency and I think you make the valid point that as long as there is any increase in efficiency we are all better off and that you're preaching to the converted there. I guess the question is knowing when you have got an increase in efficiency and, within the world of perfect information, I would take a dollar improvement in our welfare.

That was the main reason for wanting something more than that: because the consequences that follow from the declaration decision aren't necessarily always predictable and therefore, in a state of uncertainty, putting more onus to find something that was significant just seemed to us to be worthwhile rather than denying that any gain in efficiency would be helpful.

MR WILLETT: Point taken. It did occur to me that that might have been what you intended. I think that is a question about whether you deal with uncertainty by raising the hurdle and how far, if you do, do you raise the hurdle. It may be that if you take that sort of approach to an extreme you make criteria like this simply unworkable, such that nothing is ever going to be satisfied by them, particularly in the context of going to the tribunal and having to prove these things. That can be a very difficult exercise, as I think experience to date has shown, so I do wonder about whether the appropriate response to that uncertainty is to keep raising the hurdle.

MR BANKS: Although we didn't fall into your trap here by saying "lead to"; I think we said "is likely to approve" so we had anticipated that problem, I guess.

MR COSGROVE: Down the bottom of 31, in your discussion of price monitoring, you have there in the second dot point, "to clear the infrastructure of service for price

monitoring for a period of time". I don't suppose it is possible to say very much about how long that period should be. In the context you have placed it here - either declaration, not declaration or in the middle - this price monitoring arrangement, does your experience lead you to give us any advice on that score?

MR WILLETT: I think our experience would simply lead us to the view that that is probably going to vary on a case-by-case basis. It depends on the circumstances, I think. If you were quite explicitly adopting a wait-and-see approach, then that might be a reason to make it a reasonably short period of time but sufficient time such that you could test whether competition in the dependent market had actually emerged or was likely to emerge.

MR BANKS: Yes. We have a difference with you, I guess, on the question of "arbitration to require extension or expansion". This is the point - page 33, page 34. Perhaps I may just give you the opportunity to maybe elaborate on that. The point that you have raised there which I haven't thought as much about before is whether it might have some effect on incentives. Perhaps just while I'm collecting my thoughts on that, I will just give you the opportunity to comment on why you think that would be, as you put it, a significant alteration of your current operation of Part IIIA and be problematic.

MR WILLETT: Why don't I do it by way of example. I think that would probably clarify this issue the most. We're talking about an expansion of capacity here. Let's envisage a vertically-integrated rail track, train operator who builds a piece of track in the expectation of running their own trains on it. They build passing loops specifically to their needs or, perhaps, very limited passing loops at all. What that would mean is that there would be very limited capacity available to provide access to anybody else because you couldn't operate more trains on the track, and yet the capacity of that track could be relatively easily expanded quite dramatically just by extending the passing loops a little bit.

We think in that sort of situation that there would be an opportunity for the infrastructure owner to alter readily or frustrate the intent of access regulation simply by designing the infrastructure in a particular way, such that they would then provide access on their own terms free of any access obligation under Part IIIA, simply because access was dependent on some expansion of their infrastructure; that expansion which would be done at much lower cost than the construction of substitute facilities.

Similarly, in the case of a gas pipeline, you can envisage the construction of a pipeline of a certain diameter with very limited compression. Compression can be added to a pipeline to increase its capacity relatively easily. Again, the intention of access regulation could be frustrated simply by the infrastructure owner designing the infrastructure in a certain way and only installing capacity when it has a contract on its own terms and conditions to utilise that expanded capacity. These are theoretical examples but there are actually some examples of this sort of issue arising around the country.

MR BANKS: We certainly heard this morning, in our discussion with Epic, about I guess their approach to regulation in just that way; that they were seeking to have foundation contracts that occupied the whole capacity of the pipeline.

MR WILLETT: Yes.

MR BANKS: I guess what we were feeling a bit nervous about was an escalation of intrusion in a regime of this kind, where you are suddenly - I mean, it is almost to the point where you may as well nationalise the facility because you're actually taking the investment decision away from the owner of the facility, so it does come down to, I guess, a question of the costs and benefits of that kind of escalation.

MR WILLETT: Indeed, and I think a recognition that some of this expansion of capacity can be carried out quite easily.

MR BANKS: Yes.

MR WILLETT: In fact it is almost a standard operating procedure for infrastructure of this sort to meet increased capacity needs in a relatively easy and straightforward way and, in those sorts of circumstances, we do question whether there is any value in distinguishing between spare capacity and developable capacity.

MR BANKS: Yes.

MR WILLETT: I think extensions of infrastructure are in quite a different category and, generally, in terms of geographic extensions of infrastructure we would see the appropriate approach would be simply to provide for interconnection, but there might be some cases where even geographic extensions could be conducted by the incumbent infrastructure owner at much less cost than any other prospective entrant. Perhaps a good example is infill of a distribution network, gas or electricity, where it might be much more costly for someone other than the incumbent infrastructure owner to provide that geographic extension of the infrastructure.

MR BANKS: Yes, okay.

MR COSGROVE: Remind me: there are enforcement mechanisms, are there, to deal with a situation in which this provision was invoked by the ACCC and the access provider said, "No, I'm not going to do it"?

MS GROVES: Extensions are explicitly recognised as one of the matters the ACCC can consider within an arbitration determination, and expansion is not excluded as one of the matters that the ACCC could consider. That would be the enforcement mechanism. There are some qualifications on the ACCC's ability to order things under those sorts of arbitrations; for example, for extensions. They can't require the service provider to pay for that extension and they can't make a determination that would somehow or other see the property rights in the facility being altered away from the current owner through some sort of determination that might be affected by extension.

Those limits aren't on the ACCC's power to make a determination in respect of expansion, as such. They might look at the same sorts of considerations. We don't know because they haven't been required to deal with those matters.

MR BANKS: What would be the logic in that, if any?

MS GROVES: The logic in?

MR BANKS: In those provisions in terms of property rights and a question of who pays.

MS GROVES: I'm not sure that there would be any logic in those same sorts of guiding disciplines over the ACCC's determination applying to expansions and extensions, but we'll think about whether there are any other consequences. It may be because it's not quite so easy to determine the cost of expansion and who should pay as it would be for an extension. I mean, extension is another bit added on and you can just see where it interconnects and it's a whole new thing and it may be extended for a particular customer.

Expansion has the ability to benefit a whole range of people, not just the person who is part of the arbitration determination at that time, and expansion may actually increase the capacity of a pipeline considerably, so there may be some of those sorts of considerations that would lead to the suggestions that the current arbitratee should not pay fully for it. There are concepts of prudent investment and those sorts of things but, at first instance, you can't see why similar criteria or similar bindings on the ACCC should not perhaps be applied, but we'll have further thought about that.

MR BANKS: Yes. I am conscious that time is moving by so we will try to be brief but, on page 37, you say the council supports - at least in this draft submission - those proposals requiring Commonwealth access regimes to be submitted for certification. You were here when the Western Australian government expressed great reservations about that, I think perhaps primarily because of - well, partly precedential effect I suppose on the state situation, but also they thought perhaps leading to some illegal uncertainty about the status of those regimes in the interim. I don't know whether you might take that on notice as to whether you would respond to those concerns - which are in their submission, I think.

MR WILLETT: Certainly. It might be worth noting at this stage that the certification process or the consideration of whether an access regime is effective even at a state and territory level doesn't call into question the legal effect of that access regime. It is still state and territory law.

MR BANKS: Right.

MR WILLETT: The only consequence in terms of state and territory access regulation presently is that, without that regime being effective against the clause 6 principles, the services regulated by that access regime - is a minimal declaration.

That's the only work that the test of effectiveness does.

MR BANKS: Yes, except in the state domain because there is not a requirement to have the regime certified, I guess the status of it uncertified is more secure perhaps than if there was a requirement in legislation for certification that hadn't been fulfilled - maybe raise more doubts but any further thoughts - - -

MR WILLETT: Okay. I understand that point and we'll give it some thought.

MR BANKS: Yes. It hadn't occurred to us but it was raised by Western Australia. They also, as you would have heard, had major fundamental concerns, I guess, about provisions that they saw as diminishing the role of the state governments and indeed clause 6 - the role of clause 6 - including the certification principles in Part IIIA - was one of those. You have said that it would be appropriate for the state and territory governments to be consulted in respect of the necessary amendments. I would be interested in any kind of assessment you had of how that might be received. We know how it would be received in Western Australia, but I don't know if there is any basis for you to comment on that.

MR WILLETT: I think we might take that one on notice, too.

MR BANKS: And you may not wish to answer it. It is interesting that we haven't had - - -

MR WILLETT: I guess that comment that you draw upon is a fall-back position from our first position, which is that we didn't support building the clause 6 principles into Part IIIA and we have said there is some benefit in providing more guidance on the principles to be applied in arbitration and undertakings, but that is different from saying that you should apply the clause 6 principles to both of those processes as well by building them into Part IIIA.

MR BANKS: I see, yes. I am sorry, I misread that last paragraph. Okay.

MS GROVES: When we were talking consultation with the state and territory governments it was more in recognition of the inclusion of an overarching objects and pricing principles clauses that are to discipline not only undertakings and arbitration - the exercise of regulatory discretion under arbitrations and undertaking processes, but presumably it is also to exercise the discipline on the council and the decision-maker in determining whether or not state regimes themselves are effective. If that is to be the case, then that would need to be taken into account when discussing that with the state and territory governments.

Even though it's a change that the Commonwealth can make unilaterally by just including it in Part IIIA, because it may affect at some level the balance of the clause 6 principles which are part of the more cooperative federalism approach to access regulation, we think it would be important that state and territories were comfortable with those objects and pricing principles being also some sort of overarching construct over certification.

That being said, we don't actually think at this point that both of those would alter the sorts of regimes that the council has considered and the minister has certified. We think they are entirely consistent with the approach taken by decision-makers to date in consideration of effective state and territory access regimes.

MR BANKS: Okay, thanks for that. In your discussion of the role of ministers you clearly weren't attracted to the argument that we had in our report, to the extent that I guess political will is reflected in the declaration criteria, and to the extent that they are reasonably clear, that that has been satisfied in a sense and it could be delegated to the regulator to make those decisions. So is it implicit in what you're saying here that there is sufficient discretion and you'd want to retain that discretion; that ministerial involvement would still be important?

MR WILLETT: I think there is some merit in retaining that role, given that in our view the policy considerations in relation to Part IIIA aren't completed with the enactment of Part IIIA, that coverage decisions are policy decisions in themselves.

MR BANKS: Yes, they are policy decisions but they are policy decisions that have significant guidance, don't they, through the criteria that are within the legislation that essentially parliament has enacted? Other points that have been made about some of the significant areas of discretion within those criteria - for example, the national significance test which has a subjective element to it, a particularly subjective element to it, I guess - and the public interest test is another one.

My understanding is that that hasn't been actually invoked, but you might want to comment on that. They are two areas in particular where you would see a legitimate claim on the minister to have final say, or at least have a say - it's not the final say. To what extent has the public interest test applied in relation to national access?

MR WILLETT: By applying you mean making a difference in - - -

MR BANKS: Being activated, or at least being used.

MR WILLETT: I can't think of one application. We'll need to check. It hasn't made a difference in terms of recommendations by the council.

MR BANKS: No.

MR WILLETT: But it may have in terms of the minister's decision.

MR BANKS: But it could have been in terms of the minister's rejection or - - -

MR WILLETT: Yes.

MR BANKS: Indeed.

MR WILLETT: I think possibly the Carpentaria decision as well, but we'll check on those.

MR BANKS: I would be interested to see that.

MR WILLETT: Yes.

MR BANKS: Okay. Under the section on review and appeals you say:

> Any attempt to restrict the discretion of an administrative body by tightly constraining jurisdiction would substantially increase the rule of jurisdictional challenge in the courts and undermine the benefits of administrative processes.

I think I agree with you, but I'm not sure in the sense that - does it all hinge on the word "tightly"? Presumably if delegation is provided with no guidance, no legislative standards to guide the administrator, then equally there's no basis in terms of appeals for the administrator's judgment to be tested. Ultimately it has to be tested by a perception of the will of parliament, which requires some guidance. So you are not saying here that you want unfettered or you see unfettered discretion as being a desirable characteristic. I'll give you an opportunity to comment on it anyway.

MR WILLETT: Yes, the point is simply that there is a risk that if you do constrain discretion by constraining jurisdiction you increase the prospects of jurisdictional challenge. We have had some examples of jurisdictional challenge that relate to the exemptions from the definition of service in Part IIIA. There is also a separate risk that if you limit the merit appeals process you also increase incentives for either jurisdictional challenge or administrative law challenge.

MR BANKS: Yes.

MR WILLETT: Because those options are still available and might be sought out by a party if a merit review was not appropriate or not available.

MR BANKS: Yes, I take that point. I think that is a useful point. In a sense you create an incentive to use what opportunities were available for getting satisfaction.

MS GROVES: I think you might also lose the benefit of being able to dictate that those sorts of issues are normally resolved by specialist tribunals, for example, who have particular skill sets in looking at these sorts of issues - the Competition Tribunal versus a Supreme Court or something like that.

MR WILLETT: Okay.

MR COSGROVE: I have a general overall question related to your presentation to us and that is I have the impression that you are generally in favour of leaving a fair degree of discretion in the hands of administrators and regulators, whereas from the

point of view of the people who are potentially going to be subject to this form of regulation, they might see a better situation - from their point of view - as being one in which there was a greater degree of guidance, if not specificity actually set down in the regime's operating principles. I don't know whether you see it that way yourself, but it's a contrast which I think has come through from the other submissions that have been presented to us during the course of these hearings.

On the whole the access providers and I think, too, the access seekers have been indicating that they would like to know more clearly how particular situations are likely to be dealt with, rather than leaving a fairly high level of discretion in the hands of the people who are making the decisions.

MR WILLETT: Yes, I am not sure that I'd go quite as far as your comments have reflected, John. Certainly we're not arguing for increased discretion in any of these sorts of processes.

MR COSGROVE: No, I agree, more a maintenance of what is there at present.

MR WILLETT: Yes, I think we're making the point that administrative institutions like the NCC and the ACCC are beneficial because they have flexibility and they are investigative bodies and they have some discretion and that makes for the efficient settlement of a lot of issues. But, at the same time, you need to make sure that the exercise of that investigation and discretion is accountable and you want to make sure that the institutions that are exercising that discretion have the right sort of focus and the right sort of incentives on them to make the right sorts of decisions.

So clearly delineating roles for those organisations is important. Setting appropriate review and appeal mechanisms on those decisions is important. I think it's a bit risky to say, "Look, we'll compromise on one of these things by tightening up on another," because I think you lose something in that. You lose some of the benefits of having these matters dealt with by administrative bodies in the first place who are focused on a particular job, if you try to compensate for the loss of accountability mechanisms by tightening their degree of discretion. I'm not saying that you need to maximise discretion or increase discretion, but there is a balance in all these things and it's very hard to trade off one against the other.

MR COSGROVE: Although you'd want accountability, whatever the level of discretion available, wouldn't you?

MR WILLETT: Indeed. That's right.

MR COSGROVE: I'm not sure that's a factor which would lead you in one direction or the other.

MR WILLETT: In terms of restricting the availability of review or appeal, or changing institutional arrangements to combine processes and seeking to compensate for the loss of delineated roles or loss of accountability mechanisms by tightening the

exercise of discretion, my point was that trying to make those sorts of trade-offs can indeed be problematic. You might be losing something across the board by making those sorts of trade-offs.

MS GROVES: A couple of specific things also flowing through some of the things that I've heard sitting through the several days of hearings were particularly from infrastructure service providers. I think you see it most in the capped case of gas pipelines, for example, where infrastructure service providers are seeking some form of certainty of outcome - although that's not necessarily, I am saying, being driven by, "We need more prescription." Their experience is in fact the exact opposite.

What they're saying is, "We need more certainty that we - greenfields pipelines in particular - need to be dealt with in a particular way. We actually would prefer, for example, to use what on the face of it is a very wide discretionary regulatory process, the undertaking process, with very few constraints at all currently on the ACCC in being able to determine what sort of things should be in that undertaking," versus what they see as a more prescriptive model with more constraints on the ACCC in accepting an access arrangement under the gas code.

I don't think it's a simple dichotomy to say - it's not as simple to say that service providers' desire for increased certainty of particular types of outcomes can in fact be delivered by removing or limiting the discretion and making things more prescriptive. At least in the case of gas pipelines, which is the area I know, they're in fact saying to some degree the opposite and have been seeking support for mechanisms to ensure that the more general, less prescriptive avenues are left open to them.

MR COSGROVE: I'm not sure about that. At least in the Part IIIA context there have been no undertakings, have there? Of course, in part people are not quite sure what the ACCC is requiring.

MS GROVES: But the Australian Pipeline Industry Association has told the National Gas Pipelines Advisory Committee - as well various individuals of their members - "We want to be able to use that mechanism or a mechanism similar to it rather than the more prescriptive approach of the regulators under the gas code." They don't see that the certainty that they want is delivered through a more prescriptive regime. The certainty they want is delivered through an increased amount of discretion, or the possibility at least of the certainty, because one hasn't gone through the process. We don't know whether or not that outcome will deliver what it is that they're looking for, but they're seeking to be able to test that possibility.

MR BANKS: It may well be that the prescription they have is just in the wrong direction and it's a prescription that they don't like and so anything else is better than that. The points you make are useful and we'll think about them. I think we've detained you long enough, although you are trapped here in Perth - which is a very nice place to be trapped - overnight anyway. Thanks very much. I don't know if there are any final comments you want to make.

MR WILLETT: No, I think we've covered all we wanted to cover today, thanks, Gary and John.

MR BANKS: Good. Thank you for that. We look forward to having the final submission and perhaps elaborate it in a couple of ways that we talked about. That would be very useful.

MR WILLETT: Indeed, if there are other areas where we might be of assistance, by all means contact with us and we'll do what we can.

MR BANKS: We'll certainly do that. Thank you.

MR WILLETT: Thanks again for the opportunity to appear today.

MR BANKS: I'll just ask, for the record, if there's anyone else who would like to appear. No-one else put their hand up. This being the final session of this round of hearings, it just remains to thank everybody who has participated in the hearings. We have really benefited enormously from the discussion we've had about the submissions and it's helped us to get to the stage where we could move on to produce a final report.

Any further submissions people may have should get to us by the end of June, if possible. Indeed we'll be seeking to have our final report in the hands of the government in September, as I indicated, along with the final report on the telecommunications regulation. It's then up to the government, within certainty statutory constraints, to choose the timing of the release of that report. With that, my colleague and I thank everybody and we close the hearings. Thank you.

AT 5.42 PM THE INQUIRY WAS ADJOURNED ACCORDINGLY

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