

25 February 2004

Productivity Commission
Locked Bag 2 Collins Street East
Melbourne VIC 8003

email:gas@pc.gov.au

Dear Sirs

REVIEW OF THE GAS ACCESS REGIME, DRAFT REPORT

Origin Energy (Origin) welcomes the release of the Review of the Gas Access Regime Draft Report and provides the following comments as a further contribution to the consultation process.

Rather than respond to all of the draft findings and recommendations listed in the draft report Origin intends to comment on those recommendations that relate to specific issues raised by Origin in its response to the issues paper. These are discussed briefly below.

1. Coverage Criteria - (Recommendation 6.3, 6.4, 6.5)

In its previous submission Origin noted its support for the existing coverage criteria particularly with regard to small distribution networks. Nevertheless, Origin also suggested that the criteria for coverage could be clarified to recognise that in some circumstances an unregulated pipeline despite having 'natural monopoly' characteristics (and thus meeting the uneconomic to develop criterion) may still enhance, or at least not distort, competition in related markets. The Tribunal duly recognised this distinction in its decision on the Duke Eastern Gas Pipeline (EGP); and so too has the Commission in chapter 2 of its draft report. Both also identified that the "promotion of competition" criterion was excessively broad and thus set too low a benchmark for the application of coverage.

Recommendations by the Commission:

- *Section 1.9(a) of the Gas Code (the first of the coverage criteria) should be amended such that access (or increased access) to Services provided by means of the Pipeline would be likely to have the effect of increasing competition to a material degree in at least one market (whether or not in Australia), other than the market for Service provided by means of the Pipeline".*
- *Section 1.9(c) (access provided without undue risk to human health or safety) should be removed from the coverage criteria of the Gas Code.*
- *The coverage criteria in section 1.9 of the Gas Code should include a new test namely, that coverage of the pipeline is likely to improve efficiency significantly.*

Origin agrees with the Commission that these recommendations improve the coverage criteria as they, correctly, raise the bar for the application of coverage and also make explicit that it is 'actual' competition rather than 'conditions' conducive to competition, which should represent the appropriate benchmark for analysis.

Such a change in legislative effect would also bring the competition test within the Code more in line with section 50 of the TPA. Origin also supports an overall objective in the Code for coverage to be applied only where it generates a significant improvement in efficiency. This is important, because this acknowledges that regulation can also impose significant costs that must be weighed against any perceived benefits. An efficiency criterion also recognises that it is net market benefits, or increases in consumer and producer surplus, rather than transfers between the two, which should provide the focus of regulation.

Nevertheless, Origin has some concern with the legal scope and practical content of the competition test in 1.9(a). While it may be somewhat straightforward to make a legal distinction between either “material” or “substantial” competition relative to no competition; the perceived separation of intensity and scope between material and substantial would appear to be much less obvious. This lack of clarity is important; because each threshold implies a substantive change in regulatory regime with associated changes in commercial impacts to participants.

In Origin’s view this could add to regulatory risk and open the process of coverage to disputes, clearly not what is intended with proposed changes to this provision. We would therefore urge the Commission to provide a greater level of content to 1.9(a) with a list of guidelines or criteria which clarifies the circumstances under which each threshold would be applied.

Origin also agrees that safety and health risk issues are more appropriately managed through other regulatory instruments.

2. Investment and Access Arrangements - (Recommendation 9.1)

Origin suggested that binding arrangements (coverage and regulation) would encourage pipeline investors by removing the regulatory or sovereign risk facing a greenfield pipeline over much of its useful life. Based on project financed pipeline experience, Origin supported the implementation of a 20 year access holiday for new pipeline developments. Origin acknowledged that a binding ruling of this term may place participants at risk if significant changes occur to market conditions and no mechanism exists to establish additional pipeline services. However Origin suggested that major changes to market conditions are unlikely to occur during the initial binding periods.

Recommendation by the Commission:

*“The Gas Access regime should be amended so that the NCC on request from a potential pipeline investor can provide a binding ruling on coverage. A binding ruling in favour of lighter handed monitoring should be of the same duration as the minimum period for lighter handed monitoring under the regulatory coverage test (five years). A binding ruling that a pipeline would not be covered should apply for **15 years**. These rulings should not be revoked unless the information relied on by the NCC is proven to be false or misleading”.*

Although the recommendation by the Commission goes a considerable way towards providing certainty for pipeline developments under binding rulings, Origin’s experience is that these projects are financed over a period of 20 years rather than the recommended 15 years.

3. Objectives and objectives clause - (Recommendation 5.1, 5.2)

Origin recognises the difficult balance that an access regime must achieve in providing efficient short term prices for transmission users while ensuring those prices also provide for long run cost recovery and an appropriate margin for risk. An excessive focus on short run efficiency objectives which equate prices to marginal cost may be incompatible with ensuring the long run viability and investment incentives for pipeline owners.

Origin agrees that the gas access regime should appropriately reflect this dichotomy and, on this basis, supports the inclusion in the Code of the overarching objects proposed by the Commission:

“To promote the economically efficient use of, and investment in, the services of transmission pipelines and distribution networks, thereby promoting competition in upstream and downstream markets”.

A second recommendation was made that the objectives in the preamble of the existing legislation and related objectives in the introduction to the Gas Code should be deleted to avoid overlap and confusion with the principal objective. Origin supports these deletions.

Origin looks forward to participating in the public hearings over the next few months and the release of the final report by the Productivity Commission in June 2004. This submission may be published on the Commission’s website.

Yours faithfully

Tony Wood
General Manager
Public & Government Affairs