

26 September 2002

The Hon Warwick Parer
Chairman
CoAG Energy Market Review
GPO Box 9839
Canberra ACT 2601

Dear Mr Parer

I am writing in response to the letter from Mr Page of 9 September regarding APIA's claims about the adverse implications of the National Gas Pipeline Access Code on gas transmission pipeline development. I welcome his advice that the Panel is viewing this issue as a serious matter.

As discussed by telephone with Mr Page, APIA is concerned that the Panel may be adopting a very narrow view on this issue by virtue of its request for details on those projects that are not proceeding solely because of the current Code.

To the best of my knowledge and recollection APIA has not, at any stage, indicated that potential pipelines are not proceeding solely because of the Code. More importantly for the review, APIA seriously questions whether the question as proposed is even relevant to a "*properly informed assessment of the claims and counter-claims*" as referred to in Mr Page's letter.

APIA has always maintained that there is a suite of issues that represent (or have in the recent past represented) barriers to transmission pipeline development including:

- The distance between major uncommitted gas resources and major markets (an issue addressed by the industry, including through APIA, by a research and development program aimed specifically at reducing costs);
- Competitiveness of natural gas as a fuel alternative/market development (essentially a market issue, but with issues such as wider producer competition and producer pricing behaviour a relevant factor);
- The new effective life tax depreciation regime (largely addressed through the new capping mechanism);
- Delays/uncertainties caused by inefficient and time consuming land and technical/licensing approvals in a number of jurisdictions (a matter under discussion between APIA and most jurisdictions); and
- Adverse implications of the Code for investment (an issue recognised by the Productivity Commission in its review of the National Access Regime).

Transmission pipeline development projects represent examples of "essential" infrastructure which present, even under favourable circumstances, marginal economics for those who make the decision to go ahead or not go ahead with the investment. There are clearly a range of factors at work - and APIA by virtue of its activities on a range of issues as reflected in its Business Plan 2002 - 2005 (October 2001) has clearly stated this to be the case.

APIA finds the very narrow nature of the question Mr Page has posed on behalf of the Panel very disturbing. This approach is very much at odds with the approach taken on other policy issues this Association has been involved in over recent years. For example, at no stage during the long process relating to consideration of "effective life" relating to the tax depreciation regime was APIA ever asked to point to projects that "*...are not proceeding solely*" because of the proposed 50 year tax life. However, this did not act as any barrier to identifying the issue as a major and legitimate concern requiring policy attention. This lack of "proof" did not act as any impediment to identification of the imminent "effective life" regime as a barrier to pipeline investment, nor did it act as any impediment to the positive policy response that was judged necessary by the Commonwealth Government (and supported by most jurisdictions). In the case of the effective life regime evidence was presented that the proposed measure would have an adverse impact on development activity; at no stage was there proof that projects would not proceed solely because of the proposal.

The case for urgent action in relation to the gas access regime is in our view more compelling than the "effective life" issue:

1. The major transmission pipeline development which has taken place since introduction of the Code has occurred (contrary to the implication contained in the NCC's submission that the Code has stimulated pipeline development activity) outside the Code based on commercial, owner offered tariffs; and
2. There are very clear signals from senior executives of pipeline companies and the investment community that "Code based" solutions are a major impediment for pipeline development.

Yesterday's decision by the Tasmanian Government to terminate the Gas Distribution and Retail tender process in that state adds further weight to the concerns we have consistently expressed in relation to major pipeline development activity. The Tasmanian Deputy Premier noted that the gas reticulation project was the first attempt to run a large scale tender under the National Gas Code.

The Deputy Premier also stated:

"Other jurisdictions are having problems with the Code and it is clearly not workable, particularly for large-scale greenfields developments." (underlining is my emphasis).

APIA agrees with this assessment, but would also point out that the issue for so called "greenfield" pipelines is part of a wider issue of inappropriate regulatory behaviour leading to negative sentiments towards gas transmission investment by regulated companies in general.

Let me also draw your attention to the following statements, including by CEO's of "merchant" pipeline companies which provide, in APIA's view, very clear and compelling evidence that the Code has acted as a major impediment to timely and efficient transmission pipeline development.

"Regulation of access to gas pipelines in Australia has been implemented in a manner inconsistent with the -light handed" approach originally envisaged by policy makers, and this implementation potentially imposes significant costs for the economy in the form of lost investments. Duke Energy International will not invest in any further pipeline developments in Australia until regulatory certainty is achieved."

Ms Julie Dill, Managing Director Duke Energy International, ACCC Conference 26 July 2002

"The present arrangements must be changed if we are to continue to pursue major Greenfield projects such as the Timor Sea or PNG projects. For such projects, we and our financial partners need the certainty that comes from long term, negotiated foundation contracts before we commit, and we need to be certain those contracts will not be second-guessed 5, 10 or 15 years down the road. "

Mr Jim McDonald, Chief Executive Officer, Australian Pipeline Trust Address to Unit Holder Information Meeting 24 October 2001.

"As far as Epic Energy is concerned, one of the most critical areas that needs addressing relates to the third party access regulatory frameworks implemented by CoAG, in particular the National Third party Access Code for Natural Gas Pipelines Systems ("National Gas Code"). It is this area that is having the most profoundly adverse impact on investment incentives. These frameworks and their application are giving rise to not only unacceptable levels of regulatory risk but also sovereign risk for investors. These risks will not only adversely affect future investment decisions to be made, but they are also affecting current investment decisions being made by incumbent owners and investors, at least in the gas pipeline industry.

As an example of the level of regulatory risk facing investors in the gas pipeline industry, when developing Epic Energy's proposal to bring Timor Sea gas to south-eastern Australia - 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.

Epic Energy Submission to National Energy Policy Review, 5 June 2002

You will appreciate that private companies are restricted in their ability to share future strategic investment plans in the pre-development phase because of the commercially sensitive nature of their plans. This arises because the transmission pipeline development sector is fully contestable at the pre-development phase, for example as evidenced by a number of competing pipeline development projects in Northern Australia. The specifics of individual projects are not a matter for APIA to report to a Government Committee in open session, nor does it represent information shared by companies with industry associations. Whilst it would be open to the Committee to seek confidential briefing from the various commercial parties contemplating development, the statements above make it clear that the Code already represents a major barrier to efficient transmission pipeline development.

APIA trusts that the CoAG Energy Market Review Panel, in the course of its investigation on this issue of the performance of the Code and the views and counter views regarding the role of the Code, is also making inquiries with other parties, including those named in the APIA submission of 3 September, as to whether the Code has stimulated pipeline development or whether, as ARIA asserts, this development has been the result of commercial arrangements and contracts with major gas users and cannot be attributed to the Code.

Yours sincerely

Allen Beasley
Executive Director

Cc Members of CoAG Ministerial Council for Energy