

EMAIL

Attention: Tony Hinton

Tony,

You will recall that at the Productivity Commission's Public Hearing in Sydney on 19 September 2003, Julie Dill - Duke Energy International's Managing Director - stated that DEI would not invest in any further pipeline developments in Australia until regulatory certainty is achieved. Julie initially made this statement at the ACCC Convention on 26 July 2003. As requested, I have attached a copy of Julie's presentation as input into the Review of the National Gas Access Regime.

Please give me a call should you have any queries with respect to this matter, or should you wish to speak to me more broadly about any matters arising out of the Review.

Regards

Stephen Livens
Senior Regulatory Analyst
Duke Energy International
Tel: +61 3 9685 1061
Fax: +61 3 9685 1001
Mob: 0408 072 428
E-mail: slivens@duke-energy.com
Web: <http://www.duke-energy.com.au>

(See attached file: Julie Dill speech to ACCC Convention 26-07-02.doc)

ACCC Conference, Friday 26 July

Speech: Julie Dill

Natural Gas Pipelines in Australia

Letting the market work

Thank you for the opportunity to speak today on Duke Energy International's approach to management of its pipeline assets. As you would well know, Australia's gas industry has changed radically in the past five years. Former state-owned monopolies have been broken up and sold to private enterprise, customer contestability has been introduced in some states, and the new environment is demanding greater domestic gas exploration to meet growing energy needs.

However, the change process has had many problems. Full retail contestability is behind schedule and has stalled in some states, and the gas industry's development is in danger of falling short of government objectives without further intervention. Additionally, energy infrastructure owners face tax and regulatory risks which are changing the complexion of investment and development of energy infrastructure.

This morning I'd like to cover three areas: firstly an update on our portfolio including the Tasmanian Gas Pipeline; an overview of the issues facing pipeline owners in relation to the current regulatory environment; and finally I'll outline a solution which I hope will provide a mutually beneficial framework for alternative compliance.

Duke Energy International has invested more than \$2 billion in this region since 1998 when we acquired the 627km Queensland Gas Pipeline which delivers gas to major industry in Gladstone and Rockhampton. In early 1999 we acquired a share in the Goldfields pipeline and we bought the rights to develop the Eastern Gas Pipeline - within 18 months of that purchase we were delivering a new and reliable source of energy to Victoria and New South Wales via this \$450 million pipeline. The project brought competition to Sydney for the first time. While construction of the Eastern Gas Pipeline was underway, our commercial group was working hard to prove the feasibility of developing a subsea pipeline and onshore laterals for the Tasmanian market. As you're aware construction of this \$400 million pipeline is nearing completion and gas will be delivered to the island state in the coming weeks.

We have been extraordinarily busy in recent years and equally, we've been diligent in our commitment to building much-needed energy infrastructure for Australia. But we don't pretend for a minute that it's been easy or that the development of these assets is a short-term exercise. Growing industry around greenfields energy developments is capital and resource-intensive and requires a long-term approach. For these reasons, Australia has too few willing energy infrastructure investors

The complexity of developing pipeline projects is well documented. Companies like Duke Energy will take the risks but must be certain in the knowledge that the risk

versus reward proposition is fair. In this regard, DEI does not believe that regulation has provided the consistent environment required for invest. 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. And we’re not alone in adopting that position.

The modern form of statutory access regulation in Australia has only existed since the mid-1990s. During this time, however, regulation has expanded dramatically and, in many cases, evolved into forms that were not originally contemplated. From the relatively “light-handed” access regulation originally envisaged to apply to “essential facilities”, there is now a more “heavy-handed” or prescriptive approach applied in some cases to infrastructure that does not even constitute an essential facility.

I commend the ACCC for acknowledging the concerns of the pipeline industry through the Draft Greenfields Guideline. **The Guideline acknowledges the special set of circumstances surrounding greenfield assets, that is, that greenfield pipelines pose significant construction risk, financing risks and demand risk for the owner. The guidelines also acknowledge the need for greater certainty surrounding regulation at the time of a company’s investment commitment. There does however exist practical problems with that theoretical model proposed.** The guideline does not succeed in making the fundamental break from the current framework which is required to ensure the ongoing development of the natural gas pipeline network in Australia. Further, the problems caused by the regulation of existing assets and the impact of such regulation on potential competing pipelines has not been addressed and still exists. **We plan to prepare a full submission in cooperation with the pipeline industry to address our concerns regarding the proposed approach. Fundamentally the pipeline industry does not believe that the current application of the Code is appropriate for greenfields pipelines.**

The current form of regulation acts as a real and serious constraint on a company’s willingness to invest in new facilities, and on their ability to maintain the investments they have made. Consequently, many operators of essential facilities are now seeking a return to a more light-handed regulatory framework – one that achieves the objectives of essential facility regulation, but at a greatly reduced cost to themselves, government and consumers.

We are firmly of the belief that the “self-regulatory” approach to providing access, which characterises operation of our Eastern Gas Pipeline, aligns more closely with the original philosophy of access regulation. This will result in greater benefits for consumers in the long term. Duke Energy International has adopted an innovative approach and has a solution which we believe will meet the needs of all parties. We are committed to a philosophy of open, transparent and non-discriminatory access by third parties to our pipelines that is, arguably, far more “pro-competitive”, and

certainly more flexible, than the existing Code arrangements. Our Non-Discriminatory Access Policy has been developed to demonstrate our commitment to transparent, even-handed operation of our unregulated pipelines.

The eight Key Principles of our policy are:

- ❑ To develop and promote effective pipeline services with market participants in response to market needs.
- ❑ To ensure that all customers can be certain that they have equal access to the tariff for a given service offering.
- ❑ To promote transparency in the market by assuring all participants that there is no preferential treatment of our associated companies.
- ❑ To assure all market participants of the non-discriminatory nature of our service offerings by ensuring ready and equal access to key service information.
- ❑ To provide customers with certainty that confidential commercial information will only be used for the purposes for which it was provided.
- ❑ To enable customers to use and freely trade pipeline services.
- ❑ To provide a high degree of transparency to all market participants as to the extent of our compliance with these Principles.
- ❑ To provide all customers or prospective customers with the confidence that in the event of a dispute they would have access to independent arbitration.

DEI's arrangements are not only more cost effective than the more heavy-handed alternatives, but are considered essential for the effective management of our commercial risk in the marketplace. We believe this approach will produce an environment more conducive to entrepreneurial investment in the gas industry. Perhaps most importantly, these arrangements avoid the distortions inherent in the more heavy handed forms of regulation that are currently applied.

The Code is overly prescriptive and restrictive. Regulation of pipelines such as the Eastern Gas Pipeline must recognise the risks inherent in building infrastructure with excess capacity to accommodate future growth. Under our non-discriminatory access approach, the EGP provides access to third parties and delivers competitive and innovative services that facilitate growth, a necessity with infrastructure such as the Eastern Gas Pipeline, which needs to grow its market. Traditionally in Australia we have seen monopoly situations and regulatory regimes which preclude the market having access to comprehensive information and to the best or most appropriate services. Our intention is to create a framework for breaking away from that rigid system.

I would like to table Duke Energy International's Non-Discriminatory Access philosophy as a real and workable alternative to the current costly, heavy-handed regulation. We are operating the Eastern Gas Pipeline according to this well-

documented approach and we intend operating the Tasmanian Gas Pipeline in the same way. It is my firm belief that if a company is operating competitive, non-discriminatory, open access infrastructure without being covered by the Code, then regulation should not apply. Why impose the burden of costly and prescriptive regulation when the desired affect can be achieved through a behavioural system such as the Non-Discriminatory Access approach. We've proven its success in the two years of EGP operations and we remain hopeful that it will become common practice. Our approach and development of the non-discriminatory access principles and supporting systems puts in place a framework whereby customers, regulators, industry, government and other interested parties can observe our behaviour and performance due to the transparency of the systems and operations we have established. We are committed to continuing to operate responsibly and will demonstrate this through our actions. I remain hopeful that this approach will ensure development of an industry which offers more innovative, customer-focussed and competitive services without need for the burden of costly economic regulation. I feel certain that such an approach will also encourage investment in infrastructure, enhancing competition and economic growth for Australia.

Copies of Duke Energy International Non-Discriminatory Access Policies and approach are available here today. Thank you.