



27 February 2009

Regulatory Burdens Review  
Productivity Commission  
GPO Box 1428  
Canberra City ACT 2601

Via email: [regulatoryburdens@pc.gov.au](mailto:regulatoryburdens@pc.gov.au)

Dear Sir/Madam

**REGULATORY BURDENS – SOCIAL AND ECONOMIC INFRASTRUCTURE SERVICES**

The Australian Pipeline Industry Association (APIA) welcomes the opportunity to make a submission to the Productivity Commissions Annual Review of Regulatory Burdens, this year focussing on social and economic infrastructure services.

The energy supply industry is one of the most heavily regulated industries in Australia. APIA representing the gas transmission sector, in this submission presents examples of regulatory burden and comments on the general approach, or philosophy, adopted by regulators of the energy supply industry.

In particular, APIA would like to draw the Commission's attention to the sections of this submission dealing with the use of information gathering powers by energy regulators and the approach of Government when consulting with industry.

We look forward to your response to our submission.

Yours sincerely

CHERYL CARTWRIGHT

Chief Executive

## Introduction

The Australian Pipeline Industry Association (APIA) welcomes the opportunity to provide input to the Productivity Commission's Annual Review of the Regulatory Burdens on Business, which in 2009 focuses on social and economic infrastructure services.

APIA is the peak national body representing the interests of Australia's transmission pipeline sector. APIA's current membership is predominantly involved in high-pressure gas transmission. APIA's members include contractors, owners, operators, advisers and engineering companies and suppliers of pipeline products and services.

APIA's members own, operate and service the gas transmission pipelines that supply today's gas market and are likely to be the key investors in new pipelines and capacity expansions of existing pipelines that will be needed in order to meet the growing needs of the energy market over the next 20 years and beyond. This investment in transmission pipeline infrastructure will be essential to Australia's economic growth and as part of Australia's strategy for reducing its greenhouse gas emissions.

Clients of APIA's member's assets include some of Australia's largest companies, including, BHP Billiton, Origin, TruEnergy, Santos, Woodside, Xstrata, ExxonMobil, AGL and major power generators. Transmission pipeline infrastructure differs from low-pressure distribution infrastructure that supplies households with water and natural gas. This submission focuses on the regulatory burdens facing long-distance, high-pressure gas transmission pipeline infrastructure service providers. APIA notes the Commission will consider previous submissions made on the matter of regulatory burdens facing social and economic infrastructure services so many of the major issues should be covered as a result of this consideration.

## Summary of Recommendations

**Recommendation 1 (Page 6): A whole of Government directory of ongoing consultations be established, so that Government agencies can better co-ordinate, both internally and externally, consultation processes to more evenly distribute the burden over time and streamline overlapping processes.**

**Recommendation 2 (Page 6): Government agencies be required to acknowledge the Commission's recommendations and provide justification in instances where they are not followed.**

**Recommendation 3 (Page 7): Greater recognition by policy makers that the greatest expertise, experience and knowledge of any industry lies within the industry itself and due consideration and acceptance of industry submissions during consultation processes should be enforced by the Office of Best Practice Regulation (OBPR) or another suitable entity.**

**Recommendation 4 (Page 7): The OBPR be required to approve all Government consultation processes and review them in order to evaluate the effectiveness of each process.**

**Recommendation 5 (Page 13): All regulators be specifically limited in their ability to request publicly available information from market participants.**

**Recommendation 6 (Page 14): All regulators should, at all times, seek to use their own resources and internal communication systems to acquire information where possible, and not be allowed to request information from industry that has already been provided in a different form or is available in the public domain.**

**Recommendation 7 (Page 15): In circumstances where a regulator claims the ability to use information provided for a particular purpose for another purpose, there should be a complementary obligation on the regulator to not request information from a party if that information has been previously provided for a different purpose.**

## **General approach to regulation of energy markets**

The current approach to regulation of energy markets is an interventionist approach which relies on policies developed by policymakers and regulators who generally have not operated within the industry. This approach assumes regulation is required and the onus is on industry to demonstrate that regulation should be removed

A major failing of this approach is that it assumes that policy makers and the regulators are better equipped to produce processes leading to desired outcomes than the industry. It also appears to assume that the industry does not understand good policy and has little to contribute. This approach creates an environment where industry finds itself managing regulation and regulators and designing their operations often in an inefficient manner in order to avoid the adverse effects of regulation rather than contributing to the development of efficient market outcomes.

This represents a significant missed opportunity as industry is the party best able to undertake innovation to achieve improved outcomes. Regulators and policy makers are not experienced in the day to day operations of industry and are therefore poorly placed to achieve improved efficiency outcomes. Industry players, with their knowledge, are best placed to help government, through communication and negotiation, arrive at good workable solutions to policy issues for a particular industry.

With the very significant issues facing the nation – such as the global financial crisis and the climate change related structural change - government should seek to draw on industry experience and knowledge to provide solutions rather than impose untested “solutions” on industry.

Examples of decisions achieved by imposing “solutions” on industry include:

- Gas Market Development - the National Gas Bulletin Board and the Short Term Trading Market. These initiatives have been imposed on the gas market despite the absence of market failure. They have been based on solutions previously developed for electricity market structures and Victorian gas market structures – and these markets substantially differ from other Australian gas markets. The proffered solutions are widely held to be a

high cost, low benefit solutions. Industry has worked with the Ministerial Council on Energy (MCE) to minimise the burden created by these initiatives, which has been taken by the MCE to be an endorsement of them.

- The Gas Statement of Opportunities (GSOO) – the GSOO is an imposed requirement that will be developed by the new Australian Energy Market Operator and aims to improve investment planning. Given that appropriate investment in the gas market has occurred to date without the GSOO, the supposed market failure the GSOO will be addressing has not been adequately demonstrated to industry. The GSOO will deliver an analysis of publicly available information yet imposes significant new information provision burdens on industry. In empowering AEMO to produce the GSOO, the Government is also legislating new information gathering powers rather than adopting the model used successfully in the Electricity Statement of Opportunities (SOO).
- The National Energy Customer Framework - introduces major new enforcement powers that are unnecessary. The proposed system of regulation confuses customer protection and access regulation. The result is much more regulatory intervention than is necessary.

APIA considers a major failing of the MCE is the drive to have policy and regulatory consistency across electricity transmission and distribution and gas transmission and distribution. There are some areas of similarity (such as information gathering for the SOO and GSOO, where the Government has actually chosen to use different mechanisms), but there are also major issues of difference for each of these that the MCE reforms have been reluctant to recognise. Seeking uniformity where it is inappropriate creates inefficiencies and additional costs.

APIA considers the current mindset of policy development is highly interventionist. It does not seek to create incentives for industry to solve policy problems but imposes approaches with little agreement from industry and apparently minimal understanding of the markets being influenced. Government should place more emphasis on developing partnerships with industry rather than the current approach of imposing regulation.

## Regulatory consultation processes

The first concern with regard to existing Commonwealth regulatory processes that APIA would like to bring to the Commission's attention is the extensive and wide-ranging consultation processes that industry is requested to participate in. For the main part, industry is typically asked to comment on modifications to all categories of regulations, as set out in the Types of Regulation on page 11 of the issues paper. On occasion, an entirely new set of regulations is being developed, and this requires a further level of input and work.

Consultation is generally and logically welcomed by industry. Whilst the decisions made by Government often lack transparency and do not reflect industry positions, improved outcomes have been achieved through these consultation processes. However, the processes consume large amounts of time and resources from business. Often they overlap with other consultation processes, including those being conducted out of the same Department.

As an indication of the burdens placed on industry, in the time since 28 November 2008, when this Review was announced, participants in the gas transmission industry have been involved in:

- A review of the *Environment Biodiversity and Protection Act* (Department of Environment, Heritage, Water and the Arts (DEWHA));
- A review of the exemption of electricity generators and electricity and gas transmitters and distributors from the Energy Efficiency Opportunity Program (Department of Resources, Energy and Tourism (DRET));
- Ongoing individual industry consultation on the Carbon Pollution Reduction Scheme (CPRS), including the release of the CPRS White Paper in December and the imminent release of the exposure draft of the legislation (Department of Climate Change (DCC));
- Consultation on the proposed amendment to public disclosure of corporate level energy production data under the National Greenhouse and Energy Reporting Act (DCC);
- Consultation on draft amendments to the NGER Regulations 2008 (DCC);
- Consultation on the External Audit process for compliance with NGER (DCC);
- Consultation on the treatment of electricity-intensive, trade-exposed industries under the expanded national Renewable Energy Target (RET) scheme (DCC);
- A review into the use of Total Factor Productivity for the determination of prices and revenues (Australian Energy Market Commission (AEMC));
- Participation in the Weighted Average Cost of Capital (WACC) Review (Australian Energy Regulator (AER));
- Consultation on Annual Compliance Guidelines (AER);
- Consultation on the Draft Access Arrangement Guidelines (AER);
- A review of Energy Markets in light of Climate Change Policies (AEMC);
- Amendments to the National Electricity Law and National Electricity Rules for the Establishment of the Australian Energy Market Operator (AEMO) (DRET);
- Amendments to the National Gas Law and National Gas Rules for the Establishment of AEMO (DRET);
- the rule change processes provided for under the National Electricity Law and the National Gas Law (AEMC);
- The development of a legislative framework for the capture, storage and transport of carbon dioxide as part of the federal government's climate change reform agenda; and
- Consultation on Harmonisation of Energy Supply Industry Technical and Safety Regulation (DRET).

This list does not cover all consultation processes, and does not include the numerous standing committees in which the gas industry participates in order to assist Government in developing and maintaining regulations and/or policy, such as:

- the Gas Statement of Opportunities Steering Committee (AEMO);
- the Gas Market Leaders group (DRET);
- the Short Term Trading Market Steering Committee (AEMO);
- the AEMO Governance Documents Reference Group (DRET);
- the Technical and Safety Regulations Leaders Group (DRET); and
- the Carbon Transport and Storage Taskforce (DRET); and
- the various Australian Standard 2885 Committees (Standards Australia).

Again, this list is not exhaustive, and neither listing includes state based consultation processes or consultations which individual members may have been involved in with regard to specific assets.

The sheer volume of consultation processes leads to the difficult position of having to choose between processes. Many of the consultation processes are accompanied by hundreds of pages of documentation for comment. Typically, lack of participation in a process is taken by Government to be seen as approval or non-concern with the proposed changes. The reality is few companies have the capacity to devote the necessary resources to remain across the issues and consultation processes involved. Furthermore, in making a choice between consultation processes, the 'value' of participation is considered – that is, whether industry has any expectation that its views might actually be considered or whether the consultation is a token exercise.

**APIA recommends that a whole of Government directory of ongoing consultations be established, so that Government agencies can better co-ordinate, both internally and externally, consultation processes to more evenly distribute the burden over time and streamline overlapping processes.**

This would also provide an overview and history of all Government consultation processes occurring at any one point in time which, to APIA's knowledge, does not exist at this time.

When a particular sector or industry's engagement is required in multiple processes concurrently, requirements should be placed on Government agencies to allow for longer consultation periods in order to ensure that appropriate consideration of each issue can occur.

Often, whether due to short timeframes or incomplete knowledge of appropriate guidelines, the processes under which these consultations are carried out are not in accordance with the Office of Best Practice Regulation's (OBPR) Guidelines for Consultation.

**APIA recommends to the Commission that the OBPR be required to approve all Government consultation processes and review them in order to evaluate the effectiveness of each process.**

If this is already the case, each consultation paper issued by Government should include an endorsement from the OBPR.

APIA acknowledges that a review of all processes might be difficult to undertake, and suggests random reviews could provide the necessary checks to ensure best practice consultation principles are followed.

Considerable resources are required by industry to participate in consultation processes. If an industry or company chooses not to participate, that lack of participation is taken to be affirmation of the process and/or the result. Often when an industry or company does participate, its concerns are ignored or are taken to be self-serving. There is a view, based on experience, in industry that consultation is undertaken by Government departments as a 'required' process rather than one which can add value to the issue being considered. Rarely has a consultation process resulted in a true change in direction or attitude of policy makers and it cannot be considered likely that policy makers articulate processes leading to efficient, let alone optimal, market outcomes in every consultation paper issued.

**There should be greater recognition by policy makers that the greatest expertise, experience and knowledge of any industry lies within the industry itself and due consideration and acceptance of industry submissions during consultation processes should be enforced by the Office of Best Practice Regulation or another suitable entity.**

For example, many of the recommendations arising from the Productivity Commission's 2004 Review of the National Gas Access Regime appropriately reflected industry positions but have subsequently been largely ignored by the Australian Energy Regulator, the Commonwealth Department of Resources, Energy and Tourism and other Commonwealth agencies. This creates ambivalence in industry toward consultation processes.

**APIA recommends that Government Agencies be required to acknowledge the Commission's recommendations and provide justification in instances where they are not followed.**

## Regulation that is unnecessarily burdensome, complex or redundant

APIA will identify various burdensome regulations according to the criteria set out by the Commission on page 12 of the Issues Paper.

### Excessive coverage, including ‘regulatory creep’

#### Unnecessary obligations for ring fencing and related service provider issues

Chapter 4, Part 2 of the National Gas Law (NGL) provides for structural and operational separation requirements (ring fencing). These provisions largely reflect a former market structure and the gas industry has not considered many of these provisions relevant since widespread separation of infrastructure and energy trading businesses occurred in the early 2000s.

The AER has used the new information-gathering powers it has under the NGL to issue a prescriptive Annual Compliance Order (the Order) which requires detailed reporting on compliance with a range of obligations under the NGL, most of which relate to ringfencing.

The gas transmission and distribution industry has been subject to ringfencing and related obligations under the Gas Pipelines Access Law and Gas Code for over 10 years. Throughout that period the industry’s compliance performance has been good.

When the gas access regime was being developed in the mid-1990s, potential users were concerned about the exposures they might face when seeking access. Potential users were especially concerned about how they would be treated by those service providers that had associated retail businesses. Those concerns were addressed through ringfencing.

Despite those early concerns, ringfencing has not been a significant issue for users or potential users since access was bedded down. That is the case for both networks and transmission. **Today, no transmission service provider within the AER’s jurisdiction has an associated retailer.**

Gas (distribution) networks were never required to report on ringfencing to jurisdictional regulators with the level of detail now required by the Order. In fact, in some jurisdictions there was no requirement for network service providers to submit formal ringfencing reports. On the other hand, the ACCC required transmission businesses to provide detailed reports for some years. Despite these differences, there is no evidence that users and potential users were any more comfortable in dealing with transmission businesses than with network businesses with regard to ringfencing.

Ringfencing obligations, while important, represent only a small proportion of a service provider's total compliance obligations. Arguably, many other obligations have equal or greater public significance and yet don't, and don't need to, attract the degree of regulatory scrutiny that the AER chooses to impose through the Order.

Rather than reducing the intrusiveness of reporting requirements in recognition of these considerations, the Order requires detailed annual reporting that is more extensive and detailed than has been considered appropriate in the past, especially for network service providers.



## Specific regulations that cover similar ground as other generic regulation

### **Part IIIA of the *Trade Practices Act (1974)* (TPA)**

As noted on the AER Website:

*Part IIIA establishes a legal regime to facilitate third party access to services of certain facilities that are considered critical to competition in related markets.*

*The regime focuses on third party access to the services provided by a limited class of facilities that have the following distinguishing features:*

- *Natural monopoly characteristics, wherein, due to economies of scale or scope, a single facility can satisfy all the demand for its services in a market at lower cost than two or more facilities;*
- *Occupation of a strategic position in an industry, so that access to the facility's service is a prerequisite for businesses to be able to compete effectively in markets upstream or downstream of the facility (often referred to as a 'bottleneck' facility);*
- *Being of national significance, having regard to its size and/or importance to interstate or international trade.*

APIA considers that Part IIIA of the TPA sufficiently provides for the regulation of gas transmission pipelines and the use of the National Gas Law 2008 (NGL) and National Gas Rules represents an inappropriate view that gas and electricity transmission markets are fundamentally comparable and should be regulated in a similar manner. This issue is described further in the following section 'Convergence of electricity and gas regulation'.

APIA's members hold the view that the gas supply chain should not be viewed as a competitor to the electricity supply chain. A major use of natural gas is as an input to electricity generation and, as such, gas supply could be regulated in the same manner as competitors such as coal supply, namely under Part IIIA of the TPA.

This view does not apply to the regulation of gas retailers, who are responsible for supplying gas to households and as such are comparable to electricity retailers.

This issue requires further exploration and APIA welcomes the opportunity to engage with the Commission during the Review.

## Blunt, poorly targeted or unnecessarily complex regulation

### **Costs of regulatory burden spread over entire industry**

The costs and burdens of regulatory reforms tend to be spread over the entire gas supply industry, with the costs outweighing the benefits to some sectors. A recent example of this is the establishment of the Natural Gas Bulletin Board (BB), which places heavy information burdens on the pipeline sector but for the most part is operated for the benefit of gas retailers and users.

The gas transmission sector is required to provide quantities of information to the BB that enable users of their services (shippers) to trade more efficiently but provide no benefits to the gas transmission sector. This information is provided to its users by the BB operator (currently VenCorp, from 1 July 2009 will be AEMO) free of charge.

Similar burdens will be placed on the gas transmission industry through the establishment of the Short Term Trading Market.

Also, in some jurisdictions, transmission pipelines already are required to directly pay the costs of regulatory agencies where there is little or no transparency in respect of these agencies' costs. For example, in Western Australia, the owners of regulated pipelines are required to pay for the costs of running the Economic Regulation Authority. These user pays arrangements do not benefit the pipeline owners and moreover are imposed in circumstances where the costs can not be passed on to the beneficiaries of the work these agencies perform – ie end users.

## **Convergence of electricity and gas regulation**

Ongoing National Energy Market Reforms will see the Australian Energy Market Operator (AEMO) commence operation on 1 July 2009. For the first time, electricity markets and gas markets will be managed by a single entity. The Government believes that many synergies between these markets exist. APIA is concerned that many regulations suitable to the electricity market will be imposed on the gas market as a result of the establishment of AEMO, without recognition of the significant differences that exist between these markets. These differences cover virtually all aspects of each market and include:

- Physical differences - gas and gas transmission pipelines have different physical characteristics from electricity and electricity assets. In particular:
  - Storage - pipelines act as storage vessels for gas.
  - Flow - in a majority of transmission pipelines gas flows in one direction, while in electricity transmission, the electricity moves multi-directionally.
  - Recoverability - the provision of electricity is instantaneous whereas for gas there is a time lag. The ability of electricity to be available when a generation plant comes back on line is almost immediate; this is not the case for gas.
  - Compressibility - gas is physically compressible. This impacts on investments considerations relating to pipeline expansion.
- Location differences – gas transmission pipelines connect naturally occurring gas fields with end users. As such, there is little discretion as to where pipelines are located. However, as electricity is generated rather than extracted, there is greater discretion as to where electricity generation and transmission assets are located.
- Market operations and arrangements differences – the gas market has a different role and structure from the electricity market.
  - Role of the grid - the role of the electricity grid in the operation of the market is significantly different from the role of gas transmission pipelines. The electricity transmission grid has a key role integrating the electricity market. In contrast gas transmission pipelines have a lesser integration role as they tend to link individual production regions to market centres over long distances with varying degrees of interconnection.
  - Market dispatch arrangements - gas has less complicated market and dispatch arrangements as gas has more predictable flows and demand due to the contracting

regime that exists in gas, the ability to use storage and fewer complex network interactions.

- Investment differences – gas pipeline investment (both greenfield and brownfield investment) is typically entrepreneurial in nature and is underpinned by commercially negotiated bilateral contracts for pipeline capacity. The commercial contracting approach results in pipeliners being focused on ensuring new investment is economic and underpinned by emerging and existing contracted demand. Electricity transmission and distribution investment is more likely than gas investment to be driven by planning and regulatory obligations and is less likely underpinned by explicit contracts.
- End use markets – gas usage is dominated by power generation, including power generation for the mining sector, and major industrial users such as fertiliser plants and mineral processing plants. In most states, gas is generally an input into electricity production rather than a competing energy source. Electricity usage is much more widely spread across different geographical and demographic markets. In addition, most gas end use markets have at least a degree of competition with alternative fuels or end user production options.
- Investment Recovery and Stranding
  - recovery of the majority of electricity transmission and distribution investment is achieved by including the investment in interconnected, regulated networks. Recovery of gas transmission investment is often more problematic due to the point-to-point nature of gas assets and the concentration of gas end users. These factors mean that non performing gas transmission investments are more easily identified and stranded. In addition, gas pipelines are also at risk of being stranded due to field depletion or large end-users seeking supplies from alternative fields, moving sites or closing sites;
  - the gas regulatory regime places transmission pipelines at the risk of having un-contracted capacity and thereby receiving no revenue (because of tariffs being set on the basis of an inflexible depreciation schedule which assumes a return of capital over the expected physical life of the pipe (in excess of 60 years)).

Some examples of electricity regulations creeping into the gas market include

- The introduction of the Natural Gas Bulletin Board (BB) and announced establishment of a Short Term Trading Market (STTM) seeks to replicate electricity market structure and procedures in the gas market. No real inefficiencies or market failures have been identified in the gas market to justify these moves. These types of features are necessary in the electricity market which requires near instantaneous matching of supply and demand, however this does not occur in the gas market.
- The introduction in 2009 of the Gas Statement of Opportunities (GSOO) seems to seek to replicate the centralised planning of the electricity market in the gas market. The GSOO is intended to provide information to the market to assist with planning, however no information failure has actually been identified and the gas market is operating efficiently in the absence of such a document.
- The proposed move to National Energy Customer Framework seeks to replace gas contracting relationship (ie linear relationship) with electricity relationship (ie triangular relationship) between participants.

- The more detailed compliance procedures under NGL Guidelines are based on electricity guidelines but have not been identified as necessary for the gas market.

## **Renewal of Access Arrangements for Covered (Regulated) Pipelines**

Access Arrangements (AAs) are documents approved by the AER (or in WA the state regulator) setting out the terms under which a shipper can access pipeline infrastructure to natural gas delivery services. AAs are typically subject to five year review intervals and it is mandatory for the pipeline service provider to undertake these reviews with the AER even in situations where there is not actually any capacity to provide new services to shippers or where capacity is currently being sold at less than the regulated tariffs.

AA reviews are complicated and expensive processes that take many months, if not years, to complete and often result in a pipeline owner incurring direct costs in excess of \$1 million and further internal costs for often limited benefits to both themselves and their shippers, as on contract carriage pipelines pipelines and shippers commercially negotiate terms, conditions and prices. As a result, owners of covered pipelines are subject to prolonged regulatory processes that incur significant costs and have no impact on the operation or tariffs applying to a pipeline. Some recent examples of AA reviews that have these characteristics include:

- The GasNet AA Review, conducted in 2007 and 2008 by the AER, incurred direct, external costs to the infrastructure owner of \$1,015,000 through the period 2006-2008. This does not include internal costs conservatively estimated at \$450,000.
- The Moomba to Sydney Pipeline AA previously set a tariff that was higher than that paid by users of the pipelines services. The infrastructure owner was subjected to a lengthy regulatory process for the benefit of its customers that ultimately had no impact on its customers. (The Moomba Sydney Pipeline is subject to competition from other gas pipelines).
- The Roma to Brisbane Pipeline was subject to an AA review in 2006, despite the fact that effectively all available capacity was contracted at commercially negotiated rates for the period 2006 to 2011 for which the AA review would apply. The overall cost of this review process is estimated to be \$800,000.
- The Dawson Valley Pipeline, a minor pipeline in Queensland, has a capital base of less than \$1 million and was subjected to the full process of an AA review in 2007. This would have resulted in incurred costs (APIA estimates above \$100,000) that represent a significant portion of the total capital base of the pipeline.

These figures were taken from submissions made to the AER, available from the AER website.

In addition, as noted above, in some jurisdictions, notably WA, pipeline owners are required to pay for the costs incurred by regulatory agencies in undertaking these regulatory processes.

## Excessive or duplicative reporting or recording requirements, including duplication of information requests

Gas transmission pipeline companies are required to provide information to a variety of sources under the National Gas Rules, and a large portion of this duplicative. One direct example that will arise with the establishment of AEMO is the provision of information to the National Gas Bulletin Board (BB) and the Gas Statement of Opportunities (GSOO)

National Gas Rules (NGR) 170-174 set out the information that a pipeline operator must provide to the BB Operator (AEMO from 1 July 2009) on a daily basis. Proposed new NGR 135 KB sets out information a pipeline operator must provide to AEMO on an annual basis for purposes of the GSOO. The information set out in NGR 135KB is twofold:

1. The maximum daily and annual capacity of the pipeline. This information is provided, or in the case of annual capacity can be derived from information provided, for purposes of the BB under NGR 170-174; and
2. Publicly announced investments in new pipelines or modifications to existing pipelines.

The GSOO information will be obtained from industry through the use of Market Information Orders (MIO) and Market Information Notices (MIN), as set out in the National Gas (AEMO) Amendment Bill 2009 s91F. In essence, AEMO is being granted a power to demand from industry the submission on information already provided for a different purpose or information that is already available in the public domain. This legislation has not yet been passed.

APIA is aware that DRET has received a substantial number of submissions objecting to the new law allowing the use of MINs and MIOs and not a single submission in support of this new information gathering tool. Despite this, APIA has been advised by the DRET that the use of MINs and MIOs will be proceeding. There is a major concern in industry that once the MIN and MIO tool is enabled in legislation its use will be expanded. This would require further modification of the NGL, which would not be difficult to achieve in industry's view.

**APIA recommends the Commission advise AEMO (and other regulators) that it should at all times seek to use its own resources and internal communication to acquire information where possible, and should not be allowed to request information from industry that has already been provided in a different form or is available in the public domain.**

## Duplicative Information Requests

APIA members consider many of the information requests that are imposed on energy market participants are unnecessary, inefficient and require the provision of information that is in the public domain. As an example of the attitude of energy market regulators on this matter, in its Draft Access Arrangement Guidelines, p31, the AER has stated:

*"In circumstances where parties wish to rely on material from, for example, websites, consultants' or experts' reports, the AER's or other regulators' papers, a court or tribunal decision, they should include a copy of the relevant documentation and information with their submission..... Even if the document has been provided in a previous submission for the same or different regulatory process, the entire document should be submitted."*

APIA believes that this requirement is unnecessary and creates additional administrative work for Service Providers. A reference in an acceptable format and a web link if the document is electronically available should be considered sufficient.

In addition, this requirement has the potential to result in absurd outcomes - eg submissions will typically refer to previous AAs, the NGL, the NGR, market rules, the previous Gas Code, previous AER decisions relating to other assets etc – providing such documents is unlikely to be beneficial, particularly as many of these documents are on the AER website and/or are quite large.

If the AER needs a full copy of a document that is not publicly available the Service Provider should make one available on request. If the reference is to a document previously provided to the AER then a reference to the date it was previously provided should be sufficient.

Whilst the example provided here is specific, APIA considers that it represents the general attitude taken by the AER and other regulators toward information requests, one that is inefficient and inappropriate. In this example, the AER is requiring parties to resubmit material already submitted to the AER, **even if it is part of an earlier submission to the ongoing regulatory process**. Often information requests require the provision of information that has already been provided for a different purpose or is available through a simple web search.

**APIA recommends that all regulators be specifically limited in their ability to request publicly available information from market participants, as such requests amount to requiring market participants to conduct research work for regulators rather than an appropriate information request.**

### **Regulators' power to use information for any purpose**

Regulators consider it appropriate that information provided for one purpose may be used for any purpose, as set out in s44AAF of the *Trade Practices Act 1974* and in the proposed NEL, s53D, and NGL, s91FD, amendments for the Australian Energy Market Operator (AEMO).

s53D of the NEL and s91FD of the NGL (proposed amendments) state:

‘Subject to this Law, the Rules and the Regulations, AEMO may use information obtained by market information instrument or in any other way for any purpose connected with the exercise of any of its statutory functions.’

The validity of this position is disputed by APIA. However, for the purposes of this Review the validity of this position is not relevant.

**It is not unreasonable to consider that if a regulator is to have the ability to use information provided for one purpose in a manner of its choosing, then there should a complementary obligation on the regulator to not request information from a party if that information has been previously provided for a different purpose.** As can be seen by the proposed policy of the AER (above) the AER does not consider this obligation to exist, even when the information has been provide in an earlier submission to the same process.

## Unduly prescriptive regulation that unnecessarily limits the ways in which businesses may meet the underlying objectives of regulation

### National Energy Customer Frameworks

The policy objective quoted below from a paper issued in 2008 by DRET indicates an intention to broaden regulations across the energy sector, including to gas transmission, which would appear to be well outside the scope of the National Energy Customer Framework's original intention.

*The existing national compliance and enforcement frameworks in the NEL and NGL will be applied where distributors and retailers are carrying out regulated functions under the national customer framework.*

*However, there will be some enhancements to the enforcement regime generally to allow greater flexibility of enforcement options and a robust compliance reporting regime for the customer framework, including enforceable undertakings and compliance monitoring systems.*

*The new enforcement mechanisms adopted for distribution and retail regulation will also apply more broadly across national energy regulation. (p. ix)*

APIA is concerned at the prospect of such "enhancements" to the enforcement and compliance regime, particularly if they are intended to apply to gas transmission pipelines. The gas transmission industry has participated in an exhaustive consultation process to ensure that the new National Gas Law and Rules would provide an appropriate framework in which the industry can operate while meeting the Government's policy objectives.

Throughout this consultative process, there was never a suggestion that the policy objectives were intended to be strengthened for transmission pipelines in the manner proposed in this policy paper. To move to change the new gas law at this very early stage of its implementation, without proper consultation is clearly inappropriate and not necessarily reflective of the Government's intentions. It should also be noted that the new gas law already includes expanded enforcement powers that have yet to be tested. To this end, in late July 2008, the AER released consultation documentation relating to compliance with the NGL. Processes under the new gas law should be developed and implemented prior to developing a further series of what could be conflicting or duplicative processes.

It is highly inappropriate to introduce new regulatory powers in the National Gas Law that are tailored to primarily to protect consumers and smaller customers and do not reflect the realities of the gas transmission sector. 'Consumers', as they relate to the gas transmission sector, are large entities that do not need the protection of the ACCC.

The new law was intended, to some extent, to allow lighter regulation in some instances. Any move to arbitrarily impose more heavy-handed obligations may run counter to the intent of the current law. It should be noted that:

- Gas transmission is facilitated by contracts between parties, (with the exception of some pipelines in Victoria where a market carriage system applies);
- Gas transmission businesses solely contract with large and sophisticated counterparties (such as AGL, Origin and large mining and manufacturing companies). These large users are already afforded legal, regulatory and contractual protections in their dealings with pipeline companies. A further layer of protection for such large companies seems at best redundant and at worst punitive.

- It has never been suggested that the relevant enforcement regimes under the Gas Code nor under the NGL were ineffective.

The types of enforcement regimes suggested by the policy paper are, therefore, unnecessary. These regimes are the subject of further consultation, but provide an example of regulation necessary for one sector of the gas supply industry being imposed on other sectors.

## Rules that inadvertently provide incentives to operate in less efficient ways

### **Economic Regulation provides no incentive for efficient investment**

Gas transmission infrastructure is classified as either covered or uncovered. Covered infrastructure is subject to Access Arrangement rulings by the AER, setting out tariffs that can be charged for transportation of natural gas. Shippers and pipeliners are free to negotiate other tariffs on the covered pipelines.

Tariffs for uncovered infrastructure are determined through commercial negotiation between the infrastructure owner and interested parties.

A pipeline will be uncovered, and thus not subject to access arrangements set by economic regulators, if it has limited market power.

Economic regulation of the energy sector in Australia is complex and regulation of the gas transmission industry is no exception. Gas pipelines tends to be perceived by policy makers as being natural monopoly infrastructure, and it is then assumed that these natural monopolies will abuse their market power. However, in reality the power of many pipeline companies is constrained by direct pipeline on pipeline competition, countervailing power of major users and competition from alternative energy sources.

APIA recognises that there is an appropriate role for regulation of natural monopoly infrastructure, where there is insufficient competitive pressure or countervailing power to constrain the market power of a natural monopoly; however, there are few pipelines which exhibit these characteristics.

**What should be noted, and is often overlooked, is the fact that transmission pipeline businesses, even the larger businesses, operate in an environment where their customers are significantly larger than the pipeline companies. These businesses operate with a degree of market power in their own markets, bringing significant countervailing market power. In such an environment excessive regulation delivers neither efficiency nor effectiveness and can be punitive to pipeline companies.**

APIA is keen to see an appropriate balance so that regulation is only applied where it is needed and to the extent that it is needed in order for the market to operate effectively and efficiently. The fact that much of Australia's gas is supplied through unregulated pipelines should indicate that the



markets developed by the private sector operate efficiently. Indeed, in the eastern markets overseen by the AER, only 34% of gas transmission pipelines are covered.<sup>1</sup>

The approach taken by economic regulators is usually to approve access arrangements for gas transmission pipelines that allow a low rate of return for pipeline investors and thus provide the users of pipelines with low transportation tariffs. This approach ignores several facts:

- unlike the relationships between energy retailers and consumers, which are also overseen by economic regulators, the relationship between gas transmission infrastructure and its users are relationships between large, sophisticated entities and, in most cases, the users are the larger parties. **Therefore, the users of gas transmission pipelines do not require government intervention to ensure efficient outcomes;**
- the legal separation of the owners and operators of transmission pipelines from gas wholesalers and retailers mandated in early industry reforms has largely removed incentives for discriminatory behavior by pipeline companies. **Government intervention in the gas transmission market is not required for the purpose of regulating competition between wholesalers and retailers in the energy market;**
- in driving down the rate of return available to gas transmission investors, the economic regulators are **decreasing the attractiveness of investment in gas transmission infrastructure and this can lead to underinvestment in this critical infrastructure;** and
- in order to avoid the risk of low rates of return mandated by a regulator, **investors can minimise regulatory exposure through a variety of means, some of which may lead to inefficient investments.**

### Regulatory Impacts on Investment Decisions

Gas transmission infrastructure is long-lived and capital intensive. Pipeline infrastructure investment is sunk which means that pipeline assets are particularly vulnerable to both commercial and regulatory stranding and regulatory risk.

Regulatory risk is a key consideration for transmission investors and financiers. In general, the risk of low 5-year regulatory tariffs creates a disincentive to build uncontracted capacity in gas transmission infrastructure. Any pipeline capacity that is not contracted or utilised can be subject to prices set by the economic regulator or alternatively can be subject to regulatory stranding.

In this environment, infrastructure investors are generally reluctant to build spare or uncontracted capacity on regulated pipelines. APIA is not aware of the provision of any spare or uncontracted capacity to market by gas transmission pipeline investors in recent times.

Building of spare or uncontracted pipeline capacity requires investors taking a risk on possible returns. While regulatory risk is not the only issue, it is a real concern. Obviously, with each access arrangement:

- there is significant cost involved in the implementation and appeal processes;
- considerable time is taken to resolve those issues (up to 3 years);

---

<sup>1</sup> Steve Edwell, AER Chairman, Presentation to APIA 2008 Conference, 14 October 2008

- the revision of those documents starts every 5 years on a very long-term asset; and
- there is a lack of incentive for regulators to consider parties other than the notional “consumer”.

Regulatory risk increases the cost of providing gas transmission services, which imposes significant social costs through:

- undermining the incentive to invest –regulators approving low returns signals to investors that only limited capital should be invested in the gas transmission sector. ;
- delaying investment – the increased risk associated with regulation means that investment can be delayed until, for example, greater throughput can be achieved (or a target level of throughput becomes more certain) making the investment less risky and thus commercial. This imposes a cost on society to the extent that the benefits from the investment are foregone for the duration of the delay; and
- distorting investment – regulatory risk will tend to result in smaller pipelines being built, or smaller pipeline augmentations being built, as a means of protecting investors against regulatory risk. Limiting pipeline size is prudent if there is a risk that regulators will strand any excess capacity without allowing an offsetting premium to be earned when at-risk capacity experiences high demand. However, reducing pipeline capacity imposes cost on the community on account of foregone scale economy benefits and increased likelihood of capacity constraints. The experience of the development of the DBNGP during the period of 2000 to 2004 is a real life example.

APIA considers the last point above to be particularly relevant. **In increasing the regulatory risk by driving down the rates of return, the economic regulators are providing an incentive to investors to build smaller, uncovered pipelines initially and subsequently expand capacity only when it is fully contracted. This investment style requires the use of greater amounts of capital than would have been required if spare capacity that was reasonably likely to be used in the foreseeable future was constructed in the initial investment phase, creating the perverse outcome of higher capital costs, which are recovered through higher transportation costs to end users of gas.**

It is not possible to say what spare capacity would be built if the position of economic regulatory agencies were to change, however it is reasonable to note that **in the current Australian gas market it is common practice to build for initial demand and then supplement additional demand with further compression and looping.** Economically, in most cases it would be more beneficial to construct a larger diameter pipeline in the first place. As noted above, only 34% of gas transmission pipelines in the AER’s jurisdiction are covered, a clear indication that industry seeks to minimise regulatory risk.

APIA believes that the challenges facing energy infrastructure industries are best addressed by economic regulators determining a reasonable range for rates of return and selecting an estimate at the higher end of the range to encourage economically efficient investment in spare capacity, and to ensure gas transmission pipelines continue to be attractive investments.

A rate of return from the upper end of the range may encourage some over-investment, however, this would result in spare capacity which, based on recent ABARE demand projections, is reasonably likely to be used in the foreseeable future. A rate of return at the lower end of the range encourages under-investment and, over time, this can result in a restriction of energy supply to consumers. Of these outcomes, the first option is less disruptive to users and potential users. Underinvestment in the maintenance and economic expansion of energy infrastructure would have a detrimental effect on long-term system operation and security of supply. The impacts of such underinvestment cannot be easily reversed.

### **Unnecessary heavy-handedness in the behaviour of regulators, including too frequent requests for information and reporting**

As mentioned above, APIA members frequently consider the behaviour of regulators, particularly relating to information requests, to be heavy-handed, and often requiring market participants to undertake work that the regulators should be conducting prior to making information requests.

As an indicative example, whilst reviewing the AA for the Roma to Brisbane Pipeline in 2006 (relevant documentation at <http://www.aer.gov.au/content/index.phtml/itemId/713594>), the AER requested copies of all contracts on the pipeline dating back to 1969 be provided by the pipeline's owner. Interestingly, these documents were not required by the AER during its 2002 review of the same AA.