



Review of the national gas access regime

Response to proposal for consultation

Garth Crawford
National Director, Government and Regulatory Affairs

Presentation to MCE Standing Committee of Officials Forum, 23 November 2005

Introduction

- Thank you for the opportunity to speak today on the proposed response to the Productivity Commission *Review of the Gas Access Regime*
- The ENA represents gas and electricity distribution networks.
- Gas and electricity network businesses are disappointed by the proposals set out in the latest Consultation Paper
- The Paper accepts only around a third of the Commission's 54 recommendations
- 17 out of 54 recommendations are deferred for consideration by the expert review panel.
- Another third of recommendations are altered by the proposals in the Paper, often with no apparent rationale for the changes
- ENA's view is that you don't achieve seamless and consistent energy access rules by deferring policy decisions
- We are also concerned that some of the alterations to the original recommendations, particularly those relating to the role of the AER and AEMC, are ill-considered
- A further point is that:
 - o amending the coverage test
 - o developing a system of monitoring and greenfields exclusions for regulation

does not represent a balanced or complete response to the problems the Productivity Commission found in the gas access regime

- These two areas mainly impact on the treatment of new or existing gas transmission pipelines under the regime. Gas transmission is an important set of assets, but they do represent a subset of assets under the gas regime.

- The over \$6 billion of gas distribution networks represent the largest single type of assets operating under the National Gas Code.
- In contrast, around \$3.3 billion of gas transmission pipelines are covered. The majority of gas transmission pipelines, around \$4.1 billion already operate outside of the Gas Code.
- Amendments to the gas regime which don't address the fundamental elements of the regime for distribution networks – such as pricing principles and the scope of regulatory discretion – leave the task half-complete.
- The Commission did not find that that the regime was operating effectively and that there were no problems with regulation for existing gas distribution networks. That argument is wrong and is simply incompatible with the significant number and detail of the recommendations the Commission made, especially in Chapter 7 of its final report.
- Recommendations in this area included providing better pricing principles, defining the regulators' task more clearly, and allowing for alternative forms of regulation not based on firm-specific costs to be proposed.
- Genuine responses to these recommendations must be developed if governments are to say they have responded in full to the Productivity Commission review. Industry is committed to ensuring these recommendations are dealt with, and will continue to push for this to occur.
- There are four specific areas where SCO have made proposed responses that I want to address and then I will turn to the formation and terms of reference of the expert panel.

Objects clause

- First, on the objects clause for the gas regime.
- The majority, in fact 95% of submissions to the MCE's previous consultation paper did not support the objects clause option that was simply copied from the NEL objective
- This makes it perplexing to industry and other stakeholders that this option is now put forward as the only preferred option. Clearly, at the moment there is a significant gap between how government and most stakeholders see the objective of the gas regime, which has to be a matter of concern.
- The NEL objective was designed as a market objective and is not suited to a simple 'cut and paste' approach which applies it to an access regime
- Energy networks strongly support the PC's recommended objective as it is consistent with the national access regime and appropriate for an access regime. The majority of other parties agreed.
- We note as well that the Utility Regulators Forum's has stated that the objects clause should refer to the objective of an access regime to promote competition in related markets. This is precisely the part of the PC's recommended clause which is missing in the 'cut and paste' NEL objective.

- The ENA would like to suggest a final compromise objective which retains the long term interests of consumer, but recognises that this is a function of efficient investment and operation of assets, not an indistinct separate consideration

Coverage test

- Moving to the coverage test, the ENA supports accepting the Productivity Commission's recommendation to amend the coverage test
- We have some concerns, however, over the proposal to replace the NCC as the coverage recommendation body with the AEMC.
- The NCC has developed considerable experience in coverage assessment through its role as the declaration recommendation body under the national access regime, and for coverage under the gas access regime.
- Moving this function to the AEMC may mean that this expertise, as well as economy wide consistency of approach, will be lost
- This move would also be in conflict with the goal of aligning the coverage criteria and the declaration criteria of Part IIIA.
- Having different bodies interpret the same test is a recipe for inconsistent application, divergence of interpretations, and investment distortions across infrastructure sectors.

Monitoring option

- Moving on to the issue of the monitoring option, we support MCE's proposal to introduce a monitoring option into the gas access regime.
- We are concerned, however, at one very significant departure in the proposal from the model recommended by the PC.
- Energy networks are opposed to giving the Australian Energy Regulator - designated by the MCE as the rule enforcing body - the new and conflicting role of being the decision-maker over the form of regulation to apply
- This approach is inconsistent with the position SCO adopted in its August consultation paper, where it accepted the Productivity Commission's recommendation that the decision about form of regulation should be made by a separate body to that responsible for applying the regulation.¹ No reasons have been offered for this change of position between the papers.
- Analysing all of the submissions posted on the MCE website responding to the Consultation paper, ENA has found that not one urges the SCO to reject this recommendation.
- We do not have confidence that having rules developed by the AEMC for this AER decision overcomes the problems with this proposal.
- This proposed approach does not effectively separate decision-making over the scope of regulation from the enforcement of regulation, as recommended by the

¹ MCE SCO Consultation Paper *Review of the Gas Access Regime Draft Response*, 15 August 2005, Response to Recommendation 12.2

Productivity Commission. It should be rejected. Minister's should make the key policy decision of what form of regulation should apply, informed by NCC recommendation. The decisions should be made under legislative criteria spelt out in the new *National Gas Law*

- Finally, we note that the proposals in the Consultation Paper envisage no new information obligations being imposed on uncovered pipelines. We endorse this approach.

Greenfields projects

- Now turning to the greenfields proposal outlined in the SCO paper.
- The ENA supports acceptance of the binding no coverage recommendation of the Productivity Commission, and supports scope for 15 year price regulation holidays.
- We do have some queries on what the Paper means by the proposed requirement that, for a distribution network to qualify for greenfield treatment, it must be "in an areas of a jurisdiction which the relevant minister has designated open for greenfields pipelines".
- At this stage our view is a criteria of this kind is unnecessary, and will potentially act as a new obstacle to greenfields distribution project, the opposite outcome to that sought by the MCE

Expert panel review

- Turning finally to the establishment of the expert review panel, which is tasked with carrying forward around one third of the Commission's original recommendations
- First, let's be clear, the expert panel is not a measure recommended by the ENA or any other industry body.
- The ENA has been pressing for some time for clarity that multiple MCE work programs won't overlap on pricing issues, and the AEMC review won't by accident or default begin to define the nature of access pricing for distribution.
- We have just as consistently been arguing that the recommendations of the PC gas review should be accepted and implemented as a package. The expert review panel risks failing to achieve all three of these objectives.
- We are concerned that the review panel is being asked to essentially review and consider a body of issues which has already been examined in detail by the Australian Government's expert advisory body on competition policy development - the Productivity Commission
- The ENA considers the first step towards a consistent energy access regime is to *accept* the recommendations of a review body which has looked at the operation of the Gas Code over the past 8 years, and give the panel the focused task of examining which of these recommendations may also be of generic benefit and applicability across electricity and gas networks.

- This provides them with some initial policy guidance, rather than asking a panel in a policy vacuum to try to reconcile what everyone agrees is the drafting disaster of the unreviewed Chapter 6 of the Electricity Code with the clearer, shorter and already examined Gas Code.
- SCO has already expressed the view that it expects the final pricing principles to flow from the expert panel to not substantially differ from the Commission's proposals.²
- It is important to retain consistency between the national access regime pricing principles and energy access pricing principles. An agreed objective of Part IIIA is to prevent unwarranted divergence between the national and industry-specific access regimes.³
- Looking in more detail at the terms of reference we have a few suggestions.
- The first is that it is not clear the scope of the expert review panel is agreed, and we are not sure whether it is clear enough that the expert review panel not only has to determine a range of generic regulatory issues, but also must deliver a response to the full number of recommendations referred to it by the proposed MCE response
- There are two additional areas of uncertainty in the mind of industry, relating to timelines and what the expected output of the panel will be

Timing issues – short timeframe, crossover with AEMC review timeline

- First, on timing.
- The panel is intended to make a determination on pricing approaches that should be applied across electricity and gas distribution and transmission by around February 2006.
- This means that 10 weeks from today the panel is assumed to have resolved the issue of appropriate network pricing principles and regulatory models applying to electricity and gas networks and pipelines.
- And in this same 10 weeks SCO or MCE will have agreed to its findings and recommendations.
- Timing is a key issue, because on the AEMC's current timetable by February 9 next year the AEMC is due to lodge its notice of proposed rule change, the result of its review of revenue determination principles and the models of regulation that should apply to electricity transmission.
- We do not think the timeline for the panel is consistent with:
 - o allowing for adequate consultation on the range of issues which will impact on assets with a sunk capital value of around \$50 billion
 - o allowing for proper consideration of the issues by the panel

² See MCE SCO Consultation Paper *Review of the Gas Access Regime Draft Response*, 15 August 2005, Appendix Table of Responses to Recommendations, p.4

³ *Australian Government Response to Productivity Commission Report on the Review of the National Access Regime*, February 2004, p.3

- or, incidentally, experience to date with MCE decision-making processes
- This timetable risks either leaving inadequate time for consideration and consultation on issues affecting \$50 billion of infrastructure, or the AEMC Chapter 6 review beginning to reach definitive findings before the completion of the expert panel.
- We support measures by governments, including amending the NEL, to extend the time for the AEMC Chapter 6 review, to ensure neither of these negative outcomes occurred.

Clarity of task – high level advice or draft rules

- Our second point of concern is about ensuring clarity over what the expert review panel is expected to deliver.
- It is very important that there is a clear and agreed set of outputs for the panel.
- The current terms of reference refer to recommending model legislative provisions, where the consultation paper talks more generally about providing advice upon a range of matters. If the taskforce is expected to deliver detailed recommended provisions, such as drafted pricing principles and other provisions, it is important that this is agreed upfront.
- A strength of the PC report was that it provided detailed, drafted recommendations.
- A process which produced another high level report to add to the list of review reports already referenced in the Terms of Reference would be a poor outcome.
- A final point to notes is that these two concerns are linked
 - If SCO wishes to have the expert panel re-review the gas access regime in the time available, the stage is set for a rushed, non-consultative process which will have little hope of being anything other than reactive to the AEMC's already commenced Chapter 6 review
 - If, instead, a more focused task is given, accepting the Commission's recommendations in relation to the gas regime, and examining which can be sensibly carried across into electricity, then the timeline is challenging, not impossible

Recommendations

Recommendation 1 - Consider a compromise objectives clause that references the interests of consumers but does not establish uncertainty over the interpretation of the clause, e.g.

The objective of the gas access regime is to promote efficient investment in, and efficient operation and use of, natural gas pipeline services ~~for~~ thereby promoting the long term interests of consumers of natural gas with respect to price, quality, reliability, safety and security of supply of natural gas

Recommendation 2 - Reject the proposal that the rule-making body, the AEMC, should be given an entirely new function relating to coverage processes, which will introduce inconsistency between the interpretation of coverage (AEMC) and declaration (NCC) thresholds

Recommendation 3 - Reject the proposal to provide the AER with power over what form of regulation (monitoring or cost-based) should apply to covered pipelines, when this decision should properly be subject to Ministerial determination

Recommendation 4 – Consider measures to ensure the current legislative time restriction placed on the AEMC with respect to its completion of the review of Chapter 6 does not compromise the undertaking of adequate consideration of issues and substantive consultation processes by the expert review panel

Recommendation 5 - Provide clear guidance to the expert panel about what is its expected output (e.g. proposed rules or advice), and provide initial policy direction by focusing the review on the generic applicability of the Productivity Commission's recommendations across electricity and gas transmission and distributions (without re-reviewing their application to gas)

Recommendation 6 - The review panel should also be required to take into account a number of sources and developments not referenced in the draft Terms of Reference. This should include the recent PM's Infrastructure Taskforce Report, relevant and recently implemented regulatory models such as the *WA Electricity Networks Access Code*, as well as the foundation competition reform documents such as the *Competition Principles Agreement* and the Hilmer Report.