



**INDEPENDENT PRICING AND REGULATORY TRIBUNAL**  
OF NEW SOUTH WALES

Our reference: 03/188

Contact Ineke Ogilvy  
Senior Analyst, Gas  
Telephone 02 92908473  
Email [ineke\\_ogilvy@ipart.nsw.gov.au](mailto:ineke_ogilvy@ipart.nsw.gov.au)

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Manager - Energy Market Reform Team  
National Energy Market Branch  
Department of Industry, Tourism and Resources  
GPO Box 9839  
CANBERRA ACT 2601

Dear Sir/Madam

**Submission to Consultation Paper on the Productivity Commission's  
recommendations for the gas access regime**

As the NSW jurisdictional regulator under the gas access regime the Tribunal is concerned that a number of the recommendations contained in the Productivity Commission's Inquiry Report, and the proposed responses by SCO, if implemented, would create significant practical difficulties for its administration of the regime.

The key areas of concern to the Tribunal are provided below for your consideration.

**Proposed objects clause (PC recommendations 5.1 and 5.4)**

The Tribunal is generally supportive of introducing an overarching objects clause based on economic efficiency into the National Gas Code. However, the removal of several of the factors in section 2.24 of the National Gas Code fails to recognise what the Tribunal sees as the key role of an economic regulator - balancing the conflicting interests of the various stakeholders. The Tribunal believes that the section 2.24 factors are critical to providing guidance for the exercise of regulatory discretion and act to prevent theoretical outcomes that are detached from reality.

The Tribunal strongly considers that explicit consideration of the impact of its decisions on stakeholders and recognition of its discretion in balancing these interests should be retained in the National Gas Code.

**Changes to the rate of return provisions (PC recommendations 7.9 to 7.11)**

The Tribunal believes that the PC has failed to address the primary issue surrounding rate of return - determination of an appropriate point estimate to be used for calculating revenue. The proposed revisions to sections 8.30 and 8.31 of the National Gas Code would require the Tribunal to approve a proposed method and rate of return where the method has a plausible conceptual basis and the underlying values lie within a range of plausible estimates.

The Tribunal considers that the CAPM, and indeed alternative approaches, can yield an extremely wide range of plausible outcomes. It is in the service provider's interests to choose a point estimate at the upper bound of this range. The Tribunal considers that the regulator should have discretion to decide whether the proposed point estimate is consistent with the National Gas Code's objectives and appropriately balances the interests of the various stakeholders.

The Tribunal believes that it would be difficult in practice to reject any rate of return proposed by a service provider based on the criteria recommended by the PC. The recommendations, to the extent that they preclude regulators from exercising discretion in determining an appropriate point estimate after taking into account all relevant factors, would seriously undermine the role of the regulator as an expert body.

The Tribunal rejects the inference in PC recommendation 7.10 that regulation poses an additional risk to service providers. Regulators are required by their legislation to have regard to a number of considerations, but there is little evidence of unwarranted risk due to regulators exercising their discretion. Regulators are conscious of this potential disincentive to investment and for that reason they are generally consistent, particularly with respect to the application of the building block approach, regulated asset values and costs of capital. The Tribunal is confident that regulated rates of return are generally accepted by the investment community, and notes that regulated assets remain attractive investments, usually trading at a premium to their regulated value.

#### **Provision of data by service providers (PC recommendations 7.12 and 7.13)**

Although the PC recommendations do address information collection problems experienced by regulators, the Tribunal does not believe they go far enough. The Tribunal asks for clarification of the scope for using section 4.2 of the Code to obtain information for use in access arrangement reviews, given that they are a part of the ring-fencing provisions of the Code. Further, the Tribunal seeks consideration for more flexibility in the list of information that must be provided pursuant to attachment A of the National Gas Code - the type of information to be provided will vary depending on the nature of the regulated pipeline and the details of the proposal made by the service provider, and there should be room for negotiation between the service provider and the regulator to allow for this.

#### **Introduction of a price monitoring regime (PC recommendation 8.1)**

The Tribunal notes there is debate about the cost effectiveness of regulating small gas networks and acknowledges the recent trend for small gas networks to apply to be un-covered and this being granted. The Tribunal also notes that the National Gas Code requires the same level of regulatory review regardless of the size of the gas pipeline/network.

The Tribunal is in the process of reviewing access arrangement revisions submitted by Country Energy Gas for the Wagga Wagga distribution network, a relatively small gas network in regional NSW. The Tribunal considers there has been some advantage from undertaking this review. The Tribunal's draft decision requires significant amendments to the access arrangement that will result in an average real price reduction of approximately 5.5 per cent rather than the proposed 23 per cent real increase in the first year of the access arrangement, while preserving adequate incentives for future investment in the Wagga Wagga natural gas distribution network. The Tribunal considers that the alternative approach of price monitoring may have resulted in substantial price increases for many customers of the network.

**Removal of discretion to extend review period (PC recommendation 11.1)**

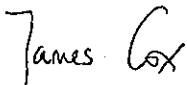
The Tribunal endorses the PC's recommendation to simplify and shorten the regulatory review by removing the requirement for a further final decision to be issued. However, the Tribunal is concerned by the recommendation to remove the ability to extend the timeframe for decisions on access arrangements beyond eight months.

This approach fails to recognise the reality of regulatory reviews and as a result has the potential to compromise effective decision making. The eight month timeframe is unrealistic for revisions that involve more than incremental changes and does not take into account the level of public consultation that stakeholders expect or the fact that regulators are often frustrated by the lack of information provided by service providers.

In order for the recommended timeframes to be met the Tribunal considers that a lengthy pre-review process would need to be undertaken. The Tribunal does not believe that this would assist in increasing the timeliness of decisions or reducing the costs of the review process.

Please do not hesitate to contact me if you wish to discuss this matter.

Yours sincerely



James Cox  
*Chief Executive Officer and Full Time Member*