

Standing Committee of Officials of the
Ministerial Council on Energy

Explanatory Material for the
Second Exposure Drafts of the
National Gas Law and National Gas Rules

July 2007

Glossary

ACCC	Australian Competition and Consumer Commission
ACT	Australian Competition Tribunal
AEMA	Australian Energy Market Agreement - the intergovernmental agreement between the Commonwealth and all of the States and Territories first made in 2004 and amended in 2006
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Expert Panel	Panel established by MCE in December 2005 to advise on a model to achieve a common approach to transmission and distribution revenue and network pricing across electricity and gas (Final Report delivered April 2006– see below for internet link to the report)
GPAL	Gas Pipelines Access Law – Schedules 1 and 2 to the <i>Gas Pipelines Access (South Australia) Act 1997</i> , including "Third party access to natural gas pipelines" (Schedule 1) and the National Third Party Access Code for Natural Gas Pipeline Systems (the Gas Code – Schedule 2)
MCE	Ministerial Council on Energy
NCC	National Competition Council
NEL	National Electricity Law, Schedule to the <i>National Electricity (South Australia) Act 1996</i>
NER	National Electricity Rules – Statutory Rules made under Part 7 of the NEL
NGL	National Gas Law, Schedule to the new <i>National Gas (South Australia) Act 2007</i>
NGR	National Gas Rules – Statutory Rules made under Chapter 7 of the NGL
SCO	Standing Committee of Officials reporting to MCE

Relevant Publications

SCO Response to Submissions on the Exposure Draft of the National Gas Rules (Energy Market Reform Bulletin No.90, 14 May 2007)

<http://www.mce.gov.au/assets/documents/mceinternet/BulletinNo%2E9020070515085807%2Epdf>

SCO Response to Submissions on the Draft of the National Electricity Law (Amendments) and the AEMC Rule-change process (Energy Market Reform Bulletin No.85, 13 April 2007)

<http://www.mce.gov.au/assets/documents/mceinternet/BulletinNo%2E8520070413171030%2Epdf>

SCO Response to Submissions on the Exposure Draft of the National Gas Law (Energy Market Reform Bulletin No.82, 1 March 2007)

<http://www.mce.gov.au/assets/documents/mceinternet/Energy%5FMarket%5FReform%5FBulletin%5FNo%2E8220070301111053%2Epdf>

MCE Decision on Review of Decision-Making in the Gas and Electricity Regulatory Frameworks, June 2006

<http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=839F2DC1-AE13-142E-8425FEF5F2E8C822>

MCE Response to the Productivity Review of the Gas Access Regime, May 2006 (PC Response)

<http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=1657B707-AD38-B43A-5CE8B8C11AFBE8E2>

Final Report of the MCE Expert Panel on Energy Access Pricing, April 2006

<http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=B0F3AD4C-A1C6-28DB-CB9CC594D2B88090>

Productivity Commission Review of the Gas Access Regime, June 2004

<http://www.pc.gov.au/inquiry/gas/finalreport/index.html>

Overview

This document accompanies the second exposure draft of the National Gas Law (NGL) and National Gas Rules (NGR). It seeks to explain the changes between this document and the first exposure draft of the NGL, which was released by the Ministerial Council on Energy's Standing Committee of Officials on 7 November 2006. Note also that a draft of the National Gas Regulations which will be released shortly with a separate explanatory note.

MCE SCO seeks stakeholder input into this second round of consultation on the NGL. To this end, SCO will be holding intensive consultation sessions with those industry and consumer associations who made substantive submissions on the first exposure draft.

The purpose of this consultation is to give stakeholders an opportunity to assess whether the second exposure draft implements agreed policy, and to raise issues of workability with the NGL and NGR.

Agreed policy in relation to the NGL/NGR regime is primarily captured by the:

- Energy Market Reform Bulletin No.82, 1 March 2007: SCO Response to Submissions on the Exposure Draft of the National Gas Law (the "SCO NGL Response"); and
- Energy Market Reform Bulletin No.90, 14 May 2007: SCO Response to Submissions on the Exposure Draft of the National Gas Rules (the "SCO NGR Response").

Elements of the SCO Response to Submissions on the Draft of the National Electricity Law (Amendments) and the AEMC Rule-change process (Energy Market Reform Bulletin No.85, 13 April 2007) are also relevant to understanding changes between the first and second exposure drafts of the NGL, such as those made to Chapter 8 of the NGL.

Due to the need for timely finalisation of the NGL and NGR, this consultation is not intended to involve significant diversions from agreed policy as outlined in the documents mentioned above, but rather to focus on whether the agreed policy has been implemented in a workable and effective manner.

Provisions moved from Law to Rules

In response to consultation on the first exposure draft of the National Gas Law, SCO has agreed to move significant amounts of legislative detail from the Law to the Rules in the second NGL exposure draft.

This change maintains the policy of establishing the essential legislative framework in the Law, whilst allowing flexibility for the detailed aspects of the regulatory regime to be amended in future through the rule-change process.

Significant parts of the first NGL exposure draft moved to the NGR include:

- Detailed aspects of the coverage application and coverage revocation processes (NGR Part 4)
- Detailed aspects of reclassification and variation of classification decisions (NGR Part 13);
- Provisions relating to the competitive tendering process (formerly Part 3.3 of the NGL, NGR Part 5);
- Detailed aspects of the light regulation determination and light regulation revocation processes (NGR Part 7);
- The access arrangement approval process (NGR Part 8);
- Detailed aspects of the greenfields pipeline incentives application process (NGR Part 12);
- Provisions relating to the facilitation of and requests for access (NGR Part 10);
- Provisions relating to safety and technical aspects of an access dispute (NGR Part 11);
- Provisions relating to access determinations that require the expansion of capacity by a service provider (NGR Part 11); and
- Provisions relating to the establishment of a scheme register by the AEMC (NGR Part 14).

Additional provisions to be included – Gas Bulletin Board

As a commitment to the good work that the Gas Market Leaders Group has done on establishment of a bulletin board and recognising its value, SCO has also agreed that the National Gas Law should include provisions for empowering a bulletin board. However, SCO was conscious that it did not want its decision to delay the release of the Exposure Draft of the Law. Accordingly, these provisions are not included in the Exposure Draft.

Work is proceeding concurrently on the bulletin board provisions with a view to including them in the Bill to be introduced into the South Australian Parliament. However, SCO is unable at this stage to confirm that drafting can be done within the current timetable.

SCO notes that most of the mechanics of the establishment and operation of the bulletin board will be in the National Gas Rules with only the minimum of provisions being in the Law. In addition, the provisions in the Law will not create binding obligations until they are supplemented by the detailed provisions in the Rules.

The Rules will be developed in consultation with the GMLG. The GMLG released a consultation paper entitled 'Bulletin Board Business and Data Requirements' and conducted consultation sessions in June on the policy issues surrounding the bulletin board. The consultation paper and submissions to it are available from the MCE website at

<http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=05153518-A00A-8738-D7588EC810441667>.

Stakeholders will be consulted on the proposed Rules for the bulletin board.

Provisions deleted from the NGL

Former section 24 – Fit for purpose

In response to concerns raised in consultation, section 24 of the first exposure draft of the NGL has been deleted. Former section 24 was intended to establish 'fit-for-purpose' decision making in the NGL.

However, as the Law no longer deals with the approval of access arrangements, the Law no longer requires a clause explicitly establishing a fit-for-purpose decision making model. Instead, the Rules must establish this model.

Accordingly, the only provision in the Law dealing with 'fit for purpose' decision making is section 73(3)(c), which provides that the Rules may confer functions or powers on, or leave any matter or thing to be decided or determined, by the AER.

This clause is sufficient to set the framework for 'fit for purpose' decision making. In particular, this clause clearly allows the Rules to specify the differing requirements the AER must satisfy when making decisions to approve or refuse to approve an access arrangement. Further detail about the implementation of a fit-for-purpose decision making model will be provided in the Second Reading Speech to the Bill.

For the initial NGR, rule 39 sets out the three types of discretion involved in a 'fit for purpose' framework.

Former section 70 – Prohibition against TFP

Similarly, section 70 of the first exposure draft of the NGL has been deleted. This clause prevented the use of "total factor productivity" (TFP) regulation, unless a regulation was passed to allow this methodology to be used.

In light of consultation, SCO considers it inappropriate to involve MCE in detailed decision-making in relation to the regulatory regime in this way. Accordingly, former section 70 has been deleted.

Summary of other principal NGL amendments

In addition to the changes made from the first exposure draft of the NGL outlined above, the following table summarises the other principle amendments which appear in the second exposure draft of the NGL.

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
CHAPTER 1 PRELIMINARY			
2	Definition of full access arrangement	N	The NGL includes a definition of full access arrangement , in contra distinction to 'limited access arrangement'. The former includes an access arrangement that provides for price or revenue regulation as well as all other matters required by the Rules to be regulated in an access arrangement. The latter makes no provision for price or revenue regulation. These two concepts are pivotal to implementing the MCE's decision to provide for light handed regulation of some pipelines.
2	Definition of associate contract	Y	The definition of associate contract has been amended so that it is now consistent with the definition in the 10.8 of the Gas Code. Associates will no longer be prescribed by Regulations.
2 and 3	Definition of civil penalty provision	Y	Provisions in the Law that are civil penalty provisions are set out in section 3. They are consistent with civil penalty provisions in the Gas Code. Other civil penalty provisions of the Law and Rules will be prescribed by the Regulations namely rules 26(4), 32(1), 35, 36, 46, 42(1), 48(4), 53(1), 105, 106, 107, 108, 109, 110, 134 and 135. The same structure applies to conduct provisions with the relevant rules being 32(1), 36, 105, 106, 107, 108, 109, 110, 113(3), 134 and 135.
2	Definition of covered pipeline service provider	N	The term covered pipeline service provider has been created to ensure that economic regulatory obligations, such as ring-fencing, are only imposed upon persons who are a service provider in respect of a covered pipeline (cf 4.1 of the Gas Code).
2	Definition of designated pipeline	N	The term designated pipeline has been introduced such that service providers of pipelines who are designated by the Regulations are unable to make applications for light regulation for those pipelines (see section 105). It is currently proposed that most covered pipelines in Victoria, South Australia and Western Australia will be

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
			designated pipelines. The Regulation-making power will be designed such that no additional pipelines may be prescribed by regulation after the initial regulations, but that pipelines may be removed from the list.
2	Definition of reference service	N	The definition of reference service (s.7 of the first exposure draft) has been revised so that it is a pipeline service specified by, or determined by the AER under, the Rules as a reference service. The Rules will retain the 'significant part of the market' test (rule 50(c)) and the AEMC must have regard to the 'form of regulation factors' in amending this test (section 271).
2, 6 and 7	Definition of regulatory obligation or requirement and regulatory compensation payment	Y	Regulatory obligation or requirement and Regulatory compensation payment replace the previously defined 'regulatory obligation or instrument'. These provisions are relevant to the revenue and pricing principles set out in section 23: among other things a service provider should be provided with a reasonable opportunity to recover at least the efficient costs the service provider incurs in complying with a regulatory obligation or requirement or making a regulatory compensation payment. Sections 26 and 266 set out the circumstances in which the AER and AEMC are required to take these principles into account. These should ensure that allowances are still made in economic regulatory decisions for an efficient level of guaranteed service level (GSL) payments.
2 and 8	Definition of service provider	N	A service provider now includes a person who 'controls' a pipeline as well as a person who owns or operates the pipeline making the NGL consistent with s 11 of the NEL. Certain gas market operators (like VENCORP and the future NEMO) are excluded from being a service provider.
9	Things done by one service provider to be treated as being done by all of service provider group	N	Section 9 is consistent with the intent of cl 10.1 of the Gas Code. It will allow one access arrangement to be submitted for a pipeline with multiple service providers.
10	Local agents of foreign service providers	N	Section 10 of the NGL sets out the accountability of a local agent appointed by a service provider that is a foreign company (under s 601CG of the <i>Corporations Act 2001</i>).

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
2 and 23	Revenue and pricing principles	Y	The revenue and pricing principles have been clarified. Two key changes include a requirement to have regard to any regulatory valuation of a pipeline in a previous relevant access arrangement decision (section 23(4)) and a requirement that a reference tariff should allow for a return commensurate with the regulatory and commercial risks involved in providing the reference service to which the tariff relates (section 23(5)). This aligns the principle to the pricing principle in s 44ZZCA(a)(ii) of the <i>Trade Practices Act 1974</i> (TPA).
CHAPTER 2 FUNCTIONS AND POWERS OF GAS MARKET REGULATORY BODIES			
42 and 43	Meaning of <i>related provider</i> and <i>contributing service</i> in relation to regulatory information instruments	Y	Related provider replaces the previously defined class of associate of a service provider . A related provider means a person who supplies a contributing service . A contributing service is one that contributes in a material way to the provision of a pipeline service by a service provider. Section 43(2) sets out the factors to which the AER must have regard in deciding the question of materiality and allows the rules to add additional matters. These definitions are pivotal in determining whether or not the AER may serve a notice on a person who is not a service provider.
47	Service and making of regulatory information instrument	Y	Section 47 specifies the 'tests' which the AER must apply before it may issue a regulatory information instrument: first the AER can only issue the instrument if it considers it is 'reasonably necessary' for the performance or exercise of its functions. Subsection 47(2) sets out what the AER must have regard to in making that decision. This includes the likely costs that may be incurred by an efficient service provider or efficient related service provider in complying with the instrument. The AER is prohibited from issuing an instrument solely for the purpose of: <ul style="list-style-type: none"> (a) investigating breaches or possible breaches of provisions of the NGL, the Regulations and the NGR; (b) instituting and conducting proceedings in relation to breaches of provisions of the NGL, Regulations and the NGR;

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
			<p>(c) instituting and conducting appeals from decisions in proceedings referred to in (b) (d) collecting information for the preparation of a report under Division 5; or (e) any application for review of a decision of the AER under Part 7.5 of Chapter 7.</p> <p>The AER is also, when considering issuing an instrument to a related service provider to have regard to:</p> <p>(a) whether the information can be provided by the relevant service provider or prepared, maintained or kept in the way specified in the instrument; (b) whether the contributing service is provided on a genuinely competitive basis; (c) the nature of any ownership or control between the service provider and the related provider; (d) the nature of any ownership or control between the different related providers supplying; and (e) any other matter the AER considers relevant.</p>
48	Serving an instrument on a related provider	Y	This section sets out additional matters the AER needs to have regard to when serving an instrument on a related provider including whether the service provider can provide the information sought, ownership and control arrangements and whether the related provider is providing its services on a genuinely competitive basis.
49	AER must consult before publishing a general regulatory information order	Y	The Rules will set out the public consultation requirements the AER consultation must comply with before it makes a regulatory information order (see rules 8 and 136)
51	Opportunity to be heard before regulatory information notice is served	Y	The AER must give written notice to a service provider of the anticipated serving of a regulatory information notice seeking representations from the service provider, in the case of an 'urgent' notice, between 7 and 14 days and, in all other cases, at least 30 days from the date of the written notice.

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
63	Preparation of service provider performance reports	Y	<p>The requirements in relation to performance reporting have been re-worked. In particular, the AER may only prepare a report on the financial performance or operational performance of a service provider(s) of a covered pipeline if it will or is likely to contribute to the achievement of the national gas objective. A report prepared under cl 63:</p> <ul style="list-style-type: none"> (a) must deal with the financial or operational performance of the service provider in relation to – <ul style="list-style-type: none"> (i) complying with pipeline service standards; and (ii) standards relating to the provision of pipeline services to users or end users; (iii) the profitability of service providers in providing pipeline services; (b) may deal with the service provider's performance in relation to other matters or things if that performance is directly related to the performance or exercise by the AER of an AER economic regulatory function or power. <p>Clause 63 also clarifies that the report may use information provided under a regulatory information instrument and may include a comparison of profitability of different service providers from the provision of pipeline services provided by those providers.</p> <p>The Rules will detail consultation requirements before the AER prepares a performance report (rule 137). The report will be published on the AER's website.</p>
67	AER enforcement guidelines	Y	<p>Consistent with the MCE Communique (dated 25 May 2007) cl 67 provides the AER may publish guidelines specifying matters to which it will have regard in deciding whether to issue an infringement notice or institute proceedings with respect to a breach of the NEL or Rules. The guidelines must be published on the AER website.</p>
CHAPTER 3 COVERAGE AND CLASSIFICATION OF PIPELINES			
88	Coverage application to be dealt with in accordance with the Rules	N	<p>The Rules will deal with the procedure for an application for coverage (Rules 14 – 19).</p>

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
103	Making of light regulation determinations when a pipeline is not a covered pipeline	N	<p>This Part reflects MCE's decision that the NCC (and not the AEMC) is the decision maker in relation to applications for covered pipelines to be subject to 'light regulation' (see also rules 33 – 38).</p> <p>This subdivision allows coverage and light regulation decisions to be made by the NCC at the same time.</p> <p>Subsection 103(2) and section 105 reflect MCE's decision that no application for a light regulation determination may be brought in respect of a “designated pipeline”: a pipeline prescribed by regulation (see definition of designated pipeline).</p>
109	When light regulation determinations take effect	N	<p>A light regulation decision now takes effect either immediately or within 90 days after it is made.</p>
116	Principles governing the making or revoking of light regulation determinations	N	<p>When making or revoking a light regulation determination the NCC is required to have regard to the national gas objective and carry out a form of 'net benefit test' as recommended by the Expert Panel – although not a strict quantitative assessment. The objective is that the net benefit from regulation is maximised after considering the potential cost imposed by regulation. The NCC is required to consider:</p> <ul style="list-style-type: none"> • the likely effectiveness of the forms of regulation to promote access to pipeline services; • the costs of an efficient service provider, efficient service users and prospective end users and likely costs of end users; • the form of regulation factors; • anything else the NCC considers is relevant.
119	AER reviews of whether a pipeline should continue to be a designated pipeline	N	<p>This provision implements MCE's decision in relation to the 'light regulation' decision maker – the MCE or a designated pipeline service provider may request the AER to conduct a review into and report to the MCE as to whether a pipeline should continue to be a designated pipeline. The AER is required to have regard to the National Gas Objective and whether there has been a material increase in competition in a market served by the designated pipeline. The AER will publish the report on its website and, if a service provider has requested the review, give a copy of the report to that service provider.</p>

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
			Note also that the MCE may also decide to remove a pipeline from the list of designated pipelines without advice from the AER.
CHAPTER 4 GENERAL REQUIREMENTS FOR PROVISION OF COVERED PIPELINE SERVICES			
126	Submission of full access arrangement in respect of pipeline services provided by means of covered pipeline	N	The requirements for making an application for a full access arrangement to the AER will be set out in the Rules (See Part 8 of the Rules)
130	Service provider providing light regulation services must not price discriminate	N	Section 130 prohibits a service provider from engaging in price discrimination, subject to the exception where the discrimination is conducive to efficient service provision. The onus will be on the service provider to demonstrate the exception applies. The criterion of 'any other rational economic basis' has been deleted because of its ambiguity and because the current test was deemed sufficient.
132	Meaning of marketing staff for the purposes of ring-fencing	N	The definition of marketing staff has been narrowed so that it is consistent with the Gas Code.
137	AER ring fencing determinations	N	The obligations on the AER in carrying out a ring fencing determination have been clarified to more accurately reflect the nature of additional ring-fencing obligations.
141-142	Prohibitions in relation to associate contracts	N	These provisions have been simplified. The prohibition is on entering into an associate contract or giving effect to a provision in an associate contract that has anti-competitive effect (141) or is inconsistent with the competitive parity rule (set out in section 142 (2)) unless the contract is an approved contract (see section 2) or the provision is in an approved contract. The approval process remains optional and is set out in Rules 31 and 32.
CHAPTER 5 GREENFIELDS PIPELINE INCENTIVES			
146, 155	Application for either Greenfields incentive to be dealt with in accordance with the Rules	N	Previously all the detail was in the NGL, now the Rules will set out how the NCC must deal with an application for a 15 year no-coverage determination and price regulation exemptions (see Part 12 of the Rules).
CHAPTER 6 ACCESS DISPUTES			
177	Parties to an access dispute	Y	A party who has made written application to the AER and been accepted by it as

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
			having a sufficient interest is included as a party to an access dispute.
181	No access determination if AER considers there is genuine competition for pipeline service	Y	The revision of section 181 in the NGL achieves consistency between the NGL and the NEL: the AER can refuse to make an access determination where the relevant pipeline service could be provided on a genuinely competitive basis by a person other than the service provider or an associate of the service provider.
184	Rules may allow determination that varies applicable access arrangement for installation of a new facility	N	Where the AER proposes to make an access determination that will require a service provider to expand a pipeline and for the user to make a relevant capital contribution the Rules will allow the AER to vary the applicable access arrangement and set bounds around its capacity to do this. This allows the rules to more closely define the economic issues involved in these types of determinations (see rules 115 and 116).
Part 6.7	Joint access dispute hearings	Y	This Part is new and replicates equivalent provisions of the TPA.
CHAPTER 7 PROCEEDINGS UNDER THE NATIONAL GAS LAW			
215	Factors in civil penalty proceedings	Y	Paragraph (e) has been clarified and will be introduced into the NEL to ensure that compliance programs are relevant in setting the level of any civil penalty.
223	Merits review definitions – reviewable regulatory decision	Y	The NGL now sets out what decisions are reviewable including a limited access arrangement decision (included as part of an applicable access arrangement decision). The Regulations may also prescribe other reviewable regulatory decisions.
223	Merits review definitions – small/medium user or consumer intervener	Y	The definition of small/medium user or consumer intervener is relevant for the operation of section 247: the Tribunal is prohibited from making a costs order against a small/medium user or consumer intervener except in certain circumstances. This means a small/medium user or consumer intervener is treated in the same way as the original decision maker.
224	Applications for review of reviewable regulatory decisions	N	Section 224 clarifies that only final decisions are subject to an application for review (ie the approval of a proposed access arrangement or the making of an access arrangement by the AER).
226	By when an application must be made	Y	The period within which an application for review must be made has been extended

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
			to 21 days (from 14 days) after publication of the reviewable regulatory decision. This is consistent with equivalent provisions in the <i>Trade Practices Act 1974</i> .
227	Tribunal must not grant leave if error is not material	Y	The test the Tribunal must apply in determining whether to grant leave to apply for review has been revised (from 'serious issue to be determined'): the Tribunal may only grant leave if it is satisfied that there is an error in the reviewable regulatory decision that, if established, would be material to the operation or effect of the decision. However, the monetary thresholds remain in section 228.
233	Leave for user or consumer intervener	Y	Section 233 of the 2 nd Exposure Draft was section 281 in the previous Exposure Draft. It has been amended to clarify that the Tribunal has a broad discretion to grant leave to a user or consumer intervener to intervene. In particular, the factors listed in section 233(3) that the Tribunal may take into account in exercising its discretion are not to limit that discretion.
Part 7.5, Division 3	Tribunal review of AER information disclosure decisions under section 308	Y	This Division is new and reflects the decision to provide for review of the AER's decision to release confidential information. The application must be made within 7 days (consistent with s 43 of the GPAL) and the Tribunal is deemed to have allowed disclosure if it does not make a decision within 30 days.
244	What determinations can do	Y	There is no longer any explicit prohibition on retrospectivity of decisions in this provision.
247	Costs in a review	Y	See the comment under section 223 – definition of small/medium consumer intervener.
248	Amount of costs	Y	The NGL has been revised so that there is no presumption an unsuccessful applicant for review should pay indemnity costs. Costs are within the discretion of the Tribunal and include an option for indemnity costs.
Part 7.6	Enforcement of Access Determinations	Y	This Part is new and is based on equivalent provisions in the <i>Trade Practices Act 1974</i> .
CHAPTER 8 THE MAKING OF THE NATIONAL GAS RULES			
269	Definitions – <i>gas market regulatory body</i>	Y	This definition is relevant for the operation of section 277 dealing with 'Fast track' rules where there has been previous public consultation by a gas market regulatory

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
			body or an AEMC review.
275	AEMC may make more preferred rule in certain cases	Y	Section 275 clarifies the AEMC may make a Rule different from the market initiated proposed Rule (defined in section 269) if it is satisfied that the different Rule will or is likely to better contribute to the achievement of the national gas objective.
277 and 278	Fees allowed for rule change applications	Y	An ability for fees to be charged for rule change applications has been added to the NGL, however the MCE has decided not to set any fees at this stage.
279	Consolidation of more than one Rule request	Y	Section 279 provides for the circumstance in which the AEMC may consolidate Rule making requests.
281	AEMC may request further information from Rule proponent in certain cases	Y	Section 281 clarifies the AEMC's capacity to request further information from a Rule proponent.
284	"Fast track" Rules where previous public consultation by gas market regulatory body or an AEMC review	Y	This section implements MCE's response to the Gas Market Leaders' Group recommendations concerning gas market regulatory bodies involvement in the rule change process. The "fast track" process allows the AEMC the discretion to go straight to a draft determination where the gas market regulatory body has requested the change and consulted with the public about that change or where the proposed change results from an AEMC review. This process is complemented by section 287(3) requiring the AEMC publish a draft determination for a "fast track" Rule within 5 weeks (rather than the usual 10 weeks for non "fast track" Rules) after publishing notification of the Rule change proposal.
291	Further draft Rule determination may be made where proposed Rule is a more proposed preferable Rule	Y	This section is designed to allow the AEMC to make an additional draft determination where the rule they intend to make differs in a material way to what has been consulted upon to date.
297	AEMC may extend period of time for making of final Rule determination for further consultation	Y	Any ability for the AEMC to extend the time period for a final determination and conduct a further period of limited consultation has been added to deal with discrete new issues that may be raised in consultation on the draft decision.
299	AEMC must publicly report on Rules not made within 12 months of public notification of requests	Y	To ensure timeliness of the rule change process, the AEMC will be asked to report each time a rule change process extends beyond 12 months. Similar reporting obligations will exist in the rules for AER decisions.
SCHEDULE 1 RULE MAKING POWERS			

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
Generally	Rule making powers	N	The rule making powers have been updated to reflect the additional matters now in the Rules.
SCHEDULE 2 INTERPRETATION			
8	“Law extrinsic material” and “Rule extrinsic material”	Y	The definition of extrinsic material has been clarified to distinguish between material relevant for the interpretation of the law and that for the rules.
SCHEDULE 3 SAVINGS AND TRANSITIONALS			
Generally		N	These provisions are new and are intended to save and transition certain existing arrangements which are common among the participating jurisdictions from the current regime into the new regime.
2	Schedule subject to jurisdictional legislation	N	The schedule is subject to any jurisdictional legislation that derogates from it or substitutes or modifies any provision of it to cater for individual jurisdictional circumstances.
3	Saving of old access law and Gas Code	N	This provision ensures that all rights and obligations accrued under the Gas Code are still enforceable. It is also intended that through this section, procedures (such as coverage or access arrangement decisions) will be subject to the existing merits review arrangements in the GPAL.
4	Pending application for the classification of pipelines lapse	N	All pending application for the classification of pipelines lapse on the commencement of the NGL as a new process is provided for.
5	Old scheme coverage determinations	N	All pipelines covered under the old scheme will remain covered through this and items 6 and 7.
6 & 7	Classification	N	Pipelines classified as either transmission or distribution under the old scheme continue to be so
8 – 10	Pending coverage determinations	N	Pending coverage determinations under the old scheme will be dealt with by the NCC and the relevant minister under the Gas Code. The resulting coverage determinations are deemed to be determinations under the NGL
11 - 13	Pending coverage revocation determinations	N	Pending coverage revocation determinations under the old scheme will be dealt with by the NCC and the relevant minister under the Gas Code. The resulting coverage revocation determinations are deemed to be determinations under the NGL

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
14	Binding no – coverage determinations	N	A binding no–coverage decision in effect under the Gas Code remains in force under the NGL
15 – 16	Pending binding no–coverage determinations	N	Pending no–coverage determinations under the old scheme will be dealt with by the NCC and the relevant minister under the Gas Code. The resulting no–coverage determinations are deemed to be 15–year no–coverage determinations under the NGL.
17 – 18	Old scheme access arrangement	N	All access arrangements under the Gas Code (including any limited access arrangements) continue in force as access arrangements under the NGL
19 – 20	Access arrangements submitted but not approved or rejected before repeal of old scheme	N	The relevant regulator must continue to assess the access arrangements (including limited access arrangements) under the Gas Code. If approved it is deemed to be an access arrangement under the NGL.
21 – 22	Extension and expansions and queuing policies	N	All policies in force under the Gas Code are deemed to be in force as requirements under the NGL. Further transitional provisions will be included into the Regulations or rules to deal with the continuance of other issues relating to the rules and Gas Code (eg fixed principles) if required.
23	Old scheme price regulation exemption	N	All old scheme price regulation exemptions under the Gas Code are deemed to be price regulation exemptions under the NGL
24 – 25	Pending price regulation exemption decisions	N	Pending price regulation exemption decisions under the old scheme will be dealt with by the NCC and the relevant minister under the Gas Code. The resulting price regulation exemption decisions are deemed to be decisions under the NGL
26 – 27	Ring fencing waivers and additional requirements	N	All additional ring fencing obligations and waivers of ring fencing obligations effective in force under the Gas Code are deemed to be valid under the NGL
28	Non – finalised access disputes	N	Non–finalised access disputes will be dealt with under the Gas Code but they will be dealt with by the AER
29 – 30	Investigations and proceedings	N	The AER will be empowered to complete any investigations or proceedings initiated by the relevant regulator and will be able to initiate investigations into breaches of the Gas Code
31	Approved associate contracts	N	All approved associate contracts in force under the Gas Code are deemed to be approved under the NGL

Provision in 2 nd Exposure Draft of the NGL	Issue	NEL issue?	Change
32	Pending tender approval requests lapse	N	All applications for approval of tender processes under the Gas Code that have not had a decision made lapse on the commencement of the NGL
33	Rights under certain change of law provisions or deeds not to be triggered	N	The commencement of the NGL is not considered a change of law under any agreement
34	References to provisions of the old access law and Gas Code	N	References to the Gas Code and GPAL are to be read as references to the equivalent provisions of the NGL or NGR.
35	References to relevant regulator in access arrangements	N	Unless the context requires otherwise all references to the relevant regulator in access arrangements are to be read as references to the AER

Summary of principal amendments to the National Gas Rules

This table sets out the key amendments to the National Gas Rules. Further explanation of the modifications to the new facilities investment criteria (rule 83) are set out in Appendix A.

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
PART 1 PRELIMINARY			
3	Definition of <i>access arrangement period</i>	NGL 69, NGR 1.2	Applicable access arrangements (other than for some voluntary and limited access arrangements) now do not expire, but are reviewed, as under the Gas Code.
3	Definition of <i>revision commencement date</i>	NGL 69, NGR 1.2	Implements the policy that applicable access arrangements (other than for some voluntary and limited access arrangements) now do not expire, but are reviewed, as under the Gas Code.
PART 2 REGULATORY ISSUES			
4-6	Public information role		These provisions have remained unchanged.
PART 3 DECISION-MAKING UNDER THE LAW			
8	Standard consultative procedure	NGR 3.1	Decision-making and consultative procedures have been consolidated in the Rules as per the policy response. The "standard consultative procedure" replaces Division 1 of Part 8.5 of the first exposure draft of the NGL.
9	Expedited consultative procedure	NGR 3.1	Decision-making and consultative procedures have been consolidated in the Rules as per the policy response. The "expedited consultative procedure" replaces Rule 18 of the first exposure draft of the NGR.
11	Calculation of time	NGR 3.4	This rule provides through subsection (b) that a notice under the Law, including a regulatory information notice, stops the clock for a decision maker.
PART 4 COVERAGE			
14-19	Coverage application and revocation processes	NGL 12	These processes have been moved from the first exposure draft of the NGL to the Rules, to give flexibility and achieve consistency with MCE's agreed governance model.

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
PART 5 COMPETITIVE TENDERING			
20-28	Competitive tender processes and coverage	NGL 68, NGR 5.3, 5.4 and 5.5	The terminology used in this part now interacts with section 120 of the NGL such that: <ul style="list-style-type: none"> • The NCC can delay consideration of a coverage application relating to a prospective CTP pipeline; • A CTP pipeline does not become covered until a tender approval decision becomes irrevocable (i.e. after approval of the tender report); and • A prospective CTP pipeline that does not receive final tender approval does not become covered under a full access arrangement.
20(2)(b)	Specification of proposed services in a tender	NGR 5.14	A proposed tender process is now only required to outline the services sought through the tender process, rather than a description of the proposed pipeline.
21(1) and (2)	Time frame for initial AER decision	NGR 5.8	The time available for the AER to make an initial decision as to whether to approve a proposed tender process as a competitive tender process has been reduced from 6 months to 60 days (with an option for a 30 day extension).
21(3)(c)(i)	Restricting access to pipeline services	NGR 5.15	The rules now specify that a tender must not limit the kinds of pipeline services to which access may be sought. The first exposure draft erroneously included all services (e.g. telecommunications services).
21(3)(d) and (4)	Essential terms and conditions in a competitive tender process	NGR 5.9, 5.10 and 5.11	The AER no longer has discretion to specify essential terms and conditions for a competitive tender process, other than those specified in the Rules. The AER's rejection of a proposed process is now primarily based on whether the process includes the essential terms and conditions specified in the Rules.
24(2)	Basis of revocation of tender approval decision	NGR 5.6	The AER can now only revoke its tender approval decision on the basis that the tender process was not conducted in accordance with the approved process. The problematic provision from the first exposure draft of the Law that allowed revocation on the basis that a condition was "unreasonable having regard to the terms and conditions of the applicable access arrangement" has been removed.
26(1)	Amendment of successful tender by agreement between tenderer and	NGR 5.16	The Rules now give flexibility for the proponent and successful tenderer to agree, with AER approval, to changes to the successful tender prior to the submission of

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
	proponent		an access arrangement for the pipeline. The access arrangement is then based upon the tender conditions which should simplify the approval process and increase regulatory certainty.
PART 6 RING-FENCING			
30(2)	Test for waiver of prohibition on carrying on of a related business	NGL 66	This rule establishes a test that replicates the test for the waiving of the prohibition on carrying on a related business in 4.15(a) of the Gas Code.
30(3)	Test for waiver of marketing staff and separate accounts ring fencing requirements	NGL 66	This rule establishes a test that replicates the test for the waiving of marketing staff and separate accounts ring fencing requirements in 4.15(b) of the Gas Code.
31-32	Associate contract processes	NGL 12	These processes have been moved from the first exposure draft of the NGL to the Rules, to give flexibility and achieve consistency with MCE's agreed governance model.
31(3)	Associate contract approval test	NGR 16.1	A broad public benefit/detriment test has been included in the NGR to allow the approval of an associate contract where it does not meet the requirements of rule 31(2). The test has similarities to the authorisation test in the <i>Trade Practices Act 1974</i> .
PART 7 LIGHT REGULATION DETERMINATIONS			
33-34 and 37-38	Processes for making and revoking light regulation determinations	NGL 12	These processes have been moved from the first exposure draft of the NGL to the Rules, to give flexibility and achieve consistency with MCE's agreed governance model.
PART 8 ACCESS ARRANGEMENTS			
39	Regulatory discretion in fit-for-purpose decision-making model	NGL 20 and 21	As per MCE's agreed fit-for-purpose decision-making model, the Rules will set out the level of regulatory discretion for different elements of an access arrangement. Rule 39 establishes the framework for this approach. Subrule 39(1) establishes what is commonly known as a 'consider-decide' framework, subrule (2) establishes a framework similar to the AEMC model for capital and operating expenditure in Chapter 6A of the National Electricity Rules (limited discretion) and

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
			subrule (3) establishes certain matters where the AER has no discretion. Rules that are limited discretion or no-discretion are accordingly marked as such throughout the draft. Nonetheless, it should be noted that nothing in this provision detracts from the AER's obligation to apply the individual rules in approving or making an access arrangement.
41-42	Access arrangement information	NGL 83	These rules achieve the policy intention of separating access arrangement information from the access arrangement itself similar to 2.7 - 2.9 of the Gas Code.
44- 45	Limited access arrangements		The process and content for limited access arrangements is now set out here in the rules.
44(1)(a) and 50(a)	Description of pipeline in access arrangement	NGL 86	An access arrangement is now simply required to identify the pipeline, and provide a reference to a website at which a full description of the pipeline can be accessed.
44(1)(b) and 50(b)	Services on offer, or to be offered	NGL 85	The Rules now require a service provider to outline services it is "offering, or proposes to offer", instead of those "provided or to be provided".
44(2)(c) and 76(1)(m)	Information required by a regulatory information instrument is access arrangement information	NGL 87	These rules make information required by a regulatory information instrument form part of the access arrangement information, rather than the access arrangement itself.
46 and 53	Requirement to submit an access arrangement		The detail of when an access arrangement is submitted now in the rules to create greater flexibility over time.
48	Division and consolidation of access arrangements		This has now been clarified to make clear that it is possible for transmission and distribution pipelines to be regulated under the same access arrangement.
50(c) and 65(4)	Designation of reference services	NGL 75	The Rules now apply the Gas Code test that a reference service is a service that is "likely to be sought by a significant part of the market". The AER is allowed to reject an access arrangement in a final decision if the access arrangement does not specify all the services the AER considers are likely to be sought by a significant part of the market.
52	Trigger events	NGR 1.3	The Rules now provide for trigger events, as per the Gas Code 3.18.

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
61(1)(c)	Timeframe for initial comments on an access arrangement	NGL 71	The timeframe for initial comments on an access arrangement has been extended to no less than 28 days.
61(3)(b)	Revision of access arrangement proposals	NGL 90	This Rule allows the AER to consent to revisions to an access arrangement proposal, giving flexibility to service providers to amend their proposals outside of the defined revision period.
62(4)(c)(iii)	Timeframe for comments on an access arrangement draft decision	NGL 71	The timeframe for comments on an access arrangement draft decision has been extended to no less than 28 days.
64(2)	Hearing in relation to an access arrangement draft decision	NGR 3.2	The time within which an interested party may request a hearing in relation to an access arrangement draft decision has been increased to 14 days.
65(6)	Commencement of an access arrangement	NGL 73	An access arrangement will commence 14 days after a final decision, or on a date specified by the AER.
67	AER power to make access arrangements		This rule clarifies that the AER's role in making an access arrangement after refusing to approve one should be based upon the access arrangement submitted to the AER and the AER's reasons for refusing to approve it.
68	General terms and conditions		This rule replicates 3.6 of the Gas Code with regards to other terms and conditions of access.
69	Queuing requirements	NGR 6.2	The Rules now do not limit the methods that may be applied as queuing requirements.
69(1)	Queuing requirements terminology	NGR 6.1	Corrects difficulties with the first exposure draft NGR's wording by making clear that a user may be a prospective user of both spare and developable capacity.
70	Capacity trading requirements	NGL 89	The capacity trading requirements have been moved to the Rules to allow future flexibility.
72(b)(i)	Change of receipt or delivery point	NGL 79	The Rules now provide that a service provider may reject a user's proposal to change receipt or delivery point on reasonable technical or commercial grounds, as per the Gas Code 3.10(c).
PART 9	PRICE AND REVENUE REGULATION		
74	Definition of <i>operating expenditure</i>	NGR 13.2	The terminology used now does not exclude non-recurrent expenditure, or other

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
			non-capital costs that cannot be classified as expenditure.
76(1)(d) and (f)	System capacity and volume assumptions, and key performance indicators, in access arrangement information	NGR 8.2	These requirements have been included as access arrangement information for full access arrangements.
76(1)(j)	Upper and lower bounds of prices	NGR 8.3	Former NGR 21(h)(ii) has not been replicated in new NGR Rule 76(1)(j) as this information can be attained through regulatory information instruments where appropriate.
80(1)	Calculation of total revenue from all pipeline services	NGR 8.1	The Gas Code approach of calculating total revenue with reference to all pipeline services (rather than only to reference services) has been reinstated.
80(2)	Removing ambiguity in building block calculation	NGR 10.1	The rules now make clear that total revenue is to be determined through the building block approach, rather than merely "based on" the building block approach as in the first exposure draft.
80(2)	Removal of capital base as a building block	NGR 10.2	The capital base is no longer listed as a building block. However, the return on the projected capital base remains a building block.
80(2)(c)	Inclusion of tax in the building blocks calculation	NGR 10.5	This rule has been worded to include corporate income tax "if applicable", so as to not pre-determine a pre- or post-tax building blocks model.
81	Roll forward of capital bases	NGR 11.1	The wording of this Rule has been clarified to ensure that roll-forward of capital bases is achieved. This is done by using the term "opening capital base" rather than "initial capital base" where appropriate, and by correcting errors with regard to the concept of a capital base rolling forward on expiry of an access arrangement. As Gas Code access arrangements do not expire, it has been specified that capital bases roll forward "at the end of an access arrangement period". This policy intention is further established by the Savings and Transitions provisions in the NGL.
81	Depreciation	NGR 11.2 and 11.4	The issue of depreciation has been further considered in light of submissions on the National Electricity Rules. While actual depreciation is appropriate for periods when a pipeline is not regulated by a full access arrangement, the choice of

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
			forecast vs actual depreciation between regulatory periods is a matter of regulatory design best determined in the access arrangement approval process.
82(b)	Forecast capital investment	NGR 10.3	The concept of the "projected capital base" has been created to include, appropriately, forecast capital expenditure in the building blocks calculation.
83	New capital investment criteria	NGR 12.1	The new capital investment criteria have been amended in line with expert advice received by SCO. Further information about the changes to this important policy issue is provided at Appendix A . This is a limited discretion rule.
84(1)	Advance determinations with regard to future capital investments	NGR 12.4	Advance determinations with regard to future capital investments now do not allow the AER to specify additional conditions, other than those provided in the written proposal of the service provider.
91	Rate of return	NGR 10.4	The wording of this rule has been amended to achieve consistency with Gas Code 8.30.
93	Depreciation		The depreciation criteria are a limited discretion rule consistent with the electricity regime.
95	Criteria governing operating expenditure	NGR 13.1 and 13.3	The wording of this rule returns to that of the Gas Code. Further, former 39(2) of the NGR has been deleted to achieve consistency in terms of approval of access arrangements with other elements of access arrangements. The rule is a limited discretion rule.
96(1) and (2)	Cost allocation provisions	NGR 14.1	Provisions have been included in the second exposure draft of the NGR to deal with the allocation of costs between reference services and non-reference services.
96(3) and (4)	Rebateable services	NGR 14.4	Provisions dealing with rebateable services have been included in the second exposure draft of the NGR similar to 8.40 of the Gas Code.
97	Control mechanisms	NGR 14.3	Rule 97 provides flexibility by allowing the five listed control mechanisms to be employed in combination, as well as individually, and provides guidance to the regulator for approval of proposed control mechanisms.
98	Level of control		The level of control (X factors) are to be neutral in net present value terms having regard to the concept of total revenue.

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
100	Determining tariffs for distribution pipelines	NGR 14.1	Additional guidance has been provided for the determination of individual reference tariffs for individual distribution reference services. This is a limited discretion rule.
101	Determining tariffs for transmission pipelines	NGR 14.1	Additional guidance has been provided for the determination of individual reference tariffs for individual transmission reference services to replicate 8.38 and 8.42 of the Gas Code. This is a limited discretion rule. SCO is further considering whether this drafting achieves the intended result and would welcome comments on this matter.
102	Prudent discounts	NGR 14.5	Provisions dealing with prudent discounts have been included in the second exposure draft of the NGR based upon 8.43 of the Gas Code.
103	Incentive mechanisms	NGR 15.1	The Rules make clear that a proposed access arrangement must include an incentive mechanism for approval by the regulator. Rule 39 provides that the regulator has significant discretion in approving proposed incentive mechanisms.
104	Fixed Principles		This rule has been clarified to reflect the intention that fixed principles must remain consistent with the rules. Any carry forward of an inconsistent fixed principle in light of a rule change would need to be addressed by transitional rules.
PART 10 FACILITATION OF, AND REQUEST FOR, ACCESS			
105	Availability of access arrangements		The rule clarifies that access arrangements are to be maintained on a service provider's website.
107(1)	Requirements for users to comply with when providing information about unutilised contracted capacity	NGR 4.3	The Rules no longer subject users to open-ended requirements (as specified by the AER) when providing information about unutilised contracted capacity
108(2)	Whether or not a distribution pipeline system should maintain a register of spare capacity	NGR 4.4	The Rules now provide that the AER should only require a distribution pipeline system to maintain a register of spare capacity where it is technically and economically feasible.
109(3)(b) and (5)	Provisions dealing with further	NGR 4.5	The Rules now include provisions similar in effect to the Gas Code allowing a

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
	investigation by a service provider about a request for a pipeline service		service provider to inform a user of the need for further investigation to examine a request for a pipeline service, and outline reasonable costs that would be incurred in complying with the request.
109(4)	Requirements for service providers to comply with when informing users of inability to meet request	NGR 4.6	The Rules no longer subject users to open-ended requirements (as specified by the AER) when informing users of an inability to meet a request for an additional pipeline service.
110	Bundling of services		The old s 193 of the Exposure draft has been reformulated here replicating the intent of 3.2 of the Gas Code. The description of services in the access arrangement (services policy) must conform to this principle.
PART 11	ACCESS DISPUTES		
113	Expert safety reports in access disputes	NGL 103, NGR 7.1	The Rules now provide for the AER to approve the appointment of an independent technical expert, but limits the AER to accepting the conclusions of the approved technical expert.
115(2)(c)	Expansion of pipeline where technically and economically feasible	NGL 102	The Rules now require an expansion of a pipeline in an access dispute to be technically and economically feasible consistent with 6.22 of the Gas Code.
PART 12	GREENFIELDS INCENTIVES		
119-127	Processes surrounding applications for, and revocation of, greenfields incentives	NGL 12	These processes have been moved from the first exposure draft of the NGL to the Rules to give flexibility and achieve consistency with MCE's agreed governance model.
PART 13	RECLASSIFICATION APPLICATIONS		
119-127	Processes surrounding reclassification applications	NGL 12	These processes have been moved from the first exposure draft of the NGL to the Rules to give flexibility and achieve consistency with MCE's agreed governance model.
PART 14	SCHEME REGISTER		
130-132	Provisions relating to the establishment and maintenance of a scheme register	NGL 12	These processes have been moved from the first exposure draft of the NGL to the Rules to give flexibility.

Rule number in 2 nd Exposure Draft of the NGR	Issue	Relevant NGL/NGR Policy response	Change
Part 15	CONFIDENTIAL INFORMATION		
134	Use and disclosure of confidential information		The effect of s 4.1(f) and (g) of the Gas Code have been replicated in this rule.
135	Disclosure of gas supply information		The rights in s 7.20 – 7.22 of the Gas Code have been replicated in this rule.
PART 16	MISCELLANEOUS		
136	Requirement to consult prior to issuing a general regulatory information order	NGL 52	This rule provides that the AER must consult according to the standard consultative procedure before issuing a general regulatory information order.
137	Consultation in relation to performance reporting	NGL 55	This rule makes further provision as to consultation requirements of the AER in relation to performance reporting

APPENDIX A

NEW CAPITAL INVESTMENT CRITERIA – CHANGES FROM FIRST NGR EXPOSURE DRAFT AND THE GAS CODE

As foreshadowed in SCO's policy responses on the first exposure drafts of the NGL and NGR, SCO has sought expert advice (from NERA Economic Consulting) to consider possible amendments to the New Capital Investment Criteria (NCIC) in light of issues with the criteria identified during consultation.

Rule 83 of the second exposure draft of the NGR includes changes from Rule 27 of the first exposure draft of the NGR, and from the equivalent provisions (8.16 and 8.17) of the Gas Code.

The policy issues

Consultation identified the difficulty of including in the capital base of a pipeline prudent, but high-cost, expansions of transmission pipelines under the 'incremental revenue test' (Gas Code 8.16(a)(ii)(A), or NGR first exposure draft 27(2)(b)(i)).

Stakeholders argued that access to expanded capacity might be demanded by users, yet not be able to be included in the capital base under the incremental revenue test due to:

- the need to employ relatively expensive technology (e.g. looping of pipeline assets) at particular stages of the pipeline expansion cycle; or
- the relatively high cost of key pipeline inputs such as steel or labour at the time at which the new capacity is demanded.

NERA's assessment

In addition to those issues identified by stakeholders, NERA identified further reasons why pipeline expansions are difficult to include in the capital base under the incremental revenue test.

NERA argued that, under the Gas Code:

“...a pipeline operating at less than its maximum annual capacity will have higher reference tariffs than would be the case if that same pipeline was at full capacity... Whilst this makes good sense in terms of the design of a revenue recovery mechanism, such an arrangement is not consistent with either... allocative efficiency... and the operation of competitive markets involving products or services with relatively high capital intensity.”

Accordingly, NERA concluded that:

“... the basic design of the incremental revenue test under the new facilities investment provisions of the Gas Code involves an inherent flaw... [because], for any given pipeline, such tariffs will be at their lowest in real terms at the very time the pipeline needs expanding.”

For this reason, NERA argued that the problems identified were not best resolved by altering the incremental revenue test itself, but by looking at alternative ways to include pipeline investments in the capital base.

The solution: altering the 'system-wide benefits' test

NERA explored how best to give regulatory certainty to pipeline investments that are technically and commercially prudent, but where the costs of the investment exceed the historical cost of past pipeline investments, and therefore which fail the incremental revenue test. Such investments may entail overall economic benefits, yet not be included in the capital base because it is unclear whether, under the wording of the Gas Code, they entail 'system-wide benefits'.

NERA's solution attempts to address the problem that

“the interpretation of the term ‘system-wide’ is unclear, and appears to constrain the type of benefits that may be considered with the consequence that investments that provide benefits to participants in the gas market generally (such as producers, retailers and end users) are excluded [from the capital base].”

NERA argues that the benefits that are not necessarily captured by 'system-wide benefits', but which should be captured by the new formulation of the NCIC, include:

- “the value to end users of being able to purchase additional supplies of gas at the delivery location, as approximated by those users’ maximum willingness to pay (for delivered gas), net of the price they are required to pay for those additional supplies;
- the value to gas producers of being able to sell additional quantities of gas, as approximated by the incremental revenues arising from additional gas sales, less the incremental costs of gas production; and
- the value to retailers (or aggregators) - who perform an administration, contract negotiation and risk management service for producers and end-users - of being able to offer their services across a greater volume of gas sold, net of the cost of performing those services.”

NERA also emphasised that the benefits to be taken into account in this way "would not include any economic profits or producer surplus arising to gas transmission (or distribution) entities", as to do so would risk inconsistency and double-counting of benefits.

Finally, NERA emphasised that these benefits include what has previously considered by regulators to be system-wide benefits such as the competition benefits of pipeline expansion, and improved system security and reliability.

NERA argues that:

- “the *competition benefits* of expanded pipeline capacity manifest themselves as both increased producer and consumer surplus arising from *increased sales of gas*, with any price reductions arising from greater competition for the sale of *existing gas* being netted out of this calculation (since these amount to a transfer of producer surplus to consumers); and

- the benefits of *increased system security and reliability* amount to a form of consumer surplus (i.e., an increased willingness to pay to avoid the costs of less secure or reliable gas supply system), which would be available to both existing and new users, as relevant.”

NERA also emphasised that such a formulation:

- is not equivalent to the electricity regulatory test, as the regulatory test involves weighing up multiple options or alternatives to determine the greatest net benefit or lowest net cost, whereas this formulation simply seeks to "establish that there are sufficient (gross) economic benefits to meet or exceed the costs of the pipeline expansion"; and
- can be applied correctly to both distribution and transmission pipeline systems.

Finally, as requested, NERA addressed the distributional implications of such a change. In this regard, NERA concluded that:

“the NGR addresses the question of who pays for what by means of its cost allocation provisions... There is no need (indeed, it amounts to unnecessary duplication) to distort this process by adding in a specific requirement to deal with new capacity. Rather, it is preferable for the reference tariff consequences of new capital investment decisions to be addressed within the context of the cost allocation policies applying to all reference tariffs.”

Accordingly, NERA concluded that:

“Specifically, we recommend that the reference at clause 27(2)(b)(ii) to ‘system-wide benefits’ be replaced with a suitable phrase that captures the economic benefits that accrue directly to gas market participants (other than pipeline owners).”

The outcome – draft amendments to Rule 83

NERA's advice has been applied by SCO in drafting amendments to Rule 83 (New Capital Investment Criteria). Rule 83 is now as below, with key changes highlighted:

- (1) Capital expenditure made during an access arrangement period may, subject to this rule, be rolled into the opening capital base for the next access arrangement period.
- (2) The amount of the expenditure must not exceed the amount that would be invested by a **prudent** service provider acting efficiently, in accordance with accepted good industry practice, to achieve the lowest sustainable cost of providing services.
- (3) The expenditure must also be justifiable on one or more of the following grounds:
 - (a) the expected incremental revenue generated as a result of the investment exceeds the amount of the capital expenditure;
 - (b) overall the economic value of the investment is positive;**
 - (c) the investment is necessary to maintain or improve the safety and

integrity of services or to maintain the service provider's capacity to meet contractual obligations or provide services.

[Note: Compare section 8.16(a) of the Code.]

(4) In deciding whether the overall economic value of capital expenditure is positive, consideration is to be given only to the economic value directly accruing to gas producers, users and end users.

(5) The AER's discretion under this rule is limited.

Stakeholders will note firstly that Rule 27(3) from the first exposure draft of the Rules has been deleted. Rule 27(3) was broadly equivalent to section 8.17 of the Gas Code. NERA argued, and SCO agreed, that the provisions of Gas Code 8.17/Rule 27(3) "seem either redundant or duplicative" and have therefore been deleted.

27(3)(c) captured the concept of a "prudent service provider" in a way that was different from the Gas Code. The deletion of 27(3) in its entirety has necessitated the retention of the concept of a prudent service provider by the re-inclusion (as in Gas Code 8.16(a)(i)) of the word "prudent" in new Rule 83(2), as highlighted above.

The key changes to Rule 83, however, are found in 83(3)(b) and 83(4), which capture NERA's advice on replacing the system-wide benefits test with a broader concept to pick up additional economic benefits that may not have been captured under the Gas Code test.

NERA's advice that the recommended formulation simply seeks to "establish that there are sufficient (gross) economic benefits to meet or exceed the costs of the pipeline expansion" has been captured as simply as possible through the new test that "overall the economic value of the investment is positive".

Economic value reflects economic benefits less costs, and so a simple positive value demonstrates overall benefits. The question as to which benefits (and costs) should be considered is then clarified by new 83(4).

83(4) states that, "in deciding whether the overall economic value of capital expenditure is positive, consideration is to be given only to the economic value directly accruing to gas producers, users and end users".

As per NERA's advice, economic value accruing to service providers is not considered. The relevant economic value accrues to gas producers, users and end users, as these are the entities that will gain producer or consumer surplus over additional quantities of delivered gas they are able to supply or consume due to the expansion. These entities will also gain economic value due to the increased security and reliability of the delivery of existing quantities of gas, should the investment deliver security and reliability benefits.

As economic value consists of economic benefit net of costs, the cost of the pipeline investment itself will be recovered through the tariffs charged to pipeline users (producers and consumers) and therefore is reflected in the cost of **delivered** gas across both existing and new units of capacity following the investment.

Additionally, as noted by NERA, the distribution impacts of who should pay for these expansions are covered by the pricing rules (rules 100 and 101).