

3 May 2005



Mr John Feil
Executive Director
National Competition Council
GPO Box 250B
Melbourne VIC 3001

By email to info@ncc.gov.au

Dear Mr Feil

EPIC ENERGY APPLICATION FOR REVOCATION OF COVERAGE OF THE MOOMBA TO ADELAIDE PIPELINE SYSTEM

Background

The Australian Pipeline Industry Association (APIA) is the peak national body representing the Australian gas transmission sector. This letter is provided in support of Epic Energy's application for revocation of the Moomba to Adelaide Pipeline System (MAPS). Individual members of APIA have also made submissions on this matter and APIA supports the NCC having all facts available before making its decision.

Over the last ten to fifteen years we have witnessed fundamental changes to the structure, ownership and operation of the pipeline sector in Australia. This period has encompassed the implementation of the Hilmer competition reforms, the privatisation of pipelines and major investment that has led to a truly interconnected network of gas transmission pipelines in southern and eastern Australia.

This integrated pipeline network has already delivered significant benefits to gas customers, including basin on basin supply competition, supply diversity and pipeline on pipeline competition. No longer are major markets like Sydney or Adelaide limited to supply via a single transmission pipeline from a single gas field. This diversity of supply has proven essential in ameliorating the impact of the production problems that have occurred at processing plants such as Moomba.

APIA has also been pleased to see the increasing recognition of the competitiveness of the gas pipeline sector in legal and policy circles. For example, the original ACT decision with respect to the Eastern Gas Pipeline (EGP) clearly showed that being a major gas pipeline was not sufficient of itself to justify coverage under the Gas Code. APIA supported the Tribunal's recognition of the potential negative impacts of heavy-handed access regulation and the fact that it is very much a second best option to allowing the development of workable competition through the interaction of market forces within the gas pipeline sector.

Since the EGP decision, APIA has been concerned that there is a tendency on the part of regulators to narrowly define aspects of the coverage criteria and this narrow definition is against the spirit and intent of the Competition Principles Agreement and the National Third Party Access Code for Natural Gas Pipeline Systems (the Gas Code).

Criterion (b)

APIA is particularly concerned that there is a tendency on the part of regulators to narrowly define coverage criterion (b)¹. The narrow definition of service under criterion (b) has effectively made this test redundant (as there could be no economic logic supporting the regulation of parallel pipelines) and is inconsistent with well-accepted precedent for market definition.

This approach to service definition does not accord with APIA's view that the intent of criterion (b) was to establish whether it was feasible for a new pipeline (or an existing pipeline) to provide substitutable transport services for producers and purchasers of gas.

APIA disagrees with the Council's statement at para 5.12 of the Issues Paper, that it was bound by the Act's point-to-point approach to service definition originally outlined in the EGP decision. APIA notes that this narrow definition is merely an administrative (and therefore non-binding) decision of a Tribunal that in any event found that the EGP did not have, and was unlikely to have, market power so that criterion (a) was not satisfied.

APIA believes that by considering the original intent of the Gas Code and supporting legislation rather than relying on administrative decisions of the Tribunal, the NCC could reasonably consider a broader definition of service for the assessment of criterion (b). This is made all the more clear when one has regard to the potential distortions a narrow interpretation creates for the interpretation of criterion (a)², which is inherently more difficult to apply in practice as it requires the decision maker to assess the likely impact of coverage on a pipeline on competition in upstream and downstream markets over the next 15 years.

In the Minister's decision to revoke coverage on parts of the Moomba to Sydney pipeline there was a recognition that there now exists an interconnected network of gas pipelines providing multiple sources of supply to each demand centre. As such, both users and producers of gas are faced with multiple service providers and therefore, it is self evident that it has been economic to develop pipelines to provide competing services.

APIA believes that in light of the competition between the MAPS main line and the SEA Gas pipeline, the key issue is whether regulation of the MAPS lateral pipelines (the Whyalla and Angaston laterals) can be justified. APIA understands that the majority of

¹ Note - criterion (b) refers to the criterion that it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the pipeline.

² Note - criterion (a) refers to the criterion that that access (or increased access) to services provided by means of the pipeline in question would promote competition in at least one market (whether or not in Australia), other than the market for the services provided by means of the pipeline in question;

the capacity of the Whyalla pipeline is now contracted for an extended period of ten years with only minimal capacity remaining uncontracted.

APIA is not in a position to comment on many of the specific issues relating to the operation of the MAPS. However, it is clear to APIA that the construction of the SEA Gas pipeline has resulted in the installation of spare capacity (either actual or developable) into the South Australian gas market. There can be no doubt that both the downstream and upstream markets are workably competitive as a result of the pipeline-on-pipeline and basin-on-basin competition. Accordingly, coverage does not, and cannot, increase competition in these markets above that which would apply absent coverage.

Cost of Regulation (Criterion (d))

APIA, along with others including the Productivity Commission, remains concerned about the high cost of regulation under the Gas Code. APIA's September 2003 Submission to the Productivity Commission's Review of the Gas Access Regime conservatively estimated that the direct costs associated with economic regulation under the Gas Access Regime to 2001/02 were around \$35 million.

Moreover, there are a range of indirect costs which should be added to the direct costs of regulation, such as management distraction and the unintended consequences of regulation, including adverse impacts on investment incentives. APIA believes that in the case of MAPS, these costs outweigh any potential benefits of regulation given the limited capacity likely to be subject to effective regulation.

Further, it is apparent that the Angaston lateral passes in close proximity to the SEA Gas pipeline and therefore interconnection and bypass are a very real risk for Epic Energy, this will serve to constrain any potential for the exercise of market power.

Conclusion

In conclusion, APIA respectfully suggests that the NCC consider adopting a wider definition of service for the purposes of assessing criterion (b) consistent with that adopted by the Minister in deciding to revoke coverage of parts of the MSP. This would bring the interpretation of criterion (b) into line with the general principles of market definition accepted in Australian competition law.

Given the clear presence of competition in the Adelaide market between the SEA Gas pipeline and the MAPS, together with the extremely small potential for benefit from regulation of the laterals, APIA believes that continued coverage of any part of the MAPS cannot be justified.

Yours sincerely



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Chief Executive