



*Gas Transmission Australia*

## **PUBLIC SUBMISSION**

# **DRAFT RECOMMENDATION: APPLICATION FOR COVERAGE EASTERN GAS PIPELINE**

**Submitted to the  
National Competition Council**

**6 June 2000**

## EXECUTIVE SUMMARY

CMS Gas Transmission of Australia (CMS), the owner and operator of the Parmelia Pipeline in Western Australia, takes this opportunity to provide its public comments on the Draft Recommendation recently handed down by the National Competition Council (NCC) on the application for coverage of the Eastern Gas Pipeline under the National Third Party Access Code for Natural Gas Pipeline Systems (the Code).

CMS makes this submission on the basis that the overarching intent of Open Access legislation is to promote competition, and that the Draft Recommendation will inhibit this objective.

The key points of this submission are:

- 1) The Draft Recommendation potentially compromises the future development of major new pipeline infrastructure in Western Australia. The Parmelia Pipeline Northern Extension ("PP North") is planned to compete directly with the existing Dampier to Bunbury Natural Gas Pipeline (DBNGP). The PP North project may be significantly compromised if a regulatory precedent is established where directly competing pipelines are subject to the Code.
- 2) The assumptions which underpin the Code take covered pipelines to be monopolies. The Code should not apply to competing pipelines.
- 3) The Draft Recommendation is not a final position. The NCC has the opportunity to recommend against coverage of the Eastern Gas Pipeline (EGP). In doing so, the NCC would foster the development of entrepreneurial pipelines, potentially increase the number of competing pipelines and decrease the number of monopoly pipelines, and facilitate Australia's international competitiveness.

These points are expanded below.

## INTRODUCTION

The Parmelia Pipeline provides transport for gas produced in the northern part of the Perth Basin to the wider Perth area. The pipeline runs from Dongara (near the regional centre of Geraldton) to Pinjarra, some 80 kilometres south of the Perth central business district. The Parmelia Pipeline receives gas from the Dongara, Beharra Springs and Woodada fields. An interconnection between the Parmelia Pipeline and the Dampier to Bunbury Natural Gas Pipeline (DBNGP) at Mondarra (near Dongara) provides a further pipeline inlet point. Deliveries are made to a number of industrial customers in the wider Perth area. Interconnection between the Parmelia Pipeline and the AlintaGas distribution system (which supplies the Perth residential and commercial market) is to be completed during the winter of this year. This will result in two independent transmission pipelines supplying the Perth residential and commercial market.

## COMMENTS: DRAFT RECOMMENDATION

***The Draft Recommendation potentially compromises the future development of major new pipeline infrastructure in Western Australia.***

CMS and Texaco are in the process of conducting a feasibility study into the viability of constructing a second major gas pipeline linking the Carnarvon Basin (which encompasses the North West Shelf fields) and the South West of Western Australia. This potential new pipeline is the Parmelia Pipeline Northern Extension ("PP North").

It is anticipated that the PP North pipeline right of way will be adjacent to the DBNGP right of way for the majority of the latter's length. The two pipelines will receive gas from producers in the Pilbara region of Western Australia and deliver gas to end users in the Mid West and South West of the state. In order to achieve the economies of scale required to make a project of this magnitude economically viable, PP North capacity must be comparable to that of the DBNGP.

It is therefore readily apparent that PP North will compete directly with the DBNGP.

Until recently, CMS assumed that PP North would not be subject to coverage under the Code because it would compete head to head with the DBNGP. This assumption meant that concerns regarding regulatory risk arising from the interpretation and application of the Code were to a large extent in abeyance.

However, the Draft Recommendation for the Eastern Gas Pipeline (EGP) gives CMS the indication that coverage of PP North under the Code is a distinct and real possibility.

The philosophies underpinning some recent regulatory decisions are of some concern to CMS. One such area is the means of determination of the regulated Initial Capital Base (ICB) from which regulated tariffs are calculated. In two relevant Access Arrangement Draft Decisions handed down recently, circular reasoning has been either employed or accepted to yield values of ICB which differ substantially from actual construction costs. The Code nominally offers protection against such divergence for new pipelines. However, CMS considers that there is a real risk that particular interpretation and selective application of related sections of the Code and regulatory precedent could result in PP North being assigned a value of regulated Capital Base substantially below actual construction cost. In turn, this could result in regulated tariffs being substantially lower than those based on actual construction cost and used to commercially justify the project.

CMS views the increased likelihood of coverage of PP North under the Code as a potential but significant restraint on the project. If regulators continue to hand down decisions which distort risk - return relationships faced by investors in potential world scale infrastructure projects and prefer the imposition of conditions of synthetic competition over the facilitation of actual competition in the Australian gas transport industry, the probability of PP North becoming a reality will necessarily decline.

For PP North to become a reality, it must be able to compete in its market unfettered by well intentioned but inapplicable and inappropriate regulatory constraints. Application of a regulatory framework which seeks to mimic competition is unwarranted. The forces of actual competition will apply to PP North. Imposition of synthetic competition is both superfluous and potentially damaging. The regulatory regimes and the decisions made within them which are intended to generate synthetic competition do not necessarily re-create the effects of an actual competitive market. The evolution of centrally planned economies to market based economies in central and eastern Europe over the past 15 years provides compelling evidence of this.

***The Code should not apply to competing pipelines.***

The assumptions which underpin the Code take covered pipelines to be monopolies.

Not all gas pipelines in Australia are monopolies. The EGP and the Moomba to Sydney Pipeline (MSP) will compete head to head. The Parmelia Pipeline competes directly against a large and potentially overpowering rival in the DBNGP. The Interconnect is a competing pipeline. PP North will, when completed, compete head to head with the DBNGP.

The Code, which is intended to cover monopoly pipelines, is simply not applicable to pipelines which engage in actual, as opposed to synthetic, competition.

***The Draft Recommendation is not a final position.***

The current Recommendation issued by the NCC is a Draft Recommendation. It does not represent a final position. Rather, it provides an (incomplete) list of options the NCC could consider. It may reasonably be assumed that the NCC will consider public commentary (such as is provided in this submission) in reaching a final Recommendation to the Minister.

The NCC is also free to propose in its final Recommendation to the Minister outcomes which do not appear in the Draft Recommendation.

One such option would be to recommend that the entire EGP remains uncovered.

Taking this action would send a clear signal to the Australian gas transport industry and investors in the industry that new pipelines built on an entrepreneurial basis will be subject to the discipline of actual rather than synthetic market forces and will be free from regulatory intervention and its associated overheads. If new, high risk pipelines are encouraged, then the number of competing pipelines in Australia will increase. Particularly in eastern Australia, it is likely that the presence of new competing pipelines will in turn promote competition between producers.

On a wider front, promotion of the natural gas market will promote competition between gas, electricity, and other energy sources. In turn, economic efficiency will be increased and Australian society will benefit.

A Recommendation which recognises and facilitates actual competition between the EGP and the MSP would represent a breakpoint in the regulation of the Australian gas transport industry.

To date, various regulators have handed down Draft and Final Decisions which have been overly conservative, prescriptive, and bound by precedent. The Decisions handed down in Victoria have implicitly assumed the status of regulatory benchmark for all gas transmission pipelines and distribution systems. This elevated and unwarranted status exists despite specific disclaimers by both the Office of the Regulator General, Victoria and the Australian Competition and Consumer Commission when handing down the Victorian Decisions.

A Recommendation by the NCC to not cover the EGP would recognise that pipelines are different, operate in different industry structures, and serve different end user markets which are at different stages of development and maturity. It would provide the lead for directing the regulatory process towards the generation rather than (necessarily imperfect) replication of a competitive market. In turn, this would contribute to greater efficiency and promote the competitiveness of Australian products in the global market.