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Dear Mr Pankowski

ACCC submission to the Options to improve gas pipeline regulation Consultation RIS

Over the course of its two gas inquiries, the ACCC has identified a range of deficiencies in the gas pipeline regulatory framework that are leading to inefficient outcomes, which are contrary to the long term interests of consumers. We therefore welcome the opportunity to make a submission to COAG Energy Council's Options to improve gas pipeline regulation Consultation Regulation Impact Statement (RIS), to address the deficiencies in the existing framework (i.e. the status quo).

One of the main problems we identified in our first inquiry was that the coverage test, which is based on the competition test in Part IIIA of the *Competition and Consumer Act 2010*, was not constraining the behaviour of vertically separate pipeline operators. As a consequence, pipeline operators were able to engage in monopoly pricing in a relatively unconstrained manner, to the detriment of efficiency and consumers more generally. As we noted in our 2015 inquiry, the problem with the competition-oriented coverage test is that it is not designed to address the market failure that we observe with pipelines and other vertically separate infrastructure. That is, it doesn't address market power and monopoly pricing that gives rise to economic inefficiencies, with little or no effect on competition in dependent markets.¹ This market failure must instead be addressed through a hybrid market power-efficiency based test.

The introduction of the information disclosure and arbitration framework (Part 23 of the National Gas Rules) as the minimum form of regulation for pipelines providing third party access has overcome this deficiency to some extent. However, the coverage test is still used to determine whether third party access should be provided and to determine the form of regulation to be applied. Therefore, there is a serious risk of under-regulation in the current regulatory framework.

Some of the other problems that the ACCC has identified through its two inquiries include: gaps in the information available to shippers across pipelines subject to different forms of regulation, inadequacies with information disclosure made by pipeline operators under Part 23, a lack of credibility of the threat of arbitration by smaller shippers, and issues with the negotiation framework.² The ACCC has also previously observed that having three forms of

¹ As we observed in the 2015 Inquiry, the problem with using competition as a proxy for efficiency in the coverage test is that competition and efficiency are not synonymous. That is, while competition may promote efficiency, significant efficiency improvements that are in the long-term interests of gas consumers can still be achieved through access without any change in competition in a related market.

² ACCC, *ACCC submission on Review into the scope of economic regulation applied to covered pipelines Draft Report*, March 2018, p. 13. ACCC, *Gas inquiry 2017-2020 Interim Report*, July 2019, pp. 131-154, 155-157.

regulation is unnecessarily complex, costly and confusing, and therefore recommended the removal of light regulation.³

The ACCC supports Option 3 of the RIS, which best addresses the issues we have identified with the existing pipeline regulation framework. By changing the third party access test from the current coverage test, to a combined market power-National Gas Objective test, this option addresses our concerns with the coverage test, shifting the focus of the test for regulation from competition in other markets, to market power. In Option 3, the test for moving between forms of regulation also appropriately includes an assessment of the degree of market power of the pipeline operator.

In addition, Option 3 addresses many of the issues that we have identified in our current inquiry. This option addresses the current deficiencies in information provision, strengthens the credibility of the threat of arbitration by smaller shippers, and makes improvements to the negotiation framework. It proposes simplifying the regulatory framework by removing light regulation and moving to two forms of regulation, full regulation and a strengthened Part 23, which we have previously supported.⁴ Additionally, it proposes consistent information provision by all pipelines providing third party access.⁵

In our submission, we suggest minor refinements to Option 3. Among others, these include: changes to improve the utilisation of the competitive tender provisions in the National Gas Rules,⁶ including an explicit right to interconnection to regulated pipelines (along with pricing principles),⁷ removing the proposal for the regulator to act as arbitrator under Part 23 disputes involving smaller shippers,⁸ and removing the fast track arbitration provisions from regulatory arbitration.⁹

The ACCC does not support Option 2, because this option involves a rolling back of regulation. We have previously found that pipelines, both regulated and unregulated, were able to exercise market power.¹⁰ The introduction of Part 23 of National Gas Rules in 2017 helped to address this by subjecting all pipelines providing third party access to a form of regulation. The ACCC considers that this is appropriate because, even in its strengthened form, Part 23 is a relatively unintrusive form of regulation, only requiring information disclosure, unless a pipeline operator is exercising market power.¹¹

The ACCC also does not support Option 4 which mandates that all pipelines offer third party access on a non-discriminatory basis. We consider that this would result in over regulation because most pipelines that do not provide third party access are currently used to transport gas to dedicated end-user facilities. Mandating third party access on these pipelines could impose significant regulator costs on the pipeline owners, with very little benefit if no party actually seeks access.¹²

³ ACCC, *ACCC submission on Review into the scope of economic regulation applied to covered pipelines Draft Report*, March 2018, p. 12.

⁴ ACCC, *ACCC submission on Review into the scope of economic regulation applied to covered pipelines Draft Report*, March 2018, pp. 9-12.

⁵ ACCC, *ACCC submission on Review into the scope of economic regulation applied to covered pipelines Draft Report*, March 2018, pp. 12-13.

⁶ See attached submission, responses to Question 9 and 10.

⁷ See attached submission, response to Question 19.

⁸ See attached submission, response to Question 32.

⁹ See attached submission, response to Question 34.

¹⁰ ACCC, *Inquiry into the east coast gas market*, April 2016, pp. 8-12.

¹¹ See attached submission, response to Question 7.

¹² See attached submission, response to Question 11.

Implementation of Option 3, with the refinements suggested above, will help to significantly improve the operation of the gas market and put downward pressure on the prices that users and ultimately consumers pay. Further details of our views on the proposed reforms are set out in the attached Stakeholder Feedback template. We look forward to engaging further as the reform process progresses.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Rod Sims', with a stylized flourish at the end.

Rod Sims
Chair