



Review into the scope of economic regulation applied to covered pipelines

Final report

The Australian Energy Market Commission today released a package of recommended changes to how gas pipelines across Australia are regulated.

Final report

The AEMC has published a final report for the review into the regulation of covered pipelines. It includes recommendations to improve the economic regulation of full and light (together referred to as 'covered') pipelines across Australia. The purpose of these changes is to make it easier and less costly to move gas to where it is needed the most.

This final report follows the AEMC's 2016 east coast gas market review, which made recommendations to improve the operation of gas markets and make it easier to buy and sell gas across the east coast of Australia. The review's recommendations were approved by the COAG Energy Council and are now being implemented by the Gas Market Reform Group.

The natural gas export industry has become a significant driver for gas markets in eastern Australia. This has affected gas supply to gas fired electricity generators, industrials and other consumers on the east coast.

In addition, the 2016 Australian Competition & Consumer Commission (ACCC) inquiry into the gas industry concluded that there was monopoly pricing of transmission pipeline services. Gas pipeline users and consumers considered that prices and other terms to access gas pipeline services have been unfair.

As a result, the COAG Energy Council requested that the AEMC undertake this review into the economic regulation of covered pipelines to address these issues for distribution and transmission pipelines. This framework has not been comprehensively reviewed since the first national framework for the regulation of natural gas pipelines was introduced in 1997.

Gas pipelines in Australia are regulated under a negotiate-arbitrate framework. Pipeline service providers and prospective users negotiate the terms, conditions and prices for access to pipeline services. Negotiation is supported by information disclosure and regulatory decisions. Arbitration can be used if a deal cannot be agreed.

Recommendations

The AEMC has examined the framework for the economic regulation of covered pipelines to improve negotiation outcomes for pipeline users and lower prices for consumers, and has proposed 32 recommendations.

The AEMC recommends that all expansions to the capacity of covered pipelines be economically regulated in the same way as the original pipeline. This addresses the ACCC's concern that under the current rules, an expansion of the capacity of a covered pipeline may not be subject to regulation. This may provide the pipeline owner with the opportunity to use its market power in negotiations with users who seek to use that expanded capacity. The AEMC's recommendation is expected to result in services on the expanded capacity not being monopolistically priced.

The AEMC also recommends a new approach for the regulator to determine which pipeline services should be specified as 'reference services'. 'Reference services' are those services for which the regulator approves prices, terms and conditions. As a result of this change the regulators are expected to approve a larger number of reference services. This will result in more services being efficiently priced and will place a greater constraint on the use of market power by pipeline owners.

The AEMC has made 32 recommendations to improve the regulatory regime for covered pipelines

Recommendations also address regulatory decision making to lower regulatory costs for pipeline owners and regulators.

The recommendations enhance the framework for the regulatory assessment of efficient costs to lower prices.

In addition, the AEMC has designed an improved financial and pipeline usage and capacity information reporting regime. The purpose of this is to make pipeline users better informed to negotiate fairer prices, terms and conditions for pipeline services to transport gas.

The AEMC has also made recommendations to the dispute resolution framework to improve access to dispute resolution and outcome certainty as well as create a more credible threat to motivate fair access negotiations.

In conducting this review, the AEMC has found that the separate gas sector reforms that have taken place recently may not operate together smoothly. It recommends that it be tasked with reviewing all the forms of regulation applied to pipelines so that the recent reforms pull together, to maximise the benefits for pipeline users and gas consumers.

If the recommendations from this review are adopted in full, then pipeline users and gas consumers will benefit from lower prices and fairer terms and conditions of access to pipeline services.

The recommendations of the review fall under two packages, rule changes that can be actioned immediately through a rule change request to the AEMC and law changes that trigger subsequent rule changes. The AEMC recommends that both packages be implemented as soon as possible so as to apply to access arrangement reviews scheduled for 2020.

Scope of the review

The COAG Energy Council requested the AEMC to:

- make recommendations on any amendments to Parts 8 to 12 of the National Gas Rules that it considers necessary to address concerns that pipelines subject to full regulation are able to exercise market power to the detriment of economic efficiency and the long term interests of consumers
- consider whether the access dispute resolution mechanism that is set out in the NGR and National Gas Law (NGL) should be amended to more effectively constrain the exercise of market power by pipeline service providers, and become more accessible to shippers
- examine the issues in Parts 8 to 12 that the 2016 ACCC gas inquiry report identified, namely reference service definition, extension and expansion requirements and the arbitration framework
- consult with stakeholders on additional issues in Parts 8 to 12
- work closely with the Gas Market Reform Group.

Parts 8 to 12 of the National Gas Rules

Parts 8 to 12 of the National Gas Rules (NGR) set out how covered (light and full regulation) gas transmission and distribution pipelines are regulated by either the Australian Energy Regulator or the Economic Regulation Authority of Western Australia. These parts of the NGR include rules on the access arrangement process, information disclosure, revenue and price calculations, access terms and conditions, and an arbitration framework.

Ongoing redesign of Australia's gas markets

This review follows the AEMC's 2016 east coast gas market review which made recommendations to improve the operation of gas markets to make it easier to buy and sell gas across the east coast of Australia. The gas market recommendations were approved by the COAG Energy Council and are now being implemented by the Gas Market Reform Group. These market reforms include:

- concentrating trade at two trading hubs to improve liquidity

If the recommendations from this review are adopted in full, then pipeline users and gas consumers will benefit from lower prices and fairer terms and conditions of access to pipeline services.

- introducing new ways to trade unused pipeline capacity so buyers and sellers have more flexibility
- providing more and better information so buyers and sellers of gas can make informed decisions
- developing standard products and information to facilitate trade across different locations
- reducing barriers to entry to increase competitive pressure on prices.

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28 June 2018

Table 1: Overview of current forms of regulation applied to gas pipelines

Form of regulation	Overview	History	Pipelines
Full regulation 16 pipelines (Parts 8 to 12 of the NGR)	<p>Negotiate-arbitrate framework with information disclosure and dispute resolution requirements</p> <p>Regulator determines reference services and reference tariff and non-tariff terms (as contained in a full access arrangement)</p>	<p>Deemed covered when the code came into effect in 1997 or subsequently covered by the jurisdictional minister</p>	<p>Includes most major distribution and transmission pipelines such as:</p> <ul style="list-style-type: none"> - Dampier to Bunbury Natural Gas Pipeline - Roma to Brisbane Pipeline - Amadeus Gas Pipeline
Light regulation 5.5 pipelines (Parts 8 to 12 of the NGR)	<p>Negotiate-arbitrate framework with information disclosure and dispute resolution requirements</p>	<p>Deemed covered when the code came into effect in 1997 or subsequently covered by the jurisdictional minister</p> <p>Subsequently determined as light regulation by the NCC or (for Carpentaria Gas Pipeline) jurisdictional minister</p>	<p>Includes two Queensland distribution pipelines and 3.5 transmission pipelines:</p> <ul style="list-style-type: none"> - Carpentaria Gas Pipeline - Central West Pipeline - Marsden to Wilton part of Moomba-Sydney Pipeline
Access regime for non-scheme pipelines Over 200 pipelines (Part 23 of the NGR)	<p>Negotiate-arbitrate framework with information disclosure and dispute resolution requirements</p>	<p>Commenced in August 2017.</p> <p>Pipelines commissioned after the code and have not been subsequently covered by the jurisdictional minister.</p> <p>Pipelines deemed covered when the code came into effect in 1997 and have been subsequently uncovered by the jurisdictional minister.</p> <p>Pipelines granted a 15-year no coverage determination by the NCC under greenfields pipeline incentives regime</p>	<p>Includes many small distribution and transmission pipelines such as:</p> <ul style="list-style-type: none"> - Wagga Wagga distribution pipeline - Bonaparte Pipeline - Gooimbah Pipeline <p>Also includes some significant transmission pipelines such as Eastern Gas Pipeline, Moomba-Adelaide Pipeline System, SEA Gas Pipeline, South West Queensland Pipeline.</p>

Note: For a pipeline that is 'covered' either full or light regulation is applied under Parts 8-12 of the NGR

Table 2: Summary of AEMC recommendations

Recommendation	Benefit
Framework for regulation	
<div>Review into the tests and forms of pipeline regulation</div> <div><i>(new from draft recommendation)</i></div>	<div>Maximise the benefits for pipeline users and gas consumers of the recent gas sector reforms by improving the cohesiveness of the total regulatory regime</div>
Extensions and expansions	
<div>Include all expansions in an access arrangement</div> <div>Remove regulator’s discretion to exclude an expansion from light regulation</div> <div>Enable existing extensions to be included in access arrangements</div>	<div>Enable regulators to determine fairly priced services on expanded capacity of a pipeline or extended laterals to a pipeline, placing a greater constraint on the use of market power by a pipeline owners</div>
Reference services	
<div>Clarify the requirements for defining pipeline services</div> <div>Clarify the requirements for defining reference services</div> <div>Update the test for determining a reference service</div> <div>Improve the access arrangement review process and introduce a reference service setting process</div>	<div>Enable regulators to determine more efficient, cost reflective prices for more services, placing a greater constraint on the use of market power by pipeline owners</div>

Recommendation

Benefit

Access arrangements

Develop financial models to be used by service providers

Clarify the operation of revenue caps

Clarify that the regulator is to have regard to risk sharing arrangements

Extend the revision period

Clarify the process for equalising revenue during the interval of delay

Remove the limited and no discretion regulatory framework

Lower regulatory costs and improve transparency of decision making for pipeline service providers, regulators, pipeline users and gas consumers

Efficient costs

Clarify the application of the new capital expenditure criteria

Provide guidance on the allowed return for speculative capital expenditure

Require an initial capital base valuation for light regulation pipelines

Enable the addition of existing extensions and expansions to the opening capital base

Require allocation of expenditure between covered and uncovered parts of a pipeline

Amend definition of rebateable services and rebate methodology

Improve the regulatory assessment of efficient costs to result in lower prices for pipeline users and gas consumers

Recommendation

Benefit

Information reporting

Require transmission pipeline service providers to disclose Bulletin Board information

Require distribution pipeline service providers to disclose capacity and usage information

(updated from draft recommendation)

Clarify the role of the regulator in passing on information requests to service providers

Introduce a financial and offer information disclosure regime for light regulation pipelines

Remove the requirement to provide KPIs as part of the access arrangement

Improve the Scheme Register

Enable pipeline users to be better informed in order to negotiate fairer prices, terms and conditions for pipeline services to transport gas

Dispute resolution

Clarify the negotiation process and the trigger for the dispute resolution process

Clarify the role of the dispute resolution expert

Establish a reference framework for the dispute resolution body

Introduce a fast-tracked dispute resolution process

Publish dispute resolution commencement, outcome and other information

Enable joint dispute resolution hearings

Improve pipeline users' access to dispute resolution and outcome certainty as well as create a more credible threat to motivate fair access negotiations between pipeline users and owners