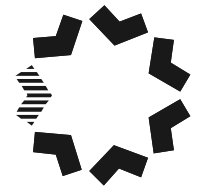


NATIONAL  
COMPETITION  
COUNCIL



# Certification of State and Territory Access Regimes

A guide to Certification under  
Part IIIA of the  
*Competition and Consumer Act  
2010 (Cth)*



**August 2011**

Version 4.0

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An appropriate citation for this paper is:

National Competition Council 2011, *Certification of State and Territory Access Regimes: A guide to Certification under Part IIIA of the Competition and Consumer Act*, Melbourne.

**The National Competition Council**

The National Competition Council was established on 6 November 1995 by the *Competition Policy Reform Act 1995* following agreement by the Australian Government and state and territory governments. It is a federal statutory authority which functions as an independent advisory body for all governments on third party access matters.

Information on the National Competition Council, its publications and its current work program can be found on the internet at [www.ncc.gov.au](http://www.ncc.gov.au) or by contacting the Council on (03) 9981 1600.

## Foreword

As a part of the Competition Principles Agreement (CPA),<sup>1</sup> Australian governments agreed that states and territories might establish or continue to operate regimes for regulating access to infrastructure and other facilities within their jurisdiction. Where these regimes are certified as effective they apply to the exclusion of other regulatory mechanisms providing for access.

Where a state or territory wishes to implement an access regime and for services that are subject to that regime to be exempt from declaration under Part IIIA of the *Competition and Consumer Act 2010* (Cth) (CCA) or from the provision of access undertakings to the Australian Competition and Consumer Commission (ACCC), it may apply to the National Competition Council (Council) for certification of the regime. The Council then considers the application and advises a decision making Commonwealth Government Minister whether the state or territory regime should be certified as effective.

The Council's consideration of a certification application includes a public submission process as well as inquiries and discussions initiated by the Council. The purpose of this guide is to assist parties considering making an application for certification to assess the merits of such an application and if appropriate to prepare their application. The guide is also intended to assist other parties with an interest in an application, including those who may wish to make a submission.

The Council issued its original guide on certification in 2003 (that guide was Part C of the three part guide entitled: *The National Access Regime - A Guide to Part IIIA of the Trade Practices Act 1974*). The Council issued an updated guide in January 2009, to reflect the Council's thinking as it had evolved through dealing with applications since 1996 and amendments to the CPA as at the date of issue and a further update in May 2009 making explicit that the Council must consider an access regime's regard to the objects of Part IIIA of the CCA and recommend on the duration of any certification. The guide was further updated in October 2010 to reflect the changes to the certification process following amendments to the then *Trade Practices Act 1974* (Cth) made by the *Trade Practices Amendment (Infrastructure Access) Act 2010* (Cth) (TPA Amendment Act), which took effect on 14 July 2010. This update (August 2011) updates the guide for the change in name of the TPA to CCA and other minor revisions evolving from the Council's recent certification work.

While the guide reflects the Council's current approach, each certification application must be considered on its particular facts and may raise unique issues. As such, the Council's thinking continues to evolve and the views expressed in the guide are not definitive.

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<sup>1</sup> Agreement between the Commonwealth of Australia and the States of New South Wales, Victoria, Queensland, Western Australia, South Australia and Tasmania, and the Australian Capital Territory and the Northern Territory, entered into on 11 April 1995 and amended several times, most recently on 13 April 2007.

The guide is principally available from the Council's website at [www.ncc.gov.au](http://www.ncc.gov.au), although the Council provides printed copies on request.

The Council will update this guide when significant developments occur, with the updated version available on line. Any person viewing a printed copy of this guide should check the Council's website or call the Council on (03) 9981 1600 to ensure they have the current version (a version number and date appear on the front cover page of this document).

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## Abbreviations

Abbreviation	Description
ACCC	Australian Competition and Consumer Commission
CCA	<i>Competition and Consumer Act 2010</i> (Cth)
clause 6 principles	The principles set out in clauses 6(2)-6(5) of the Competition Principles Agreement (as amended to 13 April 2007)
COAG	Council of Australian Governments
Commonwealth Criminal Code	<i>Criminal Code Act 1995</i> (Cth)
Council	National Competition Council
CPA	Competition Principles Agreement
Gas Pipelines Access Law	Schedule to the <i>National Gas Pipelines Access (South Australia) Act 1997</i> which was applied as law in the following jurisdictions: <i>Gas Pipelines Access (Western Australia) Act 1998</i> ; <i>Gas Pipelines Access (Victoria) Act 1998</i> , <i>Gas Pipelines Access (New South Wales) Act 1998</i> , <i>Gas Pipelines Access (Queensland) Act 1998</i> , <i>Gas Pipelines Access (ACT) Act 1998</i> , <i>Gas Pipelines Access (Northern Territory) Act 1998</i> , <i>Gas Pipelines Access (Tasmania) Act 2000</i>  This has been superseded by the National Gas Law (NGL) and Rules (NGR)
National Access Regime	The access regime set out in Part IIIA of the CCA
National Gas Code	National Third Party Access Code for Natural Gas Pipeline Systems. This has been superseded by the NGL and NGR
National Gas Rules/NGR	National Gas Rules 2008
National Gas Law/NGL	Schedule to the <i>National Gas (South Australia) Act 2008</i> which is applied as law in the following jurisdictions: <i>National Gas (New South Wales) Act 2008</i> , <i>National Gas (ACT) Act 2008</i> , <i>National Gas (Tasmania) Act 2008</i> , <i>National Gas (Queensland) Act 2008</i> , <i>National Gas (Victoria) Act 2008</i> and <i>National Gas (Northern Territory) Act 2008</i>

New South Wales Gas Regime	The New South Wales Gas Regime comprises the <i>Gas Pipelines Access (NSW) Act 1998</i> and the <i>Gas Pipelines Access (Commonwealth) Act 1998</i> . The Gas Pipelines Access (NSW) Act applied, as a law of New South Wales the Gas Pipelines Access Law
New South Wales Rail Regime	The New South Wales Rail Regime operated in conjunction with the <i>Commercial Arbitration Act 1984</i> (NSW), <i>Transport Administration Act 1988</i> (NSW), <i>Rail Safety Act 1993</i> (NSW), <i>State Owned Corporations Act 1989</i> (NSW) and <i>Independent Pricing and Regulatory Tribunal Act 1992</i> (NSW). The regime has been superseded by the NSW Rail Access Undertaking pursuant to Schedule 6AA of the <i>Transport Administration Act 1988</i> (NSW)
Northern Territory/South Australian Rail Regime	The regime consists of the AustralAsia Railway (Third Party Access) Code, embodied in a Schedule to the <i>AustralAsia Railway (Third Party Access) Act 1999</i> (NT) and in the <i>AustralAsia Railway (Third Party Access) Act 1999</i> (SA). The regime also includes two safety Acts (the <i>Northern Territory Rail Safety Act 1998</i> (NT) and the <i>Rail Safety Act 2007</i> (SA))
NT Code	Northern Territory Electricity Network Access Code
Queensland Rail Access Regime	The regime comprising the <i>Queensland Competition Authority Act 1997</i> (Qld), <i>Queensland Competition Authority Regulation 2007</i> (Qld) <i>Transport Infrastructure Act 1994</i> (Qld), <i>Transport (Rail Safety Act) 2010</i> (Qld) and the applicable access undertaking accepted by the Queensland Competition Authority
Part IIIA	Part IIIA of the <i>Competition and Consumer Act 2010</i> (Cth)
Queensland Access Regime for Gas Pipelines	The <i>Gas Pipelines Access (Queensland) Act 1998</i> (Qld). The Act applied the Gas Pipelines Access Law and the National Gas Code
Regulations	Competition and Consumer Regulations 2010 (Cth)
responsible Minister	The Premier, in case of a state, and the Chief Minister in case of a territory
South Australian Ports Access Regime	The regime established under the <i>Maritime Services (Access) Act 2000</i> (SA)

South Australian Rail Access Regime	The access regime established by the <i>Railways (Operations and Access) Act 1997 (SA)</i>
TPA	<i>Trade Practices Act 1974 (Cth)</i>
TPA Amendment Act	<i>Trade Practices Amendment (Infrastructure Access) Act 2010 (Cth)</i>
Tribunal	Australian Competition Tribunal
Western Australian Electricity Networks Access Regime	The access regime set out in Part 8 of the <i>Electricity Industry Act 2004</i> which established the Electricity Networks Access Code 2004
Western Australian Rail Access Regime	The access regime set out in the <i>Railways (Access) Act 1998 (WA)</i> and the <i>Railways (Access) Code 2000 (WA)</i>

## Version history

Version	Modifications made
August 2011	Fourth edition. Updating to reflect change in name from TPA to CCA (with effect 1 January 2011) and minor updating following recent certification decisions.
October 2010	Third edition. Redrafting and update in particular to accommodate changes to Part IIIA of the TPA (date of effect 14 July 2010) arising from the TPA Amendment Act.
May 2009	Minor redrafting of second edition, in particular to make more explicit the requirement for the Council to have regard to the objects of Part IIIA and that the Council recommends on the duration of any certification.
January 2009	Second edition. Major redrafting and update, in particular to accommodate changes to the TPA and changes to the CPA.
February 2003	First edition

## 1 Certification of access regimes

- 1.1 States and territories may establish their own regimes for access to services and for regulating the prices and other terms and conditions for such access. A state or territory, that is a party to the CPA, may apply to have an access regime certified as an 'effective access regime' for the purposes of the CCA. The certification process is set out in ss 44M–44O of the CCA.
- 1.2 Section 44M(4) of the CCA states that in deciding whether to recommend that a regime be certified to be effective the Council must:
- assess whether it is an 'effective access regime' by applying the principles set out in clauses 6(2)–6(5) of the CPA —the clause 6 principles (see Box 1-1)
  - have regard to the objects of Part IIIA of the CCA set out in s 44AA (see paragraph 2.25).<sup>2</sup>
- 1.3 Where a state or territory regime is certified as effective, that regime will exclusively govern regulation of access to the services to which it applies and those services cannot be declared under the generic provisions of the National Access Regime in Part IIIA of the CCA or subject to an access undertaking to the ACCC.
- 1.4 Following the TPA Amendment Act, for an access regime to be considered an effective access regime it must be certified. Where a regime is certified as effective the services covered by that regime cannot be declared (ss 44G(2)(e)(i) and 44H(4)(e)(i)). Certification will ordinarily ensure that the state or territory regime exclusively governs access to the services for the duration of certification. (Prior to the TPA Amendment Act services covered by an 'effective' access regime were immune from declaration under Part IIIA of the CCA whether or not the regime was certified.)
- 1.5 While a state or territory government is not required by legislation to have an access regime certified and such a regime will be enforceable irrespective of whether it is certified, certification provides access seekers, infrastructure operators, developers and other parties with certainty about how access will be regulated. Certification also assists in avoiding the scope for duplicated regulation and the imposition of conflicting regulatory requirements.

### Eligibility for certification

- 1.6 Only states and territories that are a party to the CPA may apply for certification of an access regime. If a state or territory ceases to be a party to the CPA, any certification decisions cease to have effect (s 44P).

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<sup>2</sup> This latter requirement was introduced by the *Trade Practices Amendment (National Access Regime) Act 2006* (Cth).

- 1.7 The CCA does not provide a certification process for Australian (Commonwealth) Government access regimes. Nor does it apply to non government access regimes, although businesses may obtain immunity from the declaration provisions of Part IIIA by having the ACCC approve an access undertaking under s 44ZZA of the CCA (s 44G(1)).

### **How to apply for certification**

- 1.8 To obtain certification the responsible Minister—the Premier of a state or Chief Minister of a territory—may apply, in writing, to the Council asking the Council to recommend that the Commonwealth Minister certify an access regime as effective.
- 1.9 The requirements for application to the Council for a recommendation on the effectiveness of an access regime are prescribed in regulation 6B of the *Competition and Consumer Regulations 2010* (Cth) (Regulations). (See Appendix A for an extract of regulation 6B.) An application should set out the matters required by regulation 6B including a description of the access regime (including a copy of any relevant legislation and associated subordinate legislation, rules or similar provisions) and the service(s) subject to the regime.
- 1.10 An application for certification should include explanations and evidence to support the application and, in particular explain and demonstrate how each of the clause 6 principles is satisfied in relation to the services specified. Applications should demonstrate that the access regime has regard to the objects of Part IIIA set out in s 44AA of the CCA. Applications should also include the applicant’s assessment (with supporting rationale) of the appropriate period of certification.
- 1.11 It is likely to be useful for an application to include any explanatory memoranda or parliamentary speeches or papers that assist in interpreting the relevant legislation and any guidelines or similar information that has been or will be provided to the public in relation to the regime.

### **The Council’s role in the certification process**

- 1.12 In determining whether to recommend that an access regime be certified as effective the Council:
- is guided by the clause 6 principles (s 44M(4))
  - must treat each principle as having the status of a guideline rather than a binding rule (s 44DA)
  - must have regard to the objects set out in s 44AA of Part IIIA
  - is not permitted to consider any other matters (s 44M(4)).<sup>3</sup>

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<sup>3</sup> In making its recommendation the Council must also disregard certain provisions of Commonwealth or state or territory laws relating to access to gas pipelines (see s 44M(4A) of the CCA).

- 1.13 If the Council recommends certification then it must also recommend to the Commonwealth Minister how long that certification should be in force (s 44M(5)) (see paragraphs 2.38–2.40). A certification remains in force for the duration specified in the Commonwealth Minister’s decision unless the relevant state or territory ceases to be a party to the CPA.
- 1.14 The Council must make its recommendation on an application for certification to the Commonwealth Minister within 180 days of receiving the application (s 44NC) starting at the start of the day the application is received. There is provision to stop the clock during this period in certain circumstances. The Council may also extend the period for making its recommendation in certain circumstances, for example if an application is particularly complex or where significant public holidays such as the Christmas/New Year period or other factors restrict the Council’s ability to gather information. If it does this, the Council must provide notice in writing to the Minister, the applicant and the service provider and must publish a notice in a national newspaper. In giving notice the Council must specify when it expects to make a recommendation on the application.
- 1.15 The Council consults on all applications received. Following receipt of an application for certification the Council seeks submissions and has regard to comments received in developing its recommendation. It also publishes a draft recommendation giving the reasons for its proposed recommendation and provides an opportunity for submissions on the draft recommendation. The Council allows at least 14 days for written submissions in response to the draft recommendation (s 44NE).

**Box 1-1: Submissions made and providing information to the Council**

Parties submitting information to the Council are advised that the giving of false or misleading information to a Commonwealth entity, such as the Council, is a serious offence. Section 137.1 of the Commonwealth Criminal Code makes it a criminal offence for a person to supply information to a Commonwealth body knowing that the information is false or misleading in a material particular or omitting any matter or thing without which the information is misleading in a material particular.

- 1.16 The Council informs the applicant and (where the applicant is not the service provider) the service provider when it has provided its final recommendation to the Commonwealth Minister. As soon as practicable after the Commonwealth Minister makes a decision the Council publishes its final recommendation and Minister’s decision on the its website ([www.ncc.gov.au](http://www.ncc.gov.au)) and provides a copy of the final recommendation to the applicant and the service provider (s 44NF).

**The Minister’s decision**

- 1.17 After receiving the Council’s recommendation the Commonwealth Minister must decide whether the regime is an effective access regime or whether it is not an effective access regime. If the Minister decides to certify the regime then the Minister must also specify the period for which certification will be in force (s 44N(3)). The

Minister is required to publish his or her reasons for the decision. If the Minister does not publish his or her decision on a recommendation within the period starting at the start of the day the recommendation is received and ending at the end of 60 days after that day the Minister is taken to have made a decision in accord with the recommendation of the Council and to have published that decision. If the Council recommended that the Minister decide that the regime is an effective regime then the decision is taken to be in force for the period recommended by the Council.

### **Review of Minister's decision**

- 1.18 The applicant for certification can apply to the Australian Competition Tribunal (the Tribunal) for a review of the Commonwealth Minister's decision. The application for review must be made within 21 days after the publication of the Commonwealth Minister's decision (s 44O(2)). The Tribunal may affirm, vary or reverse the original decision. Any decision of the Tribunal is to be taken to be the decision of the Commonwealth Minister (s 44O(4)).
- 1.19 The Tribunal must make a decision within 180 days starting at the start of the day the recommendation is received (s 44ZZOA(2)). This period may be extended by written notice (s 44ZZOA(7)).

## 2 The criteria for certification

- 2.1 The clause 6 principles set out the criteria for assessing the effectiveness of a state or territory access regime as part of a certification. Sections 44M(4) and 44N(2) of the CCA import the clause 6 principles as a consideration into the certification process. In addition, in assessing effectiveness the Council must have regard to the objects in Part IIIA of the CCA (s 44M(4)(aa)).
- 2.2 The relevant provisions of clause 6 of the CPA are set out in Box 2-1.

### Box 2-1: The clause 6 principles

—extract from the Competition Principles Agreement (as amended to 13 April 2007)

- 6(2) The regime to be established by Commonwealth legislation is not intended to cover a service provided by means of a facility where the State or Territory Party in whose jurisdiction the facility is situated has in place an access regime which covers the facility and conforms to the principles set out in this clause unless:
- (a) the Council determines that the regime is ineffective having regard to the influence of the facility beyond the jurisdictional boundary of the State or Territory; or
  - (b) substantial difficulties arise from the facility being situated in more than one jurisdiction.
- 6(3) For a State or Territory access regime to conform to the principles set out in this clause, it should:
- (a) apply to services provided by means of significant infrastructure facilities where:
    - (i) it would not be economically feasible to duplicate the facility;
    - (ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market; and
    - (iii) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist; and
  - (b) reasonably incorporate each of the principles referred to in subclause (4) and (except for an access regime for: electricity or gas that is developed in accordance with the Australian Energy Market Agreement; or the Tarcoola to Darwin railway) subclause (5).  
There may be a range of approaches available to a State or Territory Party to incorporate each principle. Provided the approach adopted in a State or Territory access regime represents a reasonable approach to the incorporation of a principle in subclause (4) or (5), the regime can be taken to have reasonably incorporated that principle for the purposes of paragraph (b).
- 6(3A) In assessing whether a State or Territory access regime is an effective access regime under the *Trade Practices Act 1974*, the assessing body:
- (a) should, as required by the *Trade Practices Act 1974*, and subject to section 44DA, not consider any matters other than the relevant principles in this Agreement. Matters which should not be considered include the outcome of any arbitration, or any decision, made under that access regime;
  - (b) should recognise that, as provided by ss44DA(2) of the *Trade Practices Act 1974*, an access regime may contain other matters that are not inconsistent with the relevant principles in this Agreement.

- 6(4) A State or Territory access regime should incorporate the following principles:
- (a) Wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the person seeking access.
  - (b) Where such agreement cannot be reached, governments should establish a right for persons to negotiate access to a service provided by means of a facility.
  - (c) Any right to negotiate access should provide for an enforcement process.
  - (d) Any right to negotiate access should include a date after which the right would lapse unless reviewed and subsequently extended; however, existing contractual rights and obligations should not be automatically revoked.
  - (e) The owner of a facility that is used to provide a service should use all reasonable endeavours to accommodate the requirements of persons seeking access.
  - (f) Access to a service for persons seeking access need not be on exactly the same terms and conditions.
  - (g) Where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.
  - (h) The decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved.
  - (i) In deciding on the terms and conditions for access, the dispute resolution body should take into account:
    - (i) the owner's legitimate business interests and investment in the facility;
    - (ii) the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets;
    - (iii) the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake;
    - (iv) the interests of all persons holding contracts for use of the facility;
    - (v) firm and binding contractual obligations of the owner or other persons (or both) already using the facility;
    - (vi) the operational and technical requirements necessary for the safe and reliable operation of the facility;
    - (vii) the economically efficient operation of the facility; and
    - (viii) the benefit to the public from having competitive markets.
  - (j) The owner may be required to extend, or to permit extension of, the facility that is used to provide a service if necessary but this would be subject to:
    - (i) such extension being technically and economically feasible and consistent with the safe and reliable operation of the facility;
    - (ii) the owner's legitimate business interests in the facility being protected; and
    - (iii) the terms of access for the third party taking into account the costs borne by the parties for the extension and the economic benefits to the parties resulting from the extension.
  - (k) If there has been a material change in circumstances, the parties should be able to

- apply for a revocation or modification of the access arrangement which was made at the conclusion of the dispute resolution process.
- (l) The dispute resolution body should only impede the existing right of a person to use a facility where the dispute resolution body has considered whether there is a case for compensation of that person and, if appropriate, determined such compensation.
  - (m) The owner or user of a service shall not engage in conduct for the purpose of hindering access to that service by another person.
  - (n) Separate accounting arrangements should be required for the elements of a business which are covered by the access regime.
  - (o) The dispute resolution body, or relevant authority where provided for under specific legislation, should have access to financial statements and other accounting information pertaining to a service.
  - (p) Where more than one State or Territory regime applies to a service, those regimes should be consistent and, by means of vested jurisdiction or other cooperative legislative scheme, provide for a single process for persons to seek access to the service, a single body to resolve disputes about any aspect of access and a single forum for enforcement of access arrangements.
- 6(5) A State, Territory or Commonwealth access regime (except for an access regime for: electricity or gas that is developed in accordance with the Australian Energy Market Agreement; or the Tarcoola to Darwin railway) should incorporate the following principles:
- (a) Objects clauses that promote the economically efficient use of, operation and investment in, significant infrastructure thereby promoting effective competition in upstream or downstream markets.
  - (b) Regulated access prices should be set so as to:
    - (i) generate expected revenue for a regulated service or services that is at least sufficient to meet the efficient costs of providing access to the regulated service or services and include a return on investment commensurate with the regulatory and commercial risks involved;
    - (ii) allow multi-part pricing and price discrimination when it aids efficiency;
    - (iii) not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and
    - (iv) provide incentives to reduce costs or otherwise improve productivity.
  - (c) Where merits review of decisions is provided, the review will be limited to the information submitted to the original decision-maker except that the review body:
    - (i) may request new information where it considers that it would be assisted by the introduction of such information;
    - (ii) may allow new information where it considers that it could not have reasonably been made available to the original decision-maker; and
    - (iii) should have regard to the policies and guidelines of the original decision-maker (if any) that are relevant to the decision under review.

## Applying the clause 6 principles

- 2.3 In essence, the clause 6 principles:
- identify the types of services provided by means of significant infrastructure facilities that may be subject to access regulation
  - establish the principles that the access regime should incorporate.
- 2.4 In assessing whether a state or territory regime is effective the Council must:
- apply each of the clause 6 principles as guiding principles
  - have regard to the objects of Part IIIA
  - not consider any other matters (s 44M(4) and clause 6(3A)).
- 2.5 Certification does not necessarily limit the content of an effective access regime. An effective state/territory access regime may contain additional matters as long as they are not inconsistent with the CPA principles (s 44DA(2)).
- 2.6 The Council and the Commonwealth Minister have significant flexibility in applying the clause 6 principles. Section 44DA of the CCA requires that the Council apply each individual clause 6 principle, treating each principle as a guideline rather than a binding rule. The CPA states that there may be a range of approaches available to a state or territory government in incorporating a principle, and that where a state or territory access regime adopts a reasonable approach to the incorporation of a principle, the regime can be taken to have reasonably incorporated the principle as required by clause 6(3).
- 2.7 While an effective access regime needs to reflect each of the clause 6 principles, the Council recognises that a range of regulatory arrangements are capable of delivering efficient outcomes.
- 2.8 There will often be significant interdependencies between one aspect of a regime and another. Consequently in considering whether an access regime is effective and satisfies the clause 6 principles, it is necessary to undertake a holistic assessment of the access regime.
- 2.9 While the underlying objective of access regulation has always been the promotion of efficiency, the CPA makes explicit that the goals of access regulation are to promote the efficient use and operation of, and investment in, significant infrastructure to promote competition in activities in upstream and downstream markets that rely on the use of the infrastructure.<sup>4</sup>
- 2.10 In assessing an application for certification against the clause 6 principles, the Council generally organises its consideration of the principles into five categories.

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<sup>4</sup> This is consistent with the Part IIIA objects clause which requires the Council and the Minister, along with other regulators and decision makers, to have regard to efficiency and competition objectives in dealing with third party access matters.

- Scope of an access regime – 6(3), 6(4)(d)
  - Treatment of interstate issues – 6(2), 6(4)(p)
  - Negotiation framework – 6(4)(a)–(c), (e), (f), (g)-(i), (m), (n), (o)
  - Dispute resolution – 6(4)(a)–(c), (g), (h), (i), (j), (k), (l), (o), 6(5)(c)
  - Efficiency promoting terms and conditions of access – 6(4)(a)–(c), (e), (f), (i), (k), (n), 6(5)
- 2.11 In addition, the Council must have regard to the objects of Part IIIA (s 44M(4)(aa) of the CCA) (see paragraphs 2.25–2.36).
- 2.12 The Council considers that the above categorisation (the CPA elements and the Part IIIA objects) provides a logical framework for analysis and helps to clarify how a regime addresses the necessary elements of an effective access regime. The categorisation does not replace the clause 6 principles and regard to the Part IIIA objects as the basis for assessing a regime’s effectiveness.
- 2.13 The Council will generally structure its recommendation on the basis of the above categories (in paragraphs 2.10 and 2.11). In forming its view as to the effectiveness of a regime, the Council considers each relevant clause 6 principle, and, as required by clause 6(3A)(a), only the relevant clause 6 principles, as well as having regard to the objects of Part IIIA. The Council encourages applicants to define the regime submitted for certification and discuss it in terms of these categories, while ensuring that their application addresses all relevant clause 6 principles and the objects of Part IIIA.
- 2.14 Recognising that several of the clause 6 principles relate to more than one of the categories, this guide discusses each principle sequentially (with the exception that it discusses clause 6(2) concurrently with the related clause 6(4)(p)).

### **The service(s) covered by an effective access regime**

- 2.15 Section 44M(1) of the CCA and clause 6(3) of the CPA limit the application of effective regimes to a ‘service’ as defined in s 44B of the CCA. Therefore, only applications for certification of access regimes that relate to services that fall within the definition in s 44B may be considered.
- 2.16 Section 44B provides that:
- ‘service’ means a service provided by means of a facility and includes:
- (a) the use of an infrastructure facility such as a road or railway line;
  - (b) handling or transporting things such as goods or people;
  - (c) a communications service or similar service;
- but does not include:
- (d) the supply of goods; or
  - (e) the use of intellectual property; or
  - (f) the use of a production process;

except to the extent that it is an integral but subsidiary part of the service.

- 2.17 A service is distinct from a facility; although it may consist merely of the use of a facility. In *Rail Access Corporation v New South Wales Minerals Council Ltd*,<sup>5</sup> for example, the Full Court of the Federal Court said:

The definition of ‘service’ in section 44B of the TPA makes clear that a service is something separate and distinct from a facility. A service may, however, consist merely of the use of a facility. The definition of ‘service’ distinguishes between the use of an infrastructure facility, such as a road or railway line, and the handling or transporting of things such as goods or people, by the use of a road or railway line. (at [524])

- 2.18 In *BHP Billiton Iron Ore Pty Ltd v National Competition Council* [2008] HCA 45 the High Court Of Australia stated that the term ‘service’ in s 44B of the then TPA does not include the supply and uses identified in any of paragraphs (d), (e) and (f) [of s 44B], except to the extent that this supply or use is ‘an integral but subsidiary part of the service’ (at [33]).

- 2.19 In relation to the exclusion in paragraph (f) of the use of a production process, having identified the relevant service and the production process, the High Court identified the relevant question as whether the use of the service [by an access seeker] also answers the description of the use of the service provider’s production process (at [41]). If the use to be made of the service ‘answers the description’ of the service provider’s production process, then the service falls within the exception created by paragraph (f).

- 2.20 The fact that the service provider’s production process uses integers (for example, the use of a specific facility or an element of a process) which an access seeker wants to use for its own purposes does not necessarily mean that a service using those integers is excluded from the definition of service in s 44B (High Court at [43]).

- 2.21 For further discussion relating to the definition of ‘service’ see the Council’s guide to declaration (NCC 2009).

- 2.22 Clause 6(3) of the CPA also limits the coverage of an effective access regime to the services provided by means of significant infrastructure facilities that are not economically feasible to duplicate and that are a bottleneck to competition in other markets. In addition, clause 6(4)(d) requires that the coverage of a regime be subject to periodic review.

- 2.23 An effective regime should therefore clearly define the service(s) and proposed service(s) that it covers (and excludes). It should also require that the services are provided by significant bottleneck infrastructure facilities.

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<sup>5</sup> In this matter the NSW Minerals Council sought declaration of the use of rail track services provided by the Rail Access Corporation. *Rail Access Corp v New South Wales Minerals Council Ltd* (1998) 87 FCR 517; (1998) 159 ALR 323; (1998) ATPR 41-663.

2.24 For the sake of administrative efficiency and to promote greater certainty over time, an access regime is usually designed to accommodate changes (additions or deletions) to the specific services and facilities it covers. Australia’s gas and electricity access regimes, for example, are designed to cover the service(s) of newly constructed transmission and distribution systems. To be part of an effective access regime such arrangements should be consistent with the clause 6 principles. That is, the coverage of the regime should be determined through rigorous and independent processes using consistent and clear criteria.

## **Objects of Part IIIA and access regulation**

2.25 The *Trade Practices Amendment (National Access Regime) Act 2006* (Cth) inserted an objects clause into Part IIIA that the Council and the Minister must have regard to when assessing the effectiveness of an access regime. Section 44AA provides that:

The objects of this Part are to:

- (a) promote the economically efficient operation of, use of and investment in the infrastructure by which services are provided, thereby promoting effective competition in upstream and downstream markets; and
- (b) provide a framework and guiding principles to encourage a consistent approach to access regulation in each industry.

2.26 Paragraph (a) is mirrored by a similar amendment in clause 6(5)(a) of the CPA that requires certain access regimes to incorporate to the following principle:

6(5)(a) Objects clauses that promote the economically efficient use of, operation of, and investment in significant infrastructure, thereby promoting effective competition in upstream and downstream markets.

2.27 While this clause does not apply to an access regime for electricity or gas developed in accord with the Australian Energy Market Agreement or the regime for the Tarcoola to Darwin railway, s 44M of the CCA requires the Council to have regard to the objects of Part IIIA in making a recommendation on the effectiveness of a state and territory access regime. The objects of Part IIIA, set out in s 44AA of the CCA, largely mirror clause 6(5)(a). Thus the Council interprets this as meaning that all state and territory access regimes should reflect the efficiency goals of access regulation whether or not there is a clear statement of purpose.

2.28 These amendments are consistent with the principles of good regulation. By clearly specifying the desired outcome of regulation there is less scope for the interpretation of the operational criteria to diverge from the intent of the regulation. It also makes clear to all parties that the desired outcome of regulating access is the promotion of efficiency and the promotion of effective competition. Clarifying the intent of an access regime can also reduce the number of disputes and misunderstandings, which in turn, saves time and reduces the cost of regulation.

2.29 Where there are many pathways for regulating access—such as state and territory access regimes, declaration or undertakings—it is important that access regimes are consistent. Paragraph (b) of s 44AA of the CCA aims to ensure that there is a

consistent approach to the way access is regulated in each industry both inter and intra state.

2.30 The application of an efficiency objective in access regulation has three broad components. It:

- ensures the efficient use of bottleneck infrastructure, especially by denying infrastructure owners the opportunity to misuse market power (in either the market for their services or in related markets) by raising prices and/or refusing access to services
- facilitates efficient investment in essential infrastructure, especially by ensuring:
  - infrastructure is maintained and developed appropriately
  - infrastructure owners (and potential owners) earn sufficient returns to provide incentives for efficient investment
  - incentives for inefficient development of competitive infrastructure and for inefficient investment in upstream and downstream activities (that is, overinvestment and underinvestment) are minimised
- promotes competition in activities that rely on the use of bottleneck infrastructure where competitive service provision is not economically feasible.

2.31 In addition to promoting efficiency, s 44AA(b) of the CCA seeks to ensure that for each industry there is a consistent approach to access regulation, both inter and intra state. Consistency is particularly important where there are a number of pathways for regulating access—such as state and territory access regimes, declarations or undertakings. The Council interprets this as meaning that no matter the avenue used for regulating access—whether it is via declaration, an undertaking or a specific state and territory access regime—the approach to regulation and the outcomes sought should largely be consistent. This does not mean that every access regime needs to be the same. The size and features of the market in which an infrastructure provider operates can and does vary and may require specific regulatory responses. Indeed in recommending that Part IIIA of the then TPA include the objects set out in s 44AA, the Productivity Commission stated that ‘the role of Part IIIA is to act ‘as a discipline on, rather than to prescribe the composition of industry-specific regimes.’ (PC 2001, p 134)

2.32 In its final recommendation on the application for certification of the Western Australian Rail Access Regime, the Council concluded that the regime did not provide a framework and guiding principles to encourage a consistent approach to railway access regulation in Western Australia and as such did not have regard to the concept of consistency in s 44AA(b) of the CCA. The Council’s findings were that railways in Western Australia were subject to varying forms of access regulation – the Western Australian Rail Access Regime, declaration under Part IIIA and potentially an access undertaking to the ACCC – and in some instances (largely for historical reasons) no regulation. Furthermore, given the various means of access regulation utilised, little

regulatory certainty existed for access to greenfield railways. As such, the Council concluded that the requirement for consistency in each industry was not met because there was inconsistency within the Western Australian rail industry (NCC 2010d). In the Commonwealth Minister's decision to certify the WA Rail Access Regime, a different view was taken of s 44AA(b). The Commonwealth Minister considered that it required consideration of how the WA Rail Access Regime sat within the framework and guiding principles established by Part IIIA and that the phrase "in each industry" referred to consistency across different industries.<sup>6</sup>

- 2.33 The Council considers that both interpretations to s 44AA(b) are open and that, depending on the circumstances of a particular application for certification, either interpretation (or both of them) may be relevant in having regard to the objects of Part IIIA.
- 2.34 In the certification process, the Council's broad focus is on whether an access regime establishes an appropriate framework for these goals to be achieved. The clause 6 principles, as agreed in 1995, draw on the Hilmer Report (1993), which advocated a negotiate/arbitrate model. Under this model an access seeker negotiates the terms of access with the service provider. The parties have recourse to arbitration where they fail to reach a commercial agreement on the terms of access. This approach seeks to keep the costs of regulatory intervention to a minimum and avoid excessive intrusion.
- 2.35 The Council's experience in certification matters—supported by material in written submissions and views expressed by stakeholders in meetings—is that a degree of regulatory intervention is often needed to deliver efficient outcomes and to facilitate access to monopoly infrastructure facilities. The extent of intervention needed, however, will often depend on the nature of the services covered by the access regime and conditions in the market for the services. Where an incumbent service provider is providing services to many, potentially relatively small, access seekers, a more interventionist and prescriptive access regime may be warranted to address significant information and negotiating power asymmetries. Addressing such asymmetries through the access regime may be necessary to facilitate effective access negotiations.
- 2.36 In contrast, where an industry is characterised by an incumbent service provider that deals with a few large and well informed access seekers, the information and negotiating power asymmetries between the parties may not be significant. As such, effective access negotiations between the parties may be able to take place in the context of a light-handed access regime with minimal regulatory intervention and prescription.

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<sup>6</sup> Bradbury, the Hon. D (Parliamentary Secretary to the Treasurer), 2011, *Decision to certify the Western Australian Rail Access Regime*, Media release no. 004, 11 February and accompanying statement of reasons.

2.37 What constitutes an 'effective' access regime has been an issue put to the Council in respect of two recent applications for certification. Submissions were made in respect of the Queensland Rail Access Regime that for a regime to be effective it must include the formal elements prescribed by the clause 6 principles and must also function to meet the objects of Part IIIA. In this respect, it was noted that where the rail infrastructure was operated by a vertically integrated service provider, the regime must constrain that service provider from treating its downstream business differently to its rival third party operators (NCC 2010a). A similar submission was made in respect of the certification application for the Western Australian Rail Access Regime, where it was put to the Council that effectiveness needed to be applied broadly and considered in the context of the particular market and industry structures and conditions that exist (NCC 2010d). In essence, these submissions demanded vertical disaggregation as a precondition to certification. In responding to such submissions, the Council took the view that vertical disaggregation was not required in order to meet the clause 6 principles and such a requirement would set a bar to certification that is too high. These issues are examined further below in respect of specific clause 6 principles and the objects clause.

### **The duration of any certification**

2.38 If the Council recommends the certification of an access regime then it must also recommend to the Commonwealth Minister how long that certification should be in force (s 44M(5)). A certification remains in force for the duration specified in the Commonwealth Minister's decision unless the relevant state or territory ceases to be a party to the CPA. There is no mechanism in the CCA for revocation or early termination of a certification.

2.39 Where an access regime has been certified as an effective access regime, in considering any application for the declaration of a service to which the regime applies the Council is bound to follow that certification and must not recommend declaration, unless it believes there have been substantial modifications to the access regime or the clause 6 principles since the regime was certified (s 44G(2)(e)(ii)). Similarly a decision making Minister may not declare a service that is subject to a certified state or territory regime unless he or she considers there have been substantial modifications to the access regime or to the clause 6 principles since the regime was certified (s 44H(4)(e)(ii)).

2.40 Applicants for certification should outline (with supporting rationale) what they consider to be the appropriate period of any certification.

### **Transitional arrangements**

2.41 A number of access regimes submitted for certification have included transitional arrangements that constrain the operation of the regime in some way. These constraints can have implications for the effectiveness of the regime.

- 2.42 Transitional arrangements may include timetables to phase in the availability of access for different classes of customer. Such transitional arrangements can provide a breathing space to help parties adjust to a competitive market. Conversely, they create delays in the commencement of competitive arrangements and may impose price penalties on consumers who would otherwise be contestable (eligible to seek access) at an earlier stage. For this reason, while an effective regime may incorporate transitional arrangements in response to demonstrated public policy issues, the arrangements should be necessary and phased out as soon as possible.
- 2.43 Under the then National Gas Code (which has been replaced by Chapter 3 of the National Gas Law), for example, contestability for different classes of customer was phased in over several years. The policy objective was to allow for contestability issues (such as household metering) to be resolved and for cross-subsidies among customer groups to be unwound. Governments argued that a staged reduction of cross-subsidies would cushion price shocks that might otherwise have a negative impact on markets and create social policy concerns (NCC 1997a, p 32; 2001b, pp 7.7–7.9).
- 2.44 In considering transitional arrangements, the Council assesses whether the arrangements derogate from the effectiveness of the regime, such that the clause 6 principles are not satisfied. In determining this the Council may need to consider the following:
- the effects of the transitional arrangements on the operation of the access regime, including the effects on regulatory processes and dispute resolution, and the ramifications for compliance with the clause 6 principles and objects of the access regime
  - the effects of the transitional arrangements on competitive outcomes in dependent upstream and downstream markets
  - the length of time for which the transitional arrangements will be in place
  - public policy matters such as sovereign risk issues.
- 2.45 In the case of the Queensland Access Regime for Gas Pipelines, the Council was unable to recommend certification because the transitional provisions raised concerns in relation to the clause 6 principles (NCC 2000b and 2002a). By contrast the Council found that transitional provisions contained in Victoria’s gas access regime were not unduly lengthy and did not derogate from the effectiveness of the regime and, therefore, were consistent with the clause 6 principles (NCC 2000c).

### **Regime changes while the Council considers an application**

- 2.46 On occasion, regimes have been amended or undertakings have been made to amend a regime between the time of application for certification of the regime and the time the Council issued its final recommendation to the Commonwealth Minister. While it is preferable that a regime be finalised (and operational) prior to an application for certification being made the Council recognises that there may be instances where

changes to a regime are advantageous or necessary and should be recognised by the Council in providing its recommendation.

- 2.47 For example, after making the application for certification of the Queensland Rail Access Regime, the Queensland Government amended the applicable legislation. In this instance, the Council considered the amendments addressed a potential deficiency in the regime concerning its coverage and inclusion of new services. Importantly, these changes were enacted prior to the issue of the draft recommendation and as such were able to be considered by interested parties in the second round of public consultation undertaken by the Council (NCC 2010a).
- 2.48 In the case of the South Australian Rail Access Regime, the Council was concerned that that the regime did not provide for a mechanism to review the coverage of the Regime and considered in its draft recommendation that the period of any certification should therefore be limited to five years, rather than the 10 years sought by the applicant. The South Australian Government responded to that concern by undertaking to amend the *Railways (Operations and Access) Act 1997 (SA)* to provide for five yearly review of the railway services covered by the regime. In making its final recommendation, the Council recognised that there was a risk that the proposed amendments would not be delivered by the South Australian parliamentary process, but considered the risk to be small and accordingly took into account the undertaking to amend the legislation, recommending to the Commonwealth Minister that the regime be certified for a period of 10 years as sought by the applicant (NCC 2010c).

## Greenfields investments

- 2.49 The Council considers that access regulation should not inappropriately deter investment in infrastructure. New investment projects that are (or potentially are) subject to access regulation commonly have long asset lives, and estimates of revenue over the life of the asset may be uncertain. An objective of access regulation is to reduce the scope for service providers to appropriate monopoly rent but also important is provision for returns to investment to appropriately reflect risk.
- 2.50 In the case of the Northern Territory/South Australian Rail Regime, which applies to the Darwin–Tarcoola rail line, the Council considered the implications of access regulation for the project’s viability. The Council approved a framework, under independent regulatory supervision, that it considered to be sufficiently flexible to account for the risk factors inherent in a greenfields investment.
- 2.51 The Council was satisfied that the framework was sufficiently flexible to adapt to significant changes in the market environment. Accordingly, the Council supported the applicant’s request to recommend certification for a relatively long period (30 years). The applicant governments argued that the 30-year period was required so that appropriate debt financing instruments could be put in place (NCC 2000a).
- 2.52 Chapter 5 of the National Gas Law and Part 13 of the National Gas Rules provide for a binding no-coverage determination and/or a price regulation exemption for greenfields pipelines. Pipelines granted a ‘binding no coverage determination’ cannot

be declared under Part IIIA of the CCA. The Council is required to disregard any such arrangements when considering the certification of any state or territory gas access regime.

- 2.53 The National Gas Law and Rules provide for the Council to assess applications for a binding no-coverage determination or a price regulation exemption using an open and transparent process that is consistent with the process for assessing applications for coverage of pipelines. Applications for a price regulation exemption for an international pipeline may, however, be subject to expedited decision-making processes in cases where the Minister has already decided against a binding no-coverage determination for the pipeline. The Council's role under the National Gas Law is the subject of a separate guide.
- 2.54 The TPA Amendment Act inserted a new division, Division 2AA, into Part IIIA which provides for services to be made ineligible to be declared. Similar to the provisions in the National Gas Law for a binding no coverage determination for greenfields pipelines, Division 2AA provides that a person with a material interest in a proposed new infrastructure facility may apply to the Council for a service provided by the proposed facility to be ineligible to be a declared service. For a proposed service to be ineligible, it must not satisfy at least one of the criteria for declaration in s 44G(2) of the CCA and be provided by the proposed facility once constructed. Applications for an ineligibility recommendation will be assessed by the Council in an open and transparent process. Should a service be made ineligible to be declared, such a decision will remain in force for a period of at least 20 years.



### 3 Assessment in terms of the clause 6 principles

#### Clause 6(3): significant infrastructure

For a State or Territory regime to conform to the principles set out in this clause, it should:

- (a) apply to services provided by means of significant infrastructure facilities where:
  - (i) it would not be economically feasible to duplicate the facility;
  - (ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market; and
  - (iii) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist; and
- (b) reasonably incorporate each of the principles referred to in subclause (4) and (except for an access regime for: electricity or gas that is developed in accordance with the Australian Energy Market Agreement; or the Tarcoola to Darwin railway) subclause (5).

There may be a range of approaches available to a State or Territory Party to incorporate each principle. Provided the approach adopted in a State or Territory access regime represents a reasonable approach to the incorporation of a principle in subclause (4) or (5), the regime can be taken to have reasonably incorporated that principle for the purposes of paragraph (b).

- 3.1 Clause 6(3)(a) sets out threshold effectiveness principles, which require that the coverage of an access regime be limited to a narrow range of services—those that open up ‘bottlenecks’ to competition and thereby unlock the potential benefits that competition in dependent markets may bring, in particular, the economic efficiency benefits likely to flow to users and to the community more generally.
- 3.2 To demonstrate that an access regime meets the clause 6(3)(a) principles it is necessary to:
  - define the service(s) covered by the access regime, and
  - demonstrate that the access regime applies only to the services of a significant infrastructure facility in the circumstances described in clause 6(3)(a).

#### Defining the service(s)

- 3.3 A clear and precise definition of the service(s) and/or proposed service(s) that an access regime covers is essential to ensuring that the regime applies only to services for which access is necessary to promote competition in upstream or downstream markets. In particular, an effective access regime should:

- describe the type of service(s) and/or proposed service(s) that it covers—for example, the transportation of gas within a gas pipeline, and
  - nominate the particular service(s) that it covers (or excludes)—for example, the gas transportation services of a nominated gas pipeline (or several nominated pipelines).
- 3.4 For the sake of administrative efficiency and to promote greater certainty, an access regime is usually designed to accommodate changes over time (additions or deletions) to the services nominated to be covered. A gas access regime, for example, may be designed to cover the service(s) of a newly constructed pipeline or of extensions to existing pipelines. To be part of an effective access regime such arrangements should be consistent with the clause 6 principles. This means that the regime should include:
- criteria for determining the service(s) or proposed service(s) that can be covered or excluded from the regime—for example, the pipeline coverage criteria under the National Gas Law, and
  - rigorous and independent processes, at the appropriate time, for assessing proposals for changes to the coverage status of service(s).
- 3.5 The Council approved a coverage mechanism of this kind in respect of the then National Gas Code.<sup>7</sup> Similarly, the Western Australian Electricity Networks Access Regime has a coverage mechanism that closely reflects the clause 6(3)(a) principles (NCC 2005). The Council has also approved regimes that adopt a coverage mechanism akin to the declaration criteria in Part IIIA, such as the Queensland Rail Access Regime (NCC 2010a).
- 3.6 In some cases, an access regime expressly excludes certain services, such as where the facility providing the excluded service is considered economically feasible to duplicate or where it has different and distinct ownership from the facility providing the covered services. The exclusion of a service from an access regime may raise certification issues if the omission poses a barrier to access, such that the clause 6 principles are not satisfied. This would be the case if, for example, the excluded service is integral to accessing the services covered by the regime.

### **Significant infrastructure facility**

- 3.7 To meet the clause 6(3)(a) principles, an access regime should apply only to the service(s) and/or proposed service(s) of a significant infrastructure facility(ies) where:
- duplication of the facility is not economically feasible (clause 6(3)(a)(i)). This principle is usually tested by considering whether, over the likely range of reasonably foreseeable demand for the service(s) covered by the regime, it would be more efficient, in terms of costs and benefits to the community as

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<sup>7</sup> The relevant provisions appear at Chapter 3 of the National Gas Law.

a whole, for the facility to provide those services than for two or more facilities to do so.<sup>8</sup>

- access is necessary to permit effective competition in an upstream or downstream market (clause 6(3)(a)(ii)). This principle is satisfied where the regulation of access by the regime will improve the conditions or environment for effective competition in a dependent market or markets. Whether the conditions for competition will be enhanced depends on whether, in the absence of the regime, the service provider has the ability and incentive to exercise monopoly power to adversely affect competition in a dependent market or markets.
- safe use of the facility by an access seeker is economically feasible and subject to appropriate regulatory arrangements (clause 6(3)(a)(iii)). This principle provides that third party access should not be required where it would pose a safety concern that appropriate regulation cannot address at an economically feasible cost.

3.8 In essence, the clause 6(3)(a) principles refer primarily to the services of significant infrastructure, that cannot be economically duplicated and that occupy a strategic position in the service delivery chain whereby access is essential for effective competition in a dependent market or markets.

### **Consistency with the declaration criteria**

3.9 The clause 6(3)(a) principles are similar to the declaration criteria (a)–(c) under s 44G(2) of the CCA though there are slight differences in the way that the principles and the declaration criteria are expressed. Given that certification of an access regime effectively displaces the opportunity for declaration of the service(s) covered by the access regime, the Council considers it appropriate to interpret the clause 6(3)(a) principles as far as possible in a manner consistent with the declaration criteria (despite the slight differences in expression). This approach is consistent with the objective of the certification process, which is to determine whether the state or territory access regime is an effective alternative to declaring (under Part IIIA of the CCA) the services covered by the regime. Moreover, s 44DA of the CCA expressly states that the clause 6 principles are to be treated as guidelines rather than binding rules.

3.10 In practice there is little that distinguishes terms such as ‘access’ versus ‘increased access’ and ‘effective competition’ versus ‘material increase in competition’ and ‘economically feasible’ as compared to ‘uneconomical for anyone’. The Council

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<sup>8</sup> The Council notes that this approach may be in doubt following the decision of the Full Federal Court in *Pilbara Infrastructure Pty Ltd v Australian Competition Tribunal* (2011) 277 ALR 282; [2011] FCAFC 58. A further update may be made in this regard depending on the outcome of current applications for special leave to appeal this decision to the High Court.

considers that the amendment of the then TPA in 2006 to add the term ‘material’ to declaration criterion (a) serves to clarify the interpretation of criterion (a) and as such does not create an inconsistency between the certification principles and the declaration criteria.

3.11 In applying clause 6(3)(a), the Council applies the same definitions (for terms such as ‘service’) as it applies in declaration matters. Similarly, the Council’s approach to matters such as the definition of ‘service’ and ‘facility’ and market definition is consistent with its approach in declaration matters. The declaration guide details the Council’s approach to interpreting the declaration criteria under Part IIIA of the CCA.

3.12 Table 3-1 sets out each element of clause 6(3)(a) and the corresponding Part IIIA declaration criterion.

**Table 3-1 The clause 6(3)(a) principles and related declaration criteria**

Clause 6(3)(a) principles	Related declaration criteria—CCA, ss 44G(2) and 44H(4)
(a) significant infrastructure facility	(c) the facility is of national significance, having regard to:  (i) the size of the facility; or  (ii) the importance of the facility to constitutional trade or commerce; or  (iii) the importance of the facility to the national economy.
(i) it would not be economically feasible to duplicate the facility	(b) it would be uneconomical for anyone to develop another facility to provide the service
(ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market	(a) access (or increased access) to the service would promote a material increase in competition in at least one market ..., other than the market for the service

3.13 While the Council approaches clause 6(3)(a) and the related declaration criteria as far as possible in a consistent manner, it notes the following distinctions.

- Under clause 6(3)(a), services subject to an effective regime should be provided by significant infrastructure facilities. The term ‘significant’ imposes a lower threshold than that imposed by the term ‘national significance’ in declaration criterion (c). For the purposes of declaration, national significance is related to size, importance to constitutional trade or commerce, or importance to the national economy. The Council’s approach is to relate ‘significant’ as used in clause 6(3)(a) to similar factors, but from a state-wide or regional perspective (NCC 1997a, pp 13–14).
- There are some differences between the terminology used for certification matters and that used for declaration matters. Under clause 6(3)(a)(i), for example, services subject to an effective access regime should be provided by a facility that ‘it would not be economically feasible to duplicate’. By

contrast, declaration criterion (b) requires that ‘it would be uneconomical for anyone to develop another facility to provide the service’. Although the terms ‘duplicate’ and ‘develop’ are distinct, the Council considers it appropriate to interpret the tests in the same way.

- The clause 6(3)(a) principles do not include an explicit public interest assessment as provided for under declaration criterion (f) (s 44G(2)(f) of the CCA). While regulation that seeks to promote economic efficiency will generally be in the public interest, the generic nature of Part IIIA means that public interest considerations need to be assessed on a case-by-case basis. State and territory governments, however, can consider the public interest effects of implementing an access regime for a particular industry as part of regulatory impact assessment processes.
- Clause 6(3)(a)(iii) raises the issue of the appropriateness of safety regulations. (Prior to 14 July 2010, the criteria for declaration included a requirement that access to a service can be provided without undue risk to human health or safety. This requirement was removed by the TPA Amendment Act.) Where safety regulations are required, they should be no more stringent than is necessary to satisfy legitimate safety considerations. The Council may consider that certification issues arise if safety regulations impose an unnecessary barrier to entry into a market (see paragraph 3.41).

### **Clauses 6(4)(a)–(c): negotiated access**

- (a) Wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the person seeking access.
- (b) Where such agreement cannot be reached, Governments should establish a right for persons to negotiate access to a service provided by means of a facility.
- (c) Any right to negotiate access should provide for an enforcement process.

3.14 The Council considers clauses 6(4)(a)–(c) together, because they relate to negotiations for third party access to a service.

3.15 Clause 6(4)(a) establishes commercial negotiation as a cornerstone in determining access outcomes. Commercial negotiation allows parties to try to reach mutually beneficial agreements.

3.16 Clauses 6(4)(b) and (c) complement and underpin the principle in clause 6(4)(a). They recognise that regulatory measures can provide an incentive to reach commercially agreed outcomes and also provide a means for dealing with situations where access providers and access seekers are unable to reach agreement.

3.17 Together clauses 6(4)(a)–(c) seek to ensure that access regimes provide an appropriate balance between commercial negotiation and regulatory intervention to facilitate access negotiations. An appropriate balance means that regulatory

arrangements support the achievement of negotiated outcomes. Therefore regulatory arrangements should not preclude negotiated outcomes.

### **Guidance on terms and conditions**

- 3.18 The Council considers that a proper consideration of clauses 6(4)(a)–(c) must include an assessment of whether regulatory arrangements establish an environment in which third parties can enter effective access negotiations. The clause 6 principles do not provide specific guidance on determining the appropriate level of intervention. Rather they provide for a range of outcomes from establishing an enforceable right of access with no further guidance (as is the case with declaration) to underpinning the right of access with regulated minimum terms and conditions. As a general principle, however, efficient outcomes are achieved by ensuring regulatory responses are proportionate to the problem. This requires consideration of the difference in the bargaining power of the service provider and users (including potential users) and the extent of information asymmetries.
- 3.19 In assessing the appropriateness of the guidance provided by an access regime the Council also has regard to the objects of the access regime, including the objects principle specified in clause 6(5)(a), where relevant, and the objects of Part IIIA.
- 3.20 The Council recognises that some regulatory intervention may be warranted to create an environment conducive to effective negotiations in accordance with the principles in clauses 6(4)(a)–(c). Such intervention may be appropriate, for example, in industries where third parties lack sufficient information and bargaining strength to negotiate reasonable terms and conditions, and where credible pricing structures may emerge only through lengthy and potentially costly arbitrations.
- 3.21 Regulatory processes can be used to address information asymmetries to some degree and give third parties a workable platform from which to enter negotiations. In the absence of such measures, an access regime may establish a theoretical right to negotiate yet leave third parties in a position of negotiating blindly with a monopoly provider or being offered potentially inappropriate prices (for example, prices that include monopoly rents) on a ‘take it or leave it’ basis. The latter scenario may amount to a denial of access, and cannot be viewed as satisfying clauses 6(4)(a)–(c).
- 3.22 Addressing information asymmetry often requires some means for providing guidance to market participants, such as a process through which third party access seekers can obtain information necessary for effective negotiation on the terms and conditions of access, together with safeguards for the provision of commercially sensitive information.

### **Independent and transparent regulation**

- 3.23 In order for regulatory intervention to be effective in promoting commercially driven outcomes access providers and access seekers must have confidence in regulatory processes.

- 3.24 The Council considers that independent, transparent and consultative regulatory processes for setting or determining the method for setting appropriate terms and conditions of access, particularly those relating to price or price boundaries are critical to the effectiveness of an access regime. Regulators that make impartial and objective decisions are critical to engendering confidence in regulatory processes. In addition, governments should ensure that regulators have sufficient resources to fulfil their duties in a competent and timely fashion.
- 3.25 Where third parties are not confident of regulatory guidance, that guidance will not facilitate effective negotiations. Unless independent processes can vet the veracity of price and other information, that information may be misleading or biased in favour of particular interests. Perceptions of bias would taint regulatory guidance, which would run counter to the rationale of addressing market power and information asymmetries to facilitate effective negotiations.
- 3.26 Independence can be achieved by vesting regulatory powers in a single independent body or by implementing a suite of independent processes. In the access regimes considered to date, the approach most often used has been to establish a single independent body: a regulator vested with the appropriate powers.
- 3.27 The essential criterion for an independent regulator is an ‘arms length’ separation from facility owners, current users, access seekers, governments and other stakeholders. Such independence needs to be guaranteed by legislation. The Council regards this degree of independence as necessary to avoid the reality or perception of conflict of interest and thus engender confidence that regulatory guidance is free from bias.
- 3.28 In general terms, the Council does not consider government Ministers or departments to be independent for the purpose of access regulation, given the potential for conflicts of interest (see NCC 2002a).
- 3.29 Independence also requires that regulatory bodies be equipped with the necessary powers to undertake their duties effectively. In particular, regulators should be:
- allocated sufficient resources to undertake their duties effectively. Adequate funding engenders public confidence in regulatory processes
  - equipped with adequate information gathering powers to obtain information that is necessary to undertake regulatory duties. This is consistent with clause 6(4)(o) of the CPA which provides that the relevant authority should have access to financial statements and other accounting information pertaining to a service.
- 3.30 In some cases, jurisdictions have conferred regulatory responsibilities across a number of industries on a generic economic regulator, such as the ACCC or the Independent Pricing and Regulatory Tribunal of New South Wales (IPART). In other cases, an industry-specific regulator has been established. (At the time the Council considered the New South Wales Rail Regime, no economic regulator had been established; rather, IPART had a number of specific regulatory tasks (NCC 1999b)).

3.31 The Council has found that the following bodies are independent and sufficiently resourced to properly carry out tasks in the context of access regulation:

- the ACCC
- the Australian Energy Market Commission
- the Australian Energy Regulator (AER)
- IPART of New South Wales
- the Essential Services Commission (ESC) of Victoria
- the Queensland Competition Authority (QCA)
- the Economic Regulation Authority (ERA) of Western Australia
- the Essential Services Commission of South Australia (ESCOSA)
- the Office of the Tasmanian Economic Regulator (OTTER)
- the Independent Competition and Regulatory Commission (ICRC) of the Australian Capital Territory, and
- the Northern Territory Utilities Commission.

3.32 Transparency is equally critical in engendering market confidence in regulatory guidance to third parties to facilitate effective negotiations. Public consultation with high levels of disclosure is an appropriate way of making regulatory processes transparent, as in the following cases:

- the then National Gas Code, which required the regulator to conduct open and transparent public processes regarding a proposed access undertaking, including in setting benchmark terms and conditions of access, and
- the Western Australian Rail Access Regime, which requires the regulator (the ERA) to conduct open and transparent public processes in setting ring fencing arrangements, a range of cost and pricing parameters, and other terms and conditions of access.

### **Price guidance**

3.33 The Council considers that developing terms of access (including price guidance) through an independent, transparent and effective regulatory process can satisfy clauses 6(4)(a)–(c). Where an access regime constrains the access terms and conditions on which the dispute resolution body can arbitrate, the Council considers that an effective access regime must include a consideration of clause 6(4)(i) and, where relevant, clause 6(5) matters as part of the regulatory process. Clause 6(5) does not apply to an access regime for electricity or gas that is developed in accordance with the Australian Energy Market Agreement or the access regime for the Tarcoola to Darwin railway. However, access regimes for electricity and gas developed in accordance with the Australian Energy Market Agreement include provisions consistent with clause 6(5).

3.34 The clause 6 principles are written from the perspective of a negotiate/arbitrate model. Clause 6(4)(i), which sets out considerations in determining terms and

conditions of access, expressly states that the dispute resolution body should take into account those matters listed in clause 6(4)(i). In many access regimes, however, the regulator has at least part responsibility for ensuring access terms and conditions meet the clause 6(4)(i) requirements. Where this occurs the regulator should be required to have regard to the clause 6(4)(i) requirements.

- 3.35 Clause 6 of the CPA specifies pricing principles: these provide guidance on appropriate pricing outcomes, recognising that industry specific access regimes often regulate terms and conditions of access. In particular, clause 6(5)(b) provides that access prices should encourage efficiency and productivity improvements, which includes allowing the service provider to earn a return sufficient to cover expected efficient costs plus a return on investment taking account of the risks involved. Such an approach to pricing is consistent with clause 6(4)(i), which provides that terms and conditions should strike a balance among a range of factors, including the legitimate business interests of the access provider, the interests of other parties, the efficient use of infrastructure and the public benefits arising from competitive markets.
- 3.36 The Council considers that the clauses 6(4)(a)–(c) model of commercial negotiation, supported by the regulatory guidance in clauses 6(4)(i) and 6(5), seek to deliver outcomes that mirror, as closely as possible, those that would be derived in an effectively competitive market—that is, outcomes that can generally be expected to lie within an efficient range.
- 3.37 Clause 6(3A)(a) provides that the Council, in assessing whether a state or territory access regime is an effective access regime, should not consider the outcome of any arbitration, or any decision, made under that access regime. The Council considers if the regime provides for independent, transparent and consultative regulatory processes by a regulatory body that is both independent and sufficiently resourced to carry out their functions, then the Council does not need to consider the outcomes of specific decisions made by that regulator under the regime.

### **Guidance on other terms and conditions of access**

- 3.38 Negotiation of access is not limited to pricing issues. Other elements of an access agreement that may require negotiation include:
- safety requirements
  - the allocation of capacity among competing users
  - interoperability issues, and
  - service quality issues.
- 3.39 In some cases, these matters may be as or more important to access seekers than price.

*Safety requirements*

- 3.40 It is appropriate for a state or territory government to determine whether and how to regulate the safe provision of services, but not to regulate safety in a manner that poses unnecessary barriers to access and competition.
- 3.41 In assessing whether a safety restriction imposes unnecessary barriers to access and competition, the Council considers, among other factors, whether the restriction has been appropriately reviewed<sup>9</sup> and found to confer a net public benefit (and whether alternative approaches to achieve the objective have been considered).
- 3.42 It is inappropriate for an access provider to establish additional safety requirements that impose an unreasonable barrier to access, as with requirements that duplicate matters covered by government regulation.
- 3.43 The issue of safety requirements acting as barriers to access has been raised with the Council in the context of a number of rail access regimes. While a significant matter has been the duplication of safety accreditation procedures across jurisdictions (NCC 1999a, pp 52–55; 1999b, pp 7–10), model rail safety reform legislation now implemented in all state jurisdictions provides a nationally consistent legislative framework for rail safety. Among other things, the framework aims to promote greater harmonisation of safety regulations and reduce the potential for safety requirements being used to impede the operation of economic regulation.

*Allocation of capacity among competing users*

- 3.44 The resolution of capacity issues is a critical matter in the negotiation of access to services.
- 3.45 In rail, for example, capacity issues are closely linked to train path allocation (that is, the timetabling of the use of various sections of rail track) and network management principles. Access seekers need to negotiate a suitable train path, day-to-day network management and mechanisms for reallocating unused train paths.
- 3.46 Transparent mechanisms that are open to independent scrutiny are needed to assure market participants that capacity issues are resolved in a manner that promotes competitive outcomes. Such an approach is especially important if the access provider also operates a vertically affiliated entity. An integrated rail service provider, for example, may have an incentive to favour its affiliated downstream freight and passenger transport services to the detriment of other competitors in matters such as capacity and train path management. Train path principles should facilitate efficient use and be competitively neutral to all market participants.
- 3.47 For example, in the then National Gas Code, pipeline capacity issues were addressed through queuing and expansion policies, and capacity trading mechanisms. In

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<sup>9</sup> An appropriate legislative review includes those conducted in a manner consistent with the requirements of clause 5 of the CPA.

addition, arbitration provisions allowed an arbitrator to require a geographic extension or an expansion of capacity to meet the needs of access seekers.

#### *Interoperability issues*

3.48 Interoperability issues may arise in access negotiations as a result of potential problems associated with:

- the interconnection of discrete geographic networks
- the relationship between the provision of a service and the use of that service.

3.49 Third party access regulation may need to address or at least recognise these sorts of problems.

3.50 Clauses 6(2) and 6(4)(p) specifically address interstate interconnection issues. The objects of Part IIIA of the CCA include the provision of a framework and guiding principles that encourage a consistent approach to access regulation in each industry (s 44AA of the CCA).

3.51 Issues regarding the interconnection of discrete geographic networks may arise entirely within a particular jurisdiction. Negotiations between access seekers and infrastructure owners may relate to:

- the interconnection of infrastructure
- the need for common or compatible operating procedures
- the terms and conditions for joint use.

3.52 In addition, interoperability issues can arise in the relationship between infrastructure and the use of the infrastructure. Different uses of the same facility can involve different operating requirements and different costs. Some train rolling stock configurations, for example, involve greater track wear than do others. The regulatory framework needs to recognise these issues.

#### **Service quality issues**

3.53 Price and service quality are seen as interdependent in the negotiation of access to certain services. The issue arises in rail, in particular, where quality of service can vary considerably. An effective rail access regime may need to ensure that contracts set performance indicators to establish the service provider's accountability, covering matters such as entry and exit times, track quality and speed restrictions.

#### *Enforcement provisions*

3.54 Under clause 6(4)(c), an effective access regime must have credible enforcement mechanisms. It may be appropriate for some provisions to be enforceable through arbitration or through regulation.

3.55 For serious breaches, such as hindering or obstructing the regulator or breaching accounting separation requirements, enforcement may include:

- an effective penalty regime—for example, the Western Australian Electricity Networks Access Regime allows for penalties of around \$100 000
- the regulator and/or an aggrieved party being able to seek an injunction to stop the breach.

3.56 Other remedies, such as criminal sanctions and civil damages, should be considered where appropriate.

### **Clause 6(4)(d): regular review**

Any right to negotiate access should include a date after which the right would lapse unless reviewed and subsequently extended; however, existing contractual rights and obligations should not be automatically revoked.

- 3.57 The Council interprets the clause 6(4)(d) principle to mean that an access regime should include periodic reviews to assess whether regulation need cover a particular service and/or facility. This principle recognises that markets change and evolve over time, which can affect the efficiency and effectiveness of regulation. It may not be economically feasible to duplicate a facility at present (and thus may warrant an access regime), yet with time technology may improve, thereby removing the need for access regulation.
- 3.58 An effective regime should mandate appropriate review requirements. It should also ensure reviews are conducted in an independent, open and transparent manner consistent with best practice regulatory processes.
- 3.59 One approach is for the access regime to include a schedule for reviews. A number of rail access regimes use this approach, which the Council found met the clause 6(4)(d) principle (see, for example, NCC 1999a, pp 59–61).
- 3.60 Alternatively, because the Council considers that the review requirements relate to coverage of particular services and the assessment of the scope of coverage, clause 6(4)(d) could be satisfied, for example, by incorporating in the regime:
- the clause 6(3)(a) principle in the making of coverage decisions
  - an independent, transparent and effectual means for revoking or reviewing coverage decisions.
- 3.61 The Council found, for example, that the revocation provisions in the then National Gas Code satisfied clause 6(4)(d) (NCC 1997b, pp 13–14). Similarly, in respect of the Western Australian Electricity Networks Access Regime, the Council found that the clause 6(4)(d) principle was satisfied by a requirement in the regime that access arrangements approved under the regime must include a date for review and may specify trigger events for a review, with the period between reviews to be 5 years unless a longer period is approved by the regulator.
- 3.62 Clause 6(4)(d) makes clear that a review of access regulation should not override commercially determined outcomes by automatically revoking any existing

contractual rights. This does not mean that they could not be revoked, but rather that some process (such as a review) would first need to be undertaken.

- 3.63 This principle recognises a legitimate need to maintain commercial certainty for infrastructure operators and users. It also recognises that foundation users, whose commitments underpin new infrastructure development, bear greater risks than those of businesses that decide to use the infrastructure after it has been built. Any review of existing contractual rights and obligations should consider these contexts.

### **Clause 6(4)(e): reasonable endeavours**

The owner of a facility that is used to provide a service should use all reasonable endeavours to accommodate the requirements of persons seeking access.

- 3.64 Clause 6(4)(e) requires that the service provider of a covered network use all reasonable endeavours to accommodate the requirements of access seekers. The Council considers that an access regime may either incorporate clause 6(4)(e) explicitly, or through general provisions that have the same effect. Access regimes considered to date that have underpinned this principle have required the service provider to:

- provide access seekers with written information on spare capacity and indicative access terms and conditions, including sufficient information for access seekers to understand the derivation of access prices or tariffs
- respond to access requests and negotiate terms and conditions within a reasonable timeframe
- provide a written explanation as to why a particular request for access cannot be accommodated, including likely prospects for future access
- use all reasonable endeavours to accommodate a person's request for access to spare capacity.

- 3.65 Thus to date the question of what constitutes 'reasonable endeavours' has largely been interpreted as relating to information disclosure, availability (for negotiation) and response times. Among these factors the nature and extent of information disclosure has generally been the most contentious issue that stakeholders have raised under clause 6(4)(e).

- 3.66 The Council considers that an access regime should ensure sufficient information is disclosed to enable the access seeker to make informed decisions—so as to facilitate effective negotiation. On the other hand, information disclosure requirements should not be so onerous as to impose unnecessary costs on service providers or unduly harm their business (see paragraphs 3.18–3.22). Care also needs to be taken to protect confidential or sensitive information. Where confidentiality issues arise information disclosure on a limited basis may be sufficient to satisfy clause 6(4)(e). Failure to recognise the interests of the service provider may mean that clause 6(4)(e)

is not satisfied particularly where information disclosure requirements have the potential to undermine confidence and/or affect investment.

- 3.67 This need to balance the interests of the access seeker and the access provider is reflected in the Council's assessment of the then National Gas Code in 1997. In relation to clause 6(4)(e) the Council stated that:

... information disclosure must be sufficient to facilitate market assessments and fair and reasonable regulatory outcomes—especially given that the regulator approved reference tariffs cannot be reassessed in arbitration. At the same time, the information disclosure provisions should not be used as a device to unduly harm the service provider's competitive position in the market, which could undermine investment in gas infrastructure and potential access to spare capacity. (NCC 1997b, p 36)

- 3.68 In the context of assessing South Australia's application for certification of its gas access regime the Council considered that the then National Gas Code achieved an appropriate balance with regard to information disclosure, and satisfied clause 6(4)(e). The Commonwealth Minister for Financial Services and Regulation accepted the Council's recommendations and certified the regime in December 1998.
- 3.69 Under s 5 of the then National Gas Code, the service provider had to establish an information package for each covered pipeline providing standard access arrangements, relevant information on each covered pipeline, including capacity and information to understand the derivation of tariffs. The regulator was able to direct additional information to be included where it considered the information would assist potential users to decide whether or not to seek access and to determine how to go about seeking access. The service provider was obliged to provide the package within 14 days of receiving a request.
- 3.70 In the case of rail, the issue of information disclosure to enable effective access is critical. Under the rail access regimes that the Council has considered, rail track operators have been required to disclose information relating to track use timetabling, network congestion management and network priority, in addition to pricing information (see NCC 1999a–b and 2000a).
- 3.71 Similarly, in respect of the Western Australian Electricity Networks Access Regime the Council found that clause 6(4)(e) was satisfied where the regime requires that the access arrangement information for a network must include sufficient information to enable prospective users and the regulator to understand the derivation of the elements in the access arrangement, including the reference tariff. The relevant information includes access pricing principles, capital costs, system capacity and key performance indicators (NCC 2005).

## Clause 6(4)(f): negotiated access

Access to a service for persons seeking access need not be on exactly the same terms and conditions.

- 3.72 The Council considers that this clause removes any doubt that access may be provided on different terms and conditions to different users. Such an approach is consistent with the principles of commercial negotiation enshrined in clause 6.
- 3.73 An access regime should not limit the scope for commercial negotiation. Rather, the terms and conditions set out in access arrangements should facilitate commercial negotiations and act as a safety net when a reasonable outcome cannot be negotiated.
- 3.74 Commercially negotiated outcomes will often result in different terms and conditions even for the same service. There can be many reasons for this including differences in bargaining skills, experience and the differences in the costs and risks associated with providing access to different users.
- 3.75 While clause 6(4)(f) may permit service providers to vary terms and conditions, including prices offered to users, it does not entitle a vertically integrated service provider to set the terms and conditions of access to the bottleneck facility in a manner designed to unfairly favour an affiliated upstream or downstream entity. In such cases, the Council considers whether the access regime contains effective mechanisms to ensure competitively neutral treatment of affiliated entities. Clause 6(4)(m), which deals with ring fencing and competitive neutrality, further addresses this issue (see page 63). Clause 6(5)(b) also deals with pricing matters, and, where relevant, recognises that regulated access prices should allow price discrimination where it aids efficiency (see paragraphs 3.223–3.224).

## Clause 6(4)(g): independent dispute resolution

Where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.

- 3.76 The clause 6 principles recognise the need for an independent arbitration mechanism to complement and encourage genuine negotiations. Clause 6(4)(g) requires an access regime to contain a mechanism to ensure that parties to a dispute have recourse to an independent dispute resolution body. That body should meet the same standards of independence as required of regulatory bodies (refer to paragraphs 3.23–3.32).

### Appointment of dispute resolution body

- 3.77 The clause 6 principles seek to encourage commercial negotiation for determining access outcomes. This includes the parties to a dispute being able to agree on an independent body to resolve disputes.

- 3.78 On occasion parties to a dispute will reach an impasse. This includes the circumstance where they cannot agree on the appointment of the dispute resolution body. An effective access regime should therefore contain a formal mechanism for appointing an independent body to resolve disputes.
- 3.79 One approach would be for the regime to specify an independent body that could resolve disputes. The Western Australian Electricity Networks Access Regime, for example, allows parties to refer a dispute to the regulator. The regulator may conciliate the dispute or may refer the dispute to the Western Australian Gas Disputes Arbitrator (NCC 2005).
- 3.80 An alternative approach is for the access regime to provide for an independent person to appoint an independent arbitrator (perhaps from a panel of arbitrators). Under the Western Australian Rail Access Regime, for example, the regulator appoints an arbitrator from a panel that is pre-selected by the regulator and the Chairman of the Western Australian Chapter of the Australian Institute of Arbitrators (NCC 2010d). Similarly, the South Australian Ports Access Regime provides that a dispute may first be referred to ESCOSA for conciliation. If the dispute is not resolved through conciliation or within 6 months of referral then ESCOSA may refer the dispute to arbitration, to be arbitrated by a person or persons who is independent of the disputing parties and not subject to control or direction of the South Australian Government (NCC 2010b).

### **Funding arrangements**

- 3.81 Clause 6(4)(g) provides that an effective access regime should require the parties to a dispute to fund some or all of the costs of having an independent body resolve the dispute. At the same time, the Council is mindful that the costs of arbitration should not deter parties from seeking access.
- 3.82 Under the Western Australian Electricity Networks Access Regime, for example, the arbitrator has discretion on the allocation of costs. In its application the Western Australian Government stated that this approach provides an incentive for parties to negotiate in good faith and in accordance with the provisions of the access code (Government of Western Australia 2005). That code requires that arbitrations be informal and be expedited as quickly as possible (expedited processes are available for queuing disputes).

### **Independence of the dispute resolution body**

- 3.83 An independent dispute resolution body is necessary to engender confidence in the process. The dispute resolution body should be independent of service providers, current users, access seekers and governments. Another consideration is independence from related regulatory bodies (see below).
- 3.84 The Council considers that the process of dispute resolution includes all of the mechanisms available for resolving disputes, including arbitration and appeals processes. The Council regards these mechanisms as a package, with different

elements capable of satisfying independence issues. Alternative approaches to independent dispute resolution may include:

- separation of the regulator from the arbitrator (for example, by vesting each function in separate bodies)
- a mechanism enabling either party to a dispute to require the arbitrator to appoint an alternative body if a question of bias arises
- an independent appeals process to address questions of arbitrator bias or independence.

3.85 The Council notes that judicial review provides a mechanism to address issues of arbitrator independence. Often however this avenue of appeal is a costly and time consuming process. As noted above an effective access regime should give consideration to the costs imposed on affected parties and the parties' capacities to bear those costs in determining appropriate independent arbitration mechanisms.

### **Independence of the arbitrator from the regulator**

3.86 The Council's work in certification has raised the question of whether an arbitrator's independence is compromised if that body also acts as the access regime regulator. The view has been put that such arrangements may create conflict or tension, such as where the body involved is called on to determine disputes about access prices that it approved in its role as a price regulator.

3.87 Conversely, there may be value in an arbitrator being able to draw on past experience in relation to an access dispute. Further, in a highly technical access dispute, a suitable alternative arbitrator may be difficult to find.

3.88 While the Council is not opposed in principle to the same body having both regulator and arbitrator roles, it recognises the potential for issues to arise. Jurisdictions must consider the inclusion of safeguards to address these issues. A combination of some or all of the following mechanisms may be appropriate:

- ring fencing of the body's arbitration functions from its regulatory functions
- the development of practice and procedure notes that the body can follow to conduct its arbitration functions independently of regulatory functions
- a mechanism enabling any party to a dispute to require the regulator to appoint an arbitrator who has not been substantially involved in regulatory decision making for the service in question
- an independent (administrative) appeals process to address questions of arbitrator bias or independence.

### **Constraints on the arbitrator**

3.89 Where an access regime constrains the arbitrator from ruling on key access terms, such as reference tariffs, the Council considers that clause 6(4)(g) is satisfied if an independent regulator initially set such access terms in accordance with effective

regulatory processes. The Council accepts that binding an arbitrator can provide incentives for parties to negotiate and that it can provide greater certainty over the terms and conditions of access. By removing an avenue for disagreement it can also, potentially, reduce the cost and time spent resolving disputes.

3.90 Under the New South Wales Gas Regime (interim), the arbitrator had the discretion to depart from the reference tariffs that the independent regulator had approved. The Council accepted that this approach fosters commercial negotiation around the reference tariffs, facilitating more literal consistency with clause 6(4)(a). It also gives the arbitrator greater flexibility to consider the particular circumstances of a dispute. Finally, it permits an arbitrator to address any deficiencies in the initial regulatory process (NCC 1997a, pp 24–5).

3.91 In considering the then National Gas Code, however, the Council was guided by the views of industry participants (on both the demand and supply sides) that the arbitrator should adhere to the reference tariffs approved by the regulator. Participants argued that this approach would: create a higher degree of certainty; reduce the risk of gaming, delays and costly arbitration; avoid the need to duplicate the processes of the regulator; and promote a more stable environment for investment (NCC 1997b, pp 28–9).

3.92 The then National Gas Code incorporated safeguards for determining regulated tariffs, including:

- extensive public consultation on an independent regulator’s approval of access arrangements
- a merits appeal mechanism in relation to the regulator’s decision
- the requirement for periodic review of access arrangements.

In recommending certification, the Council was satisfied that these safeguards provided sufficient checks and balances to ensure the resulting reference tariffs fall within an appropriate range such as to justify exempting reference tariffs from further scrutiny by an arbitrator.

3.93 In developing the initial Western Australian Rail Regime, market participants raised concerns about the skills and resourcing of potential arbitrators. The Government of Western Australia responded to these concerns by amending the regime to bind the arbitrator to the independent regulator’s previous determinations on matters such as cost parameters. This approach effectively shifted important skill requirements from the arbitrator to the regulator. It also overcame the concern of some market participants that inconsistent outcomes could arise in a situation where there are, potentially, a large number of arbitrators involved in the regime (NCC 1999a, pp 28–31).

3.94 The effectiveness of binding the arbitrator requires that good independent regulatory processes are in place for appropriate vetting of any ‘fixed’ parameters. As such, it is crucial that the regulator be independent and be resourced to perform its duties adequately.

## Quality of process

- 3.95 The arbitration framework should promote confidence among the parties. It should also be designed to produce credible and consistent outcomes.
- 3.96 Credible outcomes are more likely if the arbitrator has sufficient resources and expertise to resolve complex disputes. The Council notes the potential complexity of disputes in areas such as access pricing. In resolving a pricing dispute, for example, the arbitrator must be capable of addressing the clause 6(4)(i) criteria, which include having regard to the ‘economically efficient operation of the facility’ and the ‘benefit to the public of having competitive markets’.
- 3.97 One way in which to achieve consistency is to have a single arbitrator hear all disputes. If dispute resolution responsibilities are spread across a number of arbitrators, then other measures may be needed.
- 3.98 To ensure arbitration outcomes are credible and consistent, some or all of the following mechanisms may be necessary:
- ensuring the arbitrator has sufficient resources and expertise to fulfil its duty
  - vesting the arbitrator with adequate information gathering powers. In particular, the arbitrator should have access to financial statements and other accounting information as required under clause 6(4)(o)
  - binding the arbitrator to observe previous determinations by an independent regulator, thereby ensuring consistency and shifting important skill requirements from the arbitrator to the independent regulator
  - allowing the arbitrator to seek expert advice from an independent regulator, thus facilitating information flows and a consistent approach across different arbitrations
  - vesting the arbitrator with the power to determine the dispute resolution process, including confidentiality and timeframe matters.

## Minor disputes

- 3.99 An appropriate package of dispute resolution mechanisms may include not only regulatory processes and arbitration, but also processes for dealing with minor disputes. For issues that are specific to the parties involved, informal conciliation may provide a cost-effective mechanism for dealing with disputes, backed-up with formal arbitration if required.
- 3.100 As an illustration of this tiered approach, the Northern Territory/South Australian Rail Regime provides for:
- direction from the independent regulator during the negotiation phase
  - conciliation by the regulator, subject to the agreement of the parties
  - the regulator’s appointment of an arbitrator (NCC 2000a).

## Public access to arbitration determinations

- 3.101 It is likely to be in the public interest to publish arbitration determinations on access disputes. Making such information publicly available would help to address information asymmetry between the access seeker and service provider, as well as provide greater certainty about the arbitrator's most likely approach to resolving disputes. In turn this may encourage parties to resolve disputes themselves without arbitration.
- 3.102 Such a process must address issues of confidentiality. Much of the information needed to resolve disputes and determine access terms and conditions is commercial-in-confidence. The public release of such information could be detrimental to competition.
- 3.103 There are many ways of dealing with confidentiality concerns. Under the rail access regimes operating in New South Wales, Western Australia and the Northern Territory/South Australia, for example, the regulator/arbitrator does not have to release determinations publicly where it judges this not to be in the public interest, taking account of confidentiality concerns (see NCC 1999a, 1999b and 2000a). Other regulators/arbitrators may choose to release versions of the determinations from which confidential material has been removed. Alternatively, rather than requiring the release of determinations, regimes may provide for arbitrators/regulators to publicly release statements of findings and outcomes. Such an approach may be appropriate where determinations, rather than having general application, relate to disputes or access terms and conditions that are specific to one access seeker or service provider.

## Clause 6(4)(h): binding decisions

The decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved.

- 3.104 Clause 6(4)(h) provides that an effective access regime should have credible enforcement arrangements to ensure an arbitrator's decision is binding. The regime should give effect to the enforcement process through legislative provisions, with appropriate sanctions and remedies for non-compliance. Existing rights of appeal should be preserved. This does not require the insertion of new appeals provisions.
- 3.105 Clause 6(4)(h) is generally satisfied by setting a time in which an arbitrator's decision must be reflected in a contract between the parties. At the same time, it is appropriate to allow a limited period in which an access seeker can decide not to be bound by the arbitrator's ruling. Otherwise, an access seeker may be compelled to accept terms that it would not have agreed to in a negotiated outcome and that may not be financially viable for the operator concerned. 'Opt out' provisions of this kind appeared in the then National Gas Code, the Northern Territory/South Australian Rail Regime and, more recently, the Western Australian Rail Access Regime, for example.

- 3.106 State or territory access regimes may allow for appeal of the decision of a dispute resolution body. To satisfy clause 6(4)(h), the ultimate decision of the appeals body must also bind the parties.
- 3.107 Good regulatory practice usually provides for an ability to review the decisions of regulators and arbitrators. The nature of such reviews may be tailored to particular circumstances and should not operate to frustrate the effectiveness of an access regime through delay or otherwise. While an effective access regime need not include a mechanism for merits review of an arbitrator’s decision, to satisfy clause 6(4)(h), an effective regime should not diminish any existing rights for appeal of an arbitrator’s decision—for example, rights to seek a judicial review for bias or a breach of natural justice.
- 3.108 A decision on whether or not to include a merits-based appeal mechanism in an access regime likely depends on issues such as the complexity and extent of regulatory intervention and potential for regulation to have an impact on property rights and values. Other issues that may need to be considered include risks of gaming behaviour and access delays versus the needs to protect the rights of affected parties. After taking account of such considerations the then National Gas Code, for example, introduced a limited merits review process for appeal of a regulator’s decision to impose an access arrangement.
- 3.109 Where merits review of decisions is provided for, a state or territory must be mindful of the clause 6(5)(c) requirements. Clause 6(5)(c) requires that merits review be limited to the information submitted to the original decision-maker, except that the review body may request or allow new information under certain circumstances; may allow new information where it could not have reasonably been available to the original decision-maker; and should have regard to the policies and guidelines of the original decision-maker (if any) that are relevant to the decision under review (see paragraphs 3.228-3.233).

### **Clause 6(4)(i): principles for dispute resolution**

In deciding on the terms and conditions for access, the dispute resolution body should take into account:

- (i) the owner’s legitimate business interests and investment in the facility;
- (ii) the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets;
- (iii) the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake;
- (iv) the interests of all persons holding contracts for use of the facility;
- (v) firm and binding contractual obligations of the owner or other persons (or both) already using the facility;

- (vi) the operational and technical requirements necessary for the safe and reliable operation of the facility;
- (vii) the economically efficient operation of the facility; and
- (viii) the benefit to the public from having competitive markets.

3.110 In interpreting the clause 6 principles, the Council uses general principles of statutory interpretation. It has regard to the objects of Part IIIA of the CCA and also to relevant judicial decisions. These include the decision of the Supreme Court of Western Australia in *Re Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor* [2002] WASCA 231 (23 August 2002) (Epic decision) in which the Western Australian Full Court of the Supreme Court considered the meaning of a number of provisions of the then National Gas Code that are similar to the clause 6(4)(i) criteria. The Council also notes s 44DA(1) of the CCA, which states that the Council, in considering the effectiveness of an access regime, must treat each relevant clause 6 principle as a guideline rather than a binding rule.

3.111 The Council considers that clause 6(4)(i) applies to any body responsible for determining the terms and conditions of access—that is, both arbitrators and regulators.<sup>10</sup> Clause 6(4)(i) requires that the dispute resolution body decide on the terms and conditions of access by taking into account the factors set out in subclauses (i)–(viii). Clause 6(4)(i) covers both price and non price terms and conditions of access. Where relevant, the dispute resolution body would also need to take account of the clause 6(5)(b) principles in considering access prices (see paragraphs 3.216-3.227).

3.112 An access regime may require a dispute resolution body to take account of matters other than those specified in clause 6. To the extent that those matters are not inconsistent with clause 6(4)(i) the inclusion of additional matters does not affect the effectiveness of the regime. This is recognised in s 44DA(2) of the CCA and clause 6(3A)(b) of the CPA which both expressly state that an access regime may contain additional matters which are not inconsistent with the clause 6 principles.

3.113 While the clause 6 principles do not specify particular outcomes, the Council considers that outcomes should give weight to all the criteria listed in sub-clauses (i) to (viii) of clause 6(4)(i). That is, no one criterion should be determinative of the outcome; rather, each should be considered in light of the other criteria in clause 6(4)(i). Such an approach is consistent with the Epic decision.

3.114 At times the clause 6(4)(i) criteria may conflict. The Council would anticipate that the arbitrator (or regulator) would have regard to the objects of the regime in resolving any conflict. Clause 6(5)(a) requires, where relevant, that access regimes incorporate

<sup>10</sup> This is the approach adopted under the then National Gas Code and also under the Northern Territory/South Australian Rail Regime, for example.

an objects clause that promotes the economically efficient use of, operation and investment in, significant infrastructure (see paragraph 2.25).

- 3.115 The then National Gas Code required the regulator, as well as the arbitrator to take into account criteria similar to those set out in clause 6(4)(i). The Northern Territory/South Australian Rail Regime also requires this.
- 3.116 An access regime satisfies clause 6(4)(i) if it requires that the determination of access terms and conditions account for the clause 6(4)(i) principles, and the clause 6(5)(b) principles where applicable. This requirement may be called into play where a regulator sets reference tariffs or an arbitrator resolves a dispute. (For further discussion of appropriate regulatory processes, see the discussion of clauses 6(4)(a)–(c) from paragraph 3.14).
- 3.117 The Council does not consider the outcome of any particular arbitration, or decision made under a regime (see clause 6(3A)(a)). Therefore, the Council’s consideration of pricing issues tends to focus on:
- whether the price/revenue and underpinning cost identification and assessment principles in the regime reflect accepted methodologies, the clause 6(4)(i) principles and the clause 6(5)(b) principles where applicable, and
  - whether mechanisms are in place to ensure pricing outcomes reflect these principles over time.
- 3.118 Access regimes may seek to restrict the roles of the arbitrator and/or regulator in determining disputes or providing guidance on the terms and conditions of access. Such restrictions may be highly prescriptive, such as embedding into the access regime reference tariffs that the arbitrator/regulator cannot re-examine or overturn (see, for example, NCC 2002a). Alternatively, the regime may be less prescriptive, such as specifying asset valuation methods that the regulator is to apply when calculating reference tariffs (see, for example, the then National Gas Code).
- 3.119 In a particular gas pipelines access regime considered by the Council for certification, reference tariffs for a number of pipelines were embedded into the regulatory regime, which meant the ACCC (the regulator/arbitrator in this case) was unable to reconsider the tariffs. The Council had concerns with the regime, including issues about the independence, effectiveness and transparency of the regulatory process for deriving the reference tariffs.
- 3.120 Where a regime does not restrict the factors that a regulator or arbitrator may take into account, the scope of that consideration is a matter for the regulator or arbitrator’s discretion and the Council does not ordinarily consider how the regime interprets the various factors for the purposes of clause 6(4)(i).
- 3.121 Where the access regime requires the regulator/arbitrator, in determining the terms and conditions of access, to consider factors instead of or in addition to those specified in the clause 6(4)(i) principle, the Council assesses whether those factors are consistent with and cover all the criteria in clause 6(4)(i). This assessment requires

the Council to interpret each of the clause 6(4)(i) factors, to ensure each is dealt with in an appropriate manner in the regime.

### Criterion (i)

3.122 Criterion (i) requires that the ‘owner’s legitimate business interests and investment in the facility’ be taken into account. In considering criterion (i) the Council would take account of any pricing principles that form part of the regime to the extent that the principles are consistent with the objects of Part IIIA of the CCA. With the exception of an access regime for electricity or gas developed in accordance with the Australian Energy Market Agreement or for the Tarcoola to Darwin railway, the pricing principles specified in clause 6(5)(b) are also applicable. The principles specified in clause 6(5)(b) essentially require that regulated access prices be set in a manner that is economically efficient—that is, prices occurring in a range that reflects an effectively competitive market. Such an approach is consistent with the objects of Part IIIA of the CCA.

3.123 In addition the Council would be guided by the courts. In considering the corresponding provision to criterion (i) under what was then s 2.24(a) of the National Gas Code, the Court rejected the argument that the word ‘legitimate’ meant that the facility owner could not recover monopoly prices or tariffs because these were above the level of economically efficient prices. Rather, it found that a business interest or investment could be perceived as not ‘legitimate’ for the purposes of clause 6(4)(i) if, for example, it contravened the then TPA or involved price manipulations intended to avoid tax (at 130). On this basis, the Court concluded that the regulator, in determining relevant reference tariffs, should have taken into account under s 2.24(a) the price paid by the pipeline owner for the pipeline, notwithstanding evidence that suggested the price paid reflected an expectation of monopoly returns. However, at paragraph 154 the Court noted that ‘this is not to suggest that reckless, mistaken or highly speculative investment decisions should be accepted’.

3.124 In *Re Telstra Corporation Limited (ACN 051 775 556)* [2006] ACompT 4 (the Telstra decision), which dealt with Telstra’s access undertaking for its line sharing service under Part XIC of the then TPA, the Tribunal stated:

...that a carrier’s “legitimate business interests” is a reference to what is regarded as allowable and appropriate in commercial or business terms. In the context of section 152AH(1)(b), the expression connotes something which is allowable and appropriate when negotiating access to the carrier’s infrastructure. When looked at through the prism of a charge term and condition of access and its relationship to a carrier’s cost structure, it is a reference to the interest of a carrier in recovering the costs of its infrastructure and its operating costs and obtaining a normal return on its capital. (at 89)

3.125 The Tribunal later added that:

[w]e do not consider that Telstra’s legitimate business interests extend to it achieving a higher than normal commercial return. (at 136)

3.126 Applying the reasoning of the Court, the Council considers that criterion (i) requires the actual price paid and invested in a facility by a facility owner as one factor to be taken into account in determining the terms and conditions of access (including reference tariffs), provided such acquisition or investment took place in a legitimate manner (that is, without contravention of the law). However, legitimate commercial interests are served so long as a service provider is able to receive a normal return on its investment.

### **Criteria (ii) and (iii)**

3.127 Criterion (ii) requires that ‘the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets’ needs to be taken into account.

3.128 Criterion (iii) requires that ‘the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake’ be taken into account. ‘Economic value’ means the present value of future revenues less the present value of future costs.<sup>11</sup>

3.129 The Council considers that the ‘costs’ to be taken into account are the actual costs to the owner of providing access. Such costs do not include those incurred as a result of overcapitalisation, those unnecessarily incurred to provide access or those based on an inappropriate attribution of common costs. In addition, the second limb of criterion (ii) expressly excludes any losses arising from increased competition in upstream and downstream markets. Accordingly, monopoly rents lost as a result of access and increased competition are not taken into account in determining the terms and conditions of access.

3.130 The inclusion of inappropriate costs in the determination of economic value under criterion (iii) potentially arises, for example, where the access seeker does not have sufficient information to determine the additional investment that the facility owner is required to make.

3.131 Criterion (iii) recognises that the infrastructure owner and users (or potential users) other than the access seeker may gain benefit or economic value from the additional investment required to facilitate access. Accordingly, the cost of the additional investment may be spread across a number of users (or potential users) rather than being levied entirely on the access seeker.

### **Criterion (iv)**

3.132 Criterion (iv) requires that ‘the interests of all persons holding contracts for use of the facility’ be taken into account. In considering the corresponding provision under the

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<sup>11</sup> See [www.xrefer.com](http://www.xrefer.com), *Dictionary of Accounting and Dictionary of Business* (Oxford University Press).

then National Gas Code (s 2.24(f)), the Court noted that ‘the interests of users and prospective users are likely to be counterpoised to the service provider’s legitimate business interests and investment’. There may be scope, however, to benefit both owners/operators and the interest of users/prospective users through increased capacity by virtue of third party use (at 135).

- 3.133 The Council considers that there is significant overlap between criterion (iv) and criterion (v). As the Court noted, these two criteria are linked to criterion (i). Regimes need to consider these varying interests and give weight to them against the remaining clause 6(4)(i) criteria and the overall objectives of access regulation.

### **Criterion (v)**

- 3.134 Criterion (v) requires that ‘firm and binding contractual obligations of the owner or other persons (or both) already using the facility’ be taken into account. Although the Epic decision did not raise specific issues in relation to the corresponding provision under the then National Gas Code (s 2.24(b)), the Court stated that:

... it is instructive to notice that prices that have been contractually agreed by a service provider, even if they include monopolist rents or returns, may continue to be charged by the service provider by virtue of section 2.25 and, by section 2.24(b), they are matters the Regulator must take into account. (at 31)

### **Criterion (vi)**

- 3.135 Criterion (vi) requires that the ‘operational and technical requirements necessary for the safe and reliable operation of the facility’ be taken into account. In considering the corresponding provision under the then National Gas Code (s 2.24(c)), the Court noted that ‘[e]xpenditure necessary for this purpose must be taken into account whether or not that would occur in a competitive market or according to theories of economic efficiency’ (Epic decision at 132).

- 3.136 Consistent with the Court’s reasoning, the Council considers that actual expenditure on safety and operating reliability should be taken into account for the purposes of criterion (vi) provided the expenditure was necessary. Overcapitalisation (for example, gold plating), or the inappropriate attribution of common costs or other unnecessary expenditure, however, should not be considered under criteria (vi); rather, given the nature and the operating environment of the facility, only those costs that are required or needed to achieve the safe and reliable operation of the facility should be considered.

### **Criterion (vii)**

- 3.137 Criterion (vii) requires that ‘the economically efficient operation of the facility’ be taken into account. The Court interpreted the corresponding provision under the then National Gas Code (s 2.24(d)) as the concept of economic efficiency as generally understood by economists. Economic efficiency should be viewed from the

perspective of society as a whole rather than that of the facility owner and operator (Epic decision at 115). The Court noted that:

s 2.24(d) most naturally relates to the objective in the preamble of the promotion of a competitive market and, perhaps, also to the prevention of the abuse of monopoly power. (Epic decision at 133)

3.138 Economic efficiency is also interrelated with competition in a market. The Court noted views from experts that ‘competitive markets lead to conditions of economic efficiency’, ‘a universal goal of economic regulation is, as far as possible, to replicate the efficiency outcomes that could otherwise be expected from the existence of effective competition’ and ‘competitive markets in equilibrium will be efficient’ (Epic decision at 116).

3.139 The Council considers that criterion (vii) requires consideration of the operation of a facility in an economically efficient manner as the term is generally understood by economists. The Epic decision indicates that there may be a tension between criterion (vii) and the legitimate business interests of the facility owner, at least in the short run (at 3.110 as per criterion (i)). (For further detail on the balancing of the various clause 6(4)(i) criteria, see paragraphs 3.143–3.148). However, economic efficiency implies that the facility owner is able to earn a normal return over the long run and therefore criterion (vii) would generally be consistent with legitimate business interests of the facility owner as well as the long term interest of end-users.

### **Criterion (viii)**

3.140 Criterion (viii) requires that ‘the benefit to the public from having competitive markets’ be taken into account.

3.141 Although not directly relevant, in interpreting the then s 2.24(e) of the National Gas Code which referred to the ‘public interest in having competition and markets’, the Court interpreted the term ‘competitive market’ as used in the then National Gas Code as referring to ‘a workably competitive market’. The Court noted that a workably competitive market is one in which no firm has a substantial degree of market power. The Court described a workably competitive market as ‘not a fixed and immutable condition with any absolute or precise qualities, but a process which involves rivalrous market behaviour’ (Epic decision at 128). It went on to state:

As such, a workably competitive market will react over time and according to the nature and degree of various forces that are happening within the market. There may well be a degree of tolerance of changing pressures or unusual circumstances before there is a market reaction. The expert evidence and writings tendered in evidence suggest that a workably competitive market may well tolerate a degree of market power, even over a prolonged period. The underlying theory and expectation of economists, however, is that with workable competition market forces will increase efficiency beyond that which could be achieved in a non-competitive market, although not necessarily achieving theoretically ideal efficiency. (Epic decision at 128)

3.142 Applying this interpretation to criterion (viii), the criterion requires a consideration of the public benefit from having a workably competitive market (that is, one in which no firm has a substantial degree of market power in the longer term). The public benefit that must be taken into account under the criterion is the efficiency gain from having a workably competitive market.

### **Giving weight to the clause 6(4)(i) criteria**

3.143 Clause 6(4)(i) requires that a balancing of the various (sometimes conflicting) criteria in determining the terms and conditions of access. As noted at paragraph 3.120, where the Council is satisfied with the regulatory processes by which access terms and conditions are determined, it leaves the interpretation and the balancing of the clause 6(4)(i) criteria to the discretion of the regulator and/or the arbitrator responsible for determining the regulated outcomes within the access regime. In the Epic decision, the Court noted the potentially conflicting nature of the corresponding clause 6(4)(i) criteria under the then National Gas Code and concluded that such conflict is 'to be resolved by the Regulator in accordance with the Act and the Code and the circumstances of each particular case' (Epic decision at 185).

3.144 In giving weight to each of the clause 6(4)(i) criterion the Council considers it generally appropriate to group the criteria as follows:

- criteria (i), (iv) and (v), which account for the interests of the facility owner and existing facility users
- criteria (ii), (iii) and (vi), which account for the costs of providing access. Such costs must be necessary and must not reflect gold plating or other unnecessary measures
- criteria (vii) and (viii), which expressly account for efficiency objectives and the benefits of competitive markets.

3.145 The Council considers that the first group of criteria, by accounting for the actual investment and interest in the facility, are intended to consider the effect on the owner and existing users of any property rights being affected through access regulation. The second group of criteria require that the access regime account for only those costs necessary to facilitate access and the safe and reliable operation of the infrastructure. The final group of criteria expressly require a consideration of efficiency and the benefits of competition.

3.146 In considering the criteria to determine an appropriate range of approaches to the incorporation of the clause 6(4)(i) principles, the Council notes that the underlying objective of Part IIIA (discussed above at paragraph 2.9) is to promote efficiency. The Council considers that a universal goal for economic regulation is to replicate (as far as possible) the efficiency outcomes that could otherwise be expected from the existence of effective or workable competition (that is, a situation where no firm within the market has the market power to act in a manner unconstrained by other competitors). Effective competition can be expected to increase efficiency from that

in a non-competitive market, although it may not achieve the conditions of perfect competition.

- 3.147 With these principles in mind, the Council considers that the terms and conditions of access should be structured in a way that promotes efficient use of infrastructure and efficient investment in dependent markets. At the same time, efficient investment in infrastructure must not be deterred. As such, access prices and underlying cost structures should allow infrastructure owners to generate sufficient revenues to meet the efficient costs of providing access to the service and to earn a return on the investment commensurate with the risks involved.
- 3.148 The Council accepts, in workably competitive markets, that instances of transitory market power may arise and lead to outcomes that may not fall within an efficient range in the short term. Over the longer term, competitive pressures should cause prices and other terms of access to fall within the range of outcomes that would be expected in an effectively or workably competitive market.

### **Approaches to pricing**

- 3.149 Price is a critical term of access. Without an appropriate mechanism to determine price, an access regime is unlikely to be effective. This is because in the absence of regulation, suppliers in natural monopoly markets are able to earn monopoly returns by setting prices that effectively deny access or distort production and/or consumption patterns. In specific circumstances, commercial negotiation/arbitration alone may not be able to deliver pricing outcomes consistent with those likely to be achieved in an effectively competitive market—that is, it may not be able to deliver prices that ultimately fall within an efficient range (see paragraph 3.148). Independent regulatory processes may also be required.
- 3.150 In competitive markets, efficient pricing equates to marginal cost (that is, the cost of providing an additional unit). In the absence of capacity constraints, this may exclude fixed costs. For natural monopoly infrastructure, however, with high fixed costs and declining average costs over the range of demand, this approach may not deliver viable outcomes. Setting price to marginal cost would result in the owner failing to recoup fixed costs. Access pricing therefore needs to be adapted to apportion fixed costs across users, while ensuring revenues are not so high as to distort demand for services.
- 3.151 These characteristics pose challenges in determining an appropriate approach to pricing services. In general, efficient outcomes can be expected to lie in a band between short run (avoidable) costs and the long term efficient (full) cost of supplying the services demanded. If price exceeds long term efficient cost, then demand is inefficiently constrained, which could also result in the construction of inefficient bypass facilities. (Such an enquiry relates to the provision of the service generally rather than to a particular customer.) These outcomes impose welfare costs on the community. Conversely, if price falls below short run cost, then the service

would require cross-subsidisation, imposing a different set of resource allocation distortions.

- 3.152 The long term (or forward looking) efficient cost of supply should act as a cap on prices or revenues. Independent regulatory processes should be used to set the relevant benchmarks, including the optimised asset base, rate of return, rate of depreciation and operating costs. This process invariably involves regulatory discretion. In each case, well accepted valuation methods should be used.
- 3.153 The price or revenue cap may need to be adjusted periodically to account for changes in cost factors, including new investment, changing economies of scale and scope, efficiency gains and inflation. Over time, price/revenue caps can be structured to provide the supplier with efficiency targets and incentives for productivity gains in excess of these targets. Caps may need to be implemented in tandem with measures to ensure reductions in service quality are not disguised as efficiency gains.
- 3.154 In addition to costs, demand factors may also play a role in determining access pricing. To preserve economic efficiency, the proportion of fixed costs charged to each access seeker may need to account for differences in the access seeker's elasticity of demand (or 'willingness to pay'). The allocation of fixed costs to access seekers may be the subject of commercial negotiation between the facility owner and access seekers. The Council notes, however, that price discrimination raises issues if a facility owner is vertically integrated with commercial interests operating in a contestable downstream market. In these circumstances, the facility owner may be in a position to offer preferential pricing to an affiliated customer over independent customers.
- 3.155 The approach to pricing should be sufficiently flexible to account for varying market conditions and reflect market realities. Pricing may need to be structured to account for congestion issues, for example, if the facility is subject to capacity constraints. In electricity, a consumer may be persuaded to switch to off peak consumption if peak prices reflect the costs of capacity expansion while off peak prices reflect only marginal cost. Such an approach can optimise the efficient use of existing infrastructure and reduce the risk of unnecessary capacity expansions.
- 3.156 Also a consideration in pricing are the specific risks associated with greenfields investments compared with investments in mature infrastructure facilities. The Council notes one approach to pricing for greenfields projects in paragraphs 3.165–3.168.
- 3.157 The appropriate framework for applying these broad principles depends to some extent on the characteristics of the particular industry and infrastructure. The following subsections discuss the approach to pricing issues in some applications that the Council has approved.

### *Gas*

- 3.158 Access pricing under the then National Gas Code involved revenue caps combined with published reference tariffs (benchmark prices) approved by an independent regulator. Reference tariffs had to apply to services likely to be sought by a significant

part of the market, and they also had to be determined on the basis of charges needed to meet the total revenue requirement of the relevant gas pipeline. The tariffs had to be derived from the cost principles set out in the National Gas Code. The Code provided for the use of incentive mechanisms to promote efficiency gains over time.

- 3.159 Once approved by the regulator, reference tariffs formed a basis for commercial negotiation for both reference and non-reference services (that is, prices could vary from the reference tariff through negotiation). An access seeker had a right, however, to acquire access to spare capacity in the reference service at the reference tariff. The reference tariff for the reference service could not be varied in arbitration. In considering the certification of the then National Gas Code the Council found an advantage of the above framework was that it provides considerable guidance to access seekers and certainty to all parties (NCC 1997b).

#### *Electricity*

- 3.160 The amended Northern Territory Electricity Network Access Code (the NT Code) incorporates a pricing framework of tariffs under a revenue cap that is adjusted over time according to a CPI-X formula. The Utilities Commission, the independent Northern Territory regulator, takes a central role in the determination of tariff and revenue parameters, giving primacy to efficiency objectives.
- 3.161 The NT Code encourages the ongoing pursuit of productivity gains by providing a framework for the reasonable sharing of these gains through the application of the CPI-X formula and through periodic reconciliation of the cap against revenue outcomes.

#### *Rail*

- 3.162 The approaches to access pricing in the New South Wales, Western Australian and Northern Territory/South Australian rail access regimes reflect similarities. In each case, parties may commercially negotiate prices within a band approved by an independent regulatory process.
- 3.163 In the Western Australian Rail Access Regime, the regulator-approved floor price measures the incremental costs of providing the service (the costs that the owner would avoid in the short term if access were not provided). The ceiling price (the upper constraint on pricing) represents the stand-alone costs of providing access and covers forward looking efficient costs. The regulator-approved floor and ceiling prices form a basis for negotiation. While access seekers may negotiate prices within the band, the regime requires non-discriminatory pricing for users in the same market.<sup>12</sup> An access seeker has the right to arbitration if a dispute arises over price.

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<sup>12</sup> This provision is a response to vertical integration issues.

3.164 A similar approach exists in the Northern Territory/South Australian Rail Regime, but with additional guidance on price for services where road freight provides a competitive discipline on access prices. In effect, the rail access price for rail haulage of general freight currently transported by road is set with reference to the road freight rate.

### **Competitive tendering and access tariffs**

3.165 The Council has noted that greenfields investments, compared with mature facilities, can raise specific risk issues and that approaches to pricing may need to account for these differences.

3.166 One approach that the Council has approved is to determine access tariffs using a market-based approach. For example, under ss 3.21–3.36 of the then National Gas Code, the proponent of a new facility may elect to have tariffs determined through a competitive tender process to select the infrastructure operator. Under this approach, parties bid to become the access provider by specifying the price at which they are willing to supply the access service.

3.167 The competitive tendering model allows the market to determine prices that are efficient for consumers and viable for the operator. The effectiveness of this approach requires the tendering process to be genuinely competitive. For this reason, ex ante oversight of the tendering process is essential. Ex post vetting also may be necessary to ensure tendering outcomes are consistent with the approved process.

3.168 Oversight arrangements should be conducted through independent and transparent processes. The National Gas Rules, for example, vest these powers with an independent regulator, the AER.

### **Access pricing in secondary markets**

3.169 While regulatory intervention is an appropriate response to market power and information asymmetries in primary markets for access, the argument for its use is less convincing in secondary markets.

3.170 In a secondary market, a facility user sells capacity to other businesses that want to use the service (as opposed to the facility operator selling access to them, as occurs in the primary market). Businesses wanting to use the services of a facility can, therefore, directly approach an existing user that is not using all of its existing entitlement and seek to buy a portion of that entitlement.

3.171 Promoting secondary markets can bring three benefits:

- secondary markets can facilitate better use of existing infrastructure, so the need to expand capacity may be deferred or avoided
- existing users gain flexibility to better manage risk if, for example, they are unable to use all the capacity they have contracted to purchase from the facility owner

- secondary markets can generate useful price signals, which may promote better informed commercial negotiation in primary markets.

3.172 Some secondary market arrangements seek to overcome the natural monopoly problem by creating competition between discreet bundles of capacity in the one set of infrastructure. These arrangements include auctions, whereby capacity is sold to a number of users, or other mechanisms to vest capacity rights in favour of more than one party.

3.173 Access regimes should not impose unreasonable barriers to capacity trading in secondary markets unless there is a compelling public benefit from doing so.

### **Non price terms and conditions**

3.174 Clause 6(4)(i) covers all terms and conditions of access, not just price. In certain instances, non price terms and conditions can be as important as the issue of access pricing, and sometimes more important. As noted at paragraph 3.38, non price terms and conditions of access may include those relating to safety requirements, the allocation of capacity among competing users, interoperability issues and service quality issues.

3.175 For a number of rail regimes, for example, the Council considered the issue of whether safety requirements acted as a barrier to entry. In addition, terms and conditions relating to track capacity allocation, timetabling, track entry and exit times, track quality and speed restrictions are all significant terms and conditions to which clause 6(4)(i) applies.

### **Clause 6(4)(j): facility extension**

The owner may be required to extend, or to permit extension of, the facility that is used to provide a service if necessary but this would be subject to:

- (i) such extension being technically and economically feasible and consistent with the safe and reliable operation of the facility;
- (ii) the owner's legitimate business interests in the facility being protected; and
- (iii) the terms of access for the third party taking into account the costs borne by the parties for the extension and the economic benefits to the parties resulting from the extension.

3.176 In some situations, the needs of an access seeker can be met only by an extension of the facility's geographic range or an expansion of its capacity. These matters should be subject, in the first instance, to negotiation between the parties. When parties cannot reach an agreement, however, the arbitrator should be empowered to determine, subject to the clause 6(4)(j) criteria, whether the owner should be required to extend or permit extension of the facility.

3.177 An issue the arbitrator may need to consider is who is best placed to undertake the extension or expansion. Often it will be more efficient in some cases for the

incumbent provider to extend the facility, such as with the extension of pipes within an existing distribution network. There will be instances where requiring the owner to extend their facility does not produce the most efficient outcome. It may be more cost-effective for the access seeker to construct the extension themselves with access provided through interconnection, for example.

- 3.178 Given the range of outcomes possible, the arbitrator needs the flexibility to make the most appropriate determination. In the interests of promoting efficiency therefore, states and territories may want to consider including in their access regimes a power for the arbitrator to make rulings on interconnection, provided the clause 6(4)(j) conditions are met. The National Gas Code adopted this approach.
- 3.179 While the wording of clause 6(4)(j) refers to 'extensions' it is the Council's view that the concept of an 'extension' is broad enough to include an 'expansion'. This is consistent with the objectives of Part IIIA as often, the most efficient way of increasing the supply of a service may be for the existing provider to expand capacity, rather than requiring the access seeker (or someone else) to construct another facility to provide a service. This is true of facilities where it is efficient to expand capacity incrementally, such as gas pipelines and rail track.
- 3.180 For this reason, the clause 6(4)(j) principles apply to expansions. The National Gas Code, Western Australian Electricity Networks Access Regime and the Northern Territory/South Australian Rail Regime are among those that have adopted this framework.

### **Clause 6(4)(k): dealing with a material change in circumstances**

If there has been a material change in circumstances, the parties should be able to apply for a revocation or modification of the access arrangement which was made at the conclusion of the dispute resolution process.

- 3.181 Clause 6(4)(k) provides for an access arrangement to be revoked or modified following a material change of circumstances. The clause appears to derive from a suggestion in the Hilmer Report that a 'declaration could be revocable on the showing of a material change of circumstances' (1993, p 253).
- 3.182 The Council has been reluctant to interpret this clause in a way that would compromise the certainty of contractual arrangements. Once a contract is signed—whether through commercial negotiation or following arbitration—it should govern the relationship between the parties.
- 3.183 Given that different infrastructure users have different risk exposures, an appropriate way in which to address a material change of circumstances may be for the parties to identify in the contract any factors that would warrant the contract being reopened in the future. Parties may choose, for example, to limit the grounds to those available normally for commercial contracts under common law. At the same time, an access regime should not preclude the application of common law principles (for example, the doctrine of frustration) to matters of this nature.

3.184 An access regime could provide for parties to use an arbitrator to resolve disputes over what constitutes a material change in circumstances. This provision would allow for circumstances where commercial negotiations fail to achieve agreement.

3.185 In the Western Australian Electricity Networks Access Regime the Council considered that clause 6(4)(k) was satisfied where the regime allowed a service provider to determine in advance what constituted a material change in circumstances for inclusion in an access arrangement. When the conditions of a trigger event are met the service provider must notify the Economic Regulation Authority and submit proposed revisions to the access arrangement to the authority for approval. Also, the parties are free to negotiate specific termination or force majeure events in their individual access agreement.

### **Clause 6(4)(l): compensation**

The dispute resolution body should only impede the existing right of a person to use a facility where the dispute resolution body has considered whether there is a case for compensation of that person and, if appropriate, determined such compensation.

3.186 Clause 6(4)(l) does not mean that an access regime need allow a dispute resolution body to impede existing rights. Where a dispute resolution body can do this, however, it must also be empowered to consider and, if appropriate, determine compensation.

3.187 For example in s 10.32 of the Western Australian Electricity Networks Access Code the arbitrator cannot make an order that would impede the right of a user under an access contract unless the user agrees or is satisfied that the user is or will be appropriately compensated for the impeded right. Therefore, the Council concluded that this was consistent with clause 6(4)(l).

### **Clause 6(4)(m): hindering access**

The owner or user of a service shall not engage in conduct for the purpose of hindering access to that service by another person.

3.188 Clause 6(4)(m) requires that an effective access regime prohibit conduct for the purpose of hindering access. This principle applies both to existing users (to address the risk of problems such as hoarding) and facility owners. The Council believes that an access regime should incorporate this clause explicitly or contain other provisions that have the same effect.

3.189 In the case of vertically integrated service providers, access may be hindered in circumstances where the service provider unfairly provides favourable terms of access to its affiliated entity. In rail, for example, a vertically integrated rail track operator that provides track priority and the most favourable track use timetabling to its own above-track operator may effectively hinder access to the rail track by other above-track operators. Such conduct would be contrary to clause 6(4)(m). Where there are vertical integration issues it may be necessary for an access regime to

address the issue through, for example, ring-fencing and competitive neutrality provisions. Another way for states and territories to approach the issue may be to address vertical integration directly through structural separation.

### **Competitive neutrality**

3.190 Where vertical integration issues arise, ring fencing provisions may need to be supported by competitive neutrality provisions to assure access seekers that the service provider will not discriminate against them. Concerns can arise because certain participants enjoy advantages (cost or otherwise) over others for reasons not related to competitive behaviour. If the advantages favour less efficient businesses it can lead to resource allocation distortions in the market. Competitive neutrality refers to policies aimed at removing such distortions. In the context of access, competitive neutrality typically refers to neutralising competitive advantages enjoyed by a particular infrastructure user because it is affiliated with the infrastructure owner. This process can be distinguished from the competitive neutrality principles set out in clause 3 of the CPA, which relate to competitive advantages arising from public ownership of significant businesses.

3.191 Prohibition of anti-competitive price discrimination between affiliated users and third party access seekers operating in the same market is an example of the application of competitive neutrality in an access regime. In the Queensland Rail Access Regime, for example—in which the rail network operator also operates rail haulage services in competition with rival third party operators—the regime contains express prohibitions on unfair differentiation, both during access negotiations and in the provision of access for users of declared services. Together with other mechanisms in the regime, this provides an appropriate level of comfort that a vertically integrated service provider will be prevented from treating its related businesses more favourable than those of its competitors.

### **Clause 6(4)(n): separate accounting**

Separate accounting arrangements should be required for the elements of a business which are covered by the access regime.

3.192 Under clause 6(4)(n), an effective access regime should impose separate accounting arrangements on service providers for the elements of the business covered by the regime. That is, facility owners must make available financial information that focuses exclusively on the elements of their business subject to the regime.

3.193 The availability of relevant accounting information is necessary for access seekers and regulatory bodies (including dispute resolution bodies) to assess the terms and conditions of access. Separate accounting also helps to address the potential for anti-competitive behaviour such as using cross-subsidies between covered and uncovered services as a means for disguising monopoly pricing.

3.194 To satisfy clause 6(4)(n), an effective access regime should include provisions that require a facility owner to at least:

- maintain a separate set of accounts for each service that is the subject of an access regime
- maintain a separate consolidated set of accounts for all of the activities undertaken by the facility owner, and
- allocate any costs that are shared across multiple services in an appropriate manner.

### **Ring fencing**

3.195 Vertical integration creates opportunities for transfer pricing and preferential treatment of affiliate businesses over third parties. Ring fencing arrangements may be required in some industries, particularly those where a facility owner operates, or has interests in, the same markets as those in which third party access seekers participate.

3.196 Ring fencing involves identifying and isolating all aspects of a business that could permit an integrated entity to engage in anti-competitive behaviour designed to eliminate competitor or deter potential competitors from entering the market. This includes activities, assets, costs and revenues relating to the monopoly element (or area of the business not subject to strong competitive pressures) of an integrated entity. It also includes potential incentives or practices of a non-accounting nature that may result in anti-competitive behaviour.

3.197 Apart from segregating access-related functions from other functions ring fencing arrangements should also include measures to:

- protect confidential information disclosed by an access seeker to the facility owner from improper use and disclosure to affiliated bodies, and
- establish staffing arrangements between the facility owner and affiliated bodies that avoid conflicts of interest.

### **Clause 6(4)(o): access to financial information**

The dispute resolution body, or relevant authority where provided for under specific legislation, should have access to financial statements and other accounting information pertaining to a service.

3.198 An effective access regime should provide the dispute resolution body and other relevant bodies (for example, regulators and appeals bodies) with the right to inspect all financial documents pertaining to the service. This principle seeks to ensure that the dispute resolution body and other relevant bodies have access to all information necessary to properly assess and settle any issues relating to third party access.

3.199 For example, in the Western Australian Electricity Networks Access Regime the arbitrator (the Western Australian Gas Disputes Arbitrator) was given the power to gather information about any matter relevant to the access dispute in any way the

arbitrator thought appropriate. The regime requires the service provider to comply with any request from the arbitrator or the regulator (the Economic Regulation Authority) to inspect or make copies of the service provider's accounts and records. There are penalties for non-compliance. The Council was satisfied in relation to clause 6(4)(o).

### **Clause 6(4)(p): cross-jurisdictional regimes**

Where more than one State or Territory access regime applies to a service, those regimes should be consistent and, by means of vested jurisdiction or other co-operative legislative scheme, provide for a single process for persons to seek access to the service, a single body to resolve disputes about any aspect of access and a single forum for enforcement of access arrangements.

### **Clause 6(2): jurisdictional issues**

The regime to be established by Commonwealth legislation is not intended to cover a service provided by means of a facility where the State or Territory Party in whose jurisdiction the facility is situated has in place an access regime which covers the facility and conforms to the principles set out in this clause unless:

- (a) the Council determines that the regime is ineffective having regard to the influence of the facility beyond the jurisdictional boundary of the State or Territory; or
- (b) substantial difficulties arise from the facility being situated in more than one jurisdiction.

3.200 These clauses establish principles for the treatment of:

- services that are subject to multiple state and territory access regimes, and
- facilities with an influence beyond a single jurisdiction.

### **Multiple access regimes**

3.201 Clause 6(4)(p) provides that where a service is subject to access regimes in more than one state or territory, those regimes should be consistent and should provide for a single process, a single dispute resolution body and a single enforcement forum. To satisfy this clause, the relevant state or territory access regimes could contain provisions to facilitate a seamless and consistent approach to accessing the service. The rationale is to ensure only one set of access provisions applies to the service, promoting timely and efficient outcomes. The Council considers that this is consistent with the objectives in s 44AA of the CCA.

3.202 Clause 6(4)(p) considerations arise in the context of a service located in more than one jurisdiction, such as a service provided by a cross-border gas pipeline or railway line. They also arise where multiple access regimes apply to a service located within a particular jurisdiction.

3.203 To satisfy this clause, the relevant state access regimes could contain provisions to apply a single regime to the entire service, as per the following examples.

- The Northern Territory and South Australia passed identical legislation to establish the Northern Territory/South Australian Rail Regime, including the establishment of a single regulator.
- States and territories adopted cross-vesting arrangements under the National Gas Access Regime to ensure only one jurisdiction's access legislation applies to cross-border pipelines (NCC 1997b, pp 53–5).

### **Interstate influence of facility**

3.204 Clause 6(2) suggests that a state or territory access regime may be found to be ineffective as a result of:

- its influence beyond the jurisdictional boundary of the state or territory, or
- substantial difficulties arising because the infrastructure subject to the regime crosses a state or territory border.

3.205 The Council believes that clause 6(2), in conjunction with clause 6(4)(p), indicate that state and territory regimes should consider and, if necessary, specifically deal with the situation where a facility or service crosses jurisdictional boundaries. Clause 6(2) issues might need to be considered in the following scenarios.

- Where a facility that crosses a state border—for example, a cross-border railway track or gas pipeline— jurisdiction-based regulation could result in conflicting approaches to access on either side of the border, imposing substantial costs on business and inhibiting interstate trade. Another problem is that a piecemeal state-by-state approach could result in unregulated gaps in the network.
- Where a facility that is wholly located within a jurisdiction but part of a wider interstate network—for example, a state rail network that also forms part of an interstate network— inefficiencies could arise if access to state-based services is determined without consideration of the requirements of interstate demand.

3.206 Clause 6(2) is not interpreted in a manner that prevents the development of state or territory regimes for services that have an interstate aspect. Rather, it is interpreted to ensure that regimes deal with issues appropriately.

3.207 Issues likely to need coordination include:

- ensuring the terms and conditions of access across borders are compatible so that an access seeker is not prevented from negotiating the seamless flow of a service across borders (for example, a seamless interstate train path)
- ensuring arbitration processes are consistent, so as to avoid imposing multiple costs on parties (for example, in the Northern Territory/South

Australian Rail Regime, measures exist to provide for a common arbitrator in disputes involving cross-border services (NCC 2000a)), and

- ensuring the regulatory framework accounts for regulatory arrangements in other relevant jurisdictions.

3.208 In some cases, mechanisms such as those noted above may be sufficient to address interstate issues. In other cases, a common approach to access regulation may be needed to achieve efficient outcomes. Mechanisms for achieving this commonality include:

- a coordinated intergovernmental process to implement a uniform framework for access, as has occurred in the gas and electricity sectors
- Commonwealth Government legislation, and
- cross-vesting arrangements across relevant jurisdictions to establish a single process for access to cross-border services.

3.209 While a high degree of consistency in access regimes for cross-border services is desirable, the Council recognises that complete consistency of a state access regime with national arrangements would be an overly high hurdle for satisfying clause 6(2).

#### **The relationship between clauses 6(4)(p) and 6(2)**

3.210 Clause 6(4)(p) elaborates on one issue that may also arise under clause 6(2): the application of multiple access regimes to a single service. The scope of clause 6(2) is however wider than 6(4)(p), because it also encompasses the influence of a particular facility beyond a state border.

### **Clause 6(5)(a) and the objects of Part IIIA: promote efficiency and effective competition**

A State, Territory or Commonwealth access regime (except for an access regime for: electricity or gas that is developed in accordance with the Australian Energy Market Agreement; or the Tarcoola to Darwin railway) should incorporate the following principle:

- (a) Objects clauses that promote the economically efficient use of, operation and investment in, significant infrastructure thereby promoting effective competition in upstream or downstream markets.

The objects of Part IIIA of the CCA (s 44AA) are to:

- (a) promote the economically efficient operation of, use of and investment in the infrastructure by which services are provided, thereby promoting effective competition in upstream and downstream markets; and
- (b) provide a framework and guiding principles to encourage a consistent approach to access regulation in each industry.

3.211 Clause 6(5) (a) does not apply to an electricity or gas access regime developed in accordance with the Australian Energy Market Agreement or to the access regime for the Tarcoola to Darwin railway.

3.212 In respect of other state and territory access regimes, clause 6(5)(a) requires that an effective access regime incorporate an objects clause that provides a clear statement that the purpose of regulating third party access is to promote economic efficiency in the operation, use and investment in infrastructure thereby promoting competition in upstream and downstream markets.

3.213 A clear statement of objectives helps to guide all parties affected by the access regime. Importantly it provides clear guidance to regulators and arbitrators, which should result in more consistent decision-making. Clarifying the intent of an access regime is also likely to reduce opportunities for dispute and misunderstanding, which in turn saves time and reduces the cost of regulation.

3.214 As set out above (see paragraph 3.212), the application of an efficiency objective in access regulation has the following three broad components:

- first, ensuring the efficient use of bottleneck infrastructure, especially by denying infrastructure owners the opportunity to misuse market power (in either the market for their services or in related markets) by raising prices and/or refusing access to services
- second, facilitating efficient investment in essential infrastructure, especially by ensuring:
  - infrastructure is maintained and developed appropriately
  - infrastructure owners (and potential owners) earn sufficient returns to provide incentives for efficient investment
  - incentives for inefficient development of competitive infrastructure and for inefficient investment in upstream and downstream activities (that is, overinvestment and underinvestment) are minimised
- third, promoting competition in activities that rely on the use of bottleneck infrastructure.

3.215 One of the advantages of each state and territory access regime containing an objects clause in respect of the promotion of the efficient operation of, use and investment in infrastructure is that it may lead to consistency across the states and territories as to the operation of access regimes, which is consistent with the objective in s 44AA(b) of the CCA of ensuring a consistent approach to access regulation.

## Clause 6(5)(b): pricing should promote efficiency

- (b) Regulated access prices should be set so as to:
- (i) generate expected revenue for a regulated service or services that is at least sufficient to meet the efficient costs of providing access to the regulated service or services and include a return on investment commensurate with the regulatory and commercial risks involved;
  - (ii) allow multi-part pricing and price discrimination when it aids efficiency;
  - (iii) not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and
  - (iv) provide incentives to reduce costs or otherwise improve productivity.

3.216 Clause 6(5)(b) also does not apply to an electricity or gas access regime developed in accordance with the Australian Energy Market Agreement or to the access regime for the Tarcoola to Darwin railway.

3.217 The clause 6(5)(b) principles emphasise that to be appropriate the price of access should promote the efficient use of, operation and investment in infrastructure as a means of promoting effective competition in dependent markets (clause 6(5)(a) and s 44AA of the CCA). The pricing principles in clause 6(5)(b), while providing considerable discretion and flexibility in setting prices, require that regulated access prices be set to cover costs and provide a return on investment that is commensurate with the risks involved. The principles emphasise ongoing efficiency improvements by also requiring that regulated access prices provide incentives to reduce costs or otherwise improve productivity. A desirable outcome is that regulated prices mirror the outcomes expected of an effectively competitive market.

3.218 In recommending that pricing principles be incorporated in Part IIIA and clause 6 of the CPA the Productivity Commission also noted that ‘a key role of pricing principles is not so much to prescribe what should happen in a particular situation, but to rule out approaches and methodologies which would be inappropriate’ (PC 2001, p 142). In addition appropriate pricing principles:

- provide guidance on how the broad objectives of access regimes should be applied
- provide a measure of certainty to regulated firms and access seekers, in turn, improving the operation of the negotiation-arbitration framework
- help to prevent a regulator’s own values from unduly influencing decisions relating to the terms and conditions of access.

3.219 In reviewing access regimes for consistency with clause 6(5)(b) the Council is mindful of the requirement in clause 6(3A) that the Council must not review specific pricing outcomes.

**Principle (i): Expected revenue should be sufficient to meet the efficient costs and include a return on investment**

- 3.220 Clause 6(5)(b)(i) reflects a desire that regulated prices should not give facility owners a free rein to extract large rents (this promotes allocative efficiency and 'fairness'), but that they also should not reduce a facility owner's profits to such an extent as to deter investment in such facilities (this promotes dynamic efficiency).
- 3.221 The principle emphasises that prices should be set to reflect efficient costs, not actual costs. This provides an incentive for service providers to achieve cost efficiencies.
- 3.222 In determining efficient costs the regulator is to take account of the risks the service provider faces. The risks include those that would arise in a normal commercial setting as well as those that derive from being subject to regulation.

**Principle (ii): Multi-part pricing and price discrimination**

- 3.223 Clause 6(5)(b)(ii) recognises that multi-part pricing and price discrimination can promote efficiency.
- 3.224 The principle also reflects the fact that discriminatory prices can be used for anti-competitive reasons. Thus the principle supports clause 6(4)(m), which requires that an effective access regime prohibit conduct, such as anti-competitive price discrimination, for the purpose of hindering access.

**Principle (iii): vertically integrated access provider not to discriminate in favour of its own downstream operations**

- 3.225 Clause 6(5)(b)(iii) recognises that incentives for anti-competitive behaviour are likely to be more prevalent in vertically integrated industries. This principle expressly prohibits vertically integrated service providers from setting terms and conditions that discriminate in favour of its downstream operations. However, where the cost of providing access to an affiliate differs from the cost of providing access to other third parties terms and conditions may be varied to reflect those differences.

**Principle (iv): provide incentives to reduce costs or otherwise improve productivity**

- 3.226 In effectively competitive markets firms strive to improve their performance to gain cost and other advantages over their rivals or potential rivals. Clause 6(5)(b)(iv) seeks to replicate the discipline of a competitive market by requiring that regulated access prices be structured to provide incentives to reduce costs or otherwise improve productivity.
- 3.227 A number of regulatory regimes use, for example, a CPI-X method of providing incentives to reduce costs or otherwise improve productivity.

## Clause 6(5)(c): merits reviews of decisions

- (c) Where merits review of decisions is provided, the review will be limited to the information submitted to the original decision-maker except that the review body:
- (i) may request new information where it considers that it would be assisted by the introduction of such information;
  - (ii) may allow new information where it considers that it could not have reasonably been made available to the original decision-maker; and
  - (iii) should have regard to the policies and guidelines of the original decision-maker (if any) that are relevant to the decision under review.

3.228 Clause 6(5)(c) also does not apply to an electricity or gas access regime developed in accordance with the Australian Energy Market Agreement or the Tarcoola to Darwin railway.

3.229 Clause 6(5)(c) recognises that an important element of an access regime is the independent review of any access decisions. Merits review as available under the CCA provides for the review body (in this case the Tribunal) to remake the original decision. The remade decision then replaces the original decision. Another form of review is judicial review. Judicial review provides for decision review on various grounds including: a breach of the rules of natural justice; that the required procedures were not observed; that the decision maker did not have jurisdiction; that the decision was not authorised by the relevant Act or was an improper exercise of the power; that the decision involved an error of law; that the decision was affected by fraud or was otherwise contrary to the law; and that there was no evidence to justify the making of the decision.

3.230 The Council looks for an effective access regime to provide for the review of the decisions of regulators and arbitrators, consistent with good regulatory practice, such that decisions can be adequately tested. Where there is no provision for merits review this may involve the Council considering the availability of and arrangements for judicial review in the relevant jurisdiction.

3.231 It is important that review processes do not frustrate the effectiveness of an access regime. Lengthy delays associated with review processes must be avoided. The nature and process of review proceedings must be tailored to ensure they can be completed in commercially relevant timeframes. This is especially so where the effect of a decision is stayed by the commencement of a review.

3.232 Clause 6(5)(c) provides that where merits review is provided, then the review should be limited to information submitted to the original decision-maker except that the review body:

- may request information if it would assist the review body

- may allow new information to be submitted to the review body if that information was not reasonably available to the original decision-maker, and
- should have regard to any relevant policies and guidelines of the original decision-maker.

3.233 In part, the purpose of clause 6(5)(c) is to ensure that access providers and access seekers provide all relevant material to the original decision makers.



## 4 Duration, extension and variation of a certification

### Duration

- 4.1 When the Council recommends that a state or territory access regime be certified as effective, it is also required to recommend the period for which certification should remain in force, as per s 44M(5) of the CCA.
- 4.2 A certification remains in force for the duration specified in the Commonwealth Minister's decision, unless the relevant state or territory ceases to be a party to the CPA. There is no mechanism in the CCA for revocation or early termination of a certification, although in some circumstances, certification may no longer protect a service from declaration under Part IIIA (see paragraphs 4.7-4.8).
- 4.3 In general, the Council is aware that infrastructure owners/operators and users have a need for stability and certainty in the regulatory environment, especially in the development of new infrastructure. This suggests relatively lengthy certification periods may be appropriate. At the same time, the Council must consider other factors which may limit the period for which certification is appropriate. For example where an access regime is new and novel, or an industry is undergoing regulatory reform, there may be limited experience of the likely operation and effectiveness of the regime. In such situations the Council would consider whether the regime is a transitional measure and should only be certified for a shorter period of time. Similarly, when considering the duration of certification of a stand-alone state or territory access regime where development of a national approach to access is in the offing, the Council may consider a shortened certification period.
- 4.4 The Council recommended a relatively brief certification period for the New South Wales Rail Regime, given related regulatory developments in interstate rail access. At the time of the Council's recommendation, the likely future interface between the New South Wales Rail Regime and the proposed national regime was unclear (NCC 1999b, pp 25–6).
- 4.5 In its draft recommendation, the Council proposed to recommend a period of certification less than that sought by the applicant for the South Australian Rail Access Regime because the Council had concerns about the scope for periodic review of the regime. Following an undertaking by the South Australian Government to amend the governing legislation, the final recommendation supported certification of the regime for 10 years, as sought by the applicant (NCC 2010c).
- 4.6 In contrast, the Council recommended a long certification period (30 years) for the Northern Territory/South Australian Rail Regime. The regime partly covers an entrepreneurial greenfields project with considerable risk attached (NCC 2000a, pp 96–7).

## **The effect of certification on an application for declaration of a service**

- 4.7 Where an access regime has been certified as an effective access regime, in considering any application for declaration of a service to which the regime applies the Council must follow that decision and consequently not recommend declaration of the service, unless the Council believes there have been substantial modifications to the access regime or the clause 6 principles in the CPA since the regime was certified (s 44G(2)(e)(ii)). Similarly a decision making minister may not declare a service that is subject to a certified state or territory regime unless he or she considers there have been substantial modifications to the access regime or the clause 6 principles in the CPA since the regime was certified (s 44H(4)(e)(ii)).
- 4.8 In practice where state or territory access regimes, or the clause 6 principles, are substantially modified the exemption from declaration arising from certification may cease to operate.

## **Modifying a certified regime**

- 4.9 If a state or territory proposes amending an access regime after it has been certified, it may seek an informal view from the Council as to the ongoing effectiveness of the regime. The Council is not bound by an informal view should, for example, someone apply to have a service that is the subject of the regime declared under Part IIIA.
- 4.10 Where a jurisdiction seeks greater certainty, it may formally apply to the Council for certification of the modified access regime. Alternatively it may seek to have proposed modifications assessed as part of seeking an extension of the time for which the access regime is certified (see paragraphs 4.11–4.12).

## **Extending and varying a certification**

- 4.11 The responsible Minister for the state or territory may apply to the Council asking it to recommend that the Commonwealth Minister extend the period for which a certification is in force (s 44NA of the CCA). In applying, the responsible Minister may also propose variations to the access regime. Applications for extension are typically made when a certification is approaching expiry.
- 4.12 After receiving such an application the Council must assess the effectiveness of the access regime and any proposed variations (see paragraphs 1.12–1.16) and make a recommendation to the Commonwealth Minister on whether or not to extend certification and for how long any extension should be.

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Supreme Court of Western Australia in *Re Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor* [2002] WASCA 231 (23 August 2002)

## **Appendix A : Regulation 6B of the Competition and Consumer Regulations 2010**

### **6B Application to the Council for a recommendation on the effectiveness of an access regime**

An application to the Council under subsection 44M(2) of the Act for a recommendation on the effectiveness of a regime for access to a service must include the following information:

- (a) the name of the State or Territory on whose behalf the application is made;
- (b) the name and designation of the responsible Minister for the State or Territory;
- (c) the name and contact details of a contact officer for the State or Territory;
- (d) the responsible Minister's address for the delivery of documents, including the notification of any decision of the Commonwealth Minister or the Council, relating to the application or the recommendation;
- (e) a description of the access regime (including a copy of any relevant legislation);
- (f) a description of the service;
- (g) grounds in support of the application.