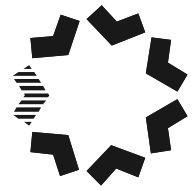


NATIONAL  
COMPETITION  
COUNCIL



## Coverage, revocation and classification of pipelines

A guide to the function and powers  
of the National Competition Council  
under the National Gas Law  
Part B – Coverage, revocation of  
coverage and classification of  
pipelines



**February 2010**

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#### **The National Competition Council**

The National Competition Council was established on 6 November 1995 by the *Competition Policy Reform Act 1995 (Cth)* 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) 9285 7474.

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## **Foreword**

The National Competition Council has preparing a Guide to its functions and powers under the National Gas Law. This guide may be of relevance to parties interested in dealing with the Council under the National Gas Law.

The Guide is in four parts. Each part is available on the Council's website at [www.ncc.gov.au](http://www.ncc.gov.au). The Guide will be updated periodically as required.

Part A examines the rationale for the reform of the national gas access regulatory regime and the passage of the National Gas Law, and provides an overview of the National Gas Law framework. This Part B examines the coverage and classification of pipelines. In particular, this Part looks at the Council's role in making coverage and coverage revocation recommendations, as well as its role in respect of the reclassification of pipelines. Part C of the Guide has been developed to assist and inform on the Council's role in making and revoking light regulation determinations. Part D concerns the Council's functions in making no-coverage recommendations and price regulation exemption recommendations in respect of greenfields pipelines.

## Glossary of terms and abbreviations

Abbreviation	Description
ACCC	Australian Competition and Consumer Commission
Access arrangement	An arrangement setting out the terms and conditions of access to pipeline services provided by means of a pipeline
Australian Energy Market Commission or AEMC	The Australian Energy Market Commission established by s 5 of the <i>Australian Energy Market Commission Establishment Act 2004</i> (SA)
Australian Energy Regulator or AER	The Australian Energy Regulator established by s 44AE of the <i>Trade Practices Act 1974</i> (Cth)
BHP Billiton Iron Ore v NCC	<i>BHP Billiton Iron Ore Pty Ltd v The National Competition Council</i> [2006] FCA 1764 (18 December 2006)
Council or NCC	National Competition Council established by s 29A of the <i>Trade Practices Act 1974</i> (Cth)
Coverage or covered	The status of a pipeline which is, or is deemed to be, the subject of a coverage determination and accordingly subject to economic regulation under the National Gas Law
Duke EGP decision	<i>Re Duke Eastern Gas Pipeline Pty Ltd</i> [2001] ACompT 2 (4 May 2001)
Economies of scale	Economies that occur where the average cost per unit of output decreases as output expands
Economies of scope	Economies that occur where the joint production of two or more products is less costly than producing the products individually
End user	A person who acquires natural gas or proposes to acquire natural gas for consumption purposes
ERA	The Economic Regulation Authority established by s 4 of the <i>Economic Regulation Act 2003</i> (WA)
Expert Panel Report	Expert Panel on Energy Access Pricing, <i>Report to the Ministerial Council on Energy</i> , April 2006
Form of regulation factors	The factors relating to market power set out in s 16 of the National Gas Law
Full regulation or access arrangement regulation	The form of regulation applicable to covered pipelines without a light regulation determination
Gas Code	The National Third party Access Code for Natural Gas Pipeline Systems set out in Schedule 2 to the <i>Gas Pipelines Access (South Australia) Act 1997</i>

Abbreviation	Description
Gas Pipelines Access Law	<i>Gas Pipelines Access (South Australia) Act 1997</i>
Hilmer Report	Report by the Independent Committee of Inquiry into National Competition Policy (Chair: Prof F G Hilmer) 1993
Light Regulation	The form of regulation applicable to a covered pipeline when a light regulation determination of the Council is in force
Limited access arrangement	An access arrangement that is not required to make provision for price or revenue regulation but deals with the matters for which the National Gas Law and the National Gas Rules require provision to be made in an access arrangement
National Competition Council or the Council or NCC	The National Competition Council established by s 29A of the <i>Trade Practices Act 1974</i> (Cth)
National Gas Law or NGL	The Schedule to the <i>National Gas (South Australia) Act 2008</i>
National Gas Objective	The objective set out in s 23 of the National Gas Law
National Gas Rules or Rules	The rules initially made by the South Australian Minister under s 294 of the National Gas Law and include any amendments to the Rules made by the AEMC under the National Gas Law
MCE	The Ministerial Council on Energy established on 8 June 2001, being the Council of Ministers with primary carriage of energy matters at a national level comprising the Ministers representing the Commonwealth, the States, the Australian Capital Territory and the Northern Territory
MCE Decision	The Ministerial Council on Energy, <i>Review of the National Gas Pipelines Access Regime – Decision</i> , May 2006
Part IIIA	Part IIIA of the <i>Trade Practices Act 1974</i> (Cth)
Productivity Commission Report	The Productivity Commission Inquiry Report No. 31, <i>Review of the Gas Access Regime</i> , 11 June 2004
Prospective user	A person who seeks or wishes to be provided with a pipeline service by means of a scheme pipeline
Queensland Wire decision	<i>Queensland Wire Industries Proprietary Limited v. The Broken Hill Proprietary Company Limited and another</i> [1989] HCA 6; (1989) 167 CLR 177 F.C. 89/004
Queuing requirements	Terms and conditions providing for the priority that a prospective user has, as against any other prospective

Abbreviation	Description
	user, to obtain access to spare capacity and developable capacity
Regulations	<i>National Gas (South Australia) Regulations</i> under Part 3 of the <i>National Gas (South Australia) Act 2008</i>
Regulator	AER, other in respect of Western Australian pipelines where it means the ERA
Rules	<i>National Gas Rules 2008</i>
Second Reading Speech	The Speech by the Hon. Mr Conlon, MP on the second reading of the <i>National Gas (South Australia) Bill 2008</i> found in the South Australian Hansard, Legislative Assembly, 9 April 2008, pp 2696-2728
Service provider	The owner, controller or operator of a pipeline
Services Sydney decision	<i>Re Services Sydney Pty Limited</i> [2005] ACompT 7 (21 December 2005)
Sydney Airport decision	<i>Re Review of declaration of freight handling services at Sydney International Airport</i> (2000) ATPR 41-754
Sydney Airport Appeal decision	<i>Re Sydney International Airport</i> [2000] ACompT 1 (1 March 2000)
Trade Practices Act or TPA	<i>Trade Practices Act 1974</i> (Cth)
Tribunal	Australian Competition Tribunal
User	A person who— a. Is a party to a contract with a service provider under which the service provider provides or intends to provide a pipeline service to that person by means of a scheme pipeline; or b. Has a right under an access determination to be provided with a pipeline service by means of a scheme pipeline
Virgin Blue decision	<i>Re Virgin Blue Airlines Pty Limited</i> (including summary and determination) [2005] ACompT 5 (12 December 2005)

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## Version history

Version	Modifications made
February 2010	Minor modifications following the commencement of <i>National Gas Access (WA) Act 2009</i> (WA) and the <i>National Gas (South Australia) (National Gas Law—Australian Energy Market Operator) Amendment Act 2009</i> (SA)
September 2009	Typographical corrections
May 2009	First published

## 1 Overview

- 1.1 The National Gas Law (NGL) is set out in the Schedule to the *National Gas (South Australia) Act 2008* (SA) which commenced on 1 July 2008. It is applied as a law of South Australia by that Act, and as a law of other jurisdictions by their Application Acts.<sup>1</sup>
- 1.2 The National Competition Council (the Council) is the body under the NGL that has the responsibility of recommending whether or not to apply access regulation in respect of a pipeline. This is called the 'coverage' process and pipelines which are subject to access regulation under the NGL are called 'covered pipelines'.
- 1.3 This Part B of the Guide outlines the Council's role in making and revoking coverage determinations under the NGL and seeks to assist parties seeking to cover or revoke coverage of a pipeline and others involved in the Council's consideration of such applications. This Part B also deals with the Council's role in determining whether a pipeline is a transmission pipeline or a distribution pipeline, and the jurisdiction which is most closely connected with a cross-boundary distribution pipeline (called classification).

## Overview of this Part B of the Guide to the National Gas Law

### Section 2, Coverage and classification – policy background

- 1.4 Section 2 sets out the policy background to the coverage and classification regime and outlines what coverage entails. In particular, it sets out the key changes to coverage and classification in the NGL, and other reforms which influence coverage.

### Section 3, Classification

- 1.5 Section 3 sets out how the Council decides to classify pipelines both as transmission or distribution pipelines and also determines which jurisdiction a cross-boundary distribution pipeline is most closely connected. It also sets out the process for reclassifying a pipeline.

### Section 4, Coverage and revocation of coverage overview

- 1.6 Section 4 outlines the common decision making framework that applies to both coverage and revocation of coverage. It also explores what coverage applies to and the concept of covering more or less of the pipeline than is set out in the original application.

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<sup>1</sup> See *National Gas (Queensland) Act 2008* (Qld); *National Gas (New South Wales) Act 2008* (NSW); *National Gas (ACT) Act 2008* (ACT); *National Gas (Victoria) Act 2008* (Vic); *National Gas (Tasmania) Act 2008* (Tas); *National Gas (Northern Territory) Act 2008* (NT); *Australian Energy Market Act 2004* (Cth). Western Australia applied the NGL in its jurisdiction on 1 January 2010 under the *National Gas Access (WA) Act 2009* (WA).

### **Section 5, Principles governing coverage and revocation of coverage**

- 1.7 Section 5 outlines the key decision making criteria for coverage and revocation of coverage – ie, the coverage criteria. It sets out how each of the criteria are to be applied, having regard to the national gas objective.

### **Section 6, Procedural requirements of coverage and revocation of coverage**

- 1.8 Section 6 goes through the procedural requirements relating to coverage and revocation of coverage decisions. In particular, it sets out the requirements for applications, the operation of the standard consultative procedure and the requirements for the Council's recommendations.

### **Section 7, Merits review of coverage decisions**

- 1.9 Section 7 notes the basic merits review rights which apply to coverage and coverage revocation decisions.

### **Section 8, Other issues and jurisdictional differences**

- 1.10 Section 8 outlines the jurisdictional differences to the light regulation framework in Western Australia and Queensland.

## 2 Coverage and Classification – Policy background

- 2.1 The NGL is set out in the Schedule to the *National Gas (South Australia) Act 2008* (SA) which commenced on 1 July 2008. It is applied as a law of South Australia by that Act, and as a law of other jurisdictions by their Application Acts.<sup>2</sup>
- 2.2 The NGL has been developed to reform the governance arrangements for the regulation of national gas pipeline services in Australia. It replaces the Gas Pipelines Access Law (including the Gas Code) which previously regulated pipeline services throughout Australia. Broadly speaking, these reforms separate high level policy direction, economic regulation, rule making and rule enforcement. They are intended to operate so as to encourage efficient investment in gas infrastructure, streamline the rule change process and increase transparency in the gas market. The NGL is modelled on the National Electricity Law.<sup>3</sup> The increased consistency between electricity and gas regulation is expected to strengthen the national character of the governance and economic regulation of the energy sector.<sup>4</sup>

### Reform of the gas access regime

- 2.3 The NGL, while replicating many aspects of the Gas Pipelines Access Law, does include a number of new aspects. The revised regime was the outcome of a number of reviews and Ministerial decisions including:
- Productivity Commission Inquiry Report No. 31, Review of the Gas Access Regime, 11 June 2004 (the Productivity Commission Report)
  - Expert Panel on Energy Access Pricing, Report to the Ministerial Council on Energy, April 2006 (the Expert Panel Report), and
  - Ministerial Council on Energy, Review of the National Gas Pipelines Access Regime – Decision May 2006 (the MCE Decision).
- 2.4 This policy background is recognised in the Second Reading Speech for the *National Gas (South Australia) Bill 2008*<sup>5</sup> (the Second Reading Speech). The Second Reading Speech sets out the following in relation to classification and coverage:

#### Coverage of pipelines

The National Gas Law retains the structure of the Gas Code where economic regulation is only applied to covered pipelines which exhibit a level of market

<sup>2</sup> See *National Gas (Queensland) Act 2008* (Qld); *National Gas (New South Wales) Act 2008* (NSW); *National Gas (ACT) Act 2008* (ACT); *National Gas (Victoria) Act 2008* (Vic); *National Gas (Tasmania) Act 2008* (Tas); *National Gas (Northern Territory) Act 2008* (NT); *National Gas Access (WA) Act 2009* (WA); *Australian Energy Market Act 2004* (Cth).

<sup>3</sup> The National Electricity Law is set out in the Schedule to the *National Electricity (South Australia) Act 1996* (SA).

<sup>4</sup> See generally the Second Reading Speech for the *National Gas (South Australia) Bill 2008*, Parliament of South Australia, Hansard, 12 June 2008 and clause 2.1 of the Australian Energy Market Agreement 2004 as amended in 2006 (AEMA).

power where the benefits of regulation outweigh the costs. Coverage of pipelines is a process for determining whether or not economic regulation should or should not be applied to the services provided by a particular pipeline. This decision is made by the relevant State or Commonwealth Minister, on the recommendation of the National Competition Council. The decision of whether or not to regulate is based upon whether the pipeline coverage criteria are satisfied. Consistent with the current Gas Code, a coverage decision may apply to more or less of the pipeline than is the subject of the application or recommendation.

The Gas Code coverage criteria have been amended in response to the Productivity Commission Review of the Gas Access Regime such that a 'material' increase in competition in at least one market is required before coverage should be applied. This, consistent with similar amendments to Part IIIA of the Trade Practices Act, ensures that the increase in competition needs to be non trivial before regulation is imposed.

The National Gas Law does not apply economic regulation to pipelines that do not meet the coverage criteria. Any person can apply to bring a pipeline under the regime or for a pipeline to become uncovered at any time, unless the pipeline has been granted a greenfields pipeline incentive.

This Bill streamlines the pipeline classification and coverage process. Under the National Gas Law, classification and coverage will be dealt with simultaneously. In this process the National Competition Council will make draft and final recommendations on coverage at the same time as making draft and final decisions on the classification of the pipeline. That final classification decision will therefore determine who is to be the relevant Minister for making the decision on whether the pipeline should be covered or uncovered under the regime. As in the Gas Pipelines Access Law, the relevant Minister so determined will make the final coverage determination based on the advice of the National Competition Council.<sup>6</sup>

2.5 Particular reforms are further highlighted below.

## **National gas objective**

2.6 A centre piece of the NGL is the national gas objective which is set out in s 23:

The objective of this Law is to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.

2.7 In the MCE Decision, the MCE indicated that the inclusion of the national gas objective is intended to clarify the policy intent of the regime; to guide and improve the accountability of all decision makers; provide greater certainty to service

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<sup>5</sup> South Australian Hansard, Legislative Assembly, 9 April 2008, pp 2696 - 2728.

<sup>6</sup> See Second Reading Speech, South Australian Hansard, Legislative Assembly, 9 April 2008, pp 2889.

providers and access seekers about possible regulatory intervention; and promote national consistency (both across jurisdictions and between access regimes). Further, the consistency achieved between the national gas objective and the national electricity objective, contained in the National Electricity Law, is intended to promote a seamless approach to energy access across the energy sector.<sup>7</sup>

## Classification of pipelines

- 2.8 The NGL applies to pipelines for the haulage of natural gas which is of consumption quality.<sup>8</sup> Pipelines are further classified into transmission pipelines whose primary function is to convey gas to a market and distribution pipelines whose primary function is to reticulate gas within a market.<sup>9</sup> The classification of a pipeline affects some of the obligations to which the service provider of the pipeline is subject and who is the relevant Minister to determine whether the pipeline should be regulated (ie covered).
- 2.9 The classification of pipelines was previously a function conferred upon Ministers with a detailed dispute resolution process in light of disagreement.<sup>10</sup> It also operated before a formal coverage process. As stated in the Second Reading Speech, in the reform of NGL it was decided to streamline the coverage and classification process so that they are dealt with simultaneously. To simplify the process the classification decision was accordingly conferred upon the Council. The classification criteria, however, have been replicated in the NGL and the previous classification of pipelines under the Gas Code has been preserved by clauses 6 and 7 of Schedule 3 to the NGL. Service providers may apply to reclassify their pipeline.<sup>11</sup>

## Regulation of covered pipelines

- 2.10 Like the Gas Pipelines Access Law before it, the NGL only applies economic regulation/third party access to 'covered pipelines'. These are pipelines which meet the coverage criteria<sup>12</sup> which in effect mirror the declaration criteria in Part IIIA of the *Trade Practices Act 1974* (Cth) (TPA). Under the NGL a pipeline may be a covered pipeline in a number of ways. In particular:

<sup>7</sup> See Ministerial Council on Energy, *Review of the National Gas Pipelines Access Regime – Decision May 2006* at p 7.

<sup>8</sup> See definitions of pipeline and natural gas in s 2. Note also that s 6A of the *National Gas Access (WA) Act 2009* (WA) allows the Western Australian law to extend to LPG distribution systems as well as natural gas.

<sup>9</sup> See the classification criteria in s 13 of the NGL.

<sup>10</sup> See ss 10 - 12 of the Gas Pipelines Access Law.

<sup>11</sup> See Part 5 of Chapter 3 of the NGL.

<sup>12</sup> See s 15 of the NGL and section 5 of this Part B of the Guide.

- (a) pipelines which were covered pipelines under the Gas Code have been deemed by items 5, 6 and 7 of Schedule 3 of the NGL to be covered pipelines under the NGL (with some exceptions in Queensland)<sup>13</sup>
- (b) any person may apply to the Council for the coverage of a particular pipeline under s 92 of the NGL and the relevant Minister<sup>14</sup> will make a decision on that application to cover or not cover the pipeline by applying the coverage criteria and having regard to a recommendation from the Council (ss 99 and 100)<sup>15</sup>
- (c) a pipeline will be covered where a service provider has been awarded a tender to construct and operate a pipeline as a result of a tender approval process which was approved under the National Gas Rules (s 126),<sup>16</sup> or
- (d) a pipeline will be covered where a service provider voluntarily submits a full access arrangement to the regulator and the regulator makes or approves that voluntary access arrangement (s 127).

2.11 Any person may apply to the Council to revoke the coverage of all or part of a pipeline at any point in time (s 102). As with coverage applications, the Council makes a recommendation to the relevant Minister who decides whether or not to revoke coverage. Pipelines covered as part of a tender process or through voluntary submission of an access arrangement become uncovered on the expiry of their access arrangements,<sup>17</sup> but all other pipelines remain covered until a coverage revocation determination is made under s 106 of the NGL.

2.12 The coverage criteria were also looked at in the reviews and affirmed as appropriate for the regulation of gas pipelines. As noted in the Second Reading Speech, the one change that was made between the Gas Pipelines Access Law and NGL was to add the words 'a material increase' into the first criterion (criterion (a)) consistent with an

<sup>13</sup> Note that a number of pipelines remain covered pipelines in light of their original inclusion in Schedule A to the Gas Code and accordingly have never had the coverage criteria independently applied to them. All of these pipelines are eligible to apply for revocation of coverage.

<sup>14</sup> The relevant Minister is the Commonwealth Minister for both cross-boundary transmission pipelines and transmission pipelines in New South Wales, Queensland, Victoria, Tasmania, Australian Capital Territory and Northern Territory and the local State Minister in all other circumstances.

<sup>15</sup> The exception is that pipelines which have been awarded a greenfields pipeline incentive (ie a 15-year no-coverage determination or a price regulation exemption under Chapter 5 of the NGL) may not be covered until the end of their exemption period (see s 158(2) and s 167(4)).

<sup>16</sup> Note that coverage through a competitive tendering process was previously recognised under the Gas Code (ss 3.21 - 3.36) and a modified version of this is now in s 126 of the NGL and Part 5 of the National Gas Rules.

<sup>17</sup> See ss 126(2) and 127(2).

equivalent amendment to the declaration criteria in Part IIIA of the TPA.<sup>18</sup> The streamlining of the coverage and classification process has also had consequences for the timelines and process of arriving at a coverage recommendation. Consistent with Part IIIA of the TPA, coverage decision makers also need to have regard to the objective<sup>19</sup> of the legislation in making their decisions.

## Two forms of regulation – light and full

- 2.13 A key change to gas regulation is that a light regulation regime has been introduced so that not all covered pipelines will necessarily be subject to 'full' regulation under the access arrangement process. Rather, eligible pipeline service providers, operating covered pipelines, will be able to apply for a 'light regulation determination' to avoid the upfront setting of reference tariffs (price regulation) under the access arrangement process.
- 2.14 This new regime is intended to implement a number of key policy considerations common to both the Productivity Commission Report and Expert Panel Report. The principal concern under the NGL is to ensure that the form of regulation is proportionate to the degree of market power that is involved.<sup>20</sup> Costly forms of regulation should be adopted only where there is the potential for significant inefficiencies to arise from the exploitation of market power.<sup>21</sup>
- 2.15 Nonetheless, full regulation (coverage) remains an option under the NGL. Where full regulation (coverage) applies, the access arrangement process involves direct control being imposed on the prices and related terms and conditions of service supply, through upfront regulatory processes. This form of regulation often leads to significant administrative costs to the regulated service provider and the regulator. Direct regulation in this manner is still considered to be an appropriate form of regulation in cases where significant market power is possessed by the pipeline service provider.<sup>22</sup>

## Bulletin Board

- 2.16 The NGL also includes provision for a Natural Gas Services Bulletin Board (in Chapter 7 of the NGL).<sup>23</sup> The objective of the Bulletin Board is to facilitate trade in gas and capacity over the relevant pipeline systems through the provision of system and

<sup>18</sup> See item 16 of Schedule 1 to the *Trade Practices Amendment (National Access Regime) Act 2006 (Cth)*.

<sup>19</sup> The National Gas Objective in s 23 of the NGL.

<sup>20</sup> Expert Panel Report p 44.

<sup>21</sup> Ibid.

<sup>22</sup> Ibid pp 44 - 45.

<sup>23</sup> Note that the Bulletin Board does not currently apply in Western Australia in accordance with clause 5 of Schedule 1 to the *National Gas Access (WA) Act 2009 (WA)*.

market information. The requirements apply to transmission pipelines irrespective of whether or not they are covered pipelines.<sup>24</sup>

## Key features of regulatory arrangements for covered pipelines

- 2.17 It is important to understand the regulatory framework that applies to a pipeline if a coverage determination is made compared to pipelines which are not covered. Many obligations of the regime are common for light regulation and full regulation pipelines, with the requirement to submit a full access arrangement being the key difference between the forms of regulation. These obligations fall primarily on the 'service provider' of the pipeline who is any person who owns, controls or operates the pipeline.<sup>25</sup> Where the service provider is a group s 10 of the NGL allows one service provider of the group to comply with the NGL on behalf of the other persons in the service provider group.
- 2.18 The primary requirements for a service provider of a covered pipeline are as follows:
- (a) subject to general duties (i.e. must be a specified legal entity (s 131), must not engage in conduct to prevent or hinder access (s 133) and obliged to disclose gas supply information in certain circumstances (r 138))
  - (b) subject to 'ring-fencing' requirements including:
    - (i) not carrying on a related business (s 139)
    - (ii) keeping marketing staff separate from associate's related businesses (s 140)
    - (iii) keeping consolidated and separate accounts (s 141)
    - (iv) keeping sensitive information confidential (r 137)
  - (c) controls over contracts with associates which are likely to substantially lessen competition in a market for natural gas services or breach the competitive parity rule (ss 147 and 148)
  - (d) subject to particular rules relating to facilitating requests for access and information disclosure (e.g. rr 107 - 112)
  - (e) subject to the access dispute process in Chapter 6 of the NGL whereby the dispute resolution body (usually the AER)<sup>26</sup> may make a determination regarding any aspect of access to pipeline services provided by means of the covered pipeline
  - (f) must comply with queuing requirements in an approved access arrangement (s 135)<sup>27</sup>

<sup>24</sup> See Bulletin Board.

<sup>25</sup> Section 8 of the NGL.

<sup>26</sup> Other than in Western Australia where the Energy Disputes Arbitrator will perform this function.

<sup>27</sup> Note a light regulation pipeline may not have a limited access arrangement and so this provision would not apply in that situation.

- (g) subject to any regulatory information instrument about information reporting (s 48),<sup>28</sup> and
- (h) must, unless an exempt distribution network, maintain a register of spare capacity on its website (r 111).

2.19 A service provider of a full regulation (covered) pipeline must also:

- (a) submit and have in force a full access arrangement which sets out the terms and conditions of access and reference tariffs for services likely to be sought by a significant part of the market (s 132). Importantly:
  - (i) non-price conditions are subject to approval by the regulator, including capacity trading requirements, changes of receipt and delivery points, extension and expansion requirements and queuing requirements (rr 103 - 106)
  - (ii) total revenue is to be set by the regulator taking into account the revenue and pricing principles (ss 24 and 28) and using the building blocks approach to economic regulation (r 76)
  - (iii) an access arrangement is likely to include an annual approval/compliance process (r 97), and
  - (iv) access arrangements need to be accompanied by access arrangement information (rr 42 - 43 and 72).

2.20 Service providers of light regulation pipelines do not need to submit an access arrangement but:

- (a) may submit a limited access arrangement dealing with non-price matters (s 116)
- (b) are prohibited from engaging in price discrimination unless that discrimination is conducive to efficient service provision (s 136)
- (c) must report annually to the regulator on access negotiations (r 37), and
- (d) must publish terms and conditions of access, including prices on offer, on its website (r 36).

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<sup>28</sup> Note also that in November 2008 the AER released its Annual Compliance Guideline which deals with the annual compliance information to be provided to the AER under the NGL and Rules (see [www.aer.gov.au](http://www.aer.gov.au)).

- 2.21 Note also that apart from the enforcement of access arrangements in access disputes (s 189), a number of the obligations are also enforceable by the regulator as civil penalties and by other parties as conduct provisions.<sup>29</sup>
- 2.22 Pipelines covered as part of a tender process under s 126 of the NGL are regulated like other pipelines on an access arrangement, but the content of their access arrangements and variation process does not need to comply with the ordinary rules in Parts 8, 9 and 10 of the National Gas Rules (see r 29). This is on the basis that competition for the market in question has produced an efficient access outcome for the initial customers of the pipeline (i.e. until the expiry of that arrangement when third parties can apply to re-cover the pipeline if they feel it meets the coverage criteria).

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<sup>29</sup> The NGL and *National Gas (South Australia) Regulations 2008* prescribe ss 56, 57, 91BE(1), 91BF(1), 91BJ(1), 91BN(5), 91FC(3) & (4), 91LB(1), 91MB(6), 131, 133, 134, 135, 136, 139, 140, 141, 143(6), 147, 148, 168, 169(3), 170, 195, 223 and 225 and rr 27(4), 33(1), 36, 37, 43(1), 46, 52(1), 53(6), 107, 108, 109, 110, 111, 112, 135CE(2), 137, 138, 138A(2) and 138A(4) as civil penalties and ss 91AB, 133, 134, 135, 136, 147, 148 and 170 and rr 33(1), 36, 107, 108, 109, 110, 111, 112, 115(3), 137, 138 and 138AC as conduct provisions.

### 3 Classification

- 3.1 The following table is a short overview of the key legislative provisions relevant to the Council's function of classifying pipelines, which are expanded upon below.

**Table 3-1 Key provisions relating to classification**

Section 92 applications	Any person can apply to cover a pipeline. Application dealt with in accordance with the Rules (s 93 and Part 4 of the Rules).
Section 98 decision	The Council decides whether pipeline is transmission or distribution as part of coverage recommendation, whether the pipeline is a cross-boundary pipeline and, if it is a cross-boundary distribution pipeline, which jurisdiction the pipeline is most closely connected with. Applies criteria in ss 13 and 14 of the NGL.
Part 5 of Chapter 3	Allows a service provider to apply to reclassify a pipeline and for the Council to consider such applications. (See also Part 14 of the Rules.)
Rule 26 (tender)	The Council to classify a pipeline the subject of an irrevocable tender approval decision.
Rule 47 (voluntary)	The Council to classify a pipeline which submits a voluntary access arrangement.

- 3.2 The NGL applies to pipelines for the haulage of natural gas which is of consumption quality. This is because pipeline is defined in s 2 of the NGL as follows:

***pipeline*** means—

- (a) a pipe or system of pipes for the haulage of natural gas, and any tanks, reservoirs, machinery or equipment directly attached to that pipe or system of pipes; or
- (b) a proposed pipe or system of pipes for the haulage of natural gas, and any proposed tanks, reservoirs, machinery or equipment proposed to be directly attached to the proposed pipe or system of pipes; or
- (c) a part of a pipe or system of pipes or proposed pipe or system of pipes referred to in paragraph (a) or (b),

but does not include—

- (d) unless paragraph (e) applies, anything upstream of a prescribed exit flange on a pipeline conveying natural gas from a prescribed gas processing plant; or
- (e) if a connection point upstream of an exit flange on such a pipeline is prescribed, anything upstream of that point; or

- (f) a gathering system operated as part of an upstream producing operation; or
- (g) any tanks, reservoirs, machinery or equipment used to remove or add components to or change natural gas (other than odourisation facilities) such as a gas processing plant; or
- (h) anything downstream of a point on a pipeline from which a person takes natural gas for consumption purposes;

3.3 Natural gas is defined in s 2 as:

**natural gas** means a substance that—

- (a) is in a gaseous state at standard temperature and pressure; and
- (b) consists of naturally occurring hydrocarbons, or a naturally occurring mixture of hydrocarbons and non-hydrocarbons, the principal constituent of which is methane; and
- (c) is suitable for consumption;

3.4 The specific exclusions in paragraphs (d) and (e) of the definition of a pipeline can be found in r 5 and Schedule 2 to the *National Gas (South Australia) Regulations 2008*.

3.5 From these definitions it is clear that 'wet'/unprocessed gas pipelines, processing facilities, upstream gathering lines and pipes downstream of an end user's connection point are not included in the definition of a pipeline and accordingly cannot be 'covered' by the NGL. However, the definition of 'consumption' quality gas would include gas that is fit to be consumed by industrial facilities but does not meet specifications for residential use.<sup>30</sup>

3.6 It is also important to note that 'proposed' pipelines are covered by paragraph (b) and the wording in paragraph (c). This means that applications for coverage can be made in respect of pipeline projects which are proposed and not yet complete.

3.7 Additionally, s 6A of the *National Gas Access (WA) Act 2009* allows the Western Australian law to extend to LPG distribution systems as well as natural gas.

## Coverage and the classification process

3.8 When a person applies under s 92 for a determination that a pipeline be a covered pipeline, the Council needs to classify that pipeline:

- (a) to determine whether it is a transmission or distribution pipeline (as slightly different obligations apply in each case), and
- (b) to determine the relevant Minister who will make the coverage determination in question.

<sup>30</sup> Reading the word 'consumption' down to only include residential quality gas would narrow the application of the legislation in a manner inconsistent with its objective.

3.9 Subrule 15(1)(c) requires that any application for coverage under s 92:

give details of the pipeline's classification or, if there is no classification, the classification the applicant considers appropriate;

3.10 The pipeline may have been previously classified under the NGL or Gas Pipelines Access Law and this should be specified in the application. Otherwise, the applicant should express a view on the classification of the pipeline having regard to the Council's role in making an initial classification decision in s 98 of the NGL.

3.11 As the classification decision must be made at the same time as a coverage recommendation (s 98(1)) it follows the same process as the coverage recommendation. Accordingly, consultation is conducted in accordance with the standard consultative procedure (r 16(1)) and must be completed within 4 months after receiving the application (r 16(2)).<sup>31</sup>

### Classification decisions

3.12 Section 98 governs the making of classification decisions by the Council.

#### **98—Initial classification decision to be made as part of recommendation**

- (1) The NCC must, as part of a coverage recommendation, classify the pipeline the subject of an application under section 92 as a transmission pipeline or a distribution pipeline (an *initial classification decision*). In doing so, the NCC must apply the pipeline classification criterion.
- (2) The NCC must as part of an initial classification decision—
  - (a) if it classifies the pipeline the subject of the application as a transmission pipeline—determine whether the transmission pipeline is also a cross boundary transmission pipeline;
  - (b) if it classifies the pipeline the subject of the application as a distribution pipeline—determine whether the distribution pipeline is also a cross boundary distribution pipeline.
- (3) The NCC must also determine, as part of an initial classification decision, the participating jurisdiction with which the pipeline the subject of the application under section 92 is most closely connected if the NCC determines the pipeline is also a cross boundary distribution pipeline. In doing so, the NCC must apply the jurisdictional determination criteria]

3.13 As is evident from the section, classification is focused upon:

- (a) determining whether the pipeline is a transmission or distribution pipelines by applying the pipeline classification criteria in s 13 of the NGL
- (b) determining whether the pipeline is a cross-boundary pipeline, and
- (c) determining the jurisdiction which is most closely connected with a cross boundary distribution pipeline by applying the criteria in s 14 of the NGL.

<sup>31</sup> Subject to stop the clock provisions in r 11, extensions of time in rr 12 and 16(3) and r 14 which provide that late decisions are still valid decisions.

## Transmission or distribution

3.14 The pipeline classification criterion is set out in s 13 as follows:

### 13—Pipeline classification criterion

- (1) The pipeline classification criterion is whether the primary function of the pipeline is to—
  - (a) reticulate gas within a market (which is the primary function of a distribution pipeline); or
  - (b) convey gas to a market (which is the primary function of a transmission pipeline).
- (2) Without limiting subsection (1), in determining the primary function of the pipeline, regard must also be had to whether the characteristics of the pipeline are those of a transmission pipeline or distribution pipeline having regard to—
  - (a) the characteristics and classification of, as the case requires, an old scheme transmission pipeline or an old scheme distribution pipeline;
  - (b) the characteristics of, as the case requires, a transmission pipeline or a distribution pipeline classified under this Law;
  - (c) the characteristics and classification of pipelines specified in the Rules (if any);
  - (d) the diameter of the pipeline;
  - (e) the pressure at which the pipeline is or will be designed to operate;
  - (f) the number of points at which gas can or will be injected into the pipeline;
  - (g) the extent of the area served or to be served by the pipeline;
  - (h) the pipeline's linear or dendritic configuration.

3.15 Accordingly, transmission pipelines are those whose primary function is to convey gas to a market and distribution pipelines are those whose primary function is to reticulate gas within a market. Particular regard is to be had to the current classifications of existing pipelines (both under the Gas Code and NGL) to ensure consistent treatment. The information contained within Schedule A of the Gas Code may be instructive in this regard and also information on transmission pipelines published on the Natural Gas Services Bulletin Board.

3.16 The Council notes that the words 'without limiting subsection (1)' in s 13(2) make it clear that the primary function test is the main basis for classification. The factors in s 13(2) can be informative, but are not determinative. For instance, transmission pipelines will generally have a larger diameter, use higher pressure, have fewer injection points, serve a range of separate markets and operate in a linear manner. However, transmission pipelines can also be small (e.g. Dawson Valley) and have a

range of off take points (e.g. Victorian Principal Transmission System). Accordingly the Council will balance the factors in s 13(2) in assisting it when applying the primary test in s 13(1).

- 3.17 As mentioned earlier, the classification of pipelines under the Gas Pipelines Access Law are preserved by clause 6 and 7 of Schedule 3 to the NGL. Additionally, r 3(4) of the *National Gas (Queensland) Regulation 2008* deems the Carpentaria pipeline to be a covered transmission pipeline.

### Impact of classification decision - obligations

- 3.18 The NGL applies in a similar way to both transmission and distribution pipelines. However, there are a couple of differences which are dependent upon classification:
- (a) only transmission pipelines are subject to the National Gas Services Bulletin Board requirements
  - (b) applications to seek light regulation or revoke coverage need to contain slightly different information about the area served by the pipeline (rr 18(2)(b) and (c) and 34(2)(b) and (c))
  - (c) access arrangement information on pipeline usage is different (rr 72(1)(a)(iii))
  - (d) the tariff arrangements and requirements are different (see r 95 for distribution pipelines which reflects the electricity distribution pricing rules, and r 96 for transmission pipelines which reflects the arrangements in the Gas Code), and
  - (e) queuing requirements and public registers of spare capacity for distribution pipelines are only required when the regulator determines they are necessary (rr 103 and 111 respectively).

### Cross-boundary pipelines

- 3.19 The decision on whether a pipeline is a cross-boundary pipeline is purely a matter of fact. However, it should be remembered that for the purpose of the NGL the Commonwealth offshore area (generally starting from 3 nautical miles from the coast and extending to the limits of Australia's exclusive economic zone) is another jurisdiction and so a pipeline which starts in the offshore area will be a cross-boundary pipeline.
- 3.20 The exception is Western Australia. Subsection 3(1) of the *Australian Energy Market Act 2004* (Cth) provides that an offshore Western Australian pipeline is defined as follows:

**"offshore Western Australian pipeline"** means a pipeline (within the meaning of the National Gas (Commonwealth) Law) for transporting natural gas from one or more points of origination in the offshore area of Western Australia to one or more points of termination in:

- (a) Western Australia; or

(b) the coastal waters of Western Australia;

but does not include a pipeline any part of which is situated in another State or in a Territory.

3.21 Section 11J of the *Australian Energy Market Act 2004* (Cth) then applies the Western Australian National Gas Access (Western Australia) Law to offshore Western Australian pipelines as follows:

(1) The National Gas Access (Western Australia) Law (within the meaning of the *National Gas Access (WA) Act 2009* of Western Australia) as in force from time to time:

(a) applies as a law of the Commonwealth in relation to so much of an offshore Western Australian pipeline as is situated in the offshore area of Western Australia; and

(b) so applying may be referred to as the *Offshore Western Australian Pipelines (Commonwealth) Law*.

3.22 Further to this provision, clause 9(2) of the *National Gas Access (WA) Act 2009* provides that:

A pipeline that is an offshore Western Australian pipeline as defined in section 3(1) of the *Australian Energy Market Act 2004* of the Commonwealth is to be regarded as being situated wholly within Western Australia for the purpose of determining who the relevant Minister is under the National Gas Access (Western Australia) Law.

3.23 Accordingly, a pipeline which begins in the offshore area of Western Australia and ends in Western Australia or the coastal waters of Western Australia will not be a cross-boundary pipeline and the Western Australian Minister will be the relevant Minister for determining the coverage of that pipeline.

### **Most closely connected jurisdictions**

3.24 For cross-boundary distribution pipelines it is necessary to work out which jurisdiction the pipeline is most closely connected with. The criteria for this are set out in s 14:

#### **14 Jurisdictional determination criteria—cross boundary distribution pipelines**

The pipeline jurisdictional determination criteria are—

(a) whether more gas is to be delivered by a cross boundary distribution pipeline in the jurisdictional area of 1 participating jurisdiction than in the jurisdictional area of any other participating jurisdiction;

(b) whether more customers to be served by a cross boundary distribution pipeline are resident in the jurisdictional area of 1 participating jurisdiction than in the jurisdictional area of any other participating jurisdiction;

- (c) whether more of the network for a cross boundary distribution pipeline is in the jurisdictional area of 1 participating jurisdiction than in the jurisdictional area of any other participating jurisdiction;
- (d) whether 1 participating jurisdiction has greater prospects for growth in the gas market served or to be served by a cross boundary distribution pipeline than any other participating jurisdiction;
- (e) whether the regional economic benefits from competition are likely to be greater for 1 participating jurisdiction than for any other participating jurisdiction.

3.25 Under the Gas Pipelines Access Law, the Tweed Heads distribution network was determined to be more closely connected with Queensland and the Albury network more closely connected with Victoria. These determinations have been transitioned into the new regime by clause 53 of Schedule 3 of the NGL.

### Relevant Minister

3.26 One of the primary reasons to classify a pipeline is to determine who should be the relevant Minister to determine the coverage or revocation application. The term relevant Minister is defined in s 2 of the NGL as follows:

**relevant Minister** means if, in a coverage recommendation, no-coverage recommendation, classification decision under the Rules or reclassification decision, the NCC determines the pipeline is—

- (a) a cross boundary transmission pipeline—the Commonwealth Minister;
- (b) a transmission pipeline situated wholly within a participating jurisdiction—the designated Minister;

Note—

The term designated Minister is defined in the Act of this jurisdiction that applies this Law as a law of this jurisdiction.

- (c) a distribution pipeline situated wholly within a participating jurisdiction—the Minister of the participating jurisdiction;
- (d) a cross boundary distribution pipeline—the Minister of the participating jurisdiction determined by the NCC in the recommendation as being the participating jurisdiction with which the cross boundary distribution pipeline is most closely connected;

3.27 The term 'Commonwealth Minister' is defined as:

**Commonwealth Minister** means the Minister of the Commonwealth administering the *Australian Energy Market Act 2004* of the Commonwealth;

3.28 The term 'designated Minister' is defined in the NSW, ACT, Queensland, Victoria, Tasmania and NT application Acts as the Commonwealth Minister. In South Australia and Western Australia the local State Minister is the designated Minister. Accordingly, the allocation of responsibilities can be summarised as follows:

**Table 3-2: 'designated Minister'**

Commonwealth Minister	Cross-boundary transmission pipelines and transmission pipelines wholly within NSW, ACT, Queensland, Victoria, Tasmania and NT.
South Australian and Western Australian Ministers	Transmission <sup>32</sup> and distribution pipelines within their jurisdiction and cross-boundary distribution pipelines most closely connected with it.
NSW, ACT, Queensland, Victoria, Tasmania and NT State/Territory Ministers	Distribution pipelines within their jurisdiction or most closely connected with it.

## Reclassification

- 3.29 Part 5 of Chapter 3 of the NGL allows a service provider of a pipeline which has already been classified to have their pipeline reclassified. An application must:
- identify the pipeline to which the application relates, and
  - specify the nature of the reclassification sought by the applicant, and
  - demonstrate that the reclassification would be consistent with the pipeline classification criterion, and
  - include, or be accompanied by, any further information or materials on which the applicant relies in support of the application.<sup>33</sup>
- 3.30 Accordingly, an applicant should provide the current technical and market information for the pipeline to address the matters that need to be considered under the pipeline classification criterion (ie markets served, pipeline diameter, injection/off-take points, pressure, configuration).
- 3.31 The Regulations prescribe that applications also need to be accompanied by a \$2000 application fee.<sup>34</sup> The fee must be paid by cheque at the time an application is lodged with the Council. Cheques are to be made payable to the National Competition Council.
- 3.32 Under r 132(1) the Council must deal with applications for reclassification in accordance with the expedited consultative procedure whereby:

<sup>32</sup> Note the earlier statement that pipelines within the offshore area of Western Australia and which do not extend into South Australia or the Northern Territory are deemed to be Western Australian pipelines rather than cross-boundary pipelines.

<sup>33</sup> Rule 131.

<sup>34</sup> Regulation 14 and Schedule 5 of the *National Gas (South Australia) Regulations 2008*. Fees under the NGL are prescribed by *A New Tax System (Goods and Services Tax) (Exempt Taxes, Fees and Charges) Determination 2008 (No.2)* to not be consideration for a supply pursuant to *A New Tax System (Goods and Services Tax) Act 1999*. Refer subsection 81-5(2) of *A New Tax System (Goods and Services Tax) Act 1999*.

- (a) the [Council] must, after such consultation (if any) as the decision maker considers appropriate (and any revision of the proposal that results from that consultation), make a draft decision, and
- (b) the [Council] must give copies of the draft decision to the parties to the administrative process in which the decision is to be made, and
- (c) the [Council] must publish, on its website and in any other way the decision maker considers appropriate, the draft decision together with a notice:
  - (i) stating why the decision is required, and
  - (ii) giving reasonable details of the context in which the draft decision has been made, the issues involved and the possible effects of the decision, and
  - (iii) inviting written submissions and comments on the draft decision within 15 business days from the date of the notice;
- (d) the [Council] must, within 20 business days after the end of the period allowed for making submissions and comments on the draft decision, consider all submissions and comments made within the time allowed and make its final decision.<sup>35</sup>

3.33 The Council's decision must:

- (a) be in writing, and
- (b) identify the pipeline to which the decision relates, and
- (c) include a reference to a website at which a description of the pipeline can be inspected, and
- (d) state the terms of the decision and the reasons for it.<sup>36</sup>

3.34 The criteria for the Council's decision in s 129 of the NGL replicate the decision making criteria in s 98. However, one additional criterion is that the Council must also have regard to the national gas objective. In taking the national gas objective into account the Council may consider whether the change in classification is likely to have any effects on the efficiency of pipeline access or the operation of gas markets through changing the obligations to which the pipeline's service provider is subject.<sup>37</sup> Accordingly, where a change in pipeline classification diminishes the rights of third parties in a manner inconsistent with the national gas objective, the Council may refuse to reclassify the pipeline.

3.35 The Council's decision must be delivered to the service provider and other parties involved in the Council's consideration of the issue, published on the Council's website and made available for inspection during business hours at the Council's

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<sup>35</sup> Rule 9(2).

<sup>36</sup> See rr 132(3) and 8(3).

<sup>37</sup> See paragraph 3.18 above.

office.<sup>38</sup> In accordance with s 130 of the NGL, the reclassification takes effect on the day that it is made.<sup>39</sup>

### **Classification where tender approval becomes irrevocable**

3.36 After a tender approval process has been reviewed by the regulator and it becomes irrevocable, the regulator must refer the proposed pipeline to the Council for a classification decision in accordance with the pipeline classification criterion.<sup>40</sup> The regulator must then assist the Council with information to allow the Council to classify the pipeline.<sup>41</sup> The Council must notify the regulator and the AEMC of the decision it makes. In making such a decision the Council is not required to consult, but may choose to consider the views of interested stakeholders if the classification is not straightforward.

### **Classification where submission of voluntary access arrangement**

3.37 Similarly with tender approval pipelines, when a voluntary access arrangement is submitted, the regulator must refer the pipeline to the Council for classification in accordance with the pipeline classification criterion and give the Council the relevant application.<sup>42</sup> There is also no necessity for consultation for these decisions and the decision must be given to the regulator and the AEMC. However, if the service provider withdraws their voluntary access arrangement before it is approved the Council's classification decision lapses.<sup>43</sup>

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<sup>38</sup> See r 9(4).

<sup>39</sup> Note that s 130 of the NGL overrides r 9(5) in this regard.

<sup>40</sup> See r 26(1).

<sup>41</sup> See r 26(2).

<sup>42</sup> See r 47(3)(b)

<sup>43</sup> See r 47(6)(b).

## 4 Coverage and revocation of coverage - overview

4.1 Part 1 of Chapter 3 of the NGL provides for the coverage and revocation of coverage of a pipeline.<sup>44</sup> The following table is a short overview of the key legislative provisions relevant to the applications for coverage and revocation of coverage, which are expanded upon below.

**Table 4-1 Key provisions relating to coverage**

<b>Key provisions relating to coverage (Part 1, Chapter 3 of the NGL)</b>	
<b><u>Division 1 - Coverage determinations</u></b>	
<b>Section 92 applications</b>	Any person can apply to cover a pipeline. Application dealt with in accordance with the Rules (s 93 and Part 4 of the Rules). Potential for deferral where concurrent tendering process (ss 94 and 96).
<b>Section 95 recommendation</b>	The Council makes a coverage recommendation giving effect to the coverage criteria and having regard to the national gas objective (s 97).
<b>Section 99 decision</b>	The relevant Minister makes a final decision on the application applying the same criteria as the Council (s 100).
<b><u>Division 2 - Coverage revocation determinations</u></b>	
<b>Section 102 applications</b>	Any person can apply to revoke the coverage of a pipeline. Application dealt with in accordance with the Rules (s 103 and Part 4 of the Rules).
<b>Section 104 recommendation</b>	The Council makes a coverage recommendation giving effect to the coverage criteria and having regard to the national gas objective (s 105).
<b>Section 106 decision</b>	The relevant Minister makes a final decision on the application applying the same criteria as the Council (s 100).

<sup>44</sup> A covered pipeline for the purposes of the NGL means a pipeline to which a coverage determination applies, or one that is deemed to be a covered pipeline by operation of ss 126 or 127.

## Terminology 'covered', 'coverage determination' and 'coverage revocation determination'

4.2 A 'covered pipeline' is defined in s 2 of the NGL to be a pipeline:

- (a) to which a coverage determination applies, or
- (b) deemed to be a covered pipeline by operation of ss 126 [tender approval pipelines] or 127 [voluntary access arrangements].<sup>45</sup>

4.3 Section 92 then provides that:

- (1) Any person may apply for a determination that a pipeline be a covered pipeline (a **coverage determination**).

4.4 Accordingly, a 'coverage determination' is a positive decision that a pipeline is to be a covered pipeline and, if that is not the case, the final decision is a decision not to make a coverage determination. Section 101 then confirms that:

The pipeline the subject of a coverage determination becomes a covered pipeline—

- (a) when the coverage determination takes effect; and
- (b) continues to be a covered pipeline while the coverage determination remains in effect.

4.5 Similarly with revocation determinations, s 102 provides that:

- (1) Any person may apply for a determination that a covered pipeline no longer be a covered pipeline (a **coverage revocation determination**).

4.6 Section 108 then provides that:

The pipeline the subject of a coverage revocation determination ceases to be a covered pipeline when the coverage revocation determination takes effect.

## What 'pipeline' coverage applies to

4.7 It is important to note that a coverage determination applies to a physical pipeline but that the access regulation which flows from coverage applies to the pipeline services provided by means of the covered pipeline. Pipeline services are defined by s 2 of the NGL to be:

- (a) a service provided by means of a pipeline, including—
  - (i) a haulage service (such as firm haulage, interruptible haulage, spot haulage and backhaul); and
  - (ii) a service providing for, or facilitating, the interconnection of pipelines; and
- (b) a service ancillary to the provision of a service referred to in paragraph (a),

<sup>45</sup> Note also the existing pipelines are covered by clauses 6 and 7 of Schedule 3 of the NGL.

but does not include the production, sale or purchase of natural gas or processable gas.

- 4.8 Accordingly, only network services are regulated as a result of coverage as opposed to upstream or downstream activities (although ring-fencing and other obligations are designed to limit the use of a service provider's position in providing network services to gain advantage in those markets).
- 4.9 Once covered, the NGL, like the Gas Code, provides a mechanism for extensions or expansions of a pipeline to become part of the covered pipeline, such that new applications for coverage are not required. This is set out in ss 18 and 19 of the NGL as follows:

**18—Certain extensions to, or expansion of the capacity of, pipelines to be taken to be part of a covered pipeline**

For the purposes of this Law—

- (a) an extension to, or expansion of the capacity of, a covered pipeline must be taken to be part of the covered pipeline; and
- (b) the pipeline as extended or expanded must be taken to be a covered pipeline,

if, by operation of the extension and expansion requirements under an applicable access arrangement, the applicable access arrangement will apply to pipeline services provided by means of the covered pipeline as extended or expanded.

**19—Expansions of and extensions to covered pipeline by which light regulation services are provided**

For the purposes of this Law, an extension to, or expansion of the capacity of, a covered pipeline by means of which light regulation services (and in respect of which there is no limited access arrangement) are provided, must be taken to be part of the covered pipeline unless the AER determines otherwise in writing.

- 4.10 Accordingly, the access arrangement itself (whether limited or full) for an existing pipeline determines that a new piece of the pipeline (such as a compressor, lateral or pipe system in a new suburb) is part of the covered pipeline. Where there is no access arrangement (ie for light regulation pipelines without a limited access arrangement), all extensions or expansions are still covered.
- 4.11 It is important to note that the definition of pipeline in s 2 of the NGL includes 'parts of pipes' (paragraph (c)). Accordingly, coverage need not apply to all of a pipeline system owned, controlled or operated by a particular service provider or group of service providers. Moreover, while an application for coverage or to revoke coverage may only be in relation to part of a pipeline system, the Council's recommendations and the Minister's decision may decide to apply coverage to, or revoke coverage from, a greater or lesser part of the system than requested. This is achieved through the equivalent provisions in ss 95(3), 99(7), 104(3) and 106(7). For example, s 95(3) provides that:

- (3) A recommendation under this section may recommend an outcome different from the outcome sought in the application under section 92.

Example—

An applicant may apply for a determination that the whole of a pipeline be a covered pipeline. The NCC may recommend that only a part of the pipeline the subject of the application be covered or may recommend that the pipeline not be covered.

- 4.12 The intent of this subsection is also set out in the Second Reading Speech which states that:

Consistent with the current Gas Code, a coverage decision may apply to more or less of the pipeline than is the subject of the application or recommendation.<sup>46</sup>

- 4.13 In making a decision to recommend that more or less of a pipeline will be covered, the Council will consider whether:

- (a) covering more or less of the pipeline is likely to promote the national gas objective having regard to the services prospective users are likely to seek from the pipeline, and
- (b) the impact that covering more or less of the pipeline has on the application of the coverage criteria (such that the focus on a particular grouping of pipes is not used to avoid coverage).<sup>47</sup>

### **Similarities in coverage and revocation of coverage**

- 4.14 The legal requirements applying to coverage determinations and coverage revocation determinations mirror each other. The process and considerations are intended to be identical such that the hurdle to apply coverage and remove it is the same. Essentially:

- (a) any person may make an application to the Council for a determination
- (b) the Council publishes the application on its website and there is consultation on the application for 15 business days

<sup>46</sup> See Second Reading Speech, South Australian Hansard, Legislative Assembly, 9 April 2008, pp 2889. Note that the Gas Code provided that 'If the NCC recommends that the Pipeline be Covered, the NCC may do so to a greater or lesser extent than requested by the applicant if, having regard to the part of the Pipeline that is necessary to provide Services that Prospective Users may seek, the NCC considers it appropriate. The NCC may not recommend Coverage of a greater part of a Pipeline than is owned or operated by the same Service Provider or group of Service Providers' (1.7).

<sup>47</sup> The national gas objective and coverage criteria are the two principles governing coverage recommendations set out in s 97(1) and coverage revocation recommendations in s 105(1). They are further elaborated on in the next section of this part of the Guide.

- (c) after considering submissions and potentially seeking further information from the applicant, the Council makes a draft recommendation based upon the application of the coverage criteria and national gas objective
- (d) there is consultation on the draft recommendation for at least 15 business days
- (e) the Council makes a final recommendation, delivers it to the relevant Minister and interested parties and publishes it on its website within 20 business days of the close of submissions, and
- (f) the relevant Minister must use their best endeavours to make a final decision within 20 business days after receiving the Council's recommendation based upon the coverage criteria and national gas objective.

4.15 The only exceptions to this are that:

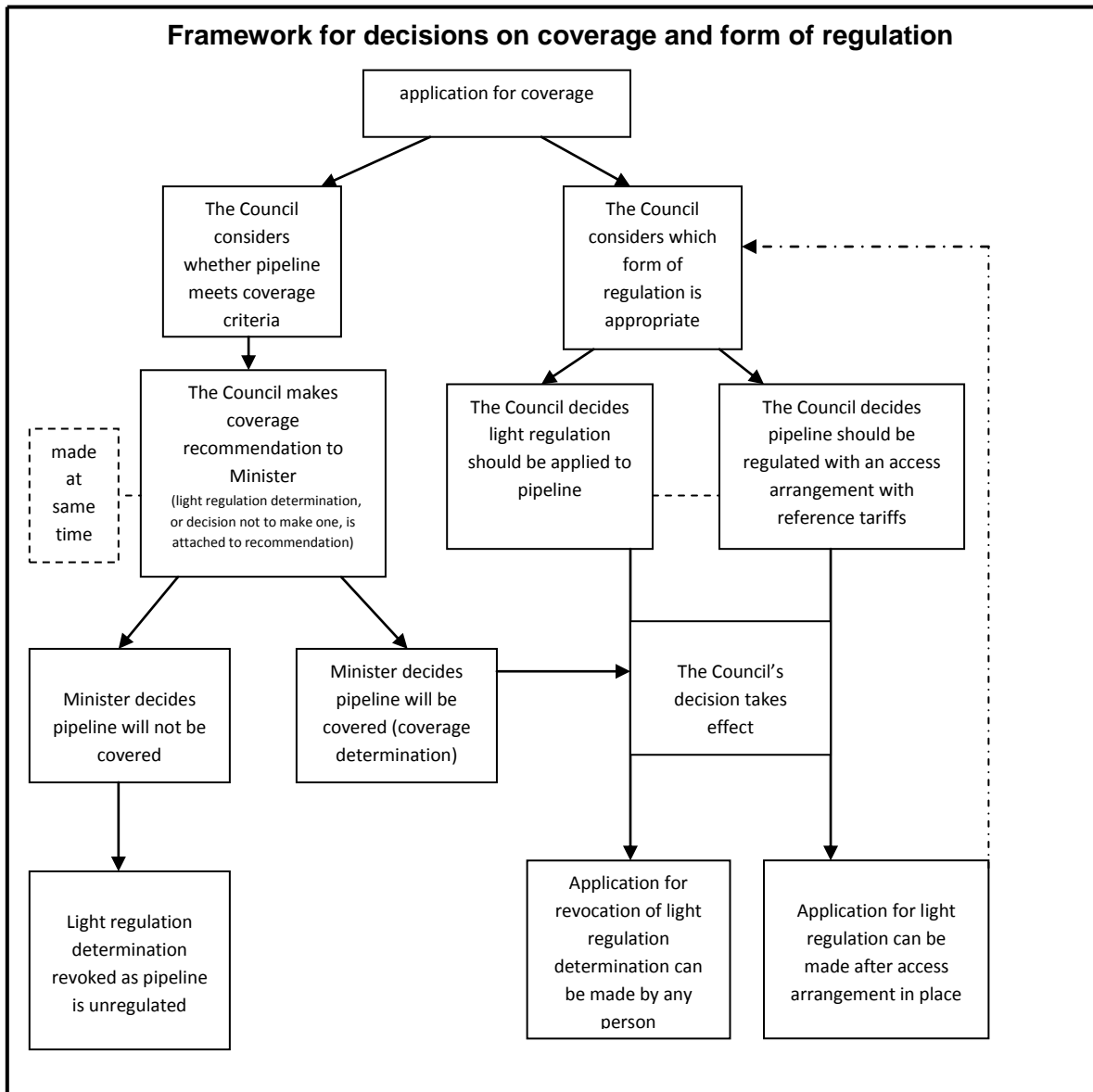
- (a) coverage also needs to deal with the classification of a pipeline whereas revocation of coverage does not (because the pipeline is already classified)
- (b) coverage needs to be assessed with a concurrent process of determining whether the pipeline should be subject to light or full regulation (see s 110, the diagram below and Part C of the Guide)
- (c) coverage processes may need to be suspended when the pipeline is going through a tender approval process which will result in the pipeline becoming covered at the end of that process (ss 94 and 96)
- (d) for a covered pipeline subject to a voluntary access arrangement which will expire, coverage can only be sought from the end of that access arrangement (r 15(2))
- (e) revocation of coverage processes require a larger amount of information from the applicant who will generally be the service provider or an associated entity (r 18), and
- (f) the coverage revocation process may need to be combined with applications to revoke a light regulation determination (see s 119 and Part C of this Guide).

4.16 8.5Appendix A highlights how the provisions surrounding coverage determinations and coverage revocation determinations relate to each other. Given these similarities, the next section of this part of the Guide focuses on the principles which govern the making of coverage determinations and coverage revocation determinations. The following section of this part of the Guide then focuses on the procedural requirements of the decisions.

### **Simultaneous consideration of light regulation**

4.17 The following diagram sets out the parallel processes for considering coverage and form of regulation under the NGL which is further expanded upon in Part C of this Guide.

**Figure1 Simultaneous consideration of coverage and form of regulation**



## 5 Principles governing coverage and revocation of coverage

### Principles governing coverage decisions

- 5.1 Where a person applies to the Council for a coverage determination (ie, that a pipeline be a covered pipeline), the Council is required to make a coverage recommendation to the relevant Minister in respect of that application. The Council's recommendation must be either that the pipeline:
- (a) be a covered pipeline, or
  - (b) not be a covered pipeline.
- 5.2 Similarly, where a person applies to the Council for a coverage revocation determination (ie that a pipeline no longer be a covered pipeline), the Council's recommendation must be either that the pipeline:
- (a) continue to be a covered pipeline, or
  - (b) not continue to be a covered pipeline.
- 5.3 The Council's recommendations must be given to the relevant Minister without delay (ss 95(4) and 104(4)).
- 5.4 On receiving the Council's recommendation, the relevant Minister must decide:
- (a) in the case of coverage, whether to make a coverage determination in respect of the pipeline to which the recommendation relates, or
  - (b) in the case of a coverage revocation, whether to make a coverage revocation determination.
- 5.5 This section of the Guide discusses the relevant principles to be applied by the Council in making coverage and coverage revocation recommendations under the NGL. These principles have been drawn from a large body of relevant background material, including:
- the Second Reading Speech
  - the Productivity Commission Report
  - the Expert Panel Report
  - the MCE Decision, and
  - relevant case law on coverage under the Gas Pipelines Access Law (Gas Code) and declaration under Part IIIA of the TPA.
- 5.6 The above materials are the key documents which underpin the reform of Australia's gas access regulatory regime which culminated in the NGL. In particular, we note that the Productivity Commission Report, the Expert Panel Report and the MCE Decision

are all expressly referred to in the Second Reading Speech. While these documents are not part of the NGL, they may be relevant in its interpretation.<sup>48</sup> To the extent to which the NGL reflects the declaration criteria in Part IIIA of the TPA, the Hilmer Report is also relevant to the economic underpinnings of the criteria.<sup>49</sup>

- 5.7 This section has also drawn on the Council's *A Guide to Declaration under Part IIIA of the Trade Practices Act 1974 (Cth)* as the coverage criteria have been drafted to reflect the declaration criteria under Part IIIA of the TPA. Interested parties are advised to separately consider the material contained within that publication in relation to the general principles underpinning the various coverage criteria.

## Principles

### Key decision making criteria

- 5.8 The principles for the Council to make coverage recommendations (s 97) and coverage revocation recommendations (s 105) mirror each other. Relevantly, s 97 provides as follows:

#### **97—Principles governing the making of a coverage recommendation**

- (1) In making a coverage recommendation, the NCC—
  - (a) must give effect to the pipeline coverage criteria; and
  - (b) in deciding whether or not the pipeline coverage criteria are satisfied must have regard to the national gas objective.
- (2) The NCC gives effect to the pipeline coverage criteria as follows:
  - (a) if the NCC is satisfied that all the pipeline coverage criteria are satisfied in relation to the pipeline—the recommendation must be in favour of the pipeline being a covered pipeline;
  - (b) if the NCC is not satisfied that all the pipeline coverage criteria are satisfied in relation to the pipeline—the recommendation must be against the pipeline being a covered pipeline.

#### *Giving effect to the pipeline coverage criteria*

- 5.9 Accordingly, the test centres around whether or not the Council is satisfied that the pipeline coverage criteria are met. Section 15 of the NGL sets out the pipeline coverage criteria as follows:

#### **15 Pipeline coverage criteria**

The pipeline coverage criteria are –

<sup>48</sup> The use of extrinsic materials in the interpretation of the NGL and Rules is discussed at Appendix B.

<sup>49</sup> Hilmer Review (Independent Committee of Inquiry into National Competition Policy) 1993, *National Competition Policy*, AGPS, Canberra. (Hilmer Report)

- (a) that access (or increased access) to pipeline services provided by means of the pipeline would promote a material increase in competition in at least 1 market (whether or not in Australia), other than the market for the pipeline services provided by means of the pipeline;
- (b) that it would be uneconomic for anyone to develop another pipeline to provide the pipeline services provided by means of the pipeline;
- (c) that access (or increased access) to the pipeline services provided by means of the pipeline can be provided without undue risk to human health or safety;
- (d) that access (or increased access) to the pipeline services provided by means of the pipeline would not be contrary to the public interest.

5.10 If the Council is satisfied that all four criteria are met, the Council must recommend that the pipeline should be or should remain covered. If the Council is not satisfied that one or more of the criteria are met, the Council must recommend that the pipeline not be covered. This is the only way in which the Council may give effect to the coverage criteria. Accordingly, in contrast to Part IIIA of the TPA, there is no residual discretion to not recommend covering a pipeline when the Council is satisfied all of the criteria are met. Each of the coverage criteria is considered separately below.

*Having regard to the national gas objective*

5.11 Subsection 97(1) makes clear that in deciding whether each criterion is satisfied, the Council must have regard to the national gas objective. Section 23 of the NGL sets out the national gas objective as follows:

The objective of this Law is to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.

5.12 The inclusion of an overarching objects clause is one of the key changes in the NGL compared to the previous regulatory regime. It is explicitly referred to as a consideration for all of the key decisions in the regime.<sup>50</sup>

5.13 The Second Reading Speech set out the key principles underlying the insertion of the objective as follows:

The national gas objective is an economic concept and should be interpreted as such.

The long term interest of consumers of gas requires the economic welfare of consumers, over the long term, to be maximised. If gas markets and access to pipeline services are efficient in an economic sense, the long term economic interests of consumers in respect of price, quality, reliability, safety and security of natural gas services will be maximised. By the promotion of an economic

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<sup>50</sup> See ss 28, 72, 97, 100, 105, 107, 154, 157, 163, 165 and 291 of the NGL.

efficiency objective in access to pipeline services, competition will be promoted in upstream and downstream markets.<sup>51</sup>

- 5.14 The national gas objective accordingly requires the consideration and balancing of productive, allocative and dynamic efficiencies in the provision of network services as well as in upstream and downstream markets where competition is the key driver of welfare gains.<sup>52</sup> The need for a 'long term' perspective is also a caution against focusing on short term benefits to consumers which undermine longer term investment and welfare gains.
- 5.15 In *Re: Application by ElectraNet Pty Limited (No 3)* [2008] ACompT 3 (30 September 2008) the Australian Competition Tribunal (Tribunal) summarised the intent of the national electricity objective as follows:

The national electricity objective provides the overarching economic objective for regulation under the Law: the promotion of efficient investment in the long term interests of consumers. Consumers will benefit in the long run if resources are used efficiently, i.e. resources are allocated to the delivery of goods and services in accordance with consumer preferences at least cost. As reflected in the revenue and pricing principles, this in turn requires prices to reflect the long run cost of supply and to support efficient investment, providing investors with a return which covers the opportunity cost of capital required to deliver the services.<sup>53</sup>

- 5.16 The requirement that the Council have regard to the national gas objective in giving effect to each coverage criteria means that the Council must take into account the economic efficiency focus in determining whether the particular criterion is met. The national gas objective reinforces the importance of the focus on the market power of the service provider in applying the coverage criteria and considering whether making or keeping the pipeline a covered pipeline is a means of mitigating that market power.

**(a) Access (or increased access) to pipeline services provided by means of the pipeline would promote a material increase in competition in at least 1 market (whether or not in Australia), other than the market for the pipeline services provided by means of the pipeline**

- 5.17 Criterion (a) in s 15 of the NGL, as with s 44G(2)(a) of the TPA, provides that the Council cannot recommend that a pipeline be covered unless it is satisfied that access (or increased access) to the pipeline services provided by means of the pipeline would promote a material increase in competition in at least one market other than the market for the service. The markets in which competition might be promoted are

<sup>51</sup> p 2697.

<sup>52</sup> See discussion in the Expert Panel Report pp 31 - 58.

<sup>53</sup> At [15].

commonly referred to as 'dependent markets'. The issue is whether access would improve the opportunities and environment for competition in dependent markets such as to promote materially more competitive outcomes. The assessment is concerned with the process of competition, rather than the particular commercial interests or pursuits of individual competitors, including an applicant for coverage, given that access that may result from coverage is not limited to the party which made the application.

- 5.18 The purpose of criterion (a) is to limit coverage to circumstances where it is likely to materially enhance the environment for competition in at least one dependent market. Whether competition will be materially enhanced depends critically on the extent to which the incumbent service provider can and is likely, in the absence of coverage, to use market power to adversely affect competition in a dependent market(s). If the service provider has market power, as well as the ability and incentive to use that power to adversely affect competition in a dependent market, coverage would be likely to improve the environment for competition, offering the prospect of tangible benefits to consumers (including reduced prices and better service provision).
- 5.19 In assessing whether criterion (a) is satisfied, the Council:
- (a) identifies the relevant dependent (upstream or downstream) markets
  - (b) considers whether the identified dependent market(s) is separate from the market for the pipeline service to which access is sought, and
  - (c) assesses whether access (or increased access) would be likely to promote a materially more competitive environment in the dependent market(s).
- 5.20 The Council's approach to each of the above steps for assessing criterion (a) is considered in detail in turn in the following sections.

### **Identifying dependent markets**

- 5.21 The Tribunal in *Re Duke Eastern Gas Pipeline Pty Ltd [2001] ACompT 2* (4 May 2001) (Duke EGP decision) adopted the findings of the then Trade Practices Tribunal in the *Re Queensland Co-Operative Milling Association Ltd* decision and relevantly described the concept of a market as follows:

All the evidence supported the definition of a market as concluded in *Re Queensland Co-Operative Milling Association Ltd* (1976) 25 FLR 169 at 190:

"A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them (if there is no close competition there is of course a monopolistic market). Within the bounds of a market there is substitution - substitution between one product and another, and between one source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive. ... Whether such substitution is feasible or likely depends [on a number of factors] ... in determining the outer boundaries

of the market we ask a quite simple but fundamental question: If the firm were to 'give less and charge more' would there be, to put the matter colloquially, much of a reaction?"<sup>54</sup>

- 5.22 This view of market has subsequently be referred to with approval by the High Court in the *Queensland Wire* decision and adopted by the Tribunal, including in the Sydney Airport decision and the Duke EGP decision. This view of market has broad application across most aspects of competition law including analysis of mergers and potentially anticompetitive conduct and for the identification of markets in the context of a declaration application under Part IIIA of the TPA and coverage under the NGL.
- 5.23 Conventionally, markets are identified or defined in terms of:
- (a) a product or service dimension
  - (b) geographic area, and
  - (c) functional level.<sup>55</sup>
- 5.24 The **product/service dimension** of a market delineates the set of products and/or services that are sufficiently substitutable so as to be considered to be traded within a single market.
- 5.25 Defining a product market requires identification of the goods and/or services traded and the sources or potential sources of substitute products. Separate product markets exist if their respective products are not closely substitutable in demand or supply. Products are demand-side substitutes if consumers would substitute one product for the other following a small but significant change in their relative prices. Supply side substitution occurs when a producer can readily switch from producing one product to producing another. Market entry can be distinguished from supply-side substitution by the requirement for significant investment in production, distribution or promotion.
- 5.26 The **geographic dimension** of a market identifies the area within which substitution in demand and supply is sufficient for the product(s)/service(s) traded at different locations to be considered in the same market.
- 5.27 Defining the relevant geographic market requires the identification of the area(s) that are supplied, or could be supplied, with the relevant product and to which consumers can practically turn. National, intrastate or regional markets, for example, may be

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<sup>54</sup> At [76].

<sup>55</sup> A time related element can also be relevant to market definition in some circumstances, although this is less likely in the context of gas pipelines where markets usually involve long lived assets and shorter term market conditions are less likely to be relevant.

defined. The wording of criterion (a) clearly includes markets outside Australia.<sup>56</sup>

- 5.28 The collective effect of substitution in demand and supply determines what is in and out of the relevant product and geographic market dimensions. The process of market definition begins with the narrowest feasible product and geographic market boundaries. If consumers would respond to an increase in price by switching to alternative products or services, then the market must be expanded and the process continues until the market boundaries include all those sources and potential sources of close substitutes, so as to identify the smallest area over which it would be profit maximising for a hypothetical monopolist to impose a small but significant and non-transitory increase in price.
- 5.29 Substitution possibilities can be gauged through cross-price elasticity assessments. However, it is often difficult to obtain sufficient data on the relevant cross-price elasticities to calculate these in order to define market boundaries and so other more qualitative, judgement-based assessments are often undertaken in defining markets.
- 5.30 Where products or services pass through a number of levels in a supply chain, it is also useful to describe the market in terms of the function being considered. The **functional dimension** identifies which of a set of vertically related markets is being considered. Defining the relevant functional market requires distinguishing between different vertical stages of production and/or distribution and identifying those that comprise the field of competition in a particular case.
- 5.31 In the context of considering applications for coverage the functional dimension of market definition often overlaps with consideration of whether a dependent market is separate from the market for the pipeline services (see paragraphs 5.40 to 5.44).
- 5.32 In its consideration of criterion (a) the Council will seek to identify one or more dependent markets where competition appears likely to be significantly affected by the availability of access to the pipeline services. Often these markets will be vertically related to the market for the pipeline service. That is, they are upstream or downstream of that market in a supply chain.
- 5.33 The Council will identify dependent markets in terms of the dimensions set out above. The Council considers, however, that an assessment of criterion (a) may not always require a precise delineation of the boundaries of the market for the service. What must be determined is whether the market(s) in which competition is said to be

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<sup>56</sup> While the promotion of competition in a market outside Australia might enable criterion (a) to be satisfied, in a situation where the only dependent market in which a material promotion of competition might result was outside Australia, it may be difficult to satisfy criterion (d) in terms of establishing that access is not contrary to the public interest as criterion (d) is concerned with the interest of the Australian public. Where the promotion of competition in a market outside Australia would reduce returns to Australia, it might be argued that access is contrary to the [Australian] public interest and criterion (d) is not met. In practice it is unlikely that the impact of access would only occur in relation to a market outside Australia or that access would materially affect competition in an international market.

promoted (the dependent market(s)) are distinct from the market for the pipeline services and the effect access will have on the conditions for competition in that dependent market(s).

- 5.34 It may also be unnecessary to consider all possible dependent markets. Criterion (a) is satisfied if access will materially promote competition in one or more dependent markets. In practice, it is unlikely that the Council will examine more than the two most likely dependent markets in relation to an application for a coverage recommendation.

*Separate markets from the market for the pipeline services*

- 5.35 For the purposes of criterion (a), the Council needs to be satisfied access (or increased access) would promote a material increase in competition in 'at least one market ... other than the market for the pipeline services provided by means of the pipeline '. This means that dependent markets must be functionally distinct markets from the market for the pipeline services.

- 5.36 In the context of the NGL, as opposed to Part IIIA of the TPA, the focus upon pipeline services, which can only be provided by means of a natural gas pipeline, simplifies this requirement. Accordingly, a promotion of competition in the provision of pipeline services to the same markets served by the pipeline will not satisfy criterion (a). The focus is on the relevant upstream and downstream markets, principally gas production/processing, the sale or retailing of gas to end users and, increasingly, the use of gas to generate electricity.

- 5.37 In the context of Part IIIA, although it is possible that Part IIIA's criterion (a) may be satisfied where the service provider is not vertically integrated into a dependent market(s), criterion (a) will in the context of Part IIIA most commonly be satisfied where the service provider is vertically integrated into the dependent market(s). The Federal Court stated in *BHP Billiton Iron Ore v NCC*<sup>57</sup> that:

... it is the very prevention of a vertically integrated organisation using its control over access to an essential facility to limit effective competition in dependent markets that is a key activity that the access regime seeks to deal.

... In these circumstances it must be established that the provision of the service provided by the facility and the vertically related activity in the dependent market occur in distinct functional markets. Where there are such overwhelming efficiencies from vertical integration, and the provision of the service and the vertically related activity occur in the same functional market, there may not be a case for facilitating access to third parties.

- 5.38 In the Sydney Airport decision, the Tribunal was concerned with the viability of vertically separate provision of products or services and found that the existence of functionally separate markets depended on whether there were overwhelming

<sup>57</sup> *BHP Billiton Iron Ore Pty Ltd v The National Competition Council* [2006] FCA 1764 at [45].

economies of joint production or joint consumption that dictated that the vertically related activities must occur within the same entity.

- 5.39 In the Services Sydney decision the Tribunal was also concerned with economic separability and relevantly stated:

[o]ne approach to assessing efficiencies of vertical integration is to posit that where the transaction costs of market coordination between vertical stages of supply exceed those of administrative coordination within the firm, there will be no separate market for the service(s). However, a literal interpretation of that test could prevent the very benefits of competition in dependent markets, which Pt IIIA is designed to achieve, from being realised. It is not difficult to imagine a situation where the coordination costs within a vertically integrated firm are less than the costs of market transactions for a particular service; but where there exists a more cost efficient potential entrant to an upstream or downstream dependent stage of the supply chain, who can more than offset the additional transaction costs with their superior efficiency. Entry of such a firm would be pro-competitive and economically efficient, yet a narrow view of the test would have the consequence that no market for the service would be defined and hence there would possibly be no declaration and no entry. The community would be denied the very kind of benefits arising from competition that were envisaged by the report of the Independent Committee of Inquiry into Competition Policy in Australia on National Competition Policy (the Hilmer Report) and which underpin the access regime principles of Pt IIIA.

A broader approach, which asks whether the complementarities of vertical integration are such as to dictate vertical integration, would not preclude declaration and competition in these circumstances. This approach was generally adopted in the NCC's Final Report and is consistent with that adopted by the Tribunal in *Re Sydney International Airport*.

...

An alternative, more precise, test could involve looking at some combination of both transaction costs and service delivery costs. If there was a demand for the service at a price which covered these combined costs, then a market could be said to exist. (at 116-118)

- 5.40 Economic separability is thus at least a necessary condition for different functional layers to constitute distinct functional markets and for a dependent market to be separate from a market for the pipeline services.
- 5.41 Services may be provided in functionally distinct markets even though there is a one-for-one relationship—ie, perfect supply side and demand side complementarity—between those services. This will be the case where those complementarities do not give rise to economies of joint consumption or joint production that dictate that the services must be performed in the same economic entity. In the Sydney Airport decision the Tribunal acknowledged “the strong supply side and demand side complementarity between other airport services and the declared services and the underlying facilities”. Nonetheless, the Tribunal found that the one-for-one relationship between airport aprons at Sydney International Airport and ramp

handling services did not mean that these two services were in the same functional market. In so finding, the Tribunal drew a comparison with the example of rail track and train services. The Tribunal stated:

The Tribunal was struck by the parallels here with the provision of railway track and train services. Though in the past usually vertically integrated, track services and the running of passenger or freight trains can be, and increasingly are, provided separately. As such, they operate in functionally distinct markets, even though there is perfect complementarity between them. To put it another way, these complementarities do not appear to give rise to economies of joint consumption or joint production that dictate the services must be performed within the same economic entity. The evidence presented to the Tribunal suggested similar considerations apply to the services provided by SIA's physical infrastructure and ramp handling and CTO services. In other words, just because there is a one for one relationship between airport aprons and ramp handling services does not mean that the supply of these two types of services are in functionally the same market. (at 97)

- 5.42 Issues from vertical integration may be less relevant in the context of gas pipelines and services given the structural and operational separation requirements of the Gas Pipelines Access Law and the NGL.
- 5.43 In determining whether the market for the pipeline service is in the same or different markets from the market in which competition is said to be promoted, the Council will identify likely dependent markets and assess whether these market are functionally distinct from the pipeline service market.
- 5.44 Where the economies of joint production or consumption between a dependent market and the market for pipeline services are such that separate provision or consumption is not economically feasible, the services will not be in functionally separate markets (Sydney Airport decision, at 97) and criterion (a) is not satisfied.

### **Access (or increased access) to pipeline services**

- 5.45 The phrase 'access (or increased access) to pipeline services' refers to the right to access pipeline services consequent upon coverage under the NGL. That is, it refers to a regulated right to access pipeline services under the NGL rather than access that may be available under voluntary commercial arrangements.
- 5.46 The context in which the phrase appears in the NGL indicates that access must be provided on terms and conditions that give effect to the efficiency objective in the NGL and, accordingly, replicate the outcome of a competitive market. The provision of services at a competitive market price, for example, will result in an optimal level of demand for access to the services. The reference to 'access (or increased access)' describes the conditions that would derive from access under the NGL as opposed to the conditions that would result in a less than effectively competitive dependent market for the services provided by means of the pipeline.

5.47 The words 'increased access' underscore the emphasis on removing structural impediments or barriers to competition in markets that rely on services provided by natural monopoly pipelines.

5.48 The phrase 'access (or increased access)' was considered by the Full Court in the Sydney Airport Appeal decision. The Full Court held that criterion (a) requires:

... a comparison of the future state of competition in the dependent market with a right or ability to use [the] service and the future state of competition in the dependent market without any right or ability or with a restricted right or ability to use the service. (at 83)

5.49 As the Tribunal noted in the Sydney Airport decision:

The purpose of an access declaration is to unlock a bottleneck so that competition can be promoted in a market other than the market for the service. The emphasis is on 'access', which leads us to the view that s 44H(4)(a) is concerned with the fostering of competition, that is to say it is concerned with the removal of barriers to entry which inhibit the opportunity for competition in the relevant downstream market. (at 107)

5.50 Criterion (a) does not require that access to the service is unavailable at the time an application for a coverage recommendation is made. In the Sydney Airport decision, the Tribunal held that "existing access to a service is no bar to a consideration whether a declaration should be made in respect of that service" (at 229). This principle was further illustrated by the Tribunal's discussion in the Duke EGP decision of criterion (a) in the Gas Code. In that case, Duke contended that the question of whether access or increased access to the service would promote competition in other markets does not arise unless, as a matter of fact, access to the Eastern Gas Pipeline was either unavailable or restricted. The Tribunal rejected this argument in the following terms:

An object of the Code, according to (d) of the introduction to it, is to provide rights of access to natural gas pipelines on conditions that are fair and reasonable to the providers of the pipeline services, and to persons wishing to use them. The Code adopts a two stage process to access regulation. The first stage consists of the Ministerial decision that the pipeline is covered or not covered. The second stage consists of the fixing of Access Arrangements which, in general, are not to displace the contractual rights of other persons already using the pipeline. If a dispute arises as to the application of the Access Arrangements, then there is provision for an arbitrated outcome. There is nothing to prevent parties from reaching a commercial agreement as to access outside the terms of any approved Access Arrangement. The aim of the Code, according to the introduction which prefaces it, is:

"To provide sufficient prescription so as to reduce substantially the number of likely arbitrations, while at the same time incorporating enough flexibility for the parties to negotiate contracts within an appropriate framework."

The object of the Code, and its structure, make it clear that criterion (a) does not have as its focus a factual question as to whether access to the pipeline services is available or restricted. Put in that way, the question would not take sufficient account of the terms on which access is offered. Rather, the question posed by criterion (a) is whether the creation of the right of access for which the Code provides would promote competition in another market. The enquiry is as to the future with coverage and without coverage. We agree with the approach adopted by the Tribunal in *Sydney International Airport* in this respect. The Tribunal must have regard to the position as it now stands, insofar as it provides a reliable guide to the future without coverage. Thus, (assuming the present is a reliable guide to the future without) account is to be taken of the EGP as an open access pipeline, and of any other pipelines supplying the upstream or downstream gas markets, in order to determine whether coverage of the EGP would promote competition in at least one of those markets.<sup>58</sup>

- 5.51 No threshold question as to whether access to a pipeline service is unavailable or restricted arises in the assessment of criterion (a). The Full Court stated in the *Sydney Airport Appeal* decision that it is not necessary ... “to identify and determine the existence and extent of a denial or restriction of access”<sup>59</sup> in order to satisfy criterion (a).

### **Material promotion of competition**

- 5.52 The notion of 'promoting ... competition' reflects the underlying national competition policy focus underpinning both the TPA and NGL. Competition is valued for serving economic, social and political goals. It is a mechanism for discovering market information and enforcing business decisions in light of this information. The basic characteristic of effective competition is that no one seller or group of sellers has undue market power. Competition is a dynamic process, generated by market pressure from alternative sources of supply and the desire to keep ahead. In this sense, competition expresses itself as rivalrous market behaviour.
- 5.53 The promotion of a material increase in competition involves an improvement in the opportunities and environment for competition such that competitive outcomes are materially more likely to occur. It is the promotion of 'competition' rather than the promotion of 'competitors'.<sup>60</sup>

<sup>58</sup> Duke EGP decision at [73] and [74]. The words of the Tribunal in *Sydney International Airport* being referred to were that 'The purpose of an access declaration is to unlock a bottleneck so that competition can be promoted in a market other than the market for the service. The emphasis is on 'access', which leads us to the view that s 44H(4)(a) is concerned with the fostering of competition, that is to say it is concerned with the removal of barriers to entry which inhibit the opportunity for competition in the relevant downstream market' at [107].

<sup>59</sup> At [ 76].

<sup>60</sup> See *Sydney Airport* decision at [121].

5.54 In the Sydney Airport decision, the Tribunal stated:

The Tribunal does not consider that the notion of ‘promoting’ competition in s 44H(4)(a) requires it to be satisfied that there would be an advance in competition in the sense that competition would be increased. Rather, the Tribunal considers that the notion of ‘promoting’ competition in s 44H(4)(a) involves the idea of creating the conditions or environment for improving competition from what it would be otherwise. That is to say, the opportunities and environment for competition given declaration, will be better than they would be without declaration.<sup>61</sup>

5.55 The Tribunal went on to say that the removal of barriers to entry in any dependent market(s) can be expected to promote competition:

We have reached this conclusion having had regard, in particular, to the two stage process of the Pt IIIA access regime. The purpose of an access declaration is to unlock a bottleneck so that competition can be promoted in a market other than the market for the service. The emphasis is on ‘access’, which leads us to the view that s 44H(4)(a) is concerned with the fostering of competition, that is to say it is concerned with the removal of barriers to entry which inhibit the opportunity for competition in the relevant downstream market. It is in this sense that the Tribunal considers that the promotion of competition involves a consideration that if the conditions or environment for improving competition are enhanced, then there is a likelihood of increased competition that is not trivial.<sup>62</sup>

5.56 The Tribunal also adopted this approach in the Duke EGP decision,<sup>63</sup> stating that ‘the question for the Tribunal is whether the opportunities and environment for competition in market(s) upstream or downstream of the EGP would be enhanced if the EGP were to be covered in terms of the Code’. This question is assessed by a comparison of the future conditions and environment for competition with and without access. Additionally, even if access will not remove all barriers to entry and actual entry may still be difficult with access, criterion (a) can still be satisfied if access would remove a significant barrier to entry and thereby promote competition.<sup>64</sup>

5.57 The object of the criterion (a) requirement that access materially promote competition is to limit coverage to pipelines to which access is essential for effective competition in a dependent market. The Hilmer Report described the rationale for access regulation as follows:

In some markets the introduction of effective competition requires competitors to have access to facilities which exhibit natural monopoly characteristics, and hence cannot be duplicated economically. ... Facilities of this kind are referred to as ‘essential facilities’.

<sup>61</sup> At [106].

<sup>62</sup> At [107].

<sup>63</sup> At [75].

<sup>64</sup> See *Re Services Sydney Pty Limited* [2005] ACompT 7 (21 December 2005) at [131].

An 'essential facility' is, by definition, a monopoly, permitting the owner to reduce output and/or service and charge monopoly prices, to the detriment of users and the economy as a whole.<sup>65</sup>

- 5.58 The reference to 'competition' in criterion (a) is a reference to effective competition, rather than any theoretical concept of perfect competition. 'Effective competition' refers to the degree of competition required for prices to be driven towards economic costs and for resources to be allocated efficiently at least in the long term. It is unlikely that the reference to 'competition' in criterion (a) is intended to refer to the theoretical concept of perfect competition, not only given the Hilmer Report's stated objective of access regulation to promote effective competition, but also because the subject matter of the criterion (a) assessment involves an assessment of the competitive conditions in a real-life industry.
- 5.59 Where a dependent market is effectively competitive access is unlikely to promote a material increase in competition and an application for coverage that seeks to add to competition in such a dependent market is unlikely to satisfy criterion (a).
- 5.60 In the Duke EGP decision, the Tribunal concluded that whether access will promote competition critically depends on whether the access provider has market power that could be used to adversely affect competition in the dependent market(s). The Tribunal said:
- Whether competition will be promoted by coverage is critically dependent on whether EGP has power in the market for gas transmission which could be used to adversely affect competition in the upstream or downstream markets. There is no simple formula or mechanism for determining whether a market participant will have sufficient power to hinder competition. What is required is consideration of industry and market structure followed by a judgment on their effects on the promotion of competition. (at [116])
- 5.61 If a service provider is unable to exercise market power in the dependent market, then a coverage determination so as to regulate the terms and conditions of access to the pipeline services would not promote competition or efficiency in that market.
- 5.62 Barriers to entry are a primary determinant of the existence of market power. Only in the presence of significant barriers to entry can a firm sustainably raise prices above economic costs without new entry taking away customers in due course.

### **Material promotion of competition**

- 5.63 The words 'a material increase' were added to criterion (a) of the Gas Code when the criterion was replicated in s 15 of the NGL. This is consistent with an equivalent amendment to the declaration criteria in Part IIIA of the TPA.<sup>66</sup> The Second Reading Speech clarified this intent as follows:

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<sup>65</sup> p 239.

<sup>66</sup> See item 16 of Schedule 1 to the *Trade Practices Amendment (National Access Regime) Act 2006* (Cth).

The Gas Code coverage criteria have been amended in response to the Productivity Commission Review of the Gas Access Regime such that a 'material' increase in competition in at least one market is required before coverage should be applied. This, consistent with similar amendments to Part IIIA of the Trade Practices Act, ensures that the increase in competition needs to be non trivial before regulation is imposed.<sup>67</sup>

- 5.64 In the Council's view, this amendment reflects the general sentiment of previous decisions on coverage, and declaration under Part IIIA of the TPA, that some non trivial level of increased competition is necessary before coverage would be recommended.
- 5.65 The ability and incentive for a service provider to exercise market power to adversely affect competition in a dependent market is a necessary (although not sufficient) condition for access to promote competition. Prima facie, regulation of the terms and conditions of the provision of the service by the service provider in these circumstances is likely to promote competition.
- 5.66 In addition, a finding that the service provider has the ability and incentive to exercise market power to adversely affect competition in a dependent market is likely to mean that the barriers to entry in that market result from the natural monopoly characteristics of the facility and its bottleneck position. In the usual case, this finding would mean that access would reduce barriers to entry and promote competition in that dependent market.
- 5.67 By contrast, the service provider may not have the ability or incentive to exercise market power to adversely affect competition in the dependent market(s) where:
- (a) the facility does not occupy a bottleneck position in the supply chain for the service
  - (b) the service provider is constrained from exercising market power in the dependent market(s), perhaps by competitive conditions in the dependent market(s) and/or the market power of other participants in the market(s),  
or
  - (c) the incentives faced by the service provider are such that its optimal strategy is to maximise competition in the dependent market(s). It may be profit maximising, for example, for a service provider to promote increased competition in the dependent market(s) and maximise demand for the services provided by its facility.
- 5.68 Access is unlikely to materially promote competition in the dependent market(s) if the service provider does not have the ability and incentive to exercise market power to adversely affect competition in the dependent market(s).
- 5.69 Finally, the Council observes that the Tribunal has made it clear that promotion of competition should not be gauged in terms of either:

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<sup>67</sup> See Second Reading Speech, South Australian Hansard, Legislative Assembly, 9 April 2008, pp 2889.

- (a) the effect of access on particular competitors, such as a particular applicant seeking to have a pipeline covered, or
- (b) the delivery of efficient outcomes.

5.70 The Council considers that the assessment of promotion of competition should focus on the impact of access on the competitive environment generally, rather than on particular competitors. In the Sydney Airport decision, the Tribunal said:

The Minister and the Tribunal do not look at the promotion of ‘competitors’ but rather the promotion of ‘competition’. Such an analysis is not made by reference to any particular applicant seeking to have a service declared. At the point of time at which a decision is to be made as to whether or not to declare a service under s 44H, it may not be known who will be seeking access if the relevant service is declared. (at 21)

5.71 It further stated:

The Tribunal is concerned with furthering competition in a forward looking way, not furthering a particular type or number of competitors. (at 108)

5.72 The Tribunal noted in the Duke EGP decision (at 109) that criterion (a) is concerned with the promotion of competition, not with whether competition is efficient.<sup>68</sup>

### **Ability and incentive to exercise market power**

5.73 Whether competition will be materially enhanced as a result of access depends critically on the extent to which the incumbent service provider can and is likely, in the absence of coverage, to use market power to adversely affect competition in a dependent market. If a service provider has market power, and the ability and incentive to use that power to adversely affect competition in a dependent market, coverage would be likely to improve the environment for competition.

5.74 In the Duke EGP decision (at 116), the Tribunal considered a range of factors in assessing whether Duke EGP could exercise market power to hinder competition in the relevant dependent markets, including:

- (a) the commercial imperatives on Duke to increase throughput, given the combination of high capital costs, low operating costs and spare capacity
- (b) the countervailing market power of other participants in the dependent markets
- (c) the existence of spare pipeline capacity, and
- (d) competition faced by Duke from alternatives to the use of the Eastern Gas Pipeline in the dependent markets.

5.75 Following its consideration of these factors, the Tribunal concluded that Duke did not have sufficient market power to hinder competition in the dependent markets.

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<sup>68</sup> The effects of access on efficiency are considered under criterion (f) where appropriate.

5.76 In the Duke EGP decision the Tribunal did not indicate that it examined all the relevant factors for assessing competitive conditions in dependent markets in all instances. Rather, it focused on the pertinent aspects of industry and market structure of specific relevance to the Eastern Gas Pipeline. As the Tribunal stated:

There is no simple formula or mechanism for determining whether a market participant will have sufficient power to hinder competition. What is required is consideration of industry and market structure followed by a judgment on their effects on the promotion of competition. (at [116])

5.77 Access will be likely to materially increase competition in the dependent market(s) where the service provider has both the incentive and ability to use its market power to adversely affect competition in the dependent market(s).

5.78 In essence, there are three mechanisms by which the use of market power in the provision of the service for which coverage is sought by a service provider may adversely affect competition in a dependent market:

- (a) a service provider with a vertically related affiliate may engage in behaviour designed to leverage its market power into a dependent market to advantage the competitive position of its affiliate
- (b) where a service provider charges monopoly prices for the provision of the service, those monopoly prices may restrict participation in that market, and/or
- (c) explicit or implicit price collusion in a dependent market may be facilitated by the use of a service provider's market power. For example a service provider's actions may prevent new market entry that would lead to the breakdown of a collusive arrangement or understanding or a service provider's market power might be used to 'discipline' a market participant that sought to operate independently.

5.79 Where competition in a dependent market(s) is not effective, a service provider may nonetheless lack the incentive to exercise market power to adversely affect competition in a dependent market. In some situations, a service provider may have an incentive to engage in strategies designed to increase competition in a dependent market(s). If, for example, a service provider has no vertical interests in a dependent market(s), and its facility has excess capacity, then it may be profit maximising for the service provider to promote increased competition in the dependent market(s), reduce margins and prices in the dependent market(s), and increase incremental demand for the services provided by the facility. In these circumstances, the service provider would not have an incentive to engage in the conduct described in paragraph 5.78 and access is unlikely to promote competition in a dependent market.

5.80 Accordingly, in assessing whether a service provider has the ability and incentive to use its market power to adversely affect competition in a dependent market, the Council asks whether the service provider has the ability and incentive to engage in any of the types of conduct described in paragraph 5.78.

## Relationships of 'market power' in coverage to 'form of regulation factors'

- 5.81 As noted in Section 7 of Part C of the Guide, there is a relationship between the issues considered at the coverage stage and the issues considered in determining the appropriate form of regulation for the pipeline. Both of these questions involve the consideration of market power of the pipeline service provider. In the context of coverage, the question is focused upon whether sufficient market power exists such that competition would be materially promoted by access. In the context of the form of regulation, the focus is on the degree of market power which impacts on the effectiveness of each form of regulation in promoting access to the pipeline services.
- 5.82 Nonetheless, the types of market power issues associated with each of the form of regulation factors are likely to have some relevance for the assessment of market power in relation to a coverage application. Interested parties may find the guidance on the form of regulation factors in Section 7 of Part C of this Guide useful in analysing market power of a particular pipeline service provider. In particular, the statutory 'form of regulation factors' relating to market power are as follows:

### 16—Form of regulation factors

The form of regulation factors are—

- (a) the presence and extent of any barriers to entry in a market for pipeline services;
- (b) the presence and extent of any network externalities (that is, interdependencies) between a natural gas service provided by a service provider and any other natural gas service provided by the service provider;
- (c) the presence and extent of any network externalities (that is, interdependencies) between a natural gas service provided by a service provider and any other service provided by the service provider in any other market;
- (d) the extent to which any market power possessed by a service provider is, or is likely to be, mitigated by any countervailing market power possessed by a user or prospective user;
- (e) the presence and extent of any substitute, and the elasticity of demand, in a market for a pipeline service in which a service provider provides that service;
- (f) the presence and extent of any substitute for, and the elasticity of demand in a market for, electricity or gas (as the case may be);
- (g) the extent to which there is information available to a prospective user or user, and whether that information is adequate, to enable the prospective user or user to negotiate on an informed basis with a service provider for the provision of a pipeline service to them by the service provider.

## Time horizon for assessment

- 5.83 To assess whether access would promote competition, it is necessary to consider the time horizon over which this should be assessed. This will differ from pipeline to pipeline depending on the nature of the markets in question. The focus of the national gas objective on the long term interests of consumers suggests that the assessment should not focus purely on the immediate future. Additionally, the Council will consider the impact of anticipated future changes to the market, such as planned interconnections, expansions or acquisitions, which may impact the application of criterion (a) and determining an appropriate time horizon for assessment.
- 5.84 A consideration of whether access would promote a material increase in competition in a dependent market must be considered in association with a time horizon. The Council recognises that a conclusion as to whether access would improve the environment for competition in a dependent market may change over time due to changes in technology or market evolution.
- 5.85 An example is provided by the AGL Cooper Basin Natural Gas Supply Arrangements decision, in which the Tribunal recognised that substitution possibilities and market boundaries are changing over time, given the dynamic quality of gas markets and the emerging competition between gas and electricity due to technological change. The Tribunal defined the relevant market at three points in time for the purpose of assessing the competition effects of the long term supply contract between Australian Gas Light Company and a group of producers of natural gas in the South Australian sector of the Cooper Basin. The Tribunal stated:
- We have concluded, as canvassed with counsel in the course of the hearing, that the appropriate approach in this matter is to think in terms of a market expanding over time — i.e. an expanding market definition. Such an approach is consistent with both commercial reality and the traditional methodology of market definition, and is apt to expose the issues in this matter.
- In considering this expanding market, we specify three dated markets of interest: the market in 1986, the market today, and the market in ‘the future’ — perhaps ten or fifteen years hence. Quite obviously the geographic market is expanding over this time period, and the product market is also expanding, as we explain below.<sup>69</sup>
- 5.86 The focus of the national gas objective on the long term interests of consumers suggests that the assessment should not focus purely on the immediate future.
- 5.87 In assessing whether access would promote a material increase in competition in a dependent market, the Council may appropriately define that market at different points in time, to account for changes in technology and/or market conditions.
- 5.88 Alternatively, changes in market conditions may not result in a changing definition of a dependent market, but may nonetheless have implications for the competitive

<sup>69</sup> *Re Alliance Petroleum Australia Pty Ltd & Ors* [1997] ACompT 2 (14 October 1997) at [12-15].

conditions in the dependent market and thus have an impact on the criterion (a) assessment. Planned new entry or capital investment in expanded capacity, for example, may increase the alternatives to the use of the service in a dependent market and thus change conditions for competition in that market. These changes may have an impact on the ability of, and incentive for, the service provider to exercise market power to adversely affect competition in the market.

5.89 The time horizon adopted by the Council for the criterion (a) assessment will vary from case to case. In its assessment, the Council will account for foreseeable changes in technology and/or market conditions, having regard to the timing and probability of those changes. The Council is less likely to conclude that criterion (a) is satisfied where:

- (a) there are foreseeable changes in conditions such that criterion (a) would no longer be satisfied, and
- (b) there is a high probability of these changes occurring in the not too distant future.

5.90 While there is a time horizon to the assessment of both criteria (a) and (b), the time horizon over which the Council accounts for relevant changes for the two assessments may not necessarily be the same.

**(b) It would be uneconomic for anyone to develop another pipeline to provide the pipeline services provided by means of the pipeline**

**Links to Part IIIA**

5.91 Criterion (b) of s 15 of the NGL mirrors s 44G(2)(b) of the TPA which provides that 'it would be uneconomic for anyone to develop another facility to provide the service'. While Part IIIA used the word 'uneconomical' and the NGL 'uneconomic', in the Duke EGP decision the Tribunal stated that 'nothing turns upon this difference in language'.<sup>70</sup> Accordingly, the case law concerning criterion (b) in Part IIIA of the TPA is particularly relevant to the interpretation of this criterion.

**Social cost benefit test**

5.92 Criterion (b) is concerned with Australia's national interest not the private interests of any particular parties. The Council and the Tribunal have consistently found that the appropriate test for assessing whether criterion (b) is met is a social test and that the term 'uneconomic' should be construed in a social cost benefit sense rather than in terms of private commercial interests. In the Sydney Airport decision on Part IIIA the Tribunal explained that:

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<sup>70</sup> At [58].

If "uneconomical" is interpreted in a private sense then the practical effect would often be to frustrate the underlying intent of the Act. This is because economies of scope may allow an incumbent, seeking to deny access to a potential entrant, to develop another facility while raising an insuperable barrier to entry to new players (a defining feature of a bottleneck). The use of the calculus of social cost benefit, however, ameliorates this problem by ensuring the total costs and benefits of developing another facility are brought to account.<sup>71</sup>

5.93 This analysis is also consistent with the requirement to have regard to the national gas objective in applying this criterion.

### **'Another pipeline'**

5.94 In contrast to Part IIIA, the use of the word 'pipeline' rather than facility in coverage criterion (b) prevents the Council from considering whether a facility other than a pipeline could provide the services provided by the pipeline that is the subject of the application for coverage. Under coverage criterion (b), the Council cannot examine, for example, whether liquefying natural gas and then transporting it by ship may provide the service of gas transportation provided by the pipeline that is the subject of the application.<sup>72</sup>

### **'Pipeline services provided by means of the pipeline'**

5.95 The test focuses attention on the pipeline services provided by means of the pipeline which is the subject of the coverage application. 'Pipeline services' is defined by s 2 of the NGL to be:

- (a) a service provided by means of a pipeline, including—
  - (i) a haulage service (such as firm haulage, interruptible haulage, spot haulage and backhaul); and
  - (ii) a service providing for, or facilitating, the interconnection of pipelines; and
- (b) a service ancillary to the provision of a service referred to in paragraph (a),
  - but does not include the production, sale or purchase of natural gas or processable gas.

5.96 It will be important to clearly specify the services which are currently provided by the pipeline. In the Duke EGP decision the Tribunal considered that there were two ways of looking at the concept of pipeline services, by the markets they serve or point to point definitions. It preferred the latter as follows:

<sup>71</sup> At [205]. See also decision at [59].

<sup>72</sup> The Council can however consider competition from gas transported in this way in its assessment of coverage criterion (a).

The question of what constitutes the services provided by the pipeline is fundamentally a mixed question of fact and the proper construction of criterion (b), rather than a matter of economic analysis. Every haulage service will of necessity be from one point to another. That is the commercial service actually provided by the pipeline operator to its customers. That service may be of different use to the producers in the origin market or to the customers in the destination market, but it is the same service. No market analysis is necessary or appropriate in the description of the services provided by the pipeline. However, questions of market definition and market power do arise in the context of criterion (a).

NCC, in its Final Recommendation, noted that there were two possible approaches to the definition of the relevant services, namely identification of the services with respect to the markets they serve, or definition of the services in terms of both the start and end points of the service. NCC said that it preferred the second approach, for a number of reasons which it gave. We have come to the same conclusion, but because of the view which we take as to the proper construction of criterion (b). We should, however, add that the Code contemplates (for example in s 1.13) that coverage may occur in relation to part of a pipeline, which lends some slight support to the proposition that a haulage service is appropriately defined on a point to point basis, rather than by reference to the market/s which it serves.<sup>73</sup>

- 5.97 Accordingly, the relevant point to point service descriptions for the pipeline in question are the comparators to determine whether it would be economic to duplicate the pipeline in question. For distribution networks, the service definition will need to include the use of system services provided to retailers to serve customers in particular areas (rather than looking at each of those end users separately).

### **Natural monopoly and uneconomic to duplicate**

- 5.98 The assessment of criterion (b) centres on identifying whether a pipeline exhibits "natural monopoly" characteristics, such that a single pipeline is capable of meeting likely demand at lower cost than two or more pipelines. Therefore, it is uneconomic to duplicate the pipeline, and society's resources are most efficiently used and costs minimised if additional pipelines are not developed. In the Duke EGP decision, the Tribunal stated:

[the] test is whether for a likely range of reasonably foreseeable demand for the services provided by means of the pipeline, it would be more efficient, in terms of costs and benefits to the community as a whole, for one pipeline to provide those services rather than more than one.<sup>74</sup>

- 5.99 Under this approach, criterion (b) limits coverage to pipelines with natural monopoly characteristics. The key characteristics of a natural monopoly relate to the presence

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<sup>73</sup> At [69] - [70].

<sup>74</sup> At [137].

of significant economies of scale and/or economies of scope in the provision of pipeline services provided by means of the pipeline, the existence of substantial fixed (or capital) costs and relatively low variable (or operating) costs, and large and lumpy investment costs.

5.100 The technical definition of natural monopoly, indicates that a natural monopoly will exist if, over the relevant range of output, any division of each and every level of output within that range among two or more firms results in greater total costs of production than result if a single firm produces that level of output.<sup>75</sup>

5.101 Put more simply, a natural monopoly exists if a single source can produce every level of output in a given range of output at a lower cost than two or more sources.

5.102 In the Duke EGP decision, the Tribunal adopted this definition of natural monopoly in giving meaning to the term 'uneconomic':

We agree with the submissions of NCC that the 'test is whether for a likely range of reasonably foreseeable demand for the services provided by the means of the pipeline, it would be more efficient, in terms of costs and benefits to the community as a whole, for one pipeline to provide those services rather than more than one'. (at 137)

5.103 In the Council's view, for the purpose of criterion (b), a natural monopoly exists if, for the relevant range of demand, it is always cheaper for a single pipeline rather than multiple pipelines to provide the pipeline services.

5.104 Therefore, in assessing whether a pipeline is a natural monopoly, the Council may consider factors such as:

- (a) the size of the initial or start-up investment
- (b) the cost structure of operating the pipeline services
- (c) the existence of any other pipelines that provide the pipeline services
- (d) the nature of demand for the pipeline service, particularly the dynamic aspects such as growth or otherwise in demand
- (e) the current and maximum potential capacity of the pipeline, and
- (f) the existence of any environmental, planning or other regulations that prevent anyone else from building their own pipeline.

5.105 Natural monopoly characteristics are common to significant pipelines, where substantial fixed costs and low operating costs combine to generate economies of scale and scope over the range of reasonably foreseeable demand. Generally, under these conditions, one pipeline can supply the entire range of demand more cheaply than two or more pipelines can. This makes it economically efficient for only one

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<sup>75</sup> This is known as the sub-additivity condition for natural monopoly. A natural monopoly exists, over the relevant range of output, if the cost function of a firm is sub-additive. The cost function of a firm is sub-additive for a particular level of output if any division of that output among two or more firms results in greater costs of production than result if a single firm produces that level of output.

pipeline to service the entire foreseeable range of demand; in other words, the development of another pipeline to provide the service would amount to a wasteful use of society's resources.

5.106 The sufficient conditions for the existence of a natural monopoly, in effect, simply recognise that the following factors determine the existence of a natural monopoly:

- (a) pervasive **economies of scale**, whereby average costs per unit of output decrease as output rises. These may occur where a pipeline require large up-front investment, but has relatively low operating costs that vary little as more of the pipeline's potential capacity is brought on line (e.g. through looping or additional compression). Building and activating a gas distribution network, for example, involves substantial fixed costs, but the variable costs of sending more gas around a network once it is operating are relatively small. Unit costs thus decrease because the initial capital costs are spread over each additional unit of output. Rather than making a competitor develop a second network to compete with the existing network, it makes more economic sense to give that competitor access to the existing network so further economies of scale can be captured
- (b) **economies of scope**, whereby a pipeline is able to provide a range of different but complementary outputs at a lower total cost than that of separate pipelines providing the pipelines services. These may occur in the case of network externalities — that is, where the benefits to consumers of being linked to a network depend on the number of other consumers linked to the network, and
- (c) **incumbency advantages** — natural, economic or technological advantages associated with the initial establishment of a pipeline. These advantages could mean that new businesses may be unable to access the same advantages as the incumbent.

### Sustainability of natural monopoly

5.107 Where one firm can supply the entire range of demand more cheaply than two or more facilities, a natural monopoly exists. However, as Ordover and Lehr<sup>76</sup> state:

... even natural monopoly does not assure that all of the demand is served by a single firm. Not all natural monopolies are sustainable against cream-skimming entry (i.e. entry that seeks to serve only a portion of the market). For a particular combination of costs and market demand, entry on a smaller scale than the size of the market may be profitable, even though the cost of meeting total demand when it is supplied by multiple firms is higher. (p. 5)

<sup>76</sup> Ordover, J and Lehr, W 2001, 'Should coverage of the Moomba-Sydney pipeline be revoked?' in National Competition Council 202, *Final recommendation on the Application for Revocation of the Moomba to Sydney Gas Pipeline and the Dalton to Canberra Lateral*, November, <http://www.ncc.gov.au/pdf/REGaMoRe-002.pdf>

5.108 A pipeline can exhibit natural monopoly characteristics whether or not there is only one pipeline. As Posner<sup>77</sup> states:

The term [natural monopoly] does not refer to the actual number of sellers in a market but to the relationship between demand and the technology of supply. If the entire demand within a relevant market can be satisfied at lowest cost by one firm rather than by two or more the market is a natural monopoly regardless of the actual number of firms in it. (p. 1)

5.109 As previously discussed, criterion (b) requires a broad social construction (rather than a commercial view) of 'uneconomical'. While social considerations and private considerations are likely to lead to similar results in many cases, private considerations can sometimes make it commercially viable for another pipeline to be built even though this would be inefficient if all social costs were considered. Coverage and the application of the NGL generally does not prevent these situations. What these provisions seek is to make available the socially optimal sharing alternative.

5.110 In these circumstances, it is possible to envisage a case where criterion (b) is satisfied even though competing pipeline services exist. Criterion (b) is a test of whether a pipeline can serve the range of foreseeable demand for the pipeline services at less cost than that of two or more pipelines. The status of a pipeline against this test does not change merely because another pipeline is inefficiently developed.

5.111 The extent to which the inefficient development of another pipeline to provide the pipeline services relevant to an application for coverage constrains the behaviour of the service provider in the dependent markets is a matter relevant to the assessment of criterion (a), not criterion (b). Criterion (b) is concerned only with whether the pipeline exhibits natural monopoly characteristics, whereas criterion (a) assesses whether access will promote a material increase in competition. Criterion (a) is unlikely to be satisfied where a second inefficient pipeline has been developed, having a direct impact on the market power of an incumbent and has effectively made the dependent markets competitive.

5.112 In the Duke EGP decision, the Tribunal considered the potential for inefficient development of another pipeline to provide the service and it recognised this difference in the roles of criterion (b) and criterion (a). The Tribunal said:

Thus we accept that if a single pipeline can meet market demand at less cost (after taking into account productive allocative and dynamic effects) than two or more pipelines, it would be 'uneconomic', in terms of criterion (b), to develop another pipeline to provide the same services. ... it is a matter for a pipeline owner to decide whether or not to construct an 'inefficient' pipeline. Generally speaking, owners act on private cost, rather than social cost considerations. If development of a competitive pipeline is economic, in a

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<sup>77</sup> Posner, 1999, *Natural Monopoly and its Regulation*, 30<sup>th</sup> edition, Cato Institute, Washington DC.

private cost sense, and is driven by opportunities in the market, then this may have implications for the assessment of criterion (a). (at [64])

- 5.113 The Tribunal acknowledged that the inefficient development of another pipeline may occur where private cost and social cost considerations diverge. Further, the inefficient development of another pipeline (or facility) based on private cost considerations will be relevant to the assessment of criterion (a), not criterion (b), which posits a test based on social cost considerations.

#### **‘another pipeline to provide the service’**

- 5.114 Criterion (b) requires that it be uneconomical for anyone to develop ‘another pipeline to provide the service’. As discussed above, the pipeline is likely to be ‘uneconomical’ to duplicate if a single pipeline is capable of meeting likely demand at lower cost than two or more pipelines. In the Council's view, in this context the 'demand' in question is the demand for the pipeline services (ie the likely level of demand in the market for the pipeline service).

- 5.115 In the Sydney Airport decision, the Tribunal emphasised that criterion (b) requires that it be uneconomical to develop another facility to provide the same service as that provided by the facility. The Tribunal stated:

It is important to understand, in the terms of s 44H(4)(b), what it is that must be uneconomical for anyone to develop. It is not simply another ‘facility’ but rather ‘another facility to provide the service’; that is to say, the service provided by the use of aprons and hard stands at SIA [Sydney International Airport] to load and unload international aircraft at SIA and the service provided by the use of an area at that airport to store equipment and to transfer freight from the loading and unloading equipment to and from trucks. It should also be noted that s 44H(4)(b) requires satisfaction that it would be uneconomical to develop ‘another facility’ to provide that service. (at 190)

- 5.116 Accordingly, the Tribunal considered that criterion (b) required that it be uneconomical to develop ‘another facility’ to provide the service of providing, or making available, the use of freight aprons, hard stands, equipment storage areas and freight transfer areas for the specified purpose, ie the same service. It found that the proposed Sydney West Airport would not provide the same service as that provided by Sydney International Airport (SIA) and thus would not constitute ‘another facility’ for the purpose of criterion (b).

Given the Tribunal’s findings in relation to the definition of facility, would it be uneconomical for anyone to develop another facility to provide the service? The answer to this question is clearly, ‘yes’. This is because the very powerful economies of scale and scope of SIA discussed above preclude anyone, even the incumbent owner and operator, from developing another facility offering the physical infrastructure and the associated rich inheritance of market attributes at SIA. Any future Sydney West airport, for which SAACL has development responsibility, does not qualify as another facility since it is not an effective substitute in an operationally sensible time scale for those seeking access to the services at SIA declared by the Minister. Also it does not qualify in terms of the

manner in which we have construed s 44H(4)(b) as it would not provide a service for use at SIA. The criterion for declaration in s 44H(4)(b) is therefore satisfied. (at 202)

### **Assessment of the natural monopoly facility test for criterion (b)**

5.117 The assessment of criterion (b) under the natural monopoly approach depends on the economic characteristics of the pipeline.

5.118 To determine whether a pipeline is a natural monopoly it generally suffices to compare reasonably foreseeable demand for the pipeline services with the capacity of the pipeline (where the relevant information is available). If the capacity of the pipeline is sufficient to meet reasonably foreseeable demand for the pipeline services, then the pipeline is a natural monopoly and uneconomical to duplicate, and criterion (b) is satisfied.

5.119 If the pipeline does not have sufficient capacity to meet reasonably foreseeable demand for the pipeline services, but would have sufficient capacity following relatively low cost modifications, then the pipeline is again likely to be a natural monopoly and uneconomical to duplicate.

5.120 By contrast, if the reasonably foreseeable demand for the pipeline services outstrips both the existing capacity and maximum achievable capacity of the pipeline, then it will likely be economical to develop another pipeline to provide the pipeline services, with the result that criterion (b) will not be satisfied.

5.121 Similarly, if another existing pipeline could be modified at lower cost to meet the additional demand for the pipeline services, then it may be economical to develop that other pipeline to provide the pipeline services, with the result that criterion (b) may not be satisfied. The Council's approach to taking account of other existing pipelines in the criterion (b) assessment is discussed at paragraphs 5.125-5.132.

5.122 In cases where reasonable estimates of demand and capacity are unavailable or are unable to be reliably or accurately determined, then the assessment of criterion (b) must turn to identifying whether the economic characteristics that underpin a natural monopoly are present. Such an examination will focus on the issues and factors discussed in paragraphs 5.104 to 5.106.

5.123 In assessing whether it is uneconomic to 'develop' another pipeline, it is appropriate to consider the scope to adapt other pipelines that already exist. In the Duke EGP decision, the Tribunal stated:

There is no logic in excluding existing pipelines from consideration in the determination of whether criterion (b) is satisfied. The policy underlying the Code would not be advanced if the Tribunal were to proceed in that blinkered way. We therefore think it appropriate to enquire whether the MSP or the Interconnect provide or could be developed to provide the services provided by means of the EGP. (at 57)

5.124 The term 'develop' is sufficiently broad to encompass modifications or enhancements to existing pipelines. If an existing pipeline does not provide the pipeline services

provided by the pipeline subject to an application for coverage, but could economically be modified or expanded to do so, this must be considered in assessing criterion (b).

- 5.125 In assessing criterion (b), therefore, the Council must consider whether it would be uneconomic to develop either new or existing pipelines to provide the pipeline services of the pipeline the subject of an application for coverage.
- 5.126 Where, however, an existing pipeline already provides (or could provide with only minor modifications or enhancements) the pipeline services provided by the pipeline the subject of an application for coverage, it does not necessarily follow that criterion (b) will not be satisfied. A pipeline can have natural monopoly characteristics whether or not it is the only one. Private commercial considerations can make it commercially viable to build an additional pipeline even where an existing pipeline can service all likely demand and building the additional pipeline is inefficient and wasteful in terms of the social test to be applied in assessing criterion (b). The existence of another pipeline that provides (or could provide with modifications or enhancements) the pipeline services must be considered in two ways when assessing likely demand for the pipeline services.
- 5.127 First, a consideration of other existing pipeline that could be developed to provide the pipeline services may be critical to the outcome of the criterion (b) assessment where the pipeline would be unable to serve the reasonably foreseeable demand for the pipeline services without some modification or augmentation. In these circumstances, the Council would need to consider whether the additional demand for the pipeline services could be served at lower cost by modification or augmentation of the other existing pipeline or by modification or augmentation of the pipeline subject to coverage. If the former holds, then criterion (b) may not be satisfied.
- 5.128 In the Duke EGP decision, the Tribunal applied criterion (b) in circumstances where foreseeable demand for the services of the pipeline subject to coverage—namely, the Eastern Gas Pipeline—was expected to exceed the current capacity of that pipeline. As a result, the Tribunal considered whether other existing pipelines—namely, the Moomba–Sydney Pipeline and the Interconnect—could provide, or be developed to provide, the services of the Eastern Gas Pipeline. After concluding that the Moomba–Sydney Pipeline was not capable of being developed to provide the services subject to coverage (at 135), the Tribunal compared the incremental costs to develop the Eastern Gas Pipeline (the pipeline subject to coverage) and the Interconnect (the existing pipeline). The Tribunal concluded that criterion (b) was satisfied — that is, that it would be uneconomic to develop the Interconnect to provide the services of the Eastern Gas Pipeline.
- 5.129 A case-by-case assessment is required to determine whether criterion (b) is satisfied in circumstances where additional demand can be served at lowest cost by modification or augmentation of an existing pipeline other than the pipeline subject to an application for coverage. Care must be taken to ensure the assessment does not

involve an implicit assumption that the construction of the other existing pipeline was efficient.

5.130 Second, the existence of another pipeline that provides the pipeline services will be relevant to the identification of the reasonably foreseeable range of demand for those pipeline services. In these circumstances, the reasonably foreseeable demand for the pipeline services is that arising from both the demand that the pipeline the subject of an application for coverage would serve and the demand the competing pipeline would be likely to serve.

### **Meaning of 'anyone'**

5.131 The term 'anyone' does not include the service provider of the pipeline.<sup>78</sup> As the Tribunal noted in the Sydney Airport decision:

This interpretation is more consistent with the underlying policy of Part IIIA and economic and commercial commonsense. If 'anyone' were to include the provider owning or operating the bottleneck facility in issue, a second facility might be developed without a second competing service being available to prospective users. The bottleneck would persist. (at [201])

5.132 Where it is economical for any party to develop an alternative pipeline criterion (b) is not met. However, criterion (b) will likely be satisfied if:

- (a) there are overwhelming economies of joint production between the pipeline subject to coverage and the alternative pipeline such that it would only be economical for the provider of the pipeline subject to coverage to develop the alternative pipeline, or
- (b) the provider of the pipeline subject to coverage has development responsibility for the alternative pipeline. For example the Tribunal observed in the Sydney Airport decision that SAFL had development responsibility for the proposed Sydney West airport which was suggested as a possible alternative facility that could have provided the services for which declaration was sought.

### **Time horizon for assessment**

5.133 Consideration of whether it would be uneconomical for someone to develop another pipeline to provide the pipeline services has temporal elements. The Council recognises that a conclusion that it would be uneconomical for anyone to develop another pipeline to provide the pipeline services may change over time as a result of

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<sup>78</sup> The ability of the provider to develop a facility to provide the service may indicate it is generally economic for a facility to be duplicated unless the existing provider has advantages available to it but not other parties. In a natural monopoly situation such advantages are likely to exist and it is more appropriate to regard facilities developed in such circumstances as expansions of the provider's existing facility rather than a new development.

changes in demand and changes in supply conditions, such as those due to technological change.<sup>79</sup>

5.134 The Council may elect not to recommend coverage of a pipeline if, as a result of predicted and likely changes in demand and supply conditions, criterion (b) would no longer be satisfied during the time horizon for the criterion (b) assessment. The time horizon over which criterion (b) must be satisfied varies from case to case, and is determined with regard to the timing and probability of the foreseeable changes in demand and supply conditions. The Council notes that the focus of the national gas objective on the long term interests of consumers highlights that the assessment should not focus on the immediate future. Where, for example, the pipeline services are expected to become contestable in the future as a result of changes in demand and supply conditions, the Council may consider such matters as the investment timetable for competing investment in determining whether contestability will be introduced in the time horizon for the criterion (b) assessment. The Council may determine, therefore, that criterion (b) is not satisfied by reason of a foreseeable change in demand and supply conditions where there is a significant probability of these changes occurring in the not too distant future.

**(c) Access (or increased access) to the pipeline services provided by means of the pipeline can be provided without undue risk to human health or safety**

5.135 Under criterion (c) in s 15 of the NGL the Council must be satisfied that access to the pipeline services can be provided without undue risk to health and safety. In considering this criterion, the Council considers the following matters:

- (a) whether there is a statutory health and safety scheme which will apply to the pipeline services in circumstances where access is granted to third parties, and
- (b) whether the terms and condition of access can adequately deal with any safety issues.

5.136 The rationale for this criterion is that coverage should not occur where access or increased access to pipeline services may pose a legitimate risk to human health or safety.

5.137 Where pipelines require a degree of spare capacity to provide appropriate safety margins, then an appropriate level of spare capacity will need to be maintained and, if necessary, the pipeline's capacity expanded to allow for this. In addition, access to pipelines may need to be governed by conduct codes and operational guidelines. For a pipeline to be covered, access must be possible without compromising system and operational integrity, and safe scheduling must be feasible.

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<sup>79</sup> Similarly, the applicability of the other declaration criteria to a particular service may change over time.

- 5.138 The Council notes that if access is already being provided (and the application is therefore one relating to increased access), then this should not be automatically construed as evidence that access is being provided safely. The Council must still be satisfied that access or increased access can be provided without undue risk to human health or safety (Sydney Airport decision, at [210–211]).
- 5.139 The existence of relevant safety regulations may satisfy this criterion where these regulations deal appropriately with any safety issues arising from access to the pipeline service. The Council understands that all jurisdictions have legislation or licence conditions dealing with the safe operation of natural gas pipelines.
- 5.140 Additionally, the NGL itself has provisions relating to the safe operation of pipelines. In particular, the access arrangement can set out detailed safety conditions as part of the terms and conditions of access to the pipeline service. These terms and conditions must be applied by the arbitrator in any access dispute<sup>80</sup> and any expansion of capacity in an access dispute must be 'consistent with the safe and reliable operation of the pipeline'.<sup>81</sup>
- 5.141 Rules 113 - 116 of the National Gas Rules also provide a robust procedure to ensure that an access determination does not compromise the safety or integrity of the pipeline. Those rules provide as follows:

#### **113 Interpretation**

In this Part:

***expert safety report*** means a report by an independent expert on whether the provision of a requested pipeline service would be unsafe;

***safety of operation notification*** means a notification by a service provider to a prospective user that the service provider believes the provision of a pipeline service requested by the prospective user would be unsafe;

...

***unsafe*** – the provision of a pipeline service is unsafe if it is not reasonably possible for the service provider to provide it consistently with:

- (a) the safe operation of the relevant pipeline; or
- (b) prudent pipeline practices in the gas industry.

#### **114 Safety of operation notification**

- (1) If a service provider refuses to provide a requested pipeline service and an access dispute arises in consequence of the refusal, the service provider may, on or before the submissions lodgement date, give a safety of operation notification.

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<sup>80</sup> Section 189 of the NGL.

<sup>81</sup> Rule 118(2)(c)(ii) of the National Gas Rules.

- (2) A safety of operation notification is given (and may be withdrawn) by notice to the relevant dispute resolution body and the other parties to the dispute.
- (3) A safety of operation notification must set out the grounds on which the notification is based, including a statement of any facts and assumptions relevant to those grounds.

#### **115 Expert safety report**

- (1) When a service provider gives a safety of operation notification, it must submit the name of an independent expert who might be engaged to provide an expert safety report.
- (2) The relevant dispute resolution body may approve the person nominated by the service provider or some other person as the independent expert to provide an expert safety report.
- (3) The service provider must, on receiving notice of the approval, immediately engage the independent expert approved by the relevant dispute resolution body to provide an expert safety report on the requested pipeline service to which the access dispute relates.

#### **Note**

This subrule is a conduct provision for the purposes of the NGL. (See the Regulations, Clause 7 and Schedule 4.)

- (4) In carrying out the investigations necessary for the expert safety report, the approved independent expert must have regard to all relevant statutory or regulatory requirements or restrictions (including those imposed under the conditions of a licence).
- (5) When the independent expert provides the service provider with the expert safety report, the service provider must immediately give copies of the report to the relevant dispute resolution body and the other parties to the dispute.

#### **116 Access determination**

In proceedings for the resolution of the access dispute, the relevant dispute resolution body is bound by the findings of an approved independent expert in an expert safety report.

5.142 Accordingly, the dispute resolution body cannot override the independent expert's view of the safe operation of the pipeline.

5.143 In order to prove that this criterion is not satisfied in relation to a particular pipeline, a party will need to demonstrate how coverage under the NGL would result in an undue risk to human health or safety despite the extensive jurisdictional regulation and provisions in the NGL and Rules which protect against adverse safety risks.

**(d) Access (or increased access) to the pipeline services provided by means of the pipeline would not be contrary to the public interest**

5.144 Under criterion (d) in s 15 of the NGL, access must not be contrary to the public interest. When applying the equivalent test in s 44H(4)(f) of the TPA, the Tribunal stated in the Services Sydney decision at [192]:

This criterion does not require the Tribunal to be affirmatively satisfied that declaration would be in the public interest. Rather it requires that it be satisfied that declaration is not contrary to the public interest. It enables consideration of the overall costs and benefits likely to result from declaration and the consideration of other public interest issues which do not fall within criteria (a)-(e).

5.145 The term 'public interest' is not defined in the NGL but the Council considers that this term allows a consideration of a broad range of issues, with a particular focus on public interest issues raised directly by the national gas objective. Apart from the national gas objective, as with Part IIIA of the TPA, the Council also considers that public interest factors may include:

- (a) ecologically sustainable development
- (b) social welfare and equity considerations, including community service obligations
- (c) government legislation and policies relating to matters such as occupational health and safety, industrial relations, access and equity
- (d) economic and regional development, including employment and investment growth
- (e) the interests of consumers generally or of a class of consumers
- (f) the competitiveness of Australian businesses, and
- (g) the efficient allocation of resources.

5.146 Consideration of this criterion does not revisit the issues considered under the other coverage criteria. Rather it draws on the Council's conclusions in relation to those criteria. For example, where the Council has concluded that access will promote a material increase in competition in one or more dependent markets, this will give rise to benefits that should be included in the assessment of this criterion. Similarly where access will aid in avoiding duplication of a pipeline that exhibits natural monopoly characteristics, this too will lead to benefits that are appropriately considered under this criterion.

5.147 In the Duke EGP decision, the Tribunal clarified the interpretation of the public interest criterion (that is, criterion (d) for coverage under the then Gas Code) as follows:

... criterion (d) does not constitute an additional positive requirement which can be used to call into question the result obtained by the application of pars (a), (b) and (c) of the criteria. Criterion (d) accepts the results derived from the application of pars (a), (b) and (c), but enquires whether there are any other

matters which lead to the conclusion that coverage would be contrary to the public interest.<sup>82</sup>

- 5.148 The existence of a bottleneck or essential facility results in an inherent tradeoff in determining whether to cover the pipeline. The efficiency gains from coverage depend on the extent of market power possessed by the service provider. Satisfaction of criterion (a) suggests that the efficiency gains from coverage are likely to be substantial, but regulation is unlikely to be perfect — for example, where the regulator does not have perfect information, coverage may impose regulatory burdens, costs and inefficiencies. Coverage may not be the most efficient policy option. The Council recognises that regulation has its own costs and should not be mandated when the potential benefits from regulation are small relative to the inefficiencies and other burdens that regulation engenders.
- 5.149 The use of the double negative in criterion (d) — requiring satisfaction that access ‘would not be contrary to the public interest’ — does not constitute an additional positive requirement for satisfaction that access would be in the public interest. Rather, the Council must be satisfied that the overall costs of coverage do not outweigh the benefits of coverage. The extent of these benefits depends on the likely effect of coverage on competition in related markets considered under criterion (a) and the resultant positive effects on economic efficiency (identified in the consideration of this criterion (d)).

## Public interest considerations

### *Economic efficiency*

- 5.150 A key public interest consideration is the net impact of coverage on economic efficiency. This is consistent with the national gas objective. Economic efficiency must be assessed from the perspective of society as a whole and in respect of the long-term interests of the consumers of natural gas. The concept of economic efficiency involves the best use of society’s resources to maximise welfare. Economic efficiency encompasses:
- (a) producing at least cost — that is, technical/productive efficiency
  - (b) ensuring services are provided to those who value them most highly — that is, allocative efficiency, and
  - (c) preserving incentives for innovation and investment — that is, dynamic efficiency.
- 5.151 In considering whether access (or increased access) would be economically efficient, it is necessary to assess the efficiency gains and costs of coverage. It is important to avoid coverage where it may yield short term static gains in technical and allocative efficiency that constrain the realisation of longer term dynamic efficiency gains.

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<sup>82</sup> At [145].

5.152 The promotion of effective competition is generally consistent with the encouragement of economic efficiency. Economists generally consider that effectively competitive markets lead to conditions that encourage economically efficient outcomes. Where access (or increased access) promotes effective competition, efficiency gains are likely to result, including for the following reasons:

- (a) in the short term, the entry, or threat of entry, of new firms in downstream markets may encourage lower production costs for services such as the supply of natural gas to households (the promotion of productive or technical efficiency)
- (b) in the longer term, competitive pressures may stimulate innovation designed to reduce costs and develop new products (the promotion of dynamic efficiency), and
- (c) if the terms and conditions of access are appropriate, then all customers who value the service more than its cost of supply will be supplied (the promotion of allocative efficiency).

5.153 In other words, a promotion of competition such as to satisfy criterion (a) is likely to be associated with efficiency gains in the dependent market(s) relevant to criterion (d).

5.154 Coverage may also impose efficiency costs in the provision of the pipeline services. Just as the promotion of effective competition by coverage is likely to result in efficiency gains, the regulatory burden associated with coverage is likely to result in efficiency losses. The regulatory burden imposed on businesses by coverage —or by regulatory failure associated with coverage— may result in inefficiencies.

5.155 Potential efficiency losses from coverage include:

- (a) in the short term, the distortion of price signals, which may result in the allocation of resources to the provision of services that are not of most value to society (a reduction in allocative efficiency)
- (b) in the longer term, the dampening of incentives for innovation (a reduction of dynamic efficiency), and
- (c) in the longer term, the deterrence of investment (a reduction of productive or technical efficiency).

5.156 In advocating the inclusion of a public interest criterion for declaration (under Part IIIA of the TPA), the Hilmer Report identified the effects of regulation on incentives for future investment in infrastructure projects as a key consideration in any public interest assessment of an application for declaration. The Hilmer Report stated:

... when considering the declaration of an access right to facilities, any assessments of the public interest would need to place special emphasis on the need to ensure access rights did not undermine the viability of long-term

investment decisions, and hence risk deterring future investment in important infrastructure projects.<sup>83</sup>

5.157 Effects of access on service providers (including increases in a service provider's costs) are generally to be reflected in access costs payable by access seekers. Where efficiency losses incurred by a service provider are addressed in access charges or are otherwise prevented or reduced by the requirements governing determination of access disputes these will not generally be relevant to the consideration of criterion (d).

### **Regulatory costs**

5.158 The Council accepts that coverage creates regulatory costs that must be considered under criterion (d). These are the costs that service providers may incur in complying with the various obligations under the NGL. They also include the costs of the regulator and other public bodies in carrying out their functions in relation to a covered pipeline. The Council recognises these inherent regulatory burdens, costs and inefficiencies associated with coverage, and in applying the public interest test, it considers whether the costs of coverage outweigh the benefits.

5.159 Where the application is for a coverage recommendation, the Council will also be deciding the form of regulation for the pipeline. As such, the costs that should be considered are the costs which are likely to result from the application of that form of regulation. Where the application is to revoke coverage of a pipeline, the assessment will ordinarily focus on costs associated with the form of regulation currently applicable to the pipeline. However, if another form of regulation is available to the pipeline and would be less costly, the Council may also take the costs of that form of regulation into account.

5.160 In determining whether the benefits of coverage are likely to outweigh the costs, it may be helpful if information is available to compare the direct costs of coverage with the potential price reductions for the provision of the service where there is evidence of monopoly pricing by the service provider.

5.161 Indirect regulatory costs that may follow coverage include:

- (a) reduced incentives to invest in essential infrastructure
- (b) reduced incentives to innovate or provide flexible services
- (c) regulatory pricing rigidities and other rigidities in access contracts, which may reduce the ability of market participants to respond to changing market conditions and could lead to inefficiencies.

5.162 The Council is of the view that the regulatory costs which are taken into account under criterion (d) do not include any costs associated with the application for coverage as these are not costs that result from access (or increased access).

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<sup>83</sup> p 25.

## Disruption costs

- 5.163 The Council recognises that the provision of access to a pipeline may involve some disruption to the operations of the service provider. However, in general terms, any disruption costs can be adequately dealt with by the various provisions of the NGL and Rules which impose obligations on service providers.
- 5.164 In the absence of specific evidence as to why the safeguards in the NGL and Rules are generally ineffective or would be ineffective in respect of any particular application the Council must accept that the provisions will operate as intended. Any service provider opposing an application for a coverage recommendation should provide clear information on why these protections do not adequately deal with disruption costs either generally or in the context of their particular pipeline.

## Investment effects

- 5.165 It is important for Australia's economy that there is sufficient investment in natural gas pipelines. This is consistent with the national gas objective. The Council accepts that the enactment of the NGL, and the possibility of coverage for pipelines that are uneconomical to duplicate, created some additional risk for investors in pipelines that they may not receive the same level of return from their investment that they otherwise would have received. This 'regulatory risk' is attendant on the establishment of both Part IIIA of the TPA, the original Gas Pipelines Access Law and the new NGL regime. Some similar risk would likely have followed from any form of intervention aimed at addressing the policy issues underlying Part IIIA and the NGL. It is reasonable to assume that the MCE and Parliaments considered that these costs were outweighed by the benefits to Australia from effective regulation of access in the circumstances allowed for under the NGL where the pipeline satisfies the criteria set out in the NGL.
- 5.166 The NGL provides for service providers to receive a risk-adjusted commercial return on covered pipelines. Investors in pipelines can therefore expect that if their pipeline is covered and a third party access seeker successfully seeks mandated access through arbitration and/or an access arrangement is put in place, they will receive an appropriate return on their investment. This fact will form the background to access negotiations, and encourage a negotiated access arrangement that allows an appropriate return on investment. Some of the protections in the NGL in this regard include the fact that the regulator and dispute resolution body in making or approving an access arrangement or in any access dispute must take into account the revenue and pricing principles set out in s 24 of the NGL which provides as follows:
- (2) A service provider should be provided with a reasonable opportunity to recover at least the efficient costs the service provider incurs in—
    - (a) providing reference services; and
    - (b) complying with a regulatory obligation or requirement or making a regulatory payment.

- (3) A service provider should be provided with effective incentives in order to promote economic efficiency with respect to reference services the service provider provides. The economic efficiency that should be promoted includes—
  - (a) efficient investment in, or in connection with, a pipeline with which the service provider provides reference services; and
  - (b) the efficient provision of pipeline services; and
  - (c) the efficient use of the pipeline.
- (4) Regard should be had to the capital base with respect to a pipeline adopted—
  - (a) in any previous—
    - (i) full access arrangement decision; or
    - (ii) decision of a relevant Regulator under section 2 of the Gas Code;
  - (b) in the Rules.
- (5) A reference tariff should allow for a return commensurate with the regulatory and commercial risks involved in providing the reference service to which that tariff relates.
- (6) Regard should be had to the economic costs and risks of the potential for under and over investment by a service provider in a pipeline with which the service provider provides pipeline services.
- (7) Regard should be had to the economic costs and risks of the potential for under and over utilisation of a pipeline with which a service provider provides pipeline services.

5.167 Additionally, in an access dispute the dispute resolution body:

- (a) cannot prevent a user obtaining a sufficient amount of a pipeline service under a contract or previous access determination to be able to meet the user's reasonably anticipated requirements, measured at the time the access dispute was notified (s 188(1)(a))
- (b) cannot prevent a prospective user or user from obtaining, by the exercise of a pre-notification right, a sufficient amount of a pipeline service to be able to meet the prospective user's or user's actual requirements (s 188(1)(b))
- (c) cannot deprive a person of a relevant protected contractual right (s 188(1)(c))
- (d) may not require the service provider to extend the geographical range of the access dispute pipeline (r 118(1)(b))
- (e) cannot require a service provider to carry out an expansion of the capacity of a light regulation pipeline unless the prospective user funds the capacity expansion in its entirety (r 118(2)(a))

- (f) cannot require a service provider to fund, in whole or part, an expansion of the capacity of a full regulation pipeline unless the extension and expansion requirements of the applicable access arrangement provide for the relevant funding (r 118(2)(b)), and
- (g) must ensure that an expansion of capacity required under an access determination is:
- technically and economically feasible, and
  - consistent with the safe and reliable operation of the pipeline (r 118(2)(c)).

5.168 There is one possible element of the return on a particular investment for which Part IIIA and the NGL does not seek to compensate a pipeline investor that is required to provide access. That is, any monopoly profits arising from its power in a dependent market. To quote the Hilmer Report:

If there are indeed profit implications associated with the application of an access regime, the revenues in question will have been obtained at the expense not only of consumers but of a more efficient economy generally.<sup>84</sup>

5.169 Access under both Part IIIA of the TPA and the NGL is designed to eliminate such monopoly profits. To the extent that the application of NGL discourages investment that is predicated on such profits, this is not a cost, as it does not discourage efficient investment in infrastructure.

5.170 The ACCC and AER in decisions across a range of industries have accepted the importance of maintaining appropriate commercial returns for investment lest such investment be inefficiently deterred. In any event, the regulator is obliged to allow appropriate commercial returns and to consider investment effects in determining access prices and other terms in any arbitration of an access dispute.

5.171 In *Re: Application by ElectraNet Pty Limited (No 3)* [2008] ACompT 3 (30 September 2008) the Tribunal further emphasised that minimising regulatory risk to promote efficient investment is a central part of the regulatory framework:

Efficient investment in the long term interests of consumers will not be promoted if investors perceive a significant risk that the rules will change and they will not be able to recover the opportunity cost of capital reasonably invested. The minimisation of regulatory risk, consistent with the promotion of efficient investment, is one of the tenets that has driven the development of regulatory regimes in Australia. That tenet is reflected in the objective of the Law and in the revenue and pricing principles embodied in the Law.<sup>85</sup>

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<sup>84</sup> p 263.

<sup>85</sup> At [201].

## 6 Procedural requirements of coverage and revocation of coverage

### Applications

- 6.1 Any person may apply to cover a pipeline (s 92) and any person may apply to revoke coverage of a pipeline (s 102). In both cases the applications must be:
- (a) made to the Council in accordance with the Rules
  - (b) contain the information required by the Rules, and
  - (c) must be accompanied by the fee prescribed in the Regulations.
- 6.2 The information and requirements for making applications for coverage and revocation of coverage are contained within rr 15 and 18 of the National Gas Rules respectively.
- 6.3 The Regulations currently prescribe a fee<sup>86</sup> of \$7,500 for each coverage application and revocation of coverage application. The fee must be paid by cheque at the time an application is lodged with the Council. Cheques are to be made payable to the National Competition Council.
- 6.4 Applications can be made to the Council by mailing a hard copy of the application and payment of the application fee to:
- National Competition Council  
GPO Box 250  
Melbourne Victoria 3001
- and emailing an electronic copy of the application to [gas@ncc.gov.au](mailto:gas@ncc.gov.au).

### Requirements for coverage applications

- 6.5 The requirements for making applications to cover a pipeline (coverage determination) in r 15 of the National Gas Rules are as follows.
- (a) state the applicant's name and contact details**
- 6.6 An applicant should clearly identify the legal person who is seeking coverage (whether a natural person or a corporation), the name of the contact person in respect of the application and relevant contact details (including mailing address, phone numbers and email).

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<sup>86</sup> Regulation 14 and Schedule 5 of the *National Gas (South Australia) Regulations 2008*. Fees under the NGL are prescribed by *A New Tax System (Goods and Services Tax) (Exempt Taxes, Fees and Charges) Determination 2008 (No.2)* to not be consideration for a supply pursuant to *A New Tax System (Goods and Services Tax) Act 1999*. Refer subsection 81-5(2) of *A New Tax System (Goods and Services Tax) Act 1999*.

**(b) identify the pipeline for which coverage is sought**

- 6.7 As noted earlier, it is important for the coverage determination to clearly identify the particular pipeline to which coverage applies and distinguish that pipeline from other connected pipelines which are not covered. Accordingly, applications should be clear about which parts of a pipeline are on that basis the subject of the application, and will be assessed by the Council (noting that the Council and Minister retain a discretion to cover more or less of an integrated pipeline system).
- 6.8 Useful information to identify a pipeline includes:
- (a) the name by which the pipeline is commonly known
  - (b) the relevant pipeline licence number, and
  - (c) a map of the pipeline marking the parts of the pipeline for which coverage is sought.
- 6.9 The Council would also find it helpful if the applicant sets out who it understands is the service provider in respect of the pipeline, and any possible relationship between that service provider and participants in upstream and downstream markets, or pipelines serving any of the markets served by the pipeline which is the subject of the application.

**(c) give details of the pipeline's classification or, if there is no classification, the classification the applicant considers appropriate**

- 6.10 An uncovered pipeline may already have been classified under the Gas Pipelines Access Law or by an earlier coverage process under the NGL. The applicant should give details of any such classification.
- 6.11 Where there is no previous classification, the applicant should set out its view on whether:
- (a) the pipeline should be classified as a transmission or distribution pipeline in accordance with the pipeline classification criteria, and
  - (b) if the pipeline is a cross-boundary distribution pipeline, the jurisdiction which the pipeline is most closely connected with.
- 6.12 The guidance in Section 3 of this part of the Guide should assist applicants come to a view on these matters.

**(d) state the applicant's reasons for seeking coverage of the pipeline (including a demonstration of how coverage of the pipeline would give effect to the pipeline coverage criteria)**

- 6.13 The applicant should set out the reasons why the applicant in particular seeks to have the pipeline covered (to ensure that the application is not frivolous or vexatious) and the general reasons why the applicant believes each of the coverage criteria are satisfied in relation to the pipeline. The applicant needs to address each of the criteria separately and would be advised to address the issues raised in relation to

each criteria set out in Section 5 of this part of the Guide. The reasons should not just focus on the applicant's own circumstances, but the general consequences of coverage on the pipeline concerned.

**(e) include any information or documents on which the applicant relies in support of the application**

- 6.14 The applicant should submit to the Council the key factual and evidential materials which are necessary to back up the arguments presented in relation to each of the coverage criteria, and rebut potential arguments that certain criteria may not be met. This may include confidential information which the Council is obliged to keep confidential in accordance with ss 90 and 331 of the NGL.
- 6.15 The Council also notes that the more relevant information about the pipeline and markets in question that can be presented with the application, the quicker and more efficiently the Council can deal with the application. The Council does not have information gathering powers to compel information and so relies on affected persons to present the necessary evidence to establish their position. As the Council and relevant Minister need to be positively satisfied of the coverage criteria to apply coverage to the pipeline, a lack of essential information may mean that the Council and relevant Minister are unable to be satisfied on the information provided. Additionally, the restrictions on new information in the merits review provisions of the NGL means that new information which may have been able to satisfy the Council or relevant Minister of the coverage criteria cannot be used to make out a ground of review.
- 6.16 In particular, the applicant would be advised to present as much information as they are able to in relation to the matters which those applying to revoke coverage of a pipeline are required to provide under s 18(2). Namely:
- (a) the capacity of the pipeline and the extent to which that capacity is currently utilised; and
  - (b) for a transmission pipeline, a description of:
    - (i) all locations served by the pipeline (i.e. all locations at which receipt or delivery points for natural gas carried by the pipeline exist); and
    - (ii) all pipelines that currently serve the same locations; and
    - (iii) all pipelines that currently pass within 100 km of any location served by the pipeline; and
  - (c) for a distribution pipeline, a description of:
    - (i) the geographical area served by the pipeline; and
    - (ii) the points at which natural gas is, or is to be, injected into the pipeline; and
  - (d) a description of the pipeline services provided, or to be provided, by the pipeline; and

- (e) an indication of any other sources of energy available to consumers of gas from the pipeline; and
- (f) the identity of the parties with an interest in the pipeline and the nature and extent of each interest; and
- (g) a description of the following relationships:
  - (i) any relationship between the owner, operator and controller of the pipeline (or any 2 of them);
  - (ii) any relationship between the owner, operator or controller of the pipeline and a user of pipeline services or a supplier or consumer of gas in a location or geographical area served by the pipeline;
  - (iii) any relationship between the owner, operator or controller of the pipeline and the owner, operator or controller of any other pipeline serving any one or more of the same locations or the same geographical area; and
- (h) an estimate of the annual cost to the service provider of regulation; and
- (i) any other information the applicant considers relevant to the application of the National Gas Objective or the pipeline coverage criteria in the circumstances of the present case.

6.17 These are further explored below.

### **Requirements for coverage revocation applications**

6.18 The requirements for making applications to revoke coverage of a pipeline (coverage revocation determination) in r 18 of the National Gas Rules are as follows.

#### **(1)(a) state the applicant's name and contact details**

6.19 An applicant should clearly identify the legal person who is seeking to revoke coverage (whether a natural person or a corporation), the name of the contact person in respect of the application and relevant contact details (including mailing address, phone numbers and email). The applicant should indicate whether or not they are the service provider of the pipeline in question.

#### **(1)(b) state whether the application is for revocation of coverage for the whole, or part only, of the covered pipeline**

6.20 As noted earlier, it is important for the coverage revocation determination to clearly identify the particular pipeline to which coverage is revoked and distinguish that pipeline from other connected pipelines which may remain covered. Accordingly, applications should be clear about which parts of a pipeline are the subject of the application for revocation, and will be assessed by the Council (noting that the Council and Minister retain a discretion to revoke coverage of more or less of the covered pipeline).

**(1)(c) state the applicant's reasons for the application (including a demonstration of how the coverage revocation determination would give effect to the pipeline coverage criteria)**

- 6.21 The applicant should set out the reasons why the applicant in particular seeks to have the coverage determination revoked (to ensure that the application is not frivolous or vexatious) and the general reasons why the applicant believes one or more of the coverage criteria are not satisfied in relation to the pipeline. The applicant needs to address the criteria separately and would be advised to address the issues raised in relation to each criteria set out in Section 5 of this part of the Guide. The reasons should not just focus on the applicant's own circumstances, but the general consequences of revocation on the pipeline concerned (including its users and end users).
- 6.22 Where the applicant does not want to dispute that one or more of the coverage criteria are met, the applicant should state this in the application and the reasons why the criterion remains satisfied.

**(1)(d) include information, and be accompanied by the documents, on which the applicant relies in support of the application.**

- 6.23 The applicant should submit to the Council the key factual and evidential materials which are necessary to back up the arguments presented in relation to the coverage criteria which it claims are not satisfied, and rebut potential arguments that certain criteria are met. This may include confidential information which the Council is obliged to keep confidential in accordance with ss 90 and 331 of the NGL.
- 6.24 The Council also notes that the more relevant information about the pipeline and markets in question that can be presented with the application, the quicker and more efficiently the Council can deal with the application. The Council relies on affected persons to present the necessary evidence to establish their position. As the Council and relevant Minister need to be satisfied that one or more of the coverage criteria are not met to revoke coverage of the pipeline, a lack of essential information may mean that the Council and relevant Minister are unable to be satisfied on the information provided. Additionally, the restrictions on new information in the merits review provisions of the NGL mean that new information which may have been able to satisfy the Council or relevant Minister cannot be used to make out a ground of review.

**(2)(a) the capacity of the pipeline and the extent to which that capacity is currently utilised**

- 6.25 This requirement primarily relates to the maximum capacity of pipeline throughput on the central parts of the pipeline (rather than every receipt point) and the manner in which that capacity is being utilised. Where pipeline usage is relatively stable and variations are due to seasonal factors, average utilisation in summer and winter may be sufficient. Where pipeline usage is more erratic and driven by peaks (such as high

electricity prices), some discussion of the utilisation in those peak periods may be necessary.

- 6.26 The information should be focused upon capacity which prospective users are likely to seek access to. Applicants are also be advised to provide information about the extent to which the capacity of the pipeline could be extended or expanded to accommodate prospective users and the potential costs of such extensions and expansions.

**(2)(b) for a transmission pipeline, a description of:**

- (i) all locations served by the pipeline (i.e. all locations at which receipt or delivery points for natural gas carried by the pipeline exist); and**
- (ii) all pipelines that currently serve the same locations; and**
- (iii) all pipelines that currently pass within 100 km of any location served by the pipeline;**

- 6.27 In respect of transmission pipelines, the applicant should describe the location of all of the receipt and delivery points for the pipeline in question and any other obvious points on the pipeline which might easily provide a new receipt or delivery point (e.g. a coal seam gas field near the pipeline or a potential load such as a mine). The applicant should then set out what other pipelines currently provide natural gas to those locations and any other pipeline which is within 100 km of any one of those locations.

**(2)(c) for a distribution pipeline, a description of:**

- (i) the geographical area served by the pipeline; and**
- (ii) the points at which natural gas is, or is to be, injected into the pipeline;**

- 6.28 In respect of distribution pipelines, the applicant should clearly set out either by a map and/or postcode areas the area served by the pipeline network and the points at which gas currently is, or is able to be, injected into the pipeline. This includes receipt points from transmission pipelines, gas production facilities and gas storage facilities.

**(2)(d) a description of the pipeline services provided, or to be provided, by the pipeline**

- 6.29 This requirement can be satisfied by setting out the basic parameters of each pipeline service provided or to be provided by means of the pipeline, including any services which differ depending on the location of the user's receipt or delivery points, and other specialised services for particular users which are being or are to be provided. The understanding of each of the services provided is essential to weighing up the market power associated with the basket of services being provided. The applicant

should describe each service in sufficient detail for the Council to analyse the consequences of continuing to apply the access regime to these services. The description of services might usefully be taken from the service provider's access arrangement, or information published by a pipeline which has been granted a light regulation determination under r 36 of the National Gas Rules.

**(2)(e) an indication of any other sources of energy available to consumers of gas from the pipeline**

6.30 This should set out the substitution possibilities for the consumers of gas served by the pipeline. Some idea of whether particular large users have dual fuel capabilities will be important, as will other potential bypass opportunities. The nature of consumers' usages, such as the reliance of end users on gas for heating or the use of natural gas as a feedstock, may be relevant to fully understanding the extent to which the other sources of energy are a realistic option for those consumers.

**(2)(f) the identity of the parties with an interest in the pipeline and the nature and extent of each interest**

6.31 This requirement relates to the structure of each pipeline service provider for the pipeline and other persons with an interest in the pipeline, such as ownership interests in a service provider. As a matter of practicality, where a pipeline service provider's shares are held by a large number of individuals an appropriate threshold will need to be found for those with 'an interest' relevant to the analysis. At the very least, shareholders owning a shareholding of 5 per cent or more of a service provider are expected to be identified. The need to explain the interests involved may differ depending upon the ability for the person to exercise control over the operation of the pipeline or profit from any exercise of market power in either the provision of pipeline services or associated upstream or downstream markets.

**(2)(g) a description of the following relationships:**

- (i) any relationship between the owner, operator and controller of the pipeline (or any 2 of them);**
- (ii) any relationship between the owner, operator or controller of the pipeline and a user of pipeline services or a supplier or consumer of gas in a location or geographical area served by the pipeline;**
- (iii) any relationship between the owner, operator or controller of the pipeline and the owner, operator or controller of any other pipeline serving any one or more of the same locations or the same geographical area**

6.32 This requirement focuses on the relationship between various service providers of a pipeline, users in upstream and downstream markets and other pipelines which may

potentially compete with the pipeline. To establish that any of these relationships are unlikely to produce anti-competitive effects or an abuse of market power, an applicant should set out what has been put in place to mitigate the likelihood of that occurring.

### **(2)(h) an estimate of the annual cost to the service provider of regulation**

- 6.33 This requirement is designed to allow the Council to clearly understand the differential costs involved in regulation under the NGL to assist in applying the public interest criterion of the coverage criteria. To make the cost estimate meaningful, a breakdown on how it was arrived at (including relevant assumptions, such as the level of access disputes or cost of access arrangement approvals) and what constitutes the annual cost will be essential. The analysis and substantiation of the various transaction costs involved in each regulatory approach will be an important factor for the decision making process.
- 6.34 The applicant should focus on costs associated with the form of regulation currently applicable to the pipeline, however if another form of regulation is available to the pipeline and would be less costly, the Council may also take the costs of that form of regulation into account.

### **(2)(i) any other information the applicant considers relevant to the application of the National Gas Objective or the pipeline coverage criteria in the circumstances of the present case**

- 6.35 This allows the applicant to bring forward other relevant material to assist the application of the coverage criteria. The applicant should ensure that the application as a whole contains all relevant information to the application of the statutory test and has not failed to disclose information which it considers material but unhelpful to its application. This may include information about significant developments which the applicant knows are likely to occur, such as a change in ownership of the pipeline in question.

### **False or misleading information**

- 6.36 Persons submitting information to the Council should note that the giving of false or misleading information is a serious offence. In particular, s 137.1 of the Commonwealth Criminal Code makes it a criminal offence for a person to supply information to a Commonwealth entity 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.

### **How the Council deals with applications**

- 6.37 The Council is required to deal with applications in accordance with the Rules (ss 93 and 103). The requirements in relation to dealing with applications can then be found in rr 16 and 19 of the National Gas Rules.

6.38 Section 95 then governs the coverage recommendation itself:

**95—NCC coverage recommendation**

- (1) Subject to sections 94 and 96, the NCC must recommend to the relevant Minister that the pipeline the subject of the application—
- (a) be a covered pipeline; or
  - (b) not be a covered pipeline.

Note—

See also Chapter 3 Part 2 Division 1 Subdivision 1.

- (2) A recommendation under this section must—
- (a) be made in accordance with this Law and the Rules; and
  - (b) be made within the time specified by the Rules; and
  - (c) contain the information required by the Rules; and
  - (d) be given to the persons specified by the Rules; and
  - (e) be made publicly available in accordance with the Rules.
- (3) A recommendation under this section may recommend an outcome different from the outcome sought in the application under section 92.

Example—

An applicant may apply for a determination that the whole of a pipeline be a covered pipeline. The NCC may recommend that only a part of the pipeline the subject of the application be covered or may recommend that the pipeline not be covered.

- (4) A recommendation under this section must be delivered to the relevant Minister without delay.

**Deferring applications associated with tender approval pipelines**

6.39 Sections 94 and 96 of the NGL are designed to ensure the integrity of processes to bring a pipeline into the regime by a competitive tendering process. It is possible that a person may seek to undermine the intent of the tendering arrangements by trying to cover a proposed pipeline and have an access arrangement apply which is not consistent with the tendering arrangements. Sections 94 and 96 provide mechanisms to stop such attempts. They provide as follows:

**94—NCC may defer consideration of application in certain cases**

- (1) This section applies if an application under section 92 is made in relation to a proposed pipeline after—
- (a) an application has been made to the AER under the Rules for the approval, by the AER, of the tender process for the construction and operation of the proposed pipeline as a competitive tender process; or

- (b) a tender approval decision has been made in respect of the tender process for the construction and operation of the proposed pipeline.
- (2) The NCC may defer consideration of whether to make a recommendation in respect of the application until—
  - (a) the application for the approval, by the AER, of the tender process for the construction and operation of the proposed pipeline as a competitive tender process has been rejected by the AER under the Rules; or
  - (b) the tender approval decision—
    - (i) has been revoked under the Rules; or
    - (ii) has lapsed as provided under the Rules.

...

**96—NCC must not make coverage recommendation if tender approval decision becomes irrevocable**

Despite anything to the contrary in this Division, the NCC—

- (a) must not make a recommendation under section 95 if the pipeline is the subject of a tender approval decision that—
  - (i) has not lapsed as provided under the Rules; or
  - (ii) is not revoked under the Rules; and
- (b) must, for the purposes of paragraph (a), treat the application as having never been made.

6.40 Similarly for coverage revocation recommendations, s 104 of the NGL is in equivalent terms to s 95. It provides as follows:

**104—NCC coverage recommendation**

- (1) The NCC must make a recommendation to the relevant Minister as to whether the covered pipeline the subject of the application should continue to be a covered pipeline.

Note—

See also section 119.

- (2) A recommendation under this section must—
  - (a) be made in accordance with this Law and the Rules; and
  - (b) be made within the time specified by the Rules; and
  - (c) contain the information required by the Rules; and
  - (d) be given to the persons specified by the Rules; and
  - (e) be made publicly available in accordance with the Rules.
- (3) A recommendation under this section may recommend an outcome different from the outcome sought in the application under section 102.

Example—

An applicant may apply for a determination that revokes the coverage of a covered pipeline by means of which the provider provides pipeline services. The NCC may recommend that the coverage of the covered pipeline be only partly revoked or not be revoked.

- (4) A recommendation under this section must be delivered to the relevant Minister without delay.

### **Applications that do not comply with the Rules**

6.41 An application received by the Council that does not comply with the requirements set out in rr 15 or 18 will not comply with the requirements in ss 92(2) and 102(2) of the NGL that the application 'be in accordance with the Rules'. The Council is not obliged to consider an application that has not been made in accordance with the Rules and has the power to reject non-compliant or frivolous proposals under r 10. That rule provides that a decision maker may, despite any other provision of the Rules, reject a proposal (i.e., an application for a coverage determination or coverage revocation determination)<sup>87</sup> on the ground that:

- (a) the proposal has not been made in accordance with the Law, or
- (b) relevant information or materials have not been provided as required by the Law, or
- (c) the proposal is frivolous or vexatious.

6.42 A decision to reject a proposal under r 10 must be made within 10 business days after receipt of the proposal by the decision maker, and the decision must also:

- (a) be made in writing, and
- (b) set out the reasons for the decision, and
- (c) be given to the proponent without delay  
(see rr 10(2) and (3)).

### **Applying the standard consultative procedure**

6.43 The central requirements in relation to dealing with valid applications are rr 16(1) and 19(1) which provide that such applications must be dealt with in accordance with the 'standard consultative procedure'. The 'standard consultative procedure' is defined in r 3 to mean the procedure for consultative decision making laid down in r 8. Rule 8(1) provides that if the Law requires a decision maker to deal with a proposal in accordance with the standard consultative procedure, the decision maker must proceed in accordance with r 8.

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<sup>87</sup> The term 'proposal' for the purposes of r 10 means: (a) an application; or (b) an access arrangement proposal; or (c) a proposal that a decision maker itself initiates for making a decision of a particular kind under the NGL (see r 7).

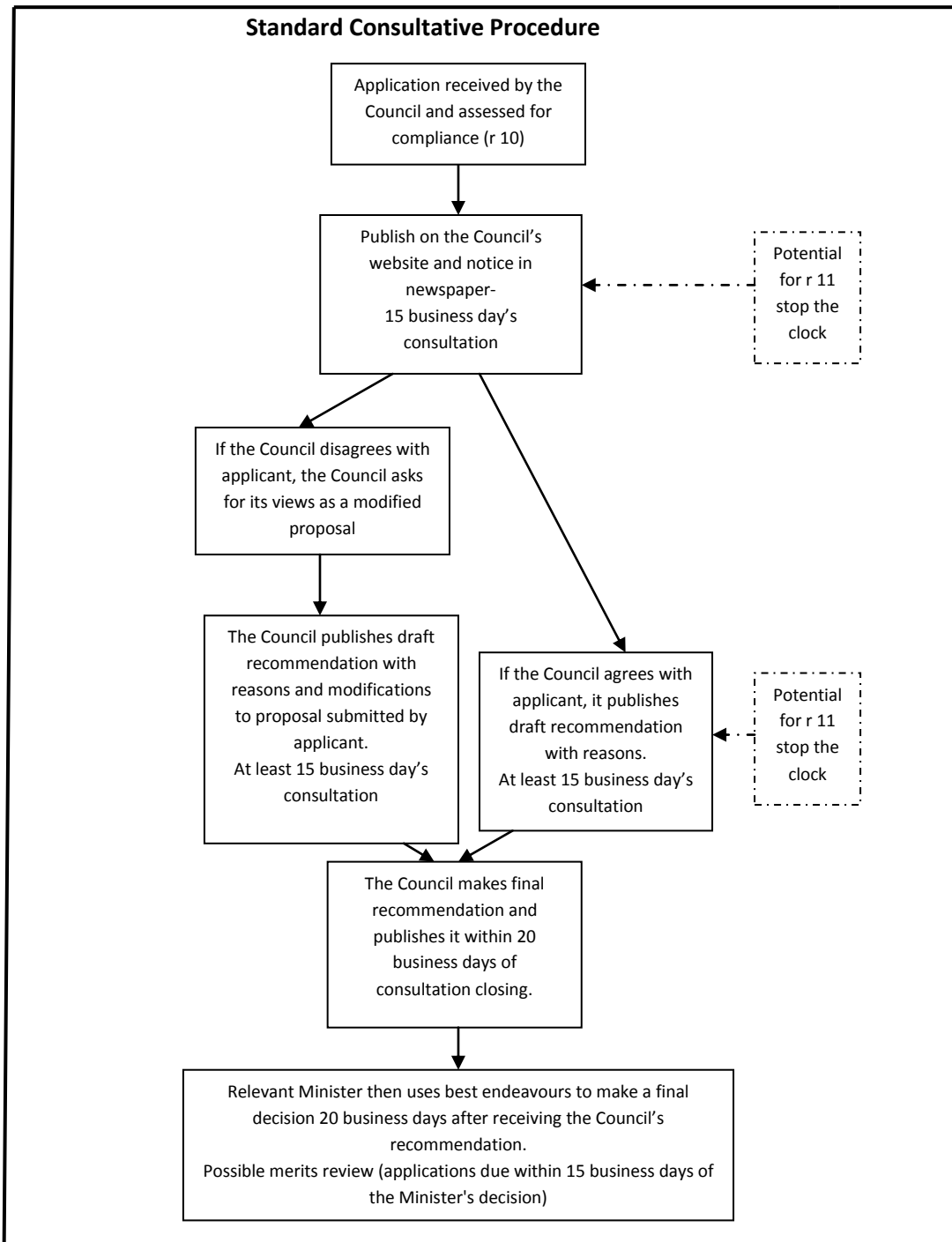
6.44 Rule 8 sets out the standard consultative procedure, and relevantly provides:

- (2) The decision maker must proceed as follows:
  - (a) the decision maker must publish a notice on its website and in a newspaper circulating generally throughout Australia:
    - (i) describing the proposal and giving the address of a website at which the proposal can be inspected; and
    - (ii) inviting written submissions on the proposal within 15 business days of the date of the notice; and
  - (b) the decision maker must, after considering relevant submissions made within the time allowed in the notice and other matters the decision maker considers relevant, make a draft decision; and
  - (c) if the draft decision identifies changes to the proposal that should, in the decision maker's opinion, be made, the decision maker must:
    - (i) ...
    - (ii) if someone else is the proponent – notify the proponent of the decision and the reasons for it and give the proponent a reasonable opportunity to modify its proposal in the light of the decision;
  - (d) the decision maker must then publish, on its website and in any other way the decision maker considers appropriate:
    - (i) the draft decision; and
    - (ii) any modification of the proposal made in the light of the draft decision; and
    - (iii) a notice inviting written submissions and comments on the draft decision, and (if applicable) the modified proposal, within a period (at least 15 business days) stated in the notice;
  - (e) the decision maker must, within 20 business days after the end of the period allowed for making submissions and comments on the draft decision, consider all submissions and comments made within the time allowed and make its final decision.
- (3) A draft or final decision must:
  - (a) be in writing; and
  - (b) state the terms of the decision and the reasons for it.
- (4) After making a final decision, the decision maker must, without delay:
  - (a) if the decision is in the nature of a recommendation – deliver the final decision to the authority or person to whom the recommendation is addressed; and

- (b) give copies of the final decision to the parties to the administrative process in which the decision is made; and
- (c) publish the final decision on the decision maker's website; and
- (d) make the final decision available for inspection during business hours at the decision maker's public offices.

In brief, the standard consultative procedure works as follows:

**Figure 2 Standard Consultative Procedure**



### Further details about the standard consultative procedure

- 6.45 It should be noted that the consultation on the original proposal is set at 15 business days by r 8(2)(a)(ii). A business day is a weekday which is not a public holiday simultaneously in all States and Territories.<sup>88</sup>
- 6.46 After consultation ends, the Council will consider all of the issues raised and make its draft recommendation. Rule 8(2)(c)(ii) then requires the Council to consider whether there are 'any changes to the proposal that should... be made' and, if so, notify the applicant of the decision, the reasons for it and give the proponent an opportunity to modify its proposal. In the context of applications for coverage or revocation of coverage, where the Council does not agree with the application, the likely application of r 8(2)(c)(ii) will mean that the Council is obliged to give the draft recommendation first to the applicant and ask them if they wish to submit a revised proposal in light of the Council's decision. The rules require this to be a 'reasonable opportunity' but do not specify a period. If the applicant chooses to submit a revised proposal in light of the draft recommendation, r 8(2)(d) requires the Council to publish on its website this proposal with the decision it first gave to the applicant. The rules do not contemplate the Council considering the revised proposal or modifying its decision in light of what has been put before publication.
- 6.47 Once a draft decision and any revised proposal have been published on the Council's website, the Council must specify a public consultation period in a notice on its website and that period must be at least 15 business days (r 8(2)(d)(iii)). The Council considers that 15 business days would ordinarily be long enough except in circumstances where the decision raises particularly difficult or complex issues.
- 6.48 The final recommendation must be:
- (a) in writing with full reasons (r 8(3))
  - (b) delivered to the relevant Minister (s 18(4)(a))
  - (c) given to the applicant and any other party which has been actively involved in the decision making process (r 8(4)(b))
  - (d) be published on the Council 's website (r 8(4)(c)), and
  - (e) available for inspection at the Council's office (r 8(4)(d)).
- 6.49 It may be necessary for confidential information to be shared between the AER, ERA and Council to ensure that a proper consideration of all the issues will be undertaken. This is possible under ss 30 and 90 of the NGL and s 44AAF of the TPA.<sup>89</sup>

<sup>88</sup> See clause 10 of Schedule 2 to the NGL.

<sup>89</sup> See in particular regulation 7, item 1.1 of the *Trade Practices Regulations* which prescribes the Council for the purpose of s 44AAF(3)(e) of the TPA.

## **Requirements for a coverage determination or coverage revocation recommendation– rr 16(4) and 19(4))**

6.50 Further to the requirements of the standard consultative procedure, rr 16(4) and 19(4) provide that Council recommendations must:

- (a) be in writing<sup>90</sup>
- (b) identify the covered pipeline to which the recommendation relates
- (c) include a reference to a website at which a description of the pipeline can be inspected, and
- (d) state the terms of the recommendation and the reasons for it.

6.51 The Council's recommendations must be given to the relevant Minister without delay (ss 95(4) and 104(4)). The relevant Minister is then required to use their best endeavours to make a final decision within 20 business days (see ss 99 and 106 and rr 17 and 20).

### **Time limits for the recommendation**

6.52 Subrules 16(2) and 19(2) provide that coverage recommendations and coverage revocation recommendations are to be made within 4 months of receiving the application. However, this period needs to be understood in the context of the provisions below.

### **Calculating time**

6.53 Rule 11 assists in calculating time. It allows a decision-maker, when calculating elapsed time (such as the 4 months provided for in rr 16(2) and 19(2)), to disregard any of the following periods:

- (a) any period allowed to the proponent for correction or revision of the proposal
- (b) any period taken by the proponent or any other person to provide information, relevant to the decision maker's decision on the proposal, in response to a notice or requirement issued or made by the decision maker under the NGL
- (c) any period allowed for public submissions on the proposal or on a draft decision on the proposal
- (d) any period allowed for submissions on a proposal by the AER to disclose confidential information, any period then taken by the AER to consider the submissions and decide whether to disclose the information, and any period occupied by a review of the decision

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<sup>90</sup> Note 'writing' is defined broadly in clause 10 of Schedule 2 to the NGL as including 'any mode of representing words in a visible form'.

- (e) the period between commencement and conclusion of court proceedings to determine questions arising from the proposal or the decision maker's handling of the proposal.

6.54 Where the Council makes a decision under r 11 to disregard a particular period, the Council must give notice of that decision to the proponent and must also publish notice of the decision on its website (see r 11(2)).

### **Extending time limits**

6.55 Under r 12(1) the Council has the power to extend time limits, such as the 4 months in which it is required to make a coverage recommendation or coverage revocation recommendation. However, under r 12(2) the power to extend the 4 month time limit can only be exercised if:

- (a) the proposal involves questions of unusual complexity or difficulty, or
- (b) the extension of time has become necessary because of circumstances beyond the Council's control.

6.56 If the Council decides to extend this 4 month time limit, it must give notice of the extension to the proponent giving reasons for the extension. Additionally, it must publish notice of the extension (and reasons) on its website and in a newspaper circulating generally throughout Australia (see rr 12(3) and (4)). However, in relation to coverage recommendations and coverage revocation recommendations, the 4 month time limit cannot be extended by more than 2 months (rr 16(3) and 19(3)).

### **Decisions made out of time**

6.57 Rule 14 operates so that where the Council fails to make a decision within 'an overall time limit', it must report on its failure to the MCE (see r 14(2) for the reporting requirements). An 'overall time limit' is defined in r 7 to mean 'the time within which a decision maker is required by the NGL to make a final decision on a proposal'. This would include, therefore, any extensions made to a time limit under r 12.

6.58 Non-compliance with a time limit does not, however, invalidate a decision made by the Council (see s 332).

### **Summary of requirements for coverage recommendations**

6.59 Accordingly, for the purposes of ss 95(2) and 104(2) a coverage recommendation or coverage revocation recommendation is:

- (a) 'made in accordance with this Law and the Rules' if it follows the standard consultative procedure and other requirements set out above
- (b) 'made within the time specified by the Rules' if it is made within the 4 month period (taking into account extensions and stop the clock requirements)
- (c) 'contain(s) the information required by the Rules' if it is in writing, identifies the covered pipeline to which the recommendation relates, includes a

reference to a website at which a description of the pipeline can be inspected and states the terms of the recommendation and the reasons for it

- (d) 'given to the persons specified by the Rules' if it is given to the applicant and all other persons involved in the administrative process of making the recommendation, and
- (e) 'made publicly available in accordance with the Rules' if it is published on the Council's website and made available for inspection at the Council's office.

## 7 Merits review of coverage decisions

- 7.1 Merits review is available under Part 5 of Chapter 8 of the NGL for reviewable regulatory decisions, including:
- (a) a coverage determination, or a decision of not to make a coverage determination, and
  - (b) a coverage revocation determination or a decision not make a coverage revocation determination.<sup>91</sup>
- 7.2 Accordingly, the decision of the relevant Minister on the Council's recommendation is merits reviewable, but the recommendation itself it not subject to merits review. Additionally, the Council's classification decisions are not subject to merits review.
- 7.3 Judicial review under the *Administrative Decisions (Judicial Review) Act 1977* (Cth) is available for decisions of the AER, the Council and Commonwealth Minister under the NGL.<sup>92</sup> This would include both the Council's classification decisions and recommendations.

### Application for review

- 7.4 An application for merits review of one of the above reviewable regulatory decisions, may be made to the Australian Competition Tribunal, with the leave of the Tribunal (s 245(1)). The application may be made on one or more of the following grounds:
- (a) the original decision maker made an error of fact in the decision maker's findings of facts, and that error of fact was material to the making of the decision
  - (b) the original decision maker made more than 1 error of fact in the decision maker's findings of facts, and those errors of fact, in combination, were material to the making of the decision
  - (c) the exercise of the original decision maker's discretion was incorrect, having regard to all the circumstances
  - (d) the original decision maker's decision was unreasonable, having regard to all the circumstances (see s 246(1)).<sup>93</sup>

### Time limitations and leave

- 7.5 The application must be made no later than 15 business days after the reviewable regulatory decision is published in accordance with the NGL or the Rules (s 247(1)).

<sup>91</sup> See ss 244 and 245. Part 5 of Chapter 8 of the NGL which deals with merits review. Note also additional procedural provisions in s 44ZZR of the TPA and Regulations 7B – 7D of the *Trade Practices Regulations*.

<sup>92</sup> See Schedule 3 of the *Administrative Decisions (Judicial Review) Act 1977* (Cth).

<sup>93</sup> See, for example, the discussion of these grounds in *Re: Application by ElectraNet Pty Limited (No 3)* [2008] ACompT 3 (30 September 2008) at [64] - [79].

- 7.6 There are also a number of situations where the Tribunal may refuse to hear an application for merits review which are set out in ss 248 – 251 of the NGL. Some of these are discussed in *Re: Application by ElectraNet Pty Ltd* [2008] ACompT 1 (23 June 2008) at [39] - [42] and [58] - [63]. In particular, s 250 requires that the Tribunal refuse leave to apply for merits review to persons who have not made submissions in relation to the making of the decision (which would include submissions to the Council in relation to coverage decisions). Additionally, leave may be refused where a service provider has:
- (a) without reasonable excuse, failed to comply with a request for information from the Council (s 251(2)(a)(i)) or conducted itself in a manner that resulted in the delay of the decision (s 251(2)(a)(ii)), or
  - (b) misled or attempted to mislead the Council in making a recommendation (s 251(2)(b)(ii)).

### **New information and matters that can be raised**

- 7.7 It should be noted that under s 261 parties are unable to introduce new information not submitted as part of the original decision making process to make out a ground of review. However, ss 261(7)(d) and (g) mean that submissions made to the Council are included in the material before the Tribunal (and so do not need to be resubmitted to the relevant Minister for them to be admissible).
- 7.8 Subsection 258(2) limits parties from raising issues not raised in submissions in relation to the making of the decision. Subsection 261(2) is also designed to ensure that the Tribunal has regard to public policy statements, such as this Guide, in conducting its review of the decision.

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## 8 Other issues and jurisdictional differences

### Jurisdictional differences

#### Western Australia

- 8.1 In Western Australia, under s 20 of the *National Gas Access (WA) Act 2009* the Kalgoorlie to Kambalda pipeline has been given 6 months after the commencement of that Act (that is, until 1 July 2010) to apply for revocation of coverage.
- 8.2 For Western Australian pipelines the WA Economic Regulatory Authority (ERA) is the regulator rather than the AER unless the pipeline is an international pipeline or crosses into South Australia or the Northern Territory (which are within AER jurisdiction).
- 8.3 The dispute resolution body in Western Australia remains the arbitrator originally established under their *Gas Pipelines Access (Western Australia) Act 1998*.

#### Queensland

- 8.4 In Queensland, Regulation 3 of the *National Gas (Queensland) Regulation 2008* deems the Queensland Gas Pipeline and South West Queensland Pipeline uncovered with no applications for coverage allowed until 1 July 2011 and 1 July 2009 respectively.
- 8.5 Regulation 3(4) of the *National Gas (Queensland) Regulation 2008* deems the Carpentaria pipeline to be a covered transmission pipeline.<sup>94</sup>

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<sup>94</sup> This pipeline was not included in Schedule A of the Gas Code and so needed to be specifically covered and classified in light of the repeal of the previous Queensland application Act.

## Appendix A Coverage and Revocation provisions

Coverage	Revocation	Difference
Section 92 application.	Section 102 application.	None
Regulation 14 and Schedule 5 - \$7500 fee.	Regulation 14 and Schedule 5 - \$7500 fee.	None
Rule 15 application requirements.	Rule 18 application requirements.	Applications for revocation need to contain a greater amount of information as the service provider should have this readily available.
Subrule 15(2)(c) Limit of applications to cover pipelines subject of voluntary access arrangements.	N/A	Deals with specific situation of covering an already covered pipeline which is soon to be uncovered on the expiry of its voluntary access arrangement.
Section 93 application dealt with according to rules.	Section 103 application dealt with according to rules.	None
Rule 16 applications dealt with in accordance with standard consultative procedure and 4 month time limit.	Rule 19 applications dealt with in accordance with standard consultative procedure and 4 month time limit.	None
Sections 94 and 96 deferral of consideration where ongoing tendering process.	N/A	Only relevant where a new pipeline is to be constructed and covered for the first time.
Section 95 requirements for Council coverage recommendations.	Section 104 requirements for Council coverage revocation recommendations.	None
Section 97 principles for recommendations.	Section 105 principles for recommendations.	None
Section 98 classification.	N/A	Covered pipelines are already classified.
Section 99 requirements for Minister's decision.	Section 106 requirements for Minister's decision.	None
Rule 17 detailed requirements relating to Minister's decision.	Rule 20 detailed requirements relating to Minister's decision.	None
Section 100 principles for Minister's decision.	Section 107 principles for Minister's decision.	None
Section 101 operation and effect of decisions.	Section 108 operation and effect of decisions.	Clarifies whether or not a pipeline is covered after the decision.

## Appendix B Use of extrinsic materials in this Guide

### Use of extrinsic materials to assist interpretation

- B.1 In developing this Guide, a range of relevant extrinsic materials are referred to in order to assist in the interpretation of the NGL. A key preliminary consideration, therefore, is the legitimacy of referring to extrinsic material for this purpose, and its relevance to the interpretation of the Law and Rules.
- B.2 Section 9(2) of the *National Gas (South Australia) Act 2008* (SA) provides that the *Acts Interpretation Act 1915* (SA) does not apply to the *National Gas (South Australia) Act 2008* (SA), which contains the NGL, or the *National Gas (South Australia) Regulations* (the Regulations).<sup>95</sup> Rather, the NGL contains its own interpretation provisions which are set out in Schedule 2.
- B.3 The interpretation provisions in Schedule 2 apply to the NGL, the Regulations and the Rules and any other statutory instrument made under the NGL (see s 20 of the NGL; see also subclause 51 of Schedule 2).

### Interpretation best achieving Law's purpose

- B.4 Subclause 7(1) of Schedule 2 provides that in the interpretation of a provision of the NGL, the interpretation that will best achieve the purpose or object of the NGL is to be preferred to any other interpretation. Subclause 7(1) applies whether or not the purpose is expressly stated in the NGL.

### Use of extrinsic material in interpretation

- B.5 Subclause 8(2) of Schedule 2 provides that in the interpretation of a provision of the NGL, consideration may be given to 'Law extrinsic material' capable of assisting in the interpretation—
- (a) if the provision is ambiguous or obscure, to provide an interpretation of it, or
  - (b) if the ordinary meaning of the provision leads to a result that is manifestly absurd or is unreasonable, to provide an interpretation that avoids such a result, or
  - (c) in any other case, to confirm the interpretation conveyed by the ordinary meaning of the provision.
- B.6 'Law extrinsic material' is defined in subclause 8(1) as 'relevant material not forming part of this Law'. That provision then goes on to list a number of examples of relevant Law extrinsic material, including an explanatory note or memorandum and the Second Reading Speech relating to the Bill that contained the provision.

<sup>95</sup> A similar provision exists in the Application Acts for the other State and Territory jurisdictions.

- B.7 Subclause 8(3) is in similar terms to subclause 8(2) but relates to the interpretation of the Rules. It provides that in the interpretation of a provision of the Rules, consideration may be given to Law extrinsic material or 'Rule extrinsic material' capable of assisting in the interpretation of a provision where its meaning is unclear. 'Rule extrinsic material' is defined in subclause 8(1) to mean:
- (a) a draft Rule determination; or
  - (b) a final Rule determination; or
  - (c) any document (however described)–
    - (i) relied on by the AEMC in making a draft Rule determination or final Rule determination; or
    - (ii) adopted by the AEMC in making a draft Rule determination or final Rule determination.
- B.8 In determining whether consideration should be given to Law extrinsic material or Rule extrinsic material, and in determining the weight to be given to that material, subclause 8(4) requires that regard is to be had to the desirability of a provision being interpreted as having its ordinary meaning; and the undesirability of prolonging proceedings without compensating advantage, as well as any other relevant matters.
- B.9 Accordingly, it may be possible in particular cases regarding pipeline services for courts to have regard to the Second Reading Speech for the NGL, and the other documents referred to therein, to help establish the object of a particular provision and to point to why the provision should be interpreted in a particular way. For this reason, we have referred to these materials in our discussion of the form of regulation factors in s 16 of the NGL.
- B.10 Importantly, however, extrinsic material cannot be used to alter the clear meaning of a provision. This point was noted, for example, in the case of *Re Bolton: Ex parte Beane* (1987) 162 CLR 514, when the High Court stated that 'the words of a Minister must not be substituted for the text of the law'.<sup>96</sup> Accordingly, while the extrinsic materials may be relevant to the interpretation process, those materials cannot be used to alter or detract from what is a clear and unambiguous meaning on the face of a provision.

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<sup>96</sup> at 518 per Mason CJ, Wilson and Dawson JJ.