GOLDFIELDS GAS TRANSMISSION

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PROPOSED TREATMENT OF THE RTIO/BHPBIO EXPANSION – ELECTION UNDER CLAUSE 10.2(a) OF THE GOLDFIELDS GAS PIPELINE ACCESS ARRANGEMENT

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1 Introduction and Summary

Goldfields Gas Transmission Pty Ltd (GGT) operates the Goldfields Gas Pipeline (GGP), on behalf of the Goldfields Gas Transmission Joint Venture (GGT JV), an unincorporated joint venture between APA subsidiaries, Southern Cross Pipelines Australia Pty Ltd and Southern Cross Pipelines (NPL) Australia Pty Ltd (88.2%), and Alinta DEWAP Pty Ltd (11.8%).

On 4 November 2013, GGT notified the Economic Regulation Authority (ERA) that:

- the capacity of the GGP was being expanded; and
- pursuant to clause 10.2(a) of the GGP Access Arrangement (AA), GGT was electing *not* to treat the expanded capacity as part of the covered pipeline for any purpose under the National Third Party Access Code for Natural Gas Pipeline Systems (Code).[1]

GGT also advised the ERA of its intention to provide further detail on both the basis upon which it was making its election, and the decision-making framework it believed should be employed by the ERA when deciding whether or not to provide its consent. It is in this context that GGT has prepared the following submission. A brief overview of the key elements of the submission is provided below.

1.1 RTIO/BHPBIO Expansion

GGT is currently expanding the capacity of the GGP to enable:

- Rio Tinto Iron Ore (RTIO) to transport gas from Yarraloola to a new delivery point at Boonamichi Well (about 110 km west of Newman). GGT understands this capacity will be used to supply a new gas fired generation plant, which is being developed by RTIO at its West Angelas site to support the expansion of its iron ore operations; [2] and
- BHP Billiton Iron Ore (BHPBIO) to transport gas from Yarraloola to a new delivery point at Yarnima (on the Newman lateral). In a similar manner to RTIO, this capacity will be used to supply a new gas fired generation plant, which is being developed by BHPBIO at Yarnima to supply its iron ore operations[3] and the Newman township.

The expansion (herein referred to as the RTIO/BHPBIO expansion) involves the installation of compressors between Yarraloola and Newman and custody transfer meter stations at Boonamichi Well and Yarnima. To underwrite this expansion, GGT has entered into long-term gas transportation agreements (GTAs) with both RTIO and BHPBIO.

1.2 Access Arrangement provisions

The extensions and expansions policy (EEP) provisions in clause 10.2(a) of the AA require GGT, with the consent of the ERA, to elect at some point in time, whether or not a proposed expansion:

1 GGT, Letter to Mr Lyndon Rowe entitled, Expansion of the capacity of the Goldfields Gas Pipeline, 4 November 2013.

2 Department of Environment and Conservation, Works Approval W5116/2011/1, 19 April 2012.

3 BHPB, New Power Station for Western Australia Iron Ore, 16 November 2011.

- should be treated as part of the covered pipeline for all purposes under the Code; or
- should not be treated as part of the covered pipeline for any purpose under the Code.

Pursuant to clause 10.2(b) of the AA, if the ERA refuses to provide its consent, it must make an express determination on whether or not the proposed expansion should be treated as part of the covered pipeline under the Code.

1.3 Decision-making framework to be employed under clause 10.2

While clause 10.2 of the AA sets out the process to be followed by GGT and the ERA when determining whether or not an expansion should form part of the covered pipeline, it does not explicitly state the matters the ERA is to have regard to when deciding whether or not to provide its consent. Similarly, neither the Code nor the National Gas Law (NGL)/National Gas Rules (NGR), provide express guidance on how a regulator should approach the question of whether or not a specific expansion should form part of the covered pipeline where the regulator has been given a decision-making role under an EEP. GGT has therefore given further consideration to the decision-making framework that should be employed by the ERA under clause 10.2(a).

In short, GGT is of the view that the ERA should:

1. Start with the election GGT has made under the EEP, as required by the EEP drafted and approved by the Electricity Review Board.
2. Determine whether to provide its consent to GGT's election having regard to the coverage criteria and the decision-making rule set out in sections 1.9 and 1.15 of the Code, respectively (or sections 15 and 100 of the NGL, respectively),[4] because it is in effect a decision as to coverage which is being made. Consistent with the decision-making rule set out in section 1.15 of the Code (or section 100 of the NGL), the ERA:
   - should consent to GGT's election that the RTIO/BHPBIO expansion *not* be treated as part of the covered pipeline, if one or more coverage criteria are *not* satisfied; and
   - may *only* refuse to provide its consent to the election if it is positively satisfied that <u>all</u> four of the coverage criteria are met.

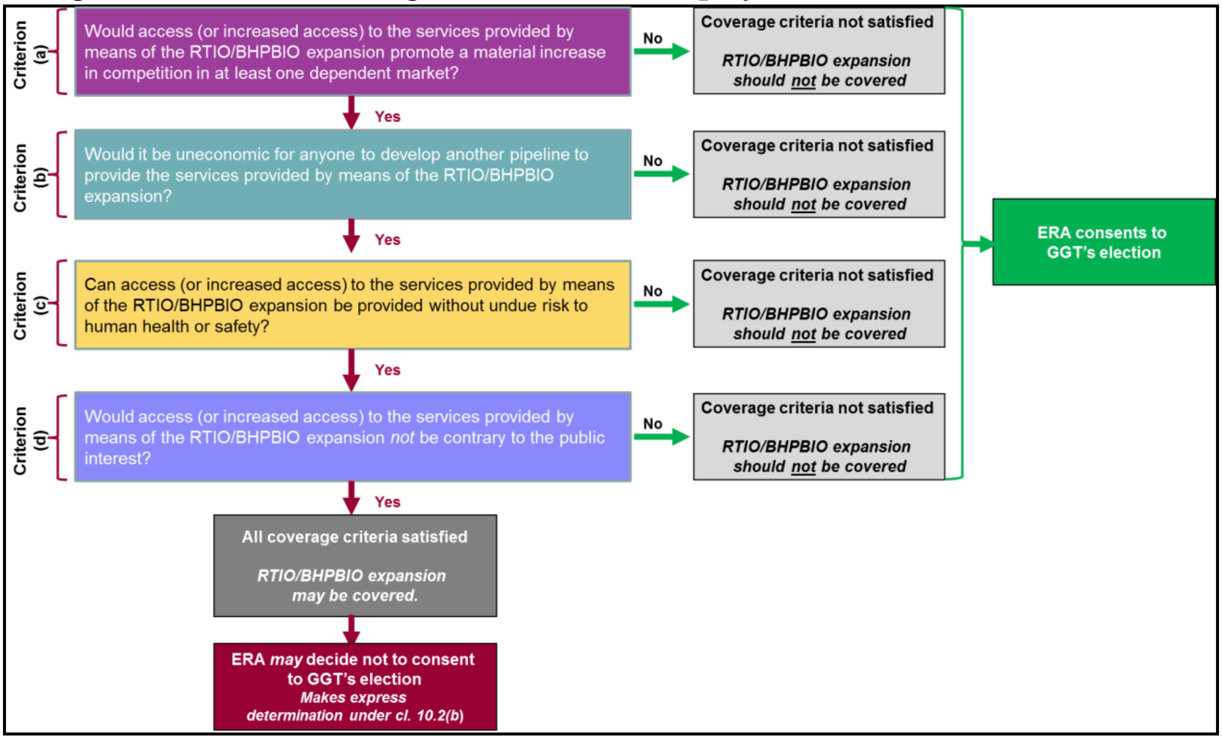
GGT further submits that, pursuant to the above decision-making framework it is not necessary for GGT to adduce material that is sufficient to satisfy the ERA that the expansion should not be covered and, if it fails to do so, that it would then be open to the ERA not to consent to GGT's election. Rather, if the ERA is going to refuse to consent to GGT's election and make a decision that the expansion is to be covered, it is only open to the ERA to do so on the basis of a body of evidence that the ERA says satisfies it that the coverage criteria are met. In the absence of such a body of material, the ERA's decision must be to consent to GGT's election.

[4] Note that there is no substantive difference between the coverage provisions in sections 1.9 and 1.15 of the Code and those in sections 15 and 100 of the NGL.

In terms of the administrative procedure to be adopted in deciding whether to consent to GGT's election, in the event the ERA is minded not to consent to GGT's election, the ERA must, as a matter of procedural fairness, explain to GGT why it believes all the coverage criteria are satisfied and provide GGT with an opportunity to respond to the matters raised by the ERA prior to it making a final decision.

The key elements of the decision-making framework that GGT considers should be employed by the ERA are depicted in Figure 1.1.

Figure 1.1: Decision-making framework to be employed under clause 10.2 of the AA



1.4 The ERA should consent to GGT's election because all the coverage criteria are not satisfied

As noted in its 4 November 2013 letter to the ERA, GGT has elected under clause 10.2(a) of the AA that the RTIO/BHPBIO expansion *not* be treated as part of the covered pipeline for any purpose under the Code and is seeking the consent of the ERA to that election.

In short, GGT has decided the RTIO/BHPBIO expansion should not form part of the covered pipeline because it does *not* satisfy criterion (a) and there is some uncertainty as to whether criterion (b) is satisfied. Because criterion (a) is not satisfied, a detailed assessment to determine whether criterion (d) is satisfied is unnecessary.[5] GGT would expect, however,

5 This is consistent with the approach adopted by the NCC and by the Australian Competition Tribunal in *Re Duke Eastern Gas Pipeline Pty Ltd* [2001] ACompT 2 [145].

that if such an assessment was undertaken and consideration given to the adverse effects that a coverage decision would have on investment, service provision and efficiency, then access (or increased access) to the RTIO/BHPBIO expansion may be found to be contrary to the public interest.

The reasons why criterion (a) is not satisfied in this case are summarised below:

- Access (or increased access) on regulated terms and conditions to the services provided by the RTIO/BHPBIO expansion will have *no* effect on competition in the dependent markets[6] serviced by the expansion over a period of some 20 years because:
  - all of the capacity has been contracted by RTIO and BHPBIO; and
  - the price and non-price terms and conditions in the RTIO and BHPBIO GTAs have been locked in for the duration of these agreements.

  Put simply, there will be *no* difference between the conditions prevailing in the dependent markets in the 'with' and 'without' regulated access states of the world for around 20 years given the operation of the GTAs. In other words, access (or increased access) will have *no* effect on competition in these markets.
- To the extent the ERA considers it relevant to have regard to the effect that coverage would have on competition in other markets serviced by the GGP (which GGT submits is an irrelevant consideration), GGT's analysis of the effect that a decision to treat the expanded capacity as part of the covered pipeline would have on the reference tariff, indicates that any change in this tariff and the delivered price of gas, would be too small to promote a material increase in competition in any of these markets.

Given that all four of the coverage criteria are not satisfied, GGT submits that the ERA should provide its consent to GGT's election that the RTIO/BHPBIO expansion *not* be treated as part of the covered pipeline for any purpose under the Code.

1.5 Structure of the submission

The remainder of this submission is structured as follows:

- Section 2 provides an overview of the RTIO/BHPBIO expansion, the contractual arrangements underpinning the expansion and GGT's understanding of what RTIO and BHPBIO intend to use the capacity for;
- Section 3 sets out the decision-making framework GGT believes should be employed by the ERA when deciding whether or not to provide its consent to an election under clause 10.2(a) of the AA;
- Section 4 outlines the way in which GGT considers the coverage criteria should be interpreted and applied by the ERA; and

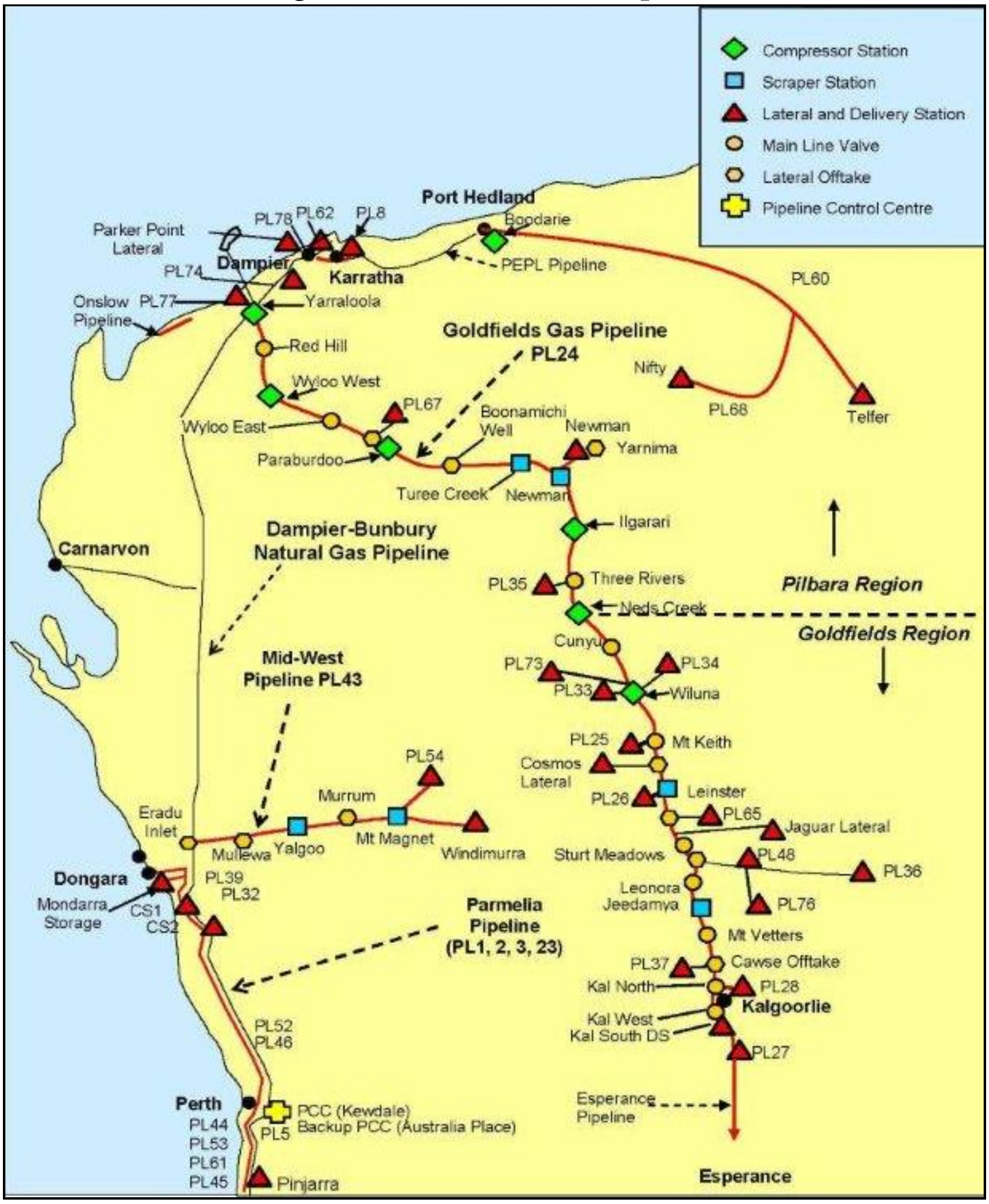
6 The dependent markets include the upstream and downstream markets that will either supply, or be supplied with, gas transported via the RTIO/BHPBIO expansion. These markets are the global seaborne iron ore market, the retail electricity market in Newman and the upstream production and gas sales market.

- Section 5 applies the decision-making framework set out in section 3 to the RTIO/BHPBIO expansion.

2 Overview of the RTIO/BHPBIO Expansion

The GGP is a transmission pipeline (~1,380 km) that enables gas to be transported from the Carnarvon Basin (via either the Dampier to Bunbury Natural Gas Pipeline (DBNGP) or from the Varanus Island gas processing facilities) to the Pilbara, Mid-West and Goldfields mining regions and the entry point of the Kalgoorlie to Kambalda pipeline. The regions traversed by the pipeline mean that it is primarily used by mining companies with interests in iron ore, gold, nickel and lead. Other users of the GGP include a small number of independent electricity generators (supplying mining operations and/or local townships) and a gas distributor supplying the Kalgoorlie township. The locations serviced by the GGP are illustrated in the map below.

Figure 2.1: Goldfields Gas Pipeline



The capacity of the GGP is currently in the process of being expanded to enable:

- RTIO to transport gas to Boonamichi Well (~110 km west of Newman); and
- BHPBIO to transport gas to Yarnima (located on the Newman lateral).

To facilitate this expansion, new compressors and two new delivery points will be installed between the receipt point at Yarraloola and existing delivery point at Newman.

All of the capacity to be made available through this expansion has been contracted by RTIO and BHPBIO under long-term GTAs for around 20 years.[7] To put the term of these GTAs into perspective, the technical life of a new compressor is around 30 years.[8] These two GTAs will therefore operate over a considerable portion of the life of the compressors that are to provide the capacity.

The remainder of this section provides further detail on:

- the capital works being carried out to provide the capacity sought by RTIO and BHPBIO; and
- GGT's understanding of what RTIO and BHPBIO intend to use the capacity for.

For the purposes of this submission the RTIO and BHPBIO expansions are treated as a single expansion. This is because, although they are contractually and commercially separate projects, the BHPBIO expansion immediately follows the completion of the RTIO expansion. From a pipeline development and construction perspective, the two expansions comprise an integrated project to expand capacity in the Pilbara region.

2.1 Capital works

To provide the capacity sought by RTIO and BHPBIO, the following capital works are being carried out by GGT:

- ***RTIO capacity*** – to enable gas to be transported from Yarraloola to Boonamichi Well, additional compressor units are being installed on the GGP. A new custody transfer meter station is also being developed in order to transport gas from the GGP to a new power station operated by RTIO.
- ***BHPBIO capacity*** – to enable gas to be transported from Yarraloola to Yarnima, additional compressor units are being installed on the GGP. A new custody transfer meter station is also being installed to supply a new power station operated by BHPBIO.

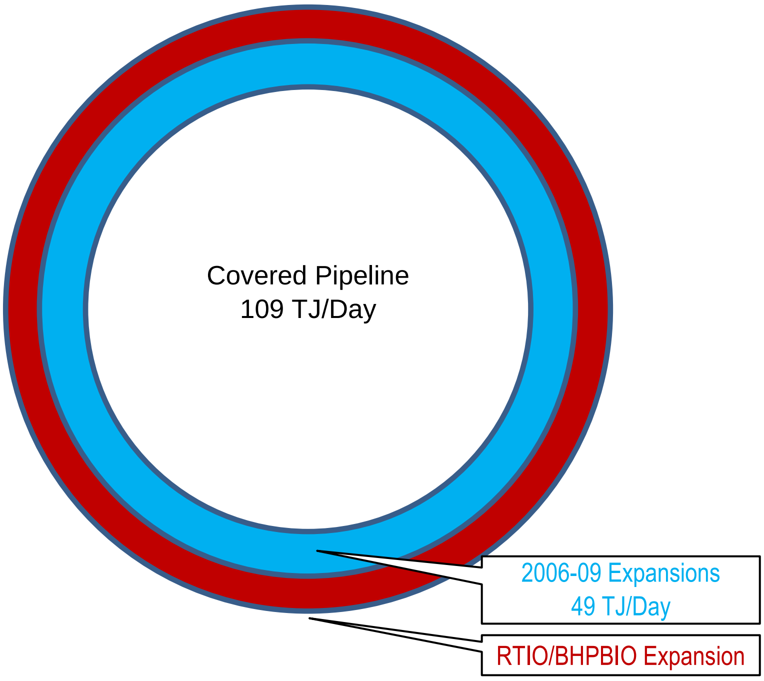
The installation of the additional compressors will increase the existing capacity of the GGP. This capacity is in addition to the existing capacity of the covered pipeline and the expansions that were completed in 2006-09, which do not form part of the covered pipeline. A highly stylised image of the capacity of the GGP and its constituent parts is set out below.

[7] The BHPBIO GTA includes two five year extension options, which can be exercised at the discretion of BHPB.

[8] This is consistent with the life assumption adopted by the ERA and the Australian Energy Regulator.

Before examining this figure, it is worth noting that some care must be taken when interpreting the capacity measurements reported in the figure.

Figure 2.2: Stylised image of GGP mainline capacity (not to scale)



The capacity of the Covered Pipeline – 109 TJ/d – is the sum of the capacities contracted to users of the pipeline facilities that existed before the 2006-09 Expansions. The contracting of these capacities to those users exhausted the potential of the GGP, as it was configured before 2006, to deliver gas to Kalgoorlie. In 2006, a second compressor was added at Paraburdoo, increasing the capacity to deliver gas to RTIO's Paraburdoo mining operations, and in 2009 compressors were installed at Wyloo West and at Ned's Creek providing capacity for delivery of gas for nickel ore processing at Murrin Murrin. The total of the capacities contracted to RTIO at Paraburdoo and to the Murrin Murrin nickel refinery was 49 TJ/d, and the contracting of these capacities exhausted the potential of the GGP to deliver gas to the entry point to the Murrin Murrin lateral.

The expansion for RTIO and BHPBIO will provide additional capacity, but *not* along the entire length of the GGP. It will provide contracted capacities for delivery of gas into RTIO's lateral, and for delivery of gas at Yarnima, effectively exhausting the capacity available at the entry point to the Newman lateral.

The highly stylised image of Figure 2.2 shows that, even if the RTIO/BHPBIO expansion does not form part of the covered pipeline, users and prospective users of the GGP will still have the ability to seek access on regulated terms and conditions to a significant part of the capacity of the GGP between Yarraloola and Kalgoorlie (although the amount of capacity that is subject to regulation depends on the way in which load distributed along the pipeline).

2.2 Use of the expanded capacity

GGT understands that both RTIO and BHPBIO intend to use the capacity to supply new gas fired generation plants and that these will be used to generate electricity for their iron ore mining operations in the Pilbara. Further detail on these two developments is provided below.

2.2.1 RTIO's use of the expanded capacity

GGT understands from publicly available information that RTIO intends to use the capacity on the GGP to supply a new 80 MW open cycle gas turbine (OCGT) electricity generation plant, which is being developed at the company's West Angelas site in the Pilbara.[9] The OCGT is to be fuelled using either distillate supplied from RTIO's West Angelas fuel hub, or from gas supplied via the GGP.[10]

The development of this power station is part of a broader programme that is being carried out by RTIO to support the expansion of its iron ore operations in the Pilbara. Further detail on RTIO's iron ore interests in the region can be found in Box 2.1.

Box 2.1: RTIO's iron ore interests

RTIO's iron ore interests in the Pilbara, stem from the interests it holds in Hamersley Iron Pty Ltd, Robe River Iron Associates, the Hope Downs JV, Eastern Range JV and Channar JV.[11] The ore bodies controlled by these entities that are in the vicinity of the GGP include, amongst others, Paraburdoo, Eastern Range, Channar, Tom Price, Marandoo, Western Turner Syncline, Brockman 2, Brockman 4, Nammuldi, Yandicoogina, Hope Downs 1, Hope Downs 4, Yandi, Hope Downs, West Angelas, Mesa A and Mesa J.[12]

In 2012 these ore bodies produced approximately 240 Mtpa[13] of iron ore, which is equivalent to 45% of Australia's iron ore exports in 2012-13.[14] Going forward, production in the area is expected to increase, with a number of significant investments being undertaken by RTIO to increase the capacity of its iron ore operations from the current level of 290 Mtpa to 360 Mtpa by the first half of 2015.[15]

2.2.2 BHPBIO's use of the expanded capacity

In a similar manner to RTIO, the capacity acquired by BHPBIO is to be used to supply gas to a new combined cycle gas turbine (CCGT) plant, which is being developed at Yarnima.[16,17] In announcing the development of this power station in 2011, BHPBIO advised that it

[9] Department of Environment and Conservation, Works Approval W5116/2011/1, 19 April 2012.

[10] ibid.

[11] Rio Tinto holds a 100% interest in Hamersley Iron, a 53% interest in Robe River Iron Associates, a 50% interest in the Hope Downs JV, a 54% interest in the Eastern Range JV and a 60% interest in the Channar JV. Rio Tinto, Annual Report 2012, pp. 53 and 64.

[12] Rio Tinto, Annual Report 2012, pp. 53 and 64.

[13] ibid, p49.

[14] According to the Bureau of Resources and Energy Economics (BREE), exports of iron ore from Australia reached 527 Mtpa in 2012-13. See BREE, Resources and Energy Quarterly, September 2013, p12.

[15] Rio Tinto, Annual Report 2012, p31.

[16] BHPB, New Power Station for Western Australia Iron Ore, 16 November 2011 and BREE, Electricity Generation Major Projects, October 2013, p29.

[17] Note that the size of this new power station has been referred to by BHPBIO and BREE (see references above) as 190 MW but the Works Approval granted by the WA Department of Environment and Conservation on 9 August 2012 refers to the capacity of the power station being 140 MW.

expected it to be used to supply its existing iron ore operations, which are currently being supplied by Alinta Energy's Newman Power Station, and 'provide a platform for further mine development in the Pilbara'.[18] Further detail on BHPBIO's iron ore interests in the Pilbara can be found in Box 2.2.

Box 2.2: BHPBIO's iron ore interests

BHPBIO's iron ore interests in this region of the Pilbara, stem from its involvement in the Mt Newman, Yandi, Mt Goldsworthy, JW4, Wheelarra and POSMAC JVs. [19] The ore bodies controlled by these JVs that are in the vicinity of the GGP[20] include Mt Whaleback, Yandi, Wheelarra, Area C and ore bodies 18 and 23-25.[21]

In 2012-13, these ore bodies produced approximately 185 Mtpa[22] of iron ore, which is equivalent to 36% of the iron ore exported from Australia in 2012-13.[23] Going forward, production in the area is expected to increase, with a new mine at Jimblebar to commence operations in December 2013.[24] Once this mine is operational, the overall capacity of these JVs' iron ore operations across the Pilbara is expected to reach 220 Mtpa.[25]

Although not referred to in BHPBIO's announcement, GGT understands that BHPBIO, through its interest in the Mt Newman JV, also supplies electricity to the Newman township.[26] This electricity is currently generated by the Newman Power Station and supplied to the township using the Mt Newman JV's transmission and distribution network.[27,28]

GGT expects that once the Yarnima Power Station is commissioned, it will take over the role currently played by the Newman Power Station.[29] GGT has therefore assumed that some of

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18 BHPB, New Power Station for Western Australia Iron Ore, 16 November 2011.

19 BHPB holds an 85% interest in the Mt Newman, Yandi and Goldsworthy joint ventures, a 68% interest in the JW4 JV, a 51% interest in the Wheelara JV and a 65% interest in the POSMAC JV. See BHPB, Annual Report 2013, pp. 32-33.

20 The Mt Goldsworthy JV also controls the Yarrie and Nimingarra ore bodies in the northern region of the Pilbara.

21 BHPB, Annual Report 2013, pp. 32-33.

22 ibid, p48. The production estimate has been estimated by grossing up BHPB's share of production using the interest estimates contained in table 2.3.2 and by excluding production from the Yarrie area.

23 See footnote 14.

24 BHPB, News Release, 17 July 2013.

25 BHPB, Annual Report 2013, p31.

26 The ability to supply the township is provided for by the *Iron Ore (Mt Newman) Agreement Act 1964*, which states the following in the mutual covenants section:

> **Water and power supplies**
>
> (a) that subject to and in accordance with proposals approved or determined under clause 6 hereof the Company for its purposes hereunder and for domestic and other purposes in relation to a townsite may to the extent determined by the Minister but notwithstanding any Act bore for water construct catchment areas store (by dams or otherwise) take and charge for water from any Crown lands available for the purpose and generate transmit supply and charge for electrical energy and the Company shall have all such powers and authorities with respect to water and electrical energy as are determined by the Minister for the purposes hereof which may include the powers of a water board under the *Water Boards Act 1904* and of a supply authority under the *Electricity Act 1945.*

27 Engineers Australia, Infrastructure report card 2010 – Western Australia, pp. 135-136.

28 Note that these transmission/distribution networks are *not* connected to the North West Interconnected System.

29 GGT understands that in the future, the Newman Power Station will be used to supply Roy Hill iron ore project. See West Australian, Alinta wins Roy Hill power battle, 30 August 2013

the expanded pipeline capacity will be used to generate electricity for supply to the Newman township. To put the size of this township into perspective, it is worth noting that the 2011 census data indicates that the population of Newman is around 6,710 and there are approximately 1,826 dwellings in the township.[30]

2.3 Contractual arrangements

The capacity expansion currently being carried out for RTIO and BHPBIO has been underwritten by long-term GTAs, which were agreed to as a result of robust commercial negotiations carried out with two well-informed and well-resourced users of the GGP.

The price and non-price terms and conditions of both GTAs have been locked in for the duration of the agreements. In effect, this means that:

- irrespective of whether or not the expansion is covered, the price and non-price terms and conditions set out in the GTAs will not change; and
- GGT will be unable to unilaterally raise prices, alter the non-price terms and conditions of access, or exercise any other form of market power over a period of around 20 years.

[30] ABS, 2011 Census QuickStats, ABS website, Tables B03 and B31– note that the 6,700 estimate includes residents and visitors: http://www.censusdata.abs.gov.au/census_services/getproduct/census/2011/quickstat/UCL514004

3 Decision-Making Framework to be Employed Under Cl. 10.2

This section sets out what GGT considers to be the relevant decision-making framework that applies to the decision the ERA will make pursuant to clause 10.2 of the AA. For the reasons set out below, GGT considers that it is relevant provisions of the Code that apply to the ERA's decision to either consent to GGT's election under clause 10.2(a), or make an express determination as to coverage under clause 10.2(b). Further, GGT considers that it is primarily the provisions that govern decisions as to coverage of pipelines that should guide the ERA's decision.

Regardless of whether the instrument that is applicable to the ERA's decision under the EEP is considered to be the Code or the NGL/NGR, there is no substantive difference between these instruments in terms of the provisions that GGT submits should guide the ERA's decision under clause 10.2 of the AA. GGT considers that these provisions are the coverage criteria and the associated decision-making rule, which are set out in sections 1.9 and 1.15 of the Code and in sections 15 and 100 of the NGL. Further detail on the coverage criteria and the decision-making rule that GGT submits the ERA should apply when considering its election under clause 10.2(a) of the AA is set out below.

This section also outlines why the decision-making framework that the ERA is required to employ is one that starts with the election by GGT and only departs from this election if the ERA determines, on the basis of a relevant body of evidence, that the coverage criteria are satisfied. It also sets out why, in the event the ERA is minded not to consent to GGT's election, the ERA must, as a matter of procedural fairness, explain to GGT why it considers the coverage criteria are satisfied and provide GGT with an opportunity to respond to the matters raised by the ERA before making a final decision under clause 10.2.

3.1 The relevant legal framework

The EEP set out in clause 10.2 of the AA creates a role for the ERA:

- in deciding whether to consent to an election made by GGT with respect to a particular extension or expansion under clause 10.2(a); and
- if the ERA decides not to provide its consent, in making an express determination about whether the particular extension or expansion is covered under clause 10.2(b).

The AA was approved under the Code and, in effect, is operating under the provisions of the Code (with some exceptions set out in the NGR) until revisions are next approved to the AA under the NGL and NGR. GGT therefore considers that, in performing its role under the EEP, the relevant framework that guides the ERA's decision is the Code.

GGT notes that the savings and transitional provision in clause 30 of Schedule 3 of the NGL explicitly provides that sections 3, 8 and 10.8 of the Code continue to apply in respect of the AA. There are a limited number of decisions that the NGR require the ERA to make pursuant to the NGR[31] when dealing with a transitional access arrangement.[32] In respect of all other decisions, it appears that the Code provisions apply.

In any event, GGT considers there to be no substantive difference as between the provisions in the Code and the NGL/NGR that the ERA should use to guide its decision-making under the EEP. GGT submits that as the decision the ERA is effectively making pursuant to clause 10.2 of the AA is one of coverage, the approach that should be adopted by the ERA is one which applies the coverage criteria in section 1.9 of the Code (section 15 of the NGL) to the issue at hand, being the expanded capacity. Further, the ERA should also apply the decision-making rule which applies to questions of coverage – which is that capacity should only be covered where all of the coverage criteria are satisfied (section 1.15 of the Code or section 100 of the NGL).

3.2 The ERA should apply the coverage criteria when making its decision

In considering the question of coverage of the RTIO/BHPBIO expansion, the ERA should be guided by the coverage criteria as it is, in effect, a decision as to coverage that is being made. The Electricity Review Board in its decision in relation to GGT's AA in 2011 confirmed that "[e]valuation of Coverage [under the EEP] should be carried out by reference to the Code Criteria"[33] and that the "evaluation of a particular extension or expansion should be undertaken in light of the prevailing circumstances of each case, as they exist at the time the extension or expansion is proposed".[34]

The coverage criteria and associated decision-making rule are set out in sections 1.9 and 1.15 of the Code (or sections 15 and 100 of the NGL). Section 1.9 relevantly provides:

> … the NCC must recommend that the Pipeline be Covered … if the NCC is satisfied of all of the following matters, and cannot recommend that the Pipeline be Covered, to any extent, if the NCC is not satisfied of one or more of the following matters:
>
> (a) that access (or increased access) to Services provided by means of the Pipeline would promote competition in at least one market (whether or not in Australia), other than the market for the Services provided by means of the Pipeline;
>
> (b) that it would be uneconomic for anyone to develop another Pipeline to provide the Services provided by means of the Pipeline;
>
> (c) that access (or increased access) to the Services provided by means of the Pipeline can be provided without undue risk to human health or safety; and
>
> (d) that access (or increased access) to the Services provided by means of the Pipeline would not be contrary to the public interest.

[32] A "transitional access arrangement" includes an access arrangement that was in force under the former access regime immediately before the date of transition (which in Western Australia is 1 January 2010) and continues in force subject to revisions made in accordance with the Code under clause 29 of Schedule 3 to the NGL.

[33] Reasons for decision by the Western Australian Electricity Review Board in respect of Applications 1 and 2 of 2010, 22 November 2011, [70].

[34] ibid [68].

Section 1.15 of the Code provides that the relevant minister must decide that the pipeline is covered (either to the extent described, or to a greater or lesser extent than that described in the application for coverage) if the relevant minister is satisfied of all of the matters set out in (a) to (d) of the above extract, but the relevant minister cannot decide that the pipeline is covered, to any extent, if not satisfied of one or more of those matters.

Further detail on the decision-making framework GGT considers should be applied by the ERA is set out below, along with GGT's view on how the term 'Services provided by means of the Pipeline' should be interpreted when applying the coverage criteria to a particular expansion. The manner in which GGT believes the coverage criteria should be interpreted and applied by the ERA is set out in section 4.

3.2.1 The decision-making framework that the ERA must apply

3.2.1.1 Starting with GGT's election

The EEP, which was drafted and approved by the Electricity Review Board, puts at its centre the election by GGT in relation to any proposed extension or expansion. The EEP provides for GGT to make its election, and then for the ERA, starting with GGT's election as the default, to decide whether to consent to that election. Accordingly, the ERA's assessment must start with the election that has been made by GGT.

3.2.1.2 Coverage criteria and decision-making rule

As noted above, GGT submits that it is the coverage criteria and the decision-making rule that applies to coverage decisions that the ERA should use and apply in guiding its decisions under the EEP.

Sections 1.9 and 1.15 of the Code (sections 97 and 100 of the NGL) provide that the NCC must be positively satisfied that all four coverage criteria are met before it recommends that a pipeline be covered, and that the relevant minister may only make a coverage determination if the relevant minister is satisfied that all of the coverage criteria are satisfied. In the absence of being positively satisfied about one or more coverage criteria, the NCC's recommendation must be against the pipeline being covered. Similarly, the relevant minister must not make a coverage determination if it is not satisfied that all the coverage criteria are met.

Accordingly, where GGT has elected that a proposed expansion *not* form part of the covered pipeline, the ERA:

- should consent to GGT's election that the RTIO/BHPBIO expansion *not* be treated as part of the covered pipeline, if one or more of the coverage criteria are *not* satisfied; or
- may *only* refuse to provide its consent to the election if it is positively satisfied that all four of the coverage criteria are met.

3.2.1.3 If expansion is to be covered, the relevant matter to be "proved" is that the coverage criteria are satisfied, not that the coverage criteria are not satisfied

Given the way in which the coverage test is cast (i.e. the decision-maker cannot make a decision to cover the capacity of a pipeline unless it is satisfied all of the coverage criteria are met), the relevant matter to be proved is that the coverage criteria are satisfied, as opposed to proving that the coverage criteria are not satisfied. That is, it is not necessary for GGT to adduce material that is sufficient to satisfy the ERA that the expansion should not be covered and, if it fails to do so, that it would then be open to the ERA not to consent to GGT's election. Rather, if the ERA is going to refuse to consent to GGT's election and make a decision that the expansion is to be covered, it is only open to the ERA to do so on the basis of a body of evidence that the ERA says satisfies it that the coverage criteria are met. In the absence of such a body of material, the ERA's decision must be to consent to GGT's election.

3.2.1.4 Administrative procedure

In terms of the administrative procedure to be adopted in deciding whether to consent to GGT's election, in the event the ERA is minded not to consent to GGT's election, the ERA must, as a matter of procedural fairness, explain to GGT why it believes all of the coverage criteria are satisfied and the material that the ERA relies on in forming that belief. The ERA must also provide GGT with an opportunity to respond to the ERA's position and the material on which it relies prior to the ERA making a final decision.

3.2.2 The ERA should interpret 'Services provided by means of the Pipeline' as 'Services provided by means of the RTIO/BHPBIO expansion'

In each of the coverage criteria, reference is made to 'Services provided by means of the Pipeline'. GGT submits that in applying the coverage criteria in the current context, which is the application of the coverage criteria to the RTIO/BHPBIO expansion pursuant to the EEP, the term 'Services provided by means of the Pipeline' is appropriately construed to be services that will be provided by means of that expansion. The decision that is being made is confined to the treatment of the expanded capacity. An enquiry by the ERA into whether it should consent to GGT's election, should therefore be directed to the effects that a decision as to coverage (or otherwise) of the RTIO/BHPBIO expansion will have.

4 How the Coverage Criteria Should be Interpreted and Applied

When applying the coverage criteria, the ERA should employ the principles and assessment frameworks used by the NCC, the Australian Competition Tribunal (Tribunal) and other judicial bodies, such as the Federal Court and High Court.

The remainder of this section provides an overview of the manner in which the coverage criteria, and the equivalent declaration criteria in Part IIIA of the *Competition and Consumer Act 2010* (CCA) (previously the *Trade Practices Act* 1974 (TPA)), have been interpreted and applied by these bodies.

4.1 Criterion (a)

Criterion (a) of the coverage criteria requires consideration to be given to whether access (or increased access) to services provided by means of the pipeline would promote competition in at least one market (whether or not in Australia), other than the market for the services provided by means of the pipeline.

The application of this criterion has been described by the NCC and the Tribunal as involving the following two stage assessment process:[35]

Stage 1: Identify economically separable dependent (upstream or downstream) markets; and

Stage 2: Assess whether access (or increased access) is likely to promote a material increase in competition in the dependent market(s) identified in Stage 1.

Through a number of coverage and declaration processes, the NCC, Tribunal and Federal Court have provided further clarity on:

- what is meant by the terms ‘market’, ‘access’ and ‘promote competition’;
- why access should promote a ‘material increase’ in competition; and
- how the Stage 2 assessment should be carried out and matters relevant to this assessment.

4.1.1 What is meant by the term ‘market’?

In *Re Queensland Cooperative Milling Association Ltd*; *Re Defiance Holdings* (1976) 25 FLR 169 (*Re QCMA*), the Tribunal described a market as being “the area of close competition between firms” or “the field of rivalry between them” (at [190]). Further, the Tribunal noted that 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”.

The case law also makes clear that the phrase ‘at least one market, other than the market for the services’ means dependent markets that are either upstream or downstream of the

[35] See for example, NCC, Gas Guide – A guide to the functions and powers of the National Competition Council under the National Gas Law (Gas Guide), October 2013, pp. 28-39.

services. For example, in *Sydney Airport Corporation Limited v Australian Competition Tribunal* [2006] FCAFC 146, the Tribunal considered that the other markets that are relevant to the assessment under section 44H(4)(a) of the TPA were dependent markets and quoted the relevant part of the Hilmer Report as follows:[36]

> 'an access regime would only apply where access to the facility is essential to permit effective competition in a dependent market (that is, one downstream or upstream from the facility) given that such linkages would provide the prime anticompetitive motive for denying or impeding access'.

4.1.2 What is meant by the term 'access'?

The term 'access' has been defined by the NCC, in its *Gas Guide – A guide to the functions and powers of the National Competition Council under the National Gas Law* (Gas Guide), as a 'regulated right' to access the relevant services, rather than access that may be available under individual commercial arrangements. The NCC has also noted that such access should be assumed to be provided on 'terms and conditions that give effect to the efficiency objective in the NGL and, accordingly, seek to replicate the outcome of a competitive market'.[37]

4.1.3 What is meant by the term 'promote competition'?

The Tribunal in *Re Sydney International Airport* [2000] ACompT 1[38] provided the following guidance on what is meant by the term 'promote competition':

> '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.'

4.1.4 Material increase in competition

On the advice of the Productivity Commission, the Australian Government decided in the early 2000s to strengthen criterion (a) by requiring access to promote a 'material increase' in competition.[39] This amendment was made to the declaration criteria in Part IIIA of the TPA (now the CCA) in 2006 and to the coverage criteria in 2008, when the NGL was enacted.

Although the term 'material increase' did not appear in criterion (a) of the Code, the NCC was, nevertheless, applying this standard when assessing coverage and revocation of coverage applications under the Code. For example, in its Final Recommendation on the

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[36] *Sydney Airport Corporation Limited v Australian Competition Tribunal* [2006] FCAFC 146, [15].

[37] NCC, Gas Guide, October 2013, p32.

[38] *Re Sydney International Airport* [2000] ACompT 1 [106].

[39] Peter Costello, Government Response to Productivity Commission Report on the Review of the National Access Regime. http://ministers.treasury.gov.au/DisplayDocs.aspx?pageID=010&doc=publications/NationalAccessRegime.htm&min=phc

application for revocation of coverage of both the Tubridgi and Griffin pipelines in 2006, the NCC stated the following: [40]

> 'In the Council's view consideration of criterion (a) requires an exploration of the facts and a comparison of the competitive conditions in the relevant market with and without coverage to determine whether coverage would **materially improve** the conditions for competition.' [emphasis added]

Similarly, in its Final Recommendation on the Dawson Valley Pipeline coverage application, published in 2005, the NCC noted that in assessing whether criterion (a) is satisfied, it must:[41]

> '…assess whether the effects of declaration are large enough to have a **material impact** on the competitive environment in the dependent market'. [emphasis added]

The standard applied by the NCC under the Code was consistent with the standard the Tribunal applied when considering the declaration criteria in Part IIIA of the TPA, prior to the legislated amendments. For example, in *Re Virgin Blue Airlines Pty Ltd* (2005) ACompT 5 [162] the Tribunal stated:

> '… we need to be satisfied that…there would be a significant, finite probability that an enhanced environment for competition and greater opportunities for competitive behaviour—in a **non-trivial sense**—would arise in the dependent market.' [emphasis added]

It follows from the preceding discussion, that if the ERA decides the Code is the relevant regulatory framework for the assessment, it should apply the 'material increase in competition' test which has been applied by both the NCC and the Tribunal.

4.1.5 Assessment of whether access is likely to promote competition

In *Sydney Airport Corporation Limited v Australian Competition Tribunal* [2006] FCAFC 146, the Full Federal Court held that criterion (a) requires consideration to be given to whether the future state of competition in a dependent market "with access" is likely to differ materially from the future state of competition "without access".[42]

Whether or not competition in a dependent market is likely to be materially different in these two states of the world will depend on a range of factors, including:

- the current state of competition in the dependent market; and
- the ability and incentive the service provider has to exercise market power to adversely affect competition in the dependent market.

[40] NCC, Final Recommendation - Application for revocation of coverage of the Tubridgi and Griffin Pipeline System under the National Gas Access Regime, 27 February 2006, p23.

[41] NCC, Final Recommendation - Dawson Valley Pipeline: Coverage application under the National Gas Code, August 2005, p24.

[42] *Sydney Airport Corporation Limited v Australian Competition Tribunal* [2006] FCAFC 146 [83].

4.1.5.1 Current state of competition in the dependent market

When assessing the likely effect of access on competition, the NCC and Tribunal have both noted the importance of considering whether the market is already effectively competitive. For example, *In the matter of Fortescue Metals Group Limited* [2010] ACompT 2, the Tribunal held that if a dependent market is already 'effectively competitive' then this criterion is likely to have 'no application'.[43] Elaborating further on this point, the NCC stated in the Gas Guide:[44]

> '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).'

Another matter the NCC has previously identified as being relevant to the consideration is the height of any other barriers to entry in the dependent market. Specifically, the NCC has stated that where there are other barriers to entry (unrelated to access) and these are prohibitive, then the pro-competitive effects of coverage are likely to be negligible.[45]

4.1.5.2 Ability and incentive to exercise market power

One of the more significant matters the NCC considers when assessing the likely effect of access on competition is whether the service provider has an incentive and ability to exercise market power to the detriment of competition in that market by engaging in the following types of actions:

- preventing or hindering access;
- raising prices above what would prevail in an effectively competitive market;
- restricting throughput; or
- reducing service quality.

Some insight into the importance the NCC places on this factor can be seen in the extract below:[46]

> '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.

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43 The Tribunal's position on this issue can be found in paragraph 1068 of *In the matter of Fortescue Metals Group Limited* [2010] ACompT 2, which is reproduced below:

> 'The position we take is that if a dependent market is already effectively competitive, intervention is not called for. That is, we read criterion (a) as having no application to a market which is effectively competitive. In any event, even if we are wrong in this approach that the dependent market is already effectively competitive, it would be an important consideration under criterion (f) and the discretion.'

44 NCC, Gas Guide, October 2013, p34.

45 NCC, Final Recommendation – Application for the revocation of coverage of the GGP under the National Gas Access Regime, November 2003, p98.

46 ibid, p36.

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.

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.

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).'

Consistent with the NCC's observations in this extract, if a service provider is unable to exercise market power in the dependent market, then a coverage determination 'would not promote competition or efficiency in that market'.[47]

These observations are further supported by the Tribunal's findings in *Application by Epic Energy South Australia Pty Ltd* [2003] ACompT 5. In that matter, the Tribunal did not accept the ACCC's submission that *any* level of market power justifies coverage. The Tribunal noted that:[48]

'What needs to be addressed is whether the alleged ability of Epic to exercise market power is such as to have a commercially and socially significant impact, both in quantum and in sustainability. It must be non-trivial, and non-transient. It must have a significant effect on some aspect of competition in a relevant market'.

4.2 Criterion (b)

Criterion (b) of the coverage criteria requires consideration to be given to whether it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the pipeline.

This criterion closely mirrors criterion (b) in ss 44G(2)(b) and 44H(4)(b) of the CCA. Given this, the recent High Court decision in the *Pilbara Infrastructure Pty Limited and Another v Australian Competition Tribunal and Others* (2012) 246 CLR 379 (Pilbara Infrastructure

47 NCC, Gas Guide, October 2013, p 35.

48 *Application by Epic Energy South Australia Pty Ltd* [2003] ACompT 5 [113].

Case)[49] is instructive as to the relevant test to apply in determining whether it is uneconomic for anyone to develop another pipeline.[50]

The High Court in the Pilbara Infrastructure Case determined that the test to apply in considering whether it was uneconomic to duplicate particular infrastructure was a 'privately profitable test' and that the term 'uneconomic' should be interpreted as "unprofitable".[51] The High Court went on to note that the profitability of developing another facility will depend on whether a "person could reasonably expect to obtain a sufficient return on capital that would be employed in developing the facility".[52] It also observed that if someone could develop an alternative facility as part of a larger project, "it would be necessary to consider the *whole* project in deciding whether the development of the alternative facility, as part of the larger project, would provide a sufficient rate of return".[53]

4.3 Criterion (c)

Criterion (c) of the coverage criteria requires consideration to be given to whether access (or increased access) to the services provided by means of the pipeline can be provided without undue risk to human health or safety.

When applying this criterion, the NCC has stated it will generally presume that provisions within the regulatory regime will provide 'effective mechanisms to preserve human health and safety'.[54] The onus is therefore on any party that disagrees with this presumption to demonstrate how coverage would result in undue risk to human health or safety.

4.4 Criterion (d)

Criterion (d) of the coverage criteria requires consideration to be given to whether access (or increased access) to the services provided by means of the pipeline would *not* be contrary to the public interest.

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49 Per French CJ, Gummow, Hayne, Crennan, Kiefel and Bell JJ.

50 It is worth noting that the NCC has also accepted that the findings in the Pilbara Infrastructure Case should be applied when assessing criterion (b) under the coverage criteria. See NCC, Gas Guide, October 2013, p 40.

51 Pilbara Infrastructure Case (2012) 246 CLR 379, 413, [83].

52 ibid.

53 ibid, [104].

54 NCC, Gas Guide, October 2013, p46.

In *Re Duke Eastern Gas Pipeline Pty Ltd* [2001] ACompT 2, the Tribunal accepted the NCC's submission that criterion (d) only has a relevant role to play when the other criteria are all satisfied. The Tribunal noted:[55]

> '… criterion (d) does not constitute an additional positive requirement... 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.'

Until recently this criterion has been viewed by the NCC as requiring an assessment of whether the benefits of access (or increased access) outweigh the costs, where:

- the benefits of access include any identified benefits under criteria (a)-(c) and other benefits not captured by these criteria that are in the public interest and are consistent with the National Gas Objective (NGO); and
- the costs of access include: the direct costs of regulation; disruption costs; losses in allocative, productive or dynamic efficiency;[56] and other matters of public interest that are consistent with the NGO.

Following the Pilbara Infrastructure Case, the NCC has stated that the application of criterion (d) does *not* require a detailed technical examination of the costs and benefits of access to be undertaken. Rather, the NCC's task under this criterion is to "identify any matter that could mean access (or increased access) might be contrary to the public interest and then assess whether the likelihood and consequences of that matter lead to a conclusion that access is contrary to the public interest".[57] Elaborating further on the inquiry required by criterion (d) and its relationship to the other coverage criteria, the NCC has noted the following:

> 'This criterion does not allow for coverage of a pipeline on 'public interest grounds' when any other coverage criterion is not satisfied; it can only operate to override coverage being available in situations where all other coverage criteria are satisfied.'[58]

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55 *Re Duke Eastern Gas Pipeline Pty Ltd* [2001] ACompT 2 [145].

56 The sources of efficiency losses that the NCC has previously recognised include: distortions in price signals, which result in a reduction in allocative efficiency; a deterred incentive to invest, which results in a reduction in productive efficiency; and a dampening of incentives to innovate, which results in a reduction in dynamic efficiency.

See NCC, Gas Guide, October 2013, pp. 49-50.

57 NCC, Gas Guide, October 2013, p 48.

58 NCC, Final Recommendation – Application for the revocation of coverage of the Wagga Wagga Distribution Network, 8 August 2013, p25.

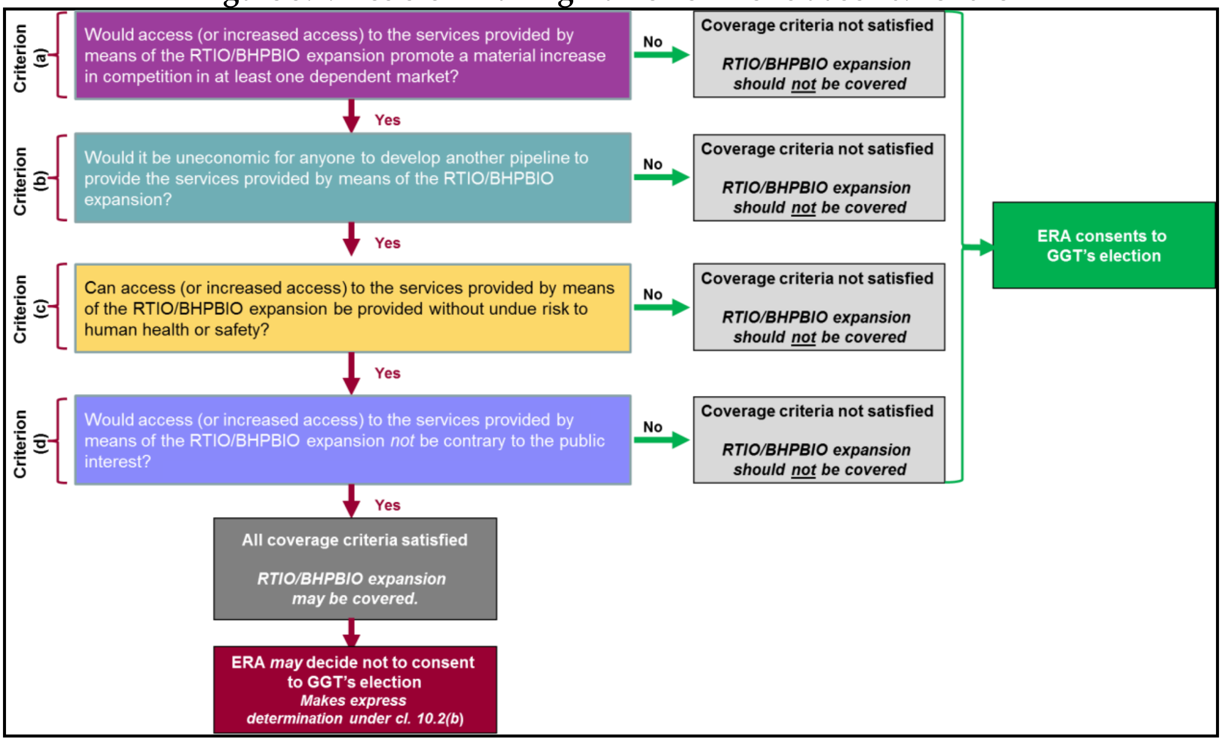
5 Application of the Decision-Making Framework

On 4 November 2013, GGT informed the ERA that, pursuant to clause 10.2(a) of the AA, it was electing *not* to treat the RTIO/BHPBIO expansion as part of the covered pipeline for any purpose under the Code. GGT is now seeking the ERA's consent to that election.

The decision-making framework that GGT believes should be employed by the ERA when considering this election is set out in summary form in Figure 5.1. In keeping with this framework, the ERA:

- should consent to GGT's election if it is not satisfied that one or more of the coverage criteria are met; and
- may *only* refuse to provide its consent to the election, if it is satisfied that <u>all</u> the coverage criteria are met.

Figure 5.1: Decision-making framework for clause 10.2 of the AA



When assessing whether or not the RTIO/BHPBIO expansion is likely to satisfy the coverage criteria, the ERA should have regard to both:

- the manner in which the coverage criteria in the Code and NGL, and the equivalent declaration criteria in Part IIIA of the CCA, have been interpreted and applied by the NCC, the Tribunal and other judicial bodies (see section 4); and
- the specific circumstances surrounding the RTIO/BHPBIO expansion, including the fact that all of the capacity has been contracted for around 20 years and the terms and conditions of access have been locked in for the duration of the GTAs (see section 2.3).

The remainder of this section considers:

- the extent to which the RTIO/BHPBIO expansion is likely to satisfy each of the coverage criteria; and
- whether, on the basis of the conclusions reached on each of the coverage criteria, the ERA should provide its consent to GGT's election.

5.1 Criterion (a)

Criterion (a) requires consideration to be given to whether access (or increased access) to the services provided by means of the RTIO/BHPBIO expansion would promote competition in at least one market, other than the market for the services provided by means of the RTIO/BHPBIO expansion.

In keeping with the manner in which this criterion has previously been interpreted and applied by the NCC, the Tribunal and the Federal Court (see section 4.1), the terms 'access', 'promote competition' and 'market, other than the market for the services' should be interpreted as follows:

- the term 'access' refers to a regulated right to access the services provided by the RTIO/BHPBIO expansion, with the terms and conditions being consistent with those that would apply under the Code (or the NGR); [59]
- the term 'promote competition' refers to the likelihood that there will be an improvement in the opportunities and environment for competition such that it promotes *materially* more competitive outcomes;[60] and
- the term 'market, other than the market for the services' refers to functionally distinct dependent markets (i.e. upstream or downstream markets) that will either supply, or be supplied with, gas transported via the RTIO/BHPBIO expansion.[61]

The remainder of this section sets out GGT's assessment of whether access (or increased access) to the RTIO/BHPBIO expansion is likely to promote a material increase in competition in any relevantly defined dependent market. Although not required by criterion (a), this section also considers the effect that coverage could have on competition in any other markets serviced by the GGP (as distinct from the dependent markets serviced by the RTIO/BHPBIO expansion).

5.1.1 Effect of access on competition in dependent markets

All of the capacity to be created by the RTIO/BHPBIO expansion has been contracted to RTIO and BHPBIO. The only dependent markets that could *potentially* be affected by access

59 See section 4.1.2.

60 See sections 4.1.3 and 4.1.4. See also, NCC, Gas Guide, October 2013, pp. 28-29.

61 See section 4.1.1. See also, NCC, Gas Guide, October 2013, p31.

(or increased access) to the services provided by this expansion over the next 20 years are therefore:

- the downstream markets that will be supplied by RTIO and BHPBIO using the gas transported via the RTIO/BHPBIO expansion, which as the information in section 2.2 indicates, are:
  - the global seaborne iron ore market,[62] in which both RTIO and BHPBIO compete; and
  - the retail electricity market in Newman, which BHPBIO supplies through its interest in the Mt Newman JV;[63] and
- the upstream production and gas sales market that will be used to supply RTIO and BHPBIO using the RTIO/BHPBIO expansion, which includes any producer in the Carnarvon Basin that is within scope of feasible interconnection to the GGP.[64]

To determine whether access (or increased access) to the RTIO/BHPBIO expansion is likely to promote a material increase in competition in any of these dependent markets, consideration must be given to whether there is likely to be a material difference between the future state of competition in the 'with' and 'without' regulated access states of the world.

In this case, the assessment of whether competition in any of the dependent markets is likely to be materially different in these two states of the world, is relatively straight forward because the terms of the GTAs are such that, irrespective of whether or not the RTIO/BHPBIO expansion is covered:

- RTIO and BHPBIO are the only parties that will be able to access the expanded capacity for around 20 years; and
- the price and non-price terms and conditions of access will be unchanged during this period.

Put simply, there will be *no* difference between the conditions prevailing in the dependent markets in the 'with' and 'without' regulated access states of the world given the operation of the GTAs. It follows that access (or increased access) to the services provided by means of the RTIO/BHPBIO expansion will *not* have any effect on competition in the dependent markets set out above over a period of around20 years. Criterion (a) is *not* therefore satisfied in this case.

62 The delineation of the bounds of this end-market is consistent with the position taken by the Tribunal *In the matter of Fortescue Metals Group Ltd* [2010] ACompT 2 [1078].

63 An equivalent retail market has not been defined for West Angelas because there is no township in this region.

64 In the NCC's GGP Final Recommendation, the geographic bounds of this market were restricted to producers located in the Varanus Island hub, because, at the time, there were a number of constraints, which limited the ability of other producers in the Carnarvon Basin located outside this hub to supply gas into the GGP. These constraints were removed in January 2007, when an interconnecting pipeline between the Dampier to Bunbury Natural Gas Pipeline (DBNGP) and the GGP was constructed.

5.1.2 Could coverage have a material effect on competition in other markets?

Criterion (a), as noted above, requires an assessment of the effect that access will have on competition in upstream and downstream markets that will either supply, or be supplied with, gas transported via the RTIO/BHPBIO expansion (i.e. dependent markets). It does not therefore require an assessment of the effect that coverage could have on competition in other markets serviced by the broader pipeline.[65]

Although not required by criterion (a) (and therefore considered to be an irrelevant matter by GGT), GGT has considered whether coverage of the RTIO/BHPBIO expansion could be said to promote a material increase in competition in any other market serviced by the GGP. In doing so, GGT has examined the effect that a coverage decision could have on the GGP reference tariff and the overall delivered price of gas that would be payable by users of the reference service located between Newman and Kalgoorlie over the next ten years.[66]

Box 5.1 contains an overview of the assumptions that GGT has made when carrying out this examination while Table 5.1 sets out GGT's estimates of the effect that a coverage decision would have on the reference tariff and the delivered price of gas at Newman and Kalgoorlie.

Before examining the estimates in Table 5.1, it is worth noting that the delivered price of gas is just one of the input costs faced by users of the GGP.[67] The estimates presented in Table 5.1 will therefore significantly overstate the relative importance of the effect that any decision to treat the expanded capacity as part of the covered pipeline could have on competition in the markets supplied by users of the reference service.

[65] It is worth noting that criterion (a) only requires consideration to be given to the effect that 'access' to the services provided by means of the RTIO/BHPBIO expansion will have on competition and not the effect that 'coverage' will have on competition. The two terms are distinguishable in this case because:

- the term access, as defined by the NCC, just refers to the regulated right to access the services provided by the RTIO/BHPBIO expansion; whereas
- the term coverage is more general and implies that other matters, like the effect that coverage will have on the reference tariff and the AA, may be relevant to the assessment of the effect on competition.

[66] It is worth noting that the only other user of the GGP located upstream of Newman is RTIO.

[67] The input costs will depend on conditions in the markets in which pipeline users acquire inputs. In general, those costs will include the costs of raw materials, labour costs, energy costs, other production costs, the costs of marketing and distributing the final product/service, overheads, taxes, levies and other government imposts.

Box 5.1: Assumptions used to estimate effect of coverage on reference tariffs and the delivered price of gas

To estimate the effect that a decision to cover the RTIO/BHPBIO expansion would have on the reference tariff and the overall delivered price of gas it has been necessary to make a number of assumptions. These assumptions are outlined below.

Reference Tariff

If the RTIO/BHPBIO expansion was to be covered the following would occur:

- the capital costs of expansion would be included in the capital base (the regulatory asset base) of the GGP;
- estimates of the costs of operating and maintaining the facilities that provide the expanded capacity would be included in the forecast of the operating costs used to determine reference tariffs for the GGP; and
- the expanded capacity, and the utilisation of that capacity (throughput), would be included in the capacities and throughputs used in reference tariff determination.

Estimates of the reference tariff for the GGP have been calculated for the next two access arrangement periods (2015-2019 and 2020-2024) on both a with coverage and without coverage basis using the nominal pre-tax method that has been used by the ERA to determine the current reference tariffs for the GGP.

Current forecasts of contracted capacity and throughput, and current estimates of other capital costs and of operating costs have also been used. Otherwise, the assumptions made for tariff calculation are the same as those that were made for current reference tariff determination, including the nominal pre-tax weighted average cost of capital, which has been assumed to be 10.48%.

Wholesale gas price

The wholesale price of gas (delivered to the Yarraloola receipt point of the GGP) in 2015-2019 and 2020-2024 has been estimated by taking the average of the nominal domestic gas price forecasts appearing in IMO's July 2013 Gas Statement of Opportunities (GSOO) over these two periods.[68] Because the GSOO only contains forecasts up to 2022, it has been necessary to make an assumption about prices in 2023 and 2024. For the purposes of this analysis, it has been assumed that the 2022 price will just rise in line with inflation (i.e. 2.5%) in these years.

Table 5.1: Estimates of the effect of coverage on the reference tariff and the delivered price of gas (nominal $/GJ)

	2015-2019			2020-2024		
	With Coverage	Without Coverage	Difference	With Coverage	Without Coverage	Difference
Newman						
Wholesale Gas Price	$6.30		n.a.	$7.35		n.a.
Reference Tariff (100% LF)	$1.233	$1.229	$0.004	$1.244	$1.270	-$0.027
Delivered Price of Gas	**$7.533**	**$7.529**	**$0.004**	**$8.594**	**$8.620**	**-$0.027**
Kalgoorlie						
Wholesale Gas Price	$6.30		n.a.	$7.35		n.a.
Reference Tariff (100% LF)	$2.702	$2.652	+$0.050	$2.727	$2.742	-$0.015
Delivered Price of Gas	**$9.002**	**$8.952**	**+$0.050**	**$10.077**	**$10.092**	**-$0.015**

68 IMO, Gas Statement of Opportunities, July 2013, Appendix 6.

As the estimates in this table indicate, if the RTIO/BHPBIO expansion formed part of the covered pipeline, it would result in the following changes over the next two AA periods:

- Over the period 2015-2019 there would be:
  - a small increase of 0.3% (0.4 cents/GJ) in the reference tariff payable for gas transported to Newman, and a 0.05% increase in the delivered price of gas at this location; and
  - an increase of 1.9% (5.0 cents/GJ) in the reference tariff payable for gas transported to Kalgoorlie, and a 0.6% increase in the delivered price of gas at this location.
- Over the period 2020-2024 there would be:
  - a reduction of 2.1% (2.7 cents/GJ) in the reference tariff payable for gas transported to Newman, and a 0.3% reduction in the delivered price of gas at this location; and
  - a reduction of 0.5% (1.5 cents/GJ) in the reference tariff payable for gas transported to Kalgoorlie, and a 0.15% reduction in the delivered price of gas at this location.

In GGT's view, the changes in the reference tariff and the delivered price of gas that would occur if the capacity created by the RTIO/BHPBIO expansion was treated as part of the covered pipeline are so small that coverage is unlikely to have any effect on competition in the other markets serviced by the GGP, let alone promote a material increase in competition. GGT is therefore of the opinion that even if the ERA found it relevant to consider the effect that coverage of the RTIO/BHPBIO expansion would have on competition in other markets (a finding that GGT does not endorse), criterion (a) would still not be satisfied.

5.1.3 Conclusion on criterion (a)

On the basis of the analysis set out above it is clear that criterion (a) is not satisfied in this case because:

- access on regulated terms and conditions to the services provided by the RTIO/BHPBIO expansion would not alter in any way the terms and conditions applying to the expanded capacity, or who can access the capacity over the next 20 years. Access (or increased access) to these services, would *not* therefore have any effect on competition in the dependent markets; and
- even if the ERA considers it relevant to have regard to the effect that coverage of the RTIO/BHPBIO expansion would have on competition in other markets served by the GGP (which is an irrelevant matter in GGT's view), the effects on the reference tariff and delivered price of gas would be too small to promote a material increase in competition in any of these markets.

5.2 Criterion (b)

Criterion (b) requires consideration to be given to whether it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the RTIO/BHPBIO expansion.

In keeping with the High Court's finding in the Pilbara Infrastructure Case (see section 4.2), when applying this criterion, consideration should be given to whether it would be privately profitable for anyone to develop another pipeline to provide the same services as the RTIO/BHPBIO expansion, on either a stand-alone basis, or as part of a larger project.

An important point to bear in mind when applying this test is that the question posed by the test is *not* whether it would be more profitable to use the existing pipeline than to develop another pipeline. Rather, the question is simply whether it would be profitable for another pipeline to be developed. Whether or not this option is less profitable than using the existing facilities, or less efficient from society's perspective because it gives rise to the duplication of assets, is irrelevant to this assessment.[69]

Another important point to note when applying this test is that if another pipeline was to be developed to provide the same services as the RTIO/BHPBIO expansion, it would *not* need to duplicate the GGP in its entirety. To the contrary, it would only need to enable RTIO's gas to be transported between Yarraloola[70] and Boonamichi Well and BHPBIO's gas to be transported between Yarraloola and Yarnima. The alternative pipeline contemplated by criterion (b) would therefore be of a much smaller scale than the GGP (both in terms of capacity and length) and optimally configured in terms of the route it traversed. In the discussion that follows, the term 'another pipeline' in criterion (b) is used to refer to a pipeline meeting this specification.

The remainder of this section sets out GGT's assessment of whether the RTIO/BHPBIO expansion is likely to satisfy this criterion.

5.2.1 Profitability of developing another pipeline as a stand-alone project

If another pipeline was to be developed on a stand-alone basis, then the profitability of that development, measured over the economic life[71,72] of the asset, would depend on both:

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69 *In the matter of Fortescue Metals Group Ltd* [2010] ACompT 2 [817].

70 It is worth noting that if a new pipeline was to be built the entry point for the gas, would not necessarily need to be Yarraloola.

71 The economic life of the assets may be less than the technical life of the assets. For example, if a pipeline is connected to a mine that has a finite life of 30 years, then the economic life of the pipeline would be 30 years.

72 To ensure some degree of consistency in this analysis, the same economic life would need to be assumed for both the new pipeline and the expanded capacity, particularly given the difference in the technical life of the two assets (i.e. the technical life of a new pipeline is around 80 years while the technical life of a new compressor is 30 years).

1. the costs that a new entrant would incur in the construction and ongoing operation of the new pipeline[73] *vis-à-vis* the costs that GGT would incur in adding new compressors and associated facilities to the GGP and the ongoing costs of providing the expanded capacity; and
2. the expected demand for the services to be provided by the new pipeline over the economic life of the asset.

GGT has not developed estimates of the costs that would be required to carry out this analysis. However, GGT would expect the costs of constructing a new pipeline to be substantially higher than the costs of expanding the GGP, particularly if the services are only required over the term of the GTAs. GGT therefore accepts it is unlikely that anyone, operating on a stand-alone basis, would find it profitable to develop another pipeline to supply the services provided by the expanded capacity.

5.2.2 Profitability of developing another pipeline as part of a larger project

Although a stand-alone development is unlikely to be profitable, it is *possible*, given the level of economic rent that may be encapsulated in iron ore prices,[74] that RTIO and/or BHPBIO *may* have found it profitable to develop such a pipeline, as part of their broader iron ore operations, rather than contracting with GGT.

The terms 'may' and 'possible' have been used in this context, because to determine whether or not it would actually have been profitable for RTIO or BHPBIO to develop such a pipeline, a detailed analysis of the profitability of this option would need to be carried out having regard to:

- the costs that would be incurred in constructing an optimally configured and sized pipeline to provide the same services as the expanded capacity, and the ongoing costs of operating that pipeline over its economic life;
- RTIO's and BHPBIO's likely utilisation of the pipeline over its economic life;
- the expected profitability of RTIO's and/or BHPBIO's iron ore operations over the economic life of the pipeline; and
- RTIO's and BHPBIO's required rates of return.

[73] Any efficiencies associated with operating a new pipeline vs an older pipeline with compressors would also need to be factored into this analysis.

[74] An indicator (albeit an imperfect indicator) of the level of economic rent that may be encapsulated in iron ore prices can be found in the margins reportedly earned by RTIO and BHPBIO per tonne of iron ore. According to information contained on page 34 of Rio Tinto's November 2013 Chartbook, over the last 4.5 years RTIO and BHPBIO have earned a 60-75% margin (measured on an earnings before interest tax depreciation and amortisation (EBITDA) basis) per tonne of iron ore. While the margin would obviously be much lower once the effects of tax, depreciation and amortisation are taken into account, these margin estimates do indicate that iron ore prices over this period have included a significant margin above operating costs.

Information on the latter two of these factors is not publicly available. GGT is not therefore in a position to carry out the analysis that would be required to reach a definitive view on whether or not it would have been profitable for either party to develop such a pipeline.

Although GGT is not in a position to assess the profitability of this option, it is aware of a number of cases in which iron ore producers appear to have found it privately profitable to either duplicate or bypass existing infrastructure. For example, BHPBIO appears to have found it privately profitable to bypass the Newman Power Station by constructing its own power station at Yarnima at an estimated cost of US$597 million.[75] Similarly, Fortescue Metals Group's decision to construct the Chichester railway line (which runs parallel to BHPBIO's Mt Newman railway line for much of its length), suggests that it too found it privately profitable to develop this infrastructure. In GGT's view, these examples lend some weight to the proposition that it may be, or may have been, profitable for BHPBIO or RTIO to develop another pipeline as part of their iron ore operations. Accordingly, this potential should not be readily dismissed.

5.2.3 Conclusion on criterion (b)

To summarise, GGT is of the view that:

- it is unlikely that it would be profitable for anyone to develop another pipeline to provide the same services as the RTIO/BHPBIO expansion on a stand-alone basis; but
- it *may* be, or may have been, profitable for RTIO or BHPBIO to develop such a pipeline as part of their iron ore expansion projects, but additional information from RTIO and BHPBIO and a detailed quantitative assessment of the profitability of this option would be required to confirm this.

As the latter of these points highlights, GGT is not currently in a position to form a concluded view on whether or not criterion (b) is satisfied. However, under the decision-making rule set out in section 1.15 of the Code (section 100 of the NGL), a finding that criterion (b) is satisfied would not alter the fact that if criterion (a) is *not* satisfied (see section 5.1.3), the RTIO/BHPBIO expansion should *not* form part of the covered pipeline. Therefore, GGT does not consider that it is necessary to reach a concluded view on criterion (b).

Having said that, if the ERA comes to an alternative view on criterion (a) then, in GGT's view, the ERA will need to form a concluded view on criterion (b) on the basis of a relevant body of evidence, if it is to reach the degree of satisfaction required by section 1.15 of the Code (or section 100 of the NGL) (see section 3.2.1.3). As a matter of procedural fairness, the ERA would need to provide GGT with an opportunity to understand why the ERA considers criterion (b) may be satisfied and to respond to that position and the material on which the ERA relies in reaching its view on criterion (b) (see section 3.2.1.4).

[75] BHPB, New Power Station for Western Australia Iron Ore, 16 November 2011.

5.3 Criterion (c)

Criterion (c) requires consideration to be given to whether access (or increased access) to the services provided by means of the RTIO/BHPIO expansion can be provided without undue risk to human health or safety.

Given that access to the expanded capacity is already to be provided to RTIO and BHPBIO without undue risk to human health or safety, GGT accepts that the RTIO/BHPBIO expansion would satisfy criterion (c).

5.4 Criterion (d)

Criterion (d) requires consideration to be given to whether access (or increased access) to the services provided by means of the RTIO/BHPBIO expansion would *not* be contrary to the public interest.

The term 'public interest' is not defined in either the Code or the NGL. However, the NCC has stated in its Gas Guide that a broad range of issues may be considered under this criterion 'with a particular focus on public interest issues raised by the national gas objective'.[76,77]

The inquiry required by criterion (d) and the relationship between this criterion and the other coverage criteria has recently been described by the NCC as follows:

> 'The Council considers that the preferable approach to coverage criterion (d) is to seek to identify any matter that could mean access (or increased access) might be contrary to the public interest and then assess whether the likelihood and consequences of that matter lead to a conclusion that access is contrary to the public interest.'[78]
>
> 'This criterion does not allow for coverage of a pipeline on 'public interest grounds' when any other coverage criterion is not satisfied; it can only operate to override coverage being available in situations where all other coverage criteria are satisfied.'[79]
>
> 'The Council's task under criterion (d) is to identify whether there is any matter that might result in access (or increased access)… being contrary to the public interest even if the other coverage criteria are met. Criterion (d) is concerned with identifying reasons why a pipeline should not be covered even when the other coverage criteria are satisfied.
>
> At best any affirmative benefits from access might offset public costs that would otherwise be assessed under this criterion. But where another coverage criterion is not satisfied that is the end of the matter—coverage is not available. Under the NGL, positive public interest factors cannot overcome a failure to satisfy one or more coverage criterion to allow coverage of a pipeline. That, for example, access might help preserve employment in a region, result in lower gas transport tariffs or result in lower gas prices

76 NCC, Gas Guide, October 2013, p46.

77 The equivalent reference point to the NGO in the Code is the objective set out in the introduction to the Code.

78 NCC, Gas Guide, October 2013, p48.

79 NCC, Final Recommendation - Application for the revocation of coverage of the Wagga Wagga Distribution Network, 8 August 2013, p25.

for consumers does not allow coverage of a pipeline when the pipeline would not materially promote competition in a dependent market.'[80]

As these extracts indicate, if one or more of the other coverage criteria are *not* satisfied, a finding that criterion (d) is satisfied would not provide a sufficient basis for the pipeline to be covered, because the decision-making rule in section 1.15 of the Code (or section 100 of the NGL) requires *all* the coverage criteria to be satisfied if a pipeline is to be covered.

The relevance of this observation to the current assessment can be summarised as follows:

1. If the ERA concurs with GGT that criterion (a) is *not* satisfied, then a finding that criterion (d) is satisfied will not alter the fact that the RTIO/BHPBIO expansion should *not* form part of the covered pipeline. Limited consideration of this criterion will therefore be required if the ERA finds that criterion (a) is not satisfied.
2. If, on the other hand, the ERA finds that criterion (a) is satisfied and criteria (b) and (c) are also satisfied, then before concluding that the RTIO/BHPBIO expansion should be covered, it must satisfy itself that access to the services provided by the RTIO/BHPBIO would *not* be contrary to the public interest.[81] A more detailed assessment of this criterion will therefore be required if the ERA finds criteria (a)-(c) are satisfied. In keeping with the approach recently advocated by the NCC, this will involve:
   - identifying any matter that could mean access (or increased access) might be contrary to the public interest; and
   - an assessment of whether the likelihood and consequences of that matter lead to a conclusion that access is contrary to the public interest.

While GGT believes there is no value in conducting a detailed assessment of criterion (d) given that criterion (a) is not satisfied, it has given some further thought to matters that would be relevant to consider in the event the ERA comes to an alternative view and finds that criteria (a)-(c) are satisfied.

In short, GGT is of the view that if the ERA finds it necessary to closely examine criterion (d), it should carefully consider the adverse effects that access (or increased access) to the RTIO/BHPBIO expansion would have on:

- GGT's incentive to undertake efficient investment in the GGP;
- the incentive GGT has to try and accommodate the needs of users and prospective users through tailor made commercially negotiated agreements, and to respond to their service requirements in a timely and efficient manner; and

80 NCC, Final Recommendation - Application for coverage of the South Eastern Pipeline System, 8 April 2013, p38.

81 Note that because criterion (d) is expressed in the negative, the ERA does not have to be satisfied that access would be in the public interest. Rather, it only has to be satisfied that access would *not* be contrary to the public interest. *Re Services Sydney Pty Ltd* [2005] ACompT7 [192].

- the productive and dynamic efficiency of the market for gas transportation services and upstream and downstream markets, over the medium to longer term.[82]

In GGT's view, these adverse effects are likely to be significant and could mean that access (or increased access) to the RTIO/BHPBIO expansion would be contrary to the public interest.

5.5 Conclusion on coverage criteria and GGT's election under cl. 10.2(a)

The decision-making rule established in section 1.15 of the Code (or section 100 of the NGL), requires *all* four of the coverage criteria to be satisfied for an affirmative decision on coverage to be made. Where one or more of the criteria are not satisfied, then the decision must be against coverage.

Applying this decision-making rule to the RTIO/BHPBIO expansion, it is clear from the analysis set out in sections 5.1-5.4 that the expansion should *not* form part of the covered pipeline because it does *not* satisfy criterion (a) and there is some uncertainty as to whether criterion (b) is satisfied. Because criterion (a) is not satisfied, it has not been necessary to undertake a detailed assessment to determine whether criterion (d) is satisfied, but given the adverse effects a coverage decision would have on investment, service provision and efficiency, it is quite possible that access (or increased access) to the RTIO/BHPBIO expansion may be contrary to the public interest.

Based on these findings, the ERA should consent to GGT's election that the RTIO/BHPBIO expansion *not* be treated as part of the covered pipeline for any purpose under the Code.

[82] The effects of productive and dynamic efficiency losses will ultimately be borne by users and prospective users (e.g. through higher transportation charges, poorer quality services, delayed investment or no investment). Any efficiency losses brought about by a coverage decision could therefore have flow on effects in upstream and downstream markets