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Australia

13 December 2002

Mr Robert Püllella
Office of Gas Access Regulator
PO Box 8469
Perth Business Centre
PERTH WA 6849

Dear Mr Püllella,

Submission on the Access Arrangements for the DBNG Pipeline and the Epic Court Case

Please find a submission from Multinet Gas Pty Ltd on the above issue of the Access Arrangements for the EPIC Dampier to Bunbury gas pipeline.

The decision by the Western Australian Supreme Court on the Epic case is a landmark decision in the same vein as the Queensland Milling and Queensland Wire decisions under the Trade Practices Act (TPA) 1974. In these cases, the Justices were not simply dealing with the merits of a particular case but writing on the fundamental interpretation of the new law. The Epic decision is the first judicial interpretation of the National Third Party Access Code for Natural Gas Pipelines and the Justices state in their decision that they dealt with the 'fundamental issues' before dealing with the peculiarities of the case.

Our submission takes the form of a summary of the AGA submission to the Victorian Essential Services Commission on the Review of the Gas Access Arrangements Draft Decision July 2002. Multinet's views of how the Regulator must assess a proposed arrangement in light of the Epic case are well encapsulated in the AGA submission. The full text is available from the web site www.esc.vic.gov.au.

Yours sincerely

A handwritten signature in black ink, appearing to read "Roger Pugsley".

ROGER PUGSLEY
Group Manager Multinet

General Principles of Regulatory Approach

The Epic Energy court decision establishes a number of important principles highly relevant to the regulation of gas distribution networks under the National Gas Code. These principles fall into two broad categories. Firstly, general principles of regulatory approach, and secondly specific principles relevant to applying the provisions of the National Gas Code.

The principles established by the Supreme Court's judgement include:

- regulatory decisions on third party access prices should take into account a number of policy principles established in Section 2.24 of the National Gas Code¹;
- in the determination of third party access prices the regulator should consider a wider range of political and social considerations, not just economic theory²;
- regulators must fully take into account the effect of their decisions on past investment made prior to the introduction of the National Gas Code to ensure that sound commercial investment decisions made in the past are not rendered lossmaking because of regulatory determinations³;
- the National Gas Code is not aimed at replicating the outcomes of a theoretically 'perfect' market, which is an abstraction. It is designed to promote outcomes similar to those that might occur in a 'workably' competitive market (which may sometimes include elements of persistent market power)⁴;
- the recovery by a regulated business of the actual price paid for an asset including a return on investment is a legitimate business interest, and for a range of social, political and public interest considerations it may be appropriate to consider asset purchase prices in establishing initial regulatory capital bases⁵;
- there is no provision of the National Gas Code that supports the views of regulators that future revenues available to the regulated business must be no more than the efficient cost of delivering the service. There may be public policy grounds in either not distorting investment, or in protecting the legitimate business interests of regulated businesses, to allow the recovery of more than 'efficient' costs⁶; and

¹ Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231, [55]

² Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231, [152-153]

³ Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231, [149]

⁴ Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231, [128]

⁵ Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231, [130]

⁶ Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor [2002] WASCA 231, [142, 206]

- the National Gas Code deliberately adopts two different standards of treating investment, one directed to investments made prior to the introduction of regulation, and investment made under the current regulatory framework.⁷

Specific Principles for Applying the National Gas Code

The judgement also establishes a number of more specific principles that give guidance on the correct interpretation and application of specific National Gas Code provisions.

These principles include:

- the assessment of proposed Access Arrangements by regulators should be guided by the factors in Section 2.24 (a)-(g), with each factor being given weight as ‘fundamental elements’;
- the factors in Section 2.24 should guide the regulator in determining how the tariff principles in Section 8.1 of the Code should be reconciled, where these principles conflict;
- the regulator may, to ensure that their decision does not distort investment in gas pipelines or in upstream or downstream industries, take into account the actual investment of a service provider in approving a reference tariff or reference tariff policy. This includes in establishing an initial capital base under Section 8.10 and 8.11 of the Code;
- the regulator may properly take into account an asset purchase, the circumstances of the purchase, and any value according to a recognised asset valuation methodology revealed by a purchase price, in deciding whether the initial capital base should be higher than the depreciated optimised replacement cost (DORC) under Section 8.11 of the Code; and
- in establishing an Initial Capital Base under the National Gas Code it is not the case that only ‘efficient’ capital investment or ‘regulated revenues’ are to be taken into account. That is, it is not true that the initial capital base should only represent a value that is consistent with future regulated revenues or efficient capital investment.

⁷ *Re: Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd & Anor* [2002] WASCA 231, [182]