



REGULATION OF GAS TRANSMISSION IN WESTERN AUSTRALIA

Presentation by

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Overview

- Objectives of the Legislation
- Role of the Regulator
- Jurisdictional Arrangements
- The Gas Pipelines Access Code
- Functions of the Regulator
- The Office of Gas Access Regulation
- The Approach in WA

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Overview

The aim of today's presentation is to provide some insight into how access to gas transmission and distribution pipelines is regulated in Western Australia.

The role of the Regulator is defined by functions legislated in the *Gas Pipelines Access (WA) Act 1998* (GPAA). The functions of the Regulator are very specific, many of which are set out in the *National Gas Pipelines Access Code for Natural Gas Pipeline Systems* (the Code).

The objectives of the legislation are listed in the preamble to the GPAA. They focus primarily on promoting competition by providing access to gas pipelines on terms and conditions that are fair and reasonable to both owners and users.

The regulatory arrangements applying in Western Australia differ slightly to those of other jurisdictions. The main difference is that the Western Australian regime covers both gas transmission and distribution whereas other State regimes cover only distribution.

The provisions of the Code apply only to a pipeline once it is "covered". Owners of covered pipelines are required to put in place an Access Arrangement detailing the terms and conditions and reference tariffs for third party access. The Regulator must approve an Access Arrangement or impose its own if agreement cannot be reached.

The approach in Western Australia is intended to be as flexible as possible in implementing the Code, but is cognisant of the fact that the Regulator is subject to appeal by both owners and users. The Code thereby reinforces the need for the Regulator to determine an appropriate balance of interests between the parties.



Objectives of the Legislation

- Preamble to the Act:
 - Facilitate a National Market for Gas
 - Prevent Abuse of Monopoly
 - Promote Competition
 - Provide Rights of Access to Gas Pipelines
 - Provide for Resolution of Disputes

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Objectives

The legislation seeks to achieve specific objectives by placing obligations on owners of “covered” pipelines. These obligations include:

1. permitting the interconnection of gas pipelines;
2. providing third party access on agreed terms;
3. complying with ring fencing arrangements detailed in the Code;
4. complying with minimum information disclosure requirements; and
5. requiring parties not to engage in “hindering” for which penalties are prescribed.

Once an Access Arrangement has been approved, the pipeline Service Provider is left to offer “reference” services in accordance with the Access Arrangement and negotiate non-reference services. The Service Provider is left to do these things substantially without involving the Regulator. There are only a few areas where the legislation empowers the Regulator to monitor or have an involvement during the currency of an Access Arrangement.

If a Prospective User is unable to obtain pipeline services where an Access Arrangement has been approved by the Regulator, the Prospective User may have any such dispute considered by the Gas Disputes Arbitrator. The Arbitrator in Western Australia is Mr Laurie James.

A User that already has a Service Agreement under an approved Access Arrangement can seek to resolve a dispute through normal commercial arbitration. The parties can agree to have the Gas Disputes Arbitrator hear a commercial dispute of this nature.



The Code

- Places up-front obligations on Service Providers
- Is quite prescriptive on some matters
- Requires high degree of information disclosure
- Sets out a specific process for assessing an Access Arrangement
- Places considerable weight on public consultation
- Requires certain principles to be included in an Access Arrangement

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The Code

The Code places up-front obligations on Service Providers of gas pipelines “covered” by the Code.

A proposed Access Arrangement is required to be lodged with the Regulator within 90 days of coverage.

Pipeline Service Providers are also required to comply with minimum ring fencing obligations within 6 months of coverage.

While the Code is very prescriptive in some respects, it provides flexibility in other respects.

The Code is very prescriptive on matters to be included in an Access Arrangement, the method for determining reference tariffs, information disclosure, minimum ring fencing obligations and the timelines within which things are to be achieved.

Flexibility to extend timelines is provided in many cases. The Code also provides flexibility in the determination of reference tariffs, for example, by providing discretion to the Regulator in determining the Initial Capital Base and to the Service Provider in selecting the method for determining Total Revenue.

The Code prohibits the Regulator disclosing information that would be unduly harmful to the legitimate business interests of the Service Provider, if confidentiality is requested.

The Access Arrangement process involves two periods of public consultation, one before the Regulator’s Draft Decision and one thereafter. A public forum to consider any relevant issue may be held at any time.

An Access Arrangement is required by the Code to address specific principles on which access is to be provided. An Access Arrangement may also address principles other than those specifically listed.



Role of the Regulator

- Main role is to approve proposed Access Arrangements
- Minimal ongoing monitoring
- Some ring fencing responsibilities
- Competitive tender responsibilities
- Approve Associate Contracts
- Approve Information Package
- Approve New Facilities Investment
- Some enforcement responsibilities

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Role of the Regulator

The main role of the Regulator is to approve proposed Access Arrangements. This includes reviewing an Access Arrangement after a period of time. Access Arrangements can be of any duration, but the Regulator must consider whether review mechanisms are to be included in an Access Arrangement extending beyond 5 years, to address the risk of forecasts proving to be inaccurate.

The only monitoring function that the Regulator has relates to a Service Provider's compliance with ring fencing obligations.

The Code requires pipeline Service Providers to comply with minimum ring fencing obligations. The Regulator is empowered to waive some of the minimum ring fencing obligations or impose other additional ring fencing obligations.

The Regulator has some responsibilities relating to competitive tender arrangements as an alternative approach to approving reference tariffs.

The Regulator is required to approve contracts between a Service Provider and an "Associate" of the Service Provider.

The Regulator may require a Service Provider to amend or include additional information in an Information Package that the Service Provider is required to make available to Prospective Users.

New Facilities Investment must be efficient for it is to be included in the Capital Base used to determine Reference Tariffs. The Regulator may approve such expenditure for inclusion in the Capital Base during the period of an Access Arrangement.

The legislation and regulations provide for the imposition of penalties for non-compliance of key provisions.



Gas Access Arrangement Process

- Coverage of Pipeline
- Lodge Access Arrangement within 90 Days
- Informal Compliance Check
- Public Consultation 1
- Draft Decision
- Public Consultation 2
- Public Forum
- Final Decision

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Access Arrangement Process

An Access Arrangement is assessed for compliance once it has been lodged formally and is then released for public consultation.

As soon as submissions are received these are posted on the *OffGAR* web page and become part of the assessment process.

There are 4 main stages in preparing a Draft Decision:

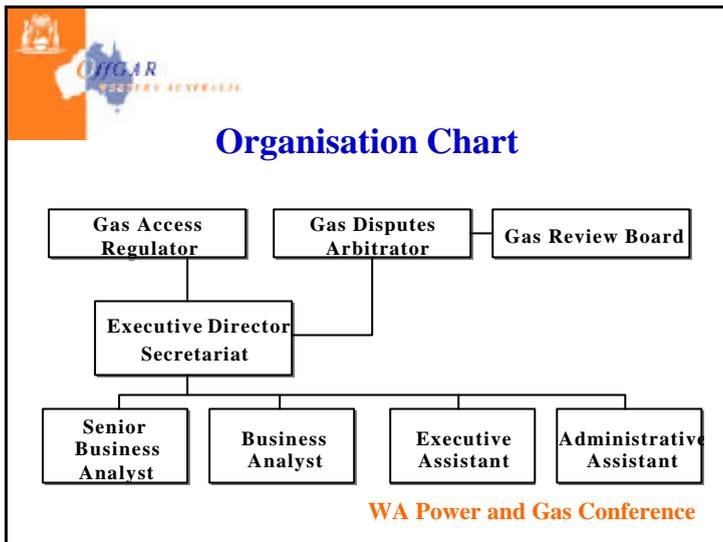
1. specialist advice is sought on the technical, financial and legal aspects of the proposed Access Arrangement;
2. financial modelling is undertaken to verify reference tariffs, the Initial Capital Base and rate of return proposed by the pipeline Service Provider;
3. issues raised in submissions are considered and analysed; and
4. the Draft Decision, listing any required changes to the proposed Access Arrangement, is prepared and issued.

A Final Decision is prepared by the Regulator after the second period of public consultation. A Public Forum may be held to consider any issues raised.

In the event that the pipeline Service Provider and the Regulator are unable to agree on required amendments to a proposed Access Arrangement, the Regulator may impose its own Access Arrangement.

The Regulator may be subject to appeal where a decision imposes specific requirements on a pipeline Service Provider.

The Regulator may also be subject to appeal by a person other than the Service Provider where that person has made a submission.



Organisational Structure

The Regulator, Arbitrator and the Gas Review Board are the main bodies that regulate access to gas pipelines covered by the Code in Western Australia.

The Office of Gas Access Regulation (*OffGAR*) has been established to assist the Regulator and Arbitrator in administering their respective functions.

As *OffGAR* has only a small permanent staff, it is substantially dependent on consultants and temporary specialist staff to undertake the required work.

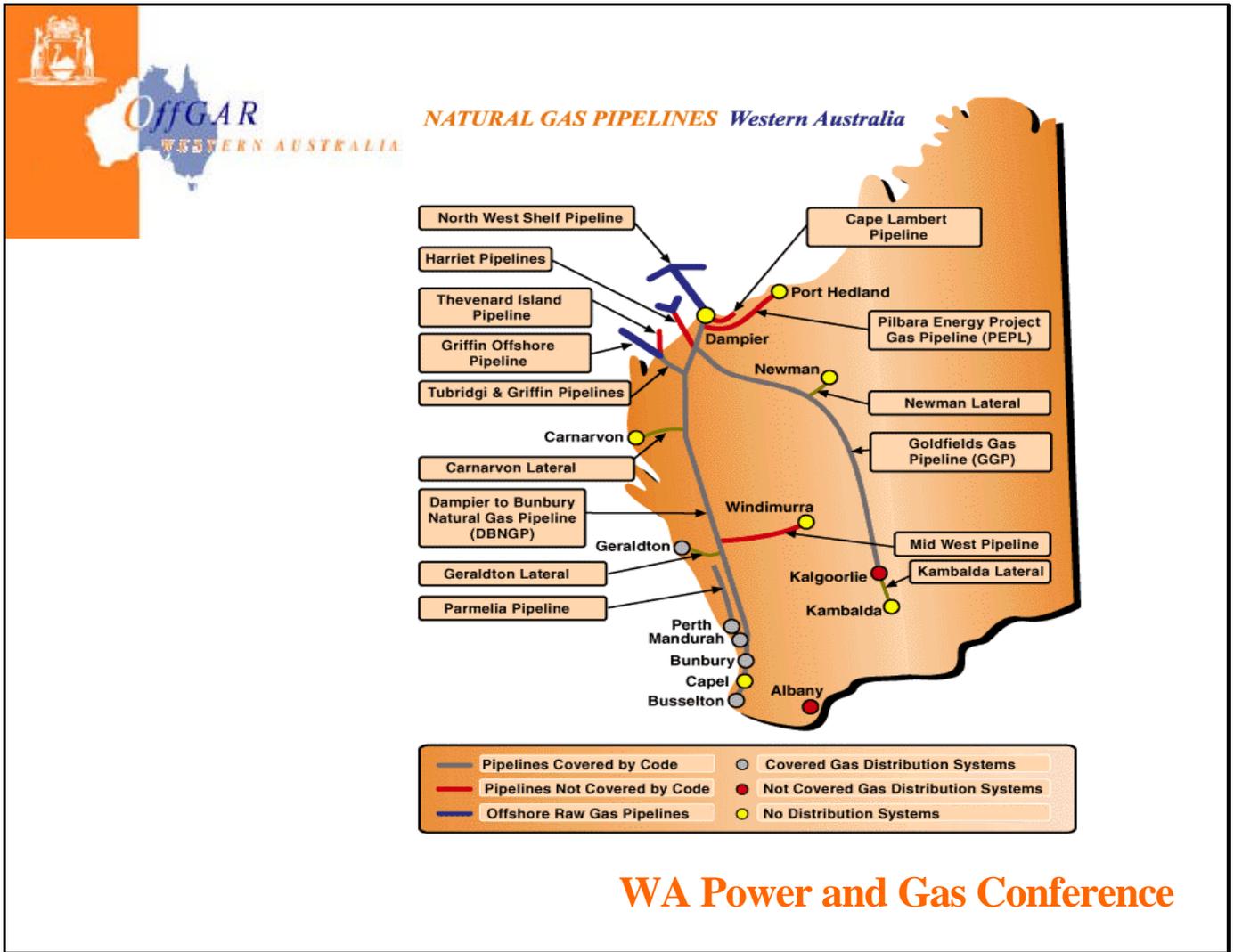
A consultancy register exists, which facilitates the tendering and selection of consultants to undertake these tasks. Currently, there are 26 consultants listed on this register.

Work areas in which consultancies have been assigned include:

1. analysis and assistance in the preparation of regulatory decisions;
2. expert legal, regulatory, financial and technical advice on proposed Access Arrangements;
3. internal audit, risk management and accounting systems development; and
4. human resources and other specialised administrative assistance and advice.

OffGAR has also had access to the Crown Solicitor's Office as a principal source of legal advice. Independent legal advice is sourced where necessary on an as required basis.

On 14 January 2000, the *Gas Pipelines Access (WA) (Funding) Regulations 1999* were introduced under section 87 of the GPAA to permit *OffGAR* to charge for services and become self-funding.



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Pipeline Systems Covered by the Code

A number of pipelines located in the State were automatically “covered” by the access regime when the GPAA was proclaimed in Western Australia on 9 February 1999 (as illustrated above).

The AlintaGas Mid-West and South-West Gas Distribution Systems were also automatically covered. Other distribution systems in Western Australia are not presently covered.

Revocation and New Pipelines

Applications have been made to the NCC for the revocation of seven pipeline laterals. Five of these applications have been successful.

There have been no applications seeking coverage of new pipelines under the Code in Western Australia.



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Gas Pipelines - Code Status

| Pipeline | Date Access Arrangement Lodged | Status |
|--|--------------------------------|---|
| AlintaGas Distribution System | 30 June 1999 | Draft Decision Issued 14 March 2000 |
| Beharra to Parmelia Pipeline | Coverage revoked | No longer covered by the Code |
| Dampier to Bunbury Natural Gas Pipeline | 15 December 1999 | Second Round Public Submissions Closed 12 May 2000 |
| Goldfields Gas Pipeline | 15 December 1999 | Public Submissions Closed 3 March 2000 |
| Kalgoorlie, Leinster and Mt Keith laterals | Coverage revoked | Laterals no longer covered by Code |
| Kambalda Lateral | Deferred | Extension granted to 1 Dec 2000 |
| Karratha to Cape Lambert Pipeline | Coverage revoked | No longer covered by the Code |
| Parmelia Pipeline | 7 May 1999 | Draft Decision Issued 27 October 1999 |
| Tubridgi Pipeline System | 21 October 1999 | Public Submissions Closed 10 December 1999 |

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Current Status

Five proposed Access Arrangements have been lodged for assessment since OffGAR was established.

Draft decisions have been issued on Access Arrangements for the Parmelia Pipeline and the Mid-West and South-West Gas Distribution Systems.

Work is well advanced on the draft decision for the Tubridgi Pipeline and final decisions on the proposed Access Arrangements for the Mid-West and South-West Gas Distribution Systems and the Parmelia Pipeline.

In addition, public submissions have closed for the Goldfields Gas Pipeline and the Dampier to Bunbury Natural Gas Pipeline and work has commenced on the preparation of the Draft Decisions for these pipelines.

Draft decisions have also been issued on applications for a waiver of ring fencing obligations for the Parmelia and Tubridgi pipeline systems.



Experience After First Year

- Provision of quality information has been problematic
- Decisions only as good as the information provided
- Two stage public consultation helpful
- Submissions have been valuable

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Experience after the First Year of Operation

While the Code seems to be working quite well, the timely provision by pipeline service providers of quality information on which to base decisions has been one of the more difficult aspects of the regulatory process thus far.

The provision of quality information has suffered, in part, because of difficulties attributed to confidentiality.

Decisions by the Regulator and other regulatory bodies are only as good as the information on which decisions are based.

Nevertheless, the two stage public consultation process has been very useful, although clearly requires more time than envisaged by the Code.

The time provided by the Code to give final approval to an Access Arrangement is also proving to be well short of that needed by regulators in Australia.

While extensions of time are available for approving an Access Arrangement, no extensions are available in other cases such as the time limits provided for granting a waiver of ring fencing obligations.

Experience in Western Australia has shown public submissions to be of a very high standard and a valuable contribution to the assessment process.



Trends in Gas Access Regulation

- Challenge:
 - Avoid being overly intrusive
 - Encourage innovation
 - Contain regulatory costs
- Trend is toward Broad Regulatory Mechanisms:
 - Incentive Regulation
 - Price Caps, Revenue Caps, Revenue Yield
 - Benchmarking

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Trends in Gas Access Regulation

One challenge for regulators is to administer a legislative regulatory framework without being overly intrusive. Regulators also need to provide the necessary guidance and constraint without unduly restricting innovation or incurring excessive costs.

In meeting these challenges, regulators can focus on broad parameters of a regulated business through incentive regulation and benchmarking. Such an approach can reduce the complexity and cost of focussing more directly on detail.

A range of incentive mechanisms has emerged in regulatory practice and such mechanisms have been included in WA decisions where appropriate.

There is, however, active debate over some of these measures including the most appropriate form of price control (ie whether a simple price cap should be used, a tariff basket approach, average revenue cap (revenue yield) or a more simple revenue cap approach).

The most appropriate form of “efficiency carry-over” (or tariff glide-path) is also under discussion.

It needs to be recognised that no one form of incentive mechanism or price control is likely to be appropriate in all situations.

While benchmarking and the use of incentive mechanisms can increase efficiency and reduce the level of intrusion, these approaches rely on detailed research that is at a very early stage.

Gas businesses in Australia are still undergoing organisational and financial changes associated with privatisation, which complicate the estimation of efficiency benchmarks.

The regulatory system is also still in its infancy and is largely preoccupied with issues of pipeline coverage and approval of Access Arrangements.

Benchmarking and incentive mechanisms have the potential to become more important as regulatory systems in Australia become more developed.



Regulatory Approach

- Promote Competition
- Encourage Economic Development
- Provide Value to Users of Pipelines and Gas
- Ensure Owners can Achieve a Reasonable Rate of Return
- Maximise Flexibility
- Balance Competing Interests of the Parties

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The Regulatory Approach in WA

To ensure that regulatory decisions are fair and reasonable, checks are made to see if objectives are met (listed above) before a decision is issued. These checks are applied after the procedures and requirements of the Code are met.

In addition, administrative arrangements have been structured to enhance consultation and cooperation.

Transparency in the assessment and decision process is maintained at a very high level.

OffGAR operates as a secretariat in providing services and advice to the Regulator.

The Regulator is free to obtain independent advice and remains at arms length from the Secretariat in the making of regulatory decisions. This provides greater flexibility to the Secretariat in consulting informally with pipeline service providers and other interested parties.



General Policies

- Open Door Policy
- Unless Confidential, Information is Made Public
- Information Made Available is Available to All
- Matters of General Interest are Made Public
- Reserve the Right to Express Views on Regulatory Process

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General Policies

In the time since commencement of operations almost 18 months ago, a number of general policies have been developed as follows:

1. An open door policy is maintained and the Regulator is available to consider all issues raised.
2. Information received is made public unless the information is determined to be confidential in which case the provisions of section 7.11 and 7.12 of the Code apply.
3. If for any reason information cannot be made public, it is referred back to the person providing that information to clarify, amend, seek concurrence of other parties (if necessary) or withdraw the information.
4. No document received by OffGAR is made available to another party unless it is made publicly available or is provided to another person with the express permission of the person providing the information.
5. Matters of general interest, unless confidential or commercially sensitive, are made public.
6. While the Office of the Regulator does not perform a policy role, the right to express views on regulatory processes is reserved.



Concluding Remarks

- Regulatory Processes are at an Early Stage in WA
- Objective to Focus on Broader Practices that are less Intrusive
- Broader Practices still in their Infancy
- Will propose Changes to Code to Streamline the Process
- Continue to Promote Competition, Encourage Investment, Provide Value to Users and Ensure Reasonable Return to Owners

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Concluding Remarks

Economic regulation is still at an early stage of development in Western Australia.

The State has substantially benefited from the experience of regulatory agencies in other Australian jurisdictions and overseas.

Regulatory practices in this State can be developed to be less intrusive by focussing greater attention on the broad parameters of a regulated business through incentive regulation and benchmarking.

In the current circumstances, the Code has been helpful in providing guidance to both pipeline service providers and the Regulator.

The Code combines prescription with some discretion providing a degree of flexibility.

It is in the common interests of the parties involved to make the Code workable, particularly in Western Australia where regulatory costs are billed directly to the pipeline Service Provider.

One of the objectives to be pursued is to propose changes to the Code to streamline the regulatory processes involved in preparation for the future review phase of Access Arrangements currently being approved.

In conclusion, the development of administrative arrangements and policies that encourage cooperation, openness and transparency are critical to effective regulation. Such arrangements are enhanced by the development and enunciation of clear objectives.

Decisions by the Regulator aim to promote competition, encourage investment and provide value to users of pipeline systems and consumers of gas, while maintaining a reasonable rate of return to pipeline service providers.