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12 July 2002

Ms Kanwaltjit Kaur  
General Manager  
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Australian Competition and Consumer Commission  
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Dear Ms Kaur

### **Moomba to Sydney Pipeline - Revised Access Arrangement**

Duke Energy International (DEI) welcomes the opportunity to comment on the revised Access Arrangement lodged by East Australian Pipeline Ltd (EAPL) for the Moomba to Sydney Pipeline (MSP).

At the outset, DEI would like to remind the ACCC that EAPL has lodged a revocation application in respect of the MSP for consideration by the National Competition Council (NCC). DEI firmly believes that the NCC has erred in its draft recommendation in respect of the revocation application. Specifically, of the four criteria that must be satisfied in order for coverage on the MSP to be maintained, DEI believes that criterion (a) is clearly not satisfied and that there are significant grounds for finding that criterion (d) is also not satisfied. DEI is therefore particularly concerned to note that the ACCC intends to proceed with the release of its Final Decision despite the uncertainty as to whether the MSP should in fact be subject to regulation.

DEI's concern stems from the ACCC's application of an intrusive and economically distorting approach to setting regulated prices which is totally unsuited to an environment where there is clear evidence of the impact of effective competition. While DEI recognises that, for the sake of expediency, it may be appropriate for the ACCC to proceed with the preparation of its Final Decision, DEI firmly believes that the release and implementation of any ACCC decision should be withheld until such time as a final Ministerial decision on the revocation application has been reached. To do otherwise potentially imposes significant, and unwarranted, financial costs on the competing pipelines.

Turning to the specifics of the MSP revised Access Arrangement. On 9 February 2001, DEI lodged its submission in response to the ACCC's Draft Decision on the Access Arrangement for the MSP. This submission noted that, as owner of the Eastern Gas Pipeline, DEI would be materially affected by the ACCC's decision because the two pipelines are in direct competition, and the Decision would profoundly affect prices and market shares for the EGP. DEI believes all of the arguments raised in its 9 February

2001 submission still stand, and urges the ACCC, in reaching its Final Decision, to give adequate regard to these arguments.

Further, DEI believes that in reaching its Draft Decision, the ACCC failed to give sufficient regard to the fact that the MSP faces direct competition from the EGP. That these two pipelines are in direct competition is evidenced by a 7 per cent reduction in the MSP tariffs since the access arrangement was initially lodged with the ACCC. This price reduction was acknowledged by the Australian Pipeline Trust to be a competitive response by EAPL to the entry of the EGP into the Sydney and Canberra markets.

Failure of the ACCC to give sufficient regard to the fact that the MSP and EGP are in direct competition will result in a number of adverse consequences. Perhaps the most profound of these will be the impact such a decision will have on incentives to invest in gas transmission pipelines. Regulatory intervention which gives almost no weight to existing competitive constraints (such as that which was shown by the ACCC in its Draft Decision on the MSP) would send a strong signal to potential constructors of other competing pipelines. Intervention, when competitive discipline is clearly effectively constraining prices, would convince investors that construction of competitive pipelines is unviable – not because of competitive behaviour, but because of the prospect of regulatory intervention. As such, regulation can actually impede investment in competing pipelines. DEI notes that such an outcome appears inconsistent with clause 2.24 of the Gas Code, which states that:

*“In assessing a proposed Access Arrangement, the Relevant Regulator must take the following into account:...*

(e) *the public interest, including the public interest in having competition in markets”.*

Where the price set on a regulated pipeline which is in direct competition with an unregulated pipeline is below the competitive price that has been established as the result of the outworking of competition between the two pipelines, there will be a significant financial impact on the unregulated pipeline as it will have no option other than to also reduce prices. The result would be the replacement of an effective market price with an arbitrary regulated price and the associated loss of price signals within the market. Such signals are essential to underpin long term, economy wide, allocative and dynamic efficiency improvements. Clearly, where potential investors see such perverse outcomes incentives to invest in competing pipelines would be severely curtailed.

DEI also notes that in its Draft Decision, the ACCC states that *“if gas transportation was a contestable market, it could be expected that tariffs and revenues would tend to follow the costs faced by a new entrant”.* This was exactly the situation that arose with the entry of the EGP into the Sydney and Canberra markets, where the price of the incumbent fell to match that of the new entrant. That is, EAPL was forced to reduce its price to reflect the competitive price that emerged as a result of the EGP. Unfortunately, despite the undeniable fact that the MSP competes with the EGP, the ACCC’s proposed tariffs in its Draft Decision in no way reflect that of a new entrant. Instead, the tariffs reflect a price which is 50% below that faced by the new entrant.

It also needs to be recognised that, as noted by the Australian Competition Tribunal (ACT) in the EGP case, a difference between the tariffs set under the Gas Code and that charged by an unregulated pipeline is not evidence of the absence of efficient competition in the market place. As the ACT noted, regulation is a second best option to competition. Further, the ACT stated:

*“The complex nature of the tariff setting process, the number of assumptions it relies on, and the fact that a reference tariff is a publicly available price which may be varied by negotiation between the pipeline owner and the user depending on the user’s requirements and conditions in the market place, all point to the fact that the reference price is not necessarily the price which would result from competition.”*

Further, it is DEI’s contention that s.8.1(b) of the Gas Code intends that pricing should reflect the behaviour in a competitive market. As noted above, the price reduction as a result of the entry of the EGP into the Sydney and Canberra markets represents a price that would occur in a competitive market, and is therefore entirely consistent with s.8.1(b) of the Code.

DEI recognises the obligation that the ACCC has under the Code to regulate covered pipelines. However, DEI believes that there is sufficient flexibility under the Code for the ACCC to recognise the effective nature of the competition existing between the MSP and EGP and as such, for the ACCC to adopt the market prices currently offered by EAPL as the reference tariffs for the reference services on the MSP.

DEI will continue to closely monitor the progress of the ACCC in its deliberations and would welcome the opportunity to clarify any of the issues raised in this (and its 9 February 2001) submission. As such, please do not hesitate to contact me on (07) 3334 5897.

Yours sincerely

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