

**Final Recommendations**

**Applications for Revocation of  
Certain Gas Pipelines in Western Australia  
from Coverage under  
WA Gas Access Regime**

June 1999

National Competition Council

## ***Introduction***

This document contains the National Competition Council's final recommendations regarding applications for revocation of coverage of gas pipelines under the Western Australian gas access regime (PLs 25, 26, 27, and 28).

While the applications are separate, the Council has found it convenient to deal with each of them in this document.

After consideration of the applications and submissions lodged by interested parties, the Council concludes that PL27 continues to meet all of the coverage criteria listed in section 1.9 of the National Code. However the Council considers that PLs 25, 26, and 28 do not meet criteria (a) or (d). Consequently, the Council recommends revocation of PLs 25, 26, and 28, but not of PL27.

This document comes in two parts.

Part A explains:

- the legislative background to the WA Gas Access Regime;
- the concepts of coverage and revocation under the Regime; and
- details of the four applications, including specification of the relevant pipelines.

Part B contains the Council's detailed consideration of the criteria against which the applications were assessed.

## ***Part A – Coverage and Revocation under the Gas Access Regime***

### **Legislative Background**

Western Australia has enacted a gas access regime to provide parties with a method for seeking access to gas transmission and distribution pipelines located in Western Australia. The regime is contained in the *Gas Pipelines Access (Western Australia) Act 1998* (the WA Gas Pipelines Act) and the *National Third Party Access Code for Natural Gas Pipeline Systems* (the National Code), at Schedule 2 of the WA Gas Pipelines Act.

The regime assists parties that wish to transport gas to negotiate a fair and reasonable contract of transportation with pipeline owner/operators. For example, a mining company may wish to buy gas from gas producers on the North West Shelf and transport it to a gas-fired power station at their mining site. Under the gas access regime, they have the opportunity to negotiate a contract for transport of the gas with the owners/operators of pipelines covered by the regime. In the absence of the regime, the owners/operators of pipelines might, by virtue of their monopoly over the transport of gas between the particular geographic regions, refuse to transport gas or demand a monopoly price for the transport of gas.

### **Coverage of Pipelines**

Pipelines can become covered under the WA gas access regime where they are listed in Schedule A of the National Code or meet the coverage criteria in section 1.9 of the National Code (see Appendix 1).<sup>1</sup>

The four pipelines the subject of the revocation applications are listed in Schedule A.

Where pipelines are covered, the owners/operators of the relevant pipelines must comply with certain obligations under the WA Gas Pipelines Act and the National Code. The WA Gas Pipelines Act and the National Code contain rules determining whether pipelines should be covered by the gas access regime, the operation and content of access arrangements (which specify the terms, conditions, and prices on which owners/operators must offer access), the provision of information by the owner and/or operator of a pipeline to parties seeking access, dispute resolution principles, and pricing principles.

### **Revocation of Coverage of a Pipeline**

The Code allows any party to seek revocation of coverage of a pipeline. The party must apply to the National Competition Council asking the Council to recommend to the relevant Minister that coverage of a pipeline be revoked. On receipt of the Council's recommendations, the relevant Minister must then decide the matter. In this case, the relevant Minister is the Western Australian Minister for Energy, Resources Development, and Education.

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<sup>1</sup> Pipelines can also become covered through other methods.

In reaching its recommendations, the Council is required to consider the criteria for coverage in section 1.9. Where it considers that a pipeline does not meet the criteria, it must recommend revocation of coverage of that pipeline.

Where revocation is granted, the owner/operator of the pipeline is released from its obligations under the WA Gas Pipelines Act and the National Code.

The Council's detailed assessment of the four applications against the criteria in section 1.9 is contained in Part B of this document.

### **The Applications**

The revocation applications relate to four gas transmission pipelines listed in Schedule A of the National Code. These pipelines are laterals running off the Goldfields Gas Transmission Pipeline (GGTP). Further details are listed in Table 1 below.

**TABLE 1 Pipelines Subject to Revocation Applications**

<b>Pipeline Owner</b>	<b>Pipeline Licence</b>	<b>Location/Route</b>	<b>Length (km)</b>	<b>Diameter (mm)</b>
Southern Cross Pipelines Australia Pty Ltd	WA – PL 25	GGTP to Mt Keith Power Station	8.1	219
Southern Cross Pipelines Australia Pty Ltd	WA – PL 26	GGTP to Leinster Power Station	5.2	219
Southern Cross Pipelines Australia Pty Ltd	WA – PL 27	Kalgoorlie to Kambalda	44.3	219
Southern Cross Pipelines (NPL) Australia Pty Ltd	WA – PL 28	GGTP to Kalgoorlie Power Station	8.2	219

The applicant in respect of PLs 25, 26 and 27 is Southern Cross Pipelines Australia Pty Ltd (**SCP**). For pipeline PL 28, the applicant is Southern Cross Pipelines (NPL) Australia Pty Ltd (**NPL**), which acquired PL 28 from the Normandy Group on 1 April 1999.

Goldfields Gas Transmission Pty Ltd operates all four pipelines.

### **Process for Considering Applications**

In determining its recommendations, the Council has followed the process laid down in the National Code. Under this process, the Council:

- acknowledged receipt of the applications, and advised the owners of the pipelines, the operator, the Western Australian Minister for Energy, Resources Development, and Education, the WA Office of Energy, the WA Competition Policy Unit, and the Code Registrar for the National Code;
- advertised receipt of the applications in the West Australian and Australian Financial Review on 6 April, and wrote to over one hundred interested parties calling for submissions;
- released a draft recommendation on 11 May, and called for further submissions; and
- issued final recommendations to the Western Australian Minister for Energy, Resources Development, and Education on 8 June.

The Council has provided copies of its final recommendations to relevant parties, including parties who made submissions.

Under the Code, the Minister must now:

- make a final decision to revoke or not revoke coverage by **29 June**;
- if the Minister decides to revoke coverage, his decision can take effect no earlier than 14 days after it is made; and
- provide copies of his decision and reasons to relevant parties, including the owner/operator and any party who made a submission.

Under section 38 of the *Gas Pipelines Access (Western Australia) Act 1998*, (contained at Schedule 1 of the WA Gas Pipelines Act) any person adversely affected by the Minister's decision (whether it is to revoke or not to revoke coverage) may appeal to the Western Australian Gas Review Board.

## ***Part B – Consideration of the Criteria under Section 1.9 of the National Code***

Under the National Code, the Council must consider whether the relevant pipelines continue to meet the criteria for coverage in section 1.9. The Council must recommend revocation in respect of a pipeline unless it meets all of the criteria.

In considering these criteria, the Council has taken into account the views of the applicants, and of parties that made submissions. A list of the parties that made submissions is at Appendix 2.

The Water Corporation of Western Australia opposed revocation of PL27 (but not PLs 25, 26, or 28), on the basis that access to PL27 would promote the construction of a seawater pipeline and associated gas pipeline between Esperance and the Eastern Goldfields region (the ‘seawater pipeline scheme’). SCP provided a written response to the Water Corporation’s submission, and also discussed the matter with staff of the Council.

The background to the seawater pipeline scheme being promoted by the Water Corporation is outlined under criteria (a). The Water Corporation’s reasons for opposing revocation, and the SCP’s response to these reasons, are discussed under the relevant criteria.

**Criterion (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.**

### **Background**

The rationale for this criterion is that access regulation is only warranted where there are, or will be, tangible benefits (for example, reduced prices or improved quality) which flow through to at least one market beyond the market for the services of the particular gas pipeline.

Before it considers that a pipeline meets this criterion, the Council must be convinced that:

- the service to which access is sought is not in the same market as the market in which competition is promoted; and
- access would actually promote more competitive *outcomes* – such as lower prices – in that other market. Greater competition in another market will be less likely where that other market is already highly competitive, or where the other market is a monopoly (because cost savings are unlikely to be passed on to consumers).

The Council must also consider whether access charges are a sufficiently significant input into the other market to have a material effect on competition. In general, while a trivial increase in competition would not be sufficient, the Council considers access would not need to substantially promote competition in order to satisfy this test.

The Council's approach is to:

- verify that the market in which competition is said to be promoted is separate from the market for the service; and (if so) then
- determine if access (or increased access) would promote competition in this separate market.

### **Views Put to the Council**

SCP and NPL argued access to the four laterals would not promote competition in other markets. They base this view on the fact that the laterals carry gas to single user facilities. In particular:

- PLs 25, 26 and 27 carry gas to Western Mining Corporation (WMC) facilities; and
- PL 28 carries gas to Normandy and AlintaGas facilities (in AlintaGas's case, the Kalgoorlie domestic distribution system).

In relation to PL 28, NPL notes that there is another barrier to competition, even if third party access were to be granted to the lateral. AlintaGas holds an exclusive franchise for the distribution of natural gas in the Kalgoorlie/Boulder area which blocks other parties from distributing gas to customers taking less than 100 TJ per annum until Jan 2002, and to customers taking less than 1 TJ per annum until 30 June 2002.<sup>2</sup>

In summary the applicants argue in relation to each pipeline that:

It is unlikely that third party shippers would wish to access a short and geographically isolated lateral which services specific end user sites. This is because it is unlikely that other end users of natural gas would establish facilities adjacent to the laterals. Therefore, competition is not a relevant issue at local, regional, national or international level.

The Council did not receive any submissions addressing this criterion in relation to PLs 25, 26, and 28.

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<sup>2</sup> section 90, WA Gas Pipelines Act. The franchise effectively blocks access to all but very large industrial customers and mining operations until January 2002, and to residential customers until July 2002.

However, the Council did receive a submission from the Water Corporation of Western Australia contesting the applicant's arguments in relation to PL 27.

The Water Corporation's submission argued that access to PL 27 could promote competition in a number of other markets, including for energy supply, and downstream markets which rely on the supply of gas.

The Water Corporation is promoting a seawater pipeline scheme as part of which a gas pipeline would be built from near Esperance to Kambalda. At Kambalda the gas pipeline would interconnect with PL27, enabling it to carry gas from Kambalda via Norseman to Esperance. The gas pipeline would supply energy to pump seawater in a seawater pipeline from near Esperance to Kalgoorlie and the surrounding region (the Eastern Goldfields region). The bulk of the seawater supplied by the seawater pipeline would be used as process water for mineral processing operations. A proportion would be desalinated at Kalgoorlie and used to supplement the existing potable (drinking) water supplies in the Eastern Goldfields region.

Apart from supplying energy to pump seawater, the pipeline could also supply gas for:

- residential, commercial, and industrial use in Norseman and Esperance; and
- gas-fired electricity generation in Esperance.

The Water Corporation considered that access to PL27 was important to facilitate the seawater pipeline scheme. Without access to PL27, the gas pipeline would (if the seawater pipeline scheme proceeded) need to extend from Esperance to Kalgoorlie.

The Water Corporation argued that access would promote competition in a number of markets, including the markets for energy (both electricity and gas) in Esperance, Norseman, and along the GGT route, and the market occupied by potable and process water in the Eastern Goldfields region.

First, the Water Corporation considered access would significantly reduce the costs of gas along the entire GGT route. This would occur because increased flows of gas down the GGT and via the Kambalda to Esperance pipeline (estimated at 10 TJ per day) would considerably increase the volume of gas on which gas transportation costs were recovered. Gas charges fall significantly as volumes increase because costs of transporting gas rise only gradually for large increases in volumes of gas transported.

The lower cost of gas supplied through the GGT would, in the Water Corporation's view, promote the ability of gas "to compete with other fuels – such as diesel fuel and LPG – for a variety of uses within the region".

Second, gas from the interconnected system could supply gas to private gas-fired electricity generators in the Eastern Goldfields region, providing competition in electricity supply in the region with the existing electricity suppliers. Currently Norseman and Esperance rely on diesel-generated electricity for their energy requirements.



Third, the Water Corporation argued that supply of water through the Esperance to Kalgoorlie seawater pipeline would promote competition in the supply of process water used in mining operations in the Eastern Goldfields region. Currently, the Eastern Goldfields region is supplied with water by a pipeline running from Mundaring Weir near Perth (owned by the Water Corporation), and aquifers in the Eastern Goldfields region.

The Water Corporation argued the seawater pipeline from Esperance to Kalgoorlie would introduce a new competitor in the supply of water to the Eastern Goldfields region because the new seawater pipeline would be owned (in whole or part) by the mining companies that draw water from it.

SCP responded to the Water Corporation's submission by arguing that competition may not be promoted because the seawater pipeline scheme may not proceed. It argued that the scheme had yet to be proven to be commercially viable. It also noted that the Water Corporation is only acting as advocate for the project, and would not be the eventual developer of the project.

### **Analysis**

The Council considers access to PL 27 is likely to promote competition, particularly in the market for process water, and in the market for energy in the Eastern Goldfields, Norseman, and Esperance.

Access to PL 27 will facilitate the construction of an interconnected gas pipeline between Kambalda and Esperance which will in turn have the following effects:

- it could be expected to provide head-to-head competition with diesel-generated electricity used in Esperance and Norseman; and
- it could be expected to promote competition between desalinated seawater from Esperance and water from aquifers as a source of process water used in mining.

First, the availability of gas in Norseman and Esperance could be expected to boost gas as a source of electricity generation compared with current forms of electricity generation. At present, electricity in Esperance and Norseman is diesel-generated.

Second, the Kambalda to Esperance pipeline could assist in competition in the process water market. It would provide mining companies and domestic and industrial users in the region with greater choice as to the source of supply.

The Council considers these markets to be separate from the services provided by the gas pipeline. In reaching this view, the Council has been guided by a test developed by Professor Henry Ergas.<sup>3</sup> In essence, the Ergas test points to a separate market if:

- the supply of a gas pipeline service is separable, from an economic point of view, from the other service (for example, an energy service or the supply of process water). This involves an assessment as to whether the transaction costs in separate provision at the two layers would not be so great as to prevent such separate provision from being feasible; and
- the assets used to provide the gas pipeline service are sufficiently specialised that supply side substitution is not achievable so readily as to unify the field of rivalry between the two layers.

In applying these tests, the Council finds that the market for gas pipeline services is clearly separate from the markets occupied by energy and process water. While the Council has not precisely delineated the boundaries of the markets occupied by energy and process water, it is satisfied that, however defined, these markets are separate from the market occupied by gas pipeline services.

The Council considers gas from the Kambalda to Esperance pipeline could compete effectively with diesel as a source of electricity generation. There are few other sources of energy in this region. Diesel generation is a relatively expensive method of generating electricity. Thus, even in a broadly defined energy market, the Council is satisfied that a new source of gas supply would promote competition.

The Council also considers water from the seawater pipeline could compete effectively with aquifer water and water from the Mundaring Weir in the supply of process water for mining operations. Again, even in a broadly defined water market, the Council is satisfied that a new source of water would promote competition.

The Council does not accept SCP's argument that competition is unlikely to eventuate because the seawater pipeline scheme is 'problematic' or unlikely to proceed. Based on the information supplied, the Council considers it is sufficiently likely the project will proceed that, on balance, the Council is satisfied that access would promote competition in another market.

The Council concludes that PL 27 meets criterion (a).

As stated above, the Council did not receive any submissions arguing PLs 25, 26, or 28 meet this criterion.

There are a number of possible markets in which competition might be affected by access to PLs 25, 26, and 28, for example for the output of mining operations. Determining these markets depends on the use to which access-seekers might put gas

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<sup>3</sup> Ergas, H, submission to the NCC in support of an application by Carpentaria Transport Pty Ltd, pp. 1-3.

if they are able to obtain it under the WA gas access regime from the relevant pipelines.

Having said that, it is clear that the primary market in which access could promote competition is in relation to energy supply. This is because, in a direct sense, access could only facilitate greater competition in other markets through the use of gas within the energy markets. In other words, access to the laterals could only promote competition in other markets, such as for the output of mining operations, to the extent that those mining operations benefited from the source of energy provided by gas transported in the laterals. Therefore, the Council has focussed its assessment on whether access to these laterals is likely to promote competition in the energy market or markets.

It is unlikely that other mining operations would wish to interconnect with PL 25 or PL 26. This is because these laterals are geographically remote and relatively short (8.1 and 5.2 kilometres respectively). As a consequence, there would be few nearby sites where it would be more cost-advantageous to interconnect with PL 25 or 26 than with the GGT.

While PL 28 is located closer to centres of population and end-user demand, it remains unknown whether third parties would be interested in seeking access.

The Council considers that in relation to PLs 25, 26, and 28, competition can only be promoted if there is a reasonable likelihood that someone will seek access. In contrast to PL 27, no-one has to date indicated a desire to seek access. On present information, therefore, it appears unlikely that parties will seek access to PLs 25, 26, and 28 in the foreseeable future. Having said that, the Council recognises it may need to re-examine this issue if some party does seek access in the future. In that event, it would be possible for the party to seek re-coverage of the relevant pipeline under the mechanisms provided in the National Code.

In summary, the Council lacks evidence to establish that access to PL 25, 26, or 28 would promote competition in another market. It cannot be satisfied, therefore, that these pipelines meet criterion (a).

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

### **Background**

The rationale for the WA Gas Pipelines Act and the National Code is that access regulation should be limited to infrastructure where it is not economically viable to build competing facilities. As such, access regulation should normally be confined to infrastructure with monopoly power, and usually to infrastructure exhibiting *natural monopoly* characteristics – that is, where a single facility can meet market demand at less cost than two or more facilities. Such a facility is normally characterised by large

up-front investment costs and low operating costs, resulting in economies of scale across a broad range of output – that is, as output increases, average costs per unit of output continue to decrease across the range of output sought.

The Council has interpreted this criterion consistent with its previous interpretations of section 44(G)(2) of the *Trade Practices Act 1974* (Commonwealth). The Council notes that section 44G(2) contains slightly different wording in that it provides for declaration of facilities where “it would be uneconomical for anyone to develop another facility to provide the service”. However, the Council considers the words in this criterion are consistent with the Council’s interpretation of the words in section 44G(2), particularly since the Gas Reform Implementation Group (in formulating the coverage criteria under section 1.9 of the National Code) indicated that they intended to replicate the words of section 44G.<sup>4</sup>

In examining whether it is economic to develop another facility, the Council applies a *social* test rather than a *private* test of the costs and benefits of developing another facility. The social test looks at whether all of the benefits associated with the development of another pipeline outweigh all of the costs, for example, whether it would be better for an industry to share infrastructure because new investment would substantially raise industry costs and therefore affect the prices paid by consumers or Australia’s competitiveness overseas. Where construction of a new facility might proceed in the absence of access, but would be socially wasteful because existing facilities can fully and more efficiently meet demand, the social test indicates that the development of another facility is uneconomic.

Some of the factors relevant to a consideration of whether it is uneconomic to develop another pipeline are:

- whether there is large excess capacity in existing pipelines;
- whether current and projected levels of demand are most cheaply supplied by one party;
- whether marginal and average costs of production per unit continue to decline for all likely levels of demand;
- whether the costs of developing another pipeline to provide the transportation capacity sought by the third party outweigh the costs of expanding capacity of the existing pipeline to meet the third parties’ needs while ensuring the owner/operator and existing users do not lose amenity;
- the number of pipelines currently supplying the market for transport of gas between the regions sought by third parties;

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<sup>4</sup> See GRIG Policy Paper on the National Gas Access regime, p. 7, quoted in *National Gas Access Regime: Recommendation to the Gas Reform Implementation Group on the National Third Party Access Regime for Natural Gas Pipeline Systems*, (National Competition Council) at p. 13.

- the height of barriers to entry (large upfront costs of developing another pipeline, particularly costs that cannot be recovered if the new investment were to be abandoned).

Gas pipelines are typically characterised by high construction costs and low operating costs such that the marginal cost of transporting a unit of gas is very low. Moreover, up to the point of fully expanded capacity, average costs of transportation of a unit of gas decline. This means that gas pipelines exhibit natural monopoly characteristics. In lay person's language, this means it is almost always cheaper to send gas through existing pipelines (if spare capacity exists or can be added) than it is to build another pipeline to carry the gas.

Moreover, investment in new pipelines is, in economic language, 'sunk'. That is, the investment is fixed or committed, and if the investment is a failure, little or none of it can be retrieved. In the case of gas pipelines, it is clear that investment in laying of new pipelines is almost totally sunk. This means that incremental or gradual entry – a common form of entry in other industries – is not feasible in the gas transportation industry.

Finally, the costs of laying a new pipeline rise slowly compared with increases in the capacity of that pipeline. In other words, it is much less expensive - per unit of capacity - to lay a large capacity pipeline than a small capacity pipeline.

In general, therefore, it is not economic to develop another pipeline where an existing pipeline has existing spare capacity (or can develop it through greater compression and/or looping), although it will always be necessary to consider the facts of particular pipelines.

### **Views Put to the Council**

The applications argue that it is *not* uneconomic to construct other pipelines which provide the same services as PLs 25, 26, 27 and 28:

... the short length and comparatively small size of the lateral(s) means that cost would be unlikely to constitute an impediment to the construction of other laterals in the unlikely event that such an option were to be considered by other parties.

The Water Corporation of Western Australia, on the other hand, considered that it *was* uneconomic to develop another lateral from Kalgoorlie to Kambalda (the path travelled by PL 27).

The Council did not receive any submissions addressing whether it would be uneconomic to develop another pipeline to provide the services provided by PLs 25, 26, or 28.

In relation to PL 27, both the Water Corporation submission and the SCP response raised the issue of whether it was likely to be more attractive to build a new pipeline alongside PL27 or obtain access to PL27. The Water Corporation considered that

PL27 had “more than adequate capacity to carry the long-term requirements of the SeaWater Pipeline Scheme in addition to WMC’s requirements at Kambalda”. However, SCP considered that to carry the requirements of the gas pipeline from Kambalda to Esperance would require significant new investment in adding capacity to PL27. On this basis, SCP considered that “[g]iven the scale of new regional developments alluded to by the Water Corporation, a new, larger diameter pipeline could represent a competitive and more effective long term alternative compared to piecemeal expansion of the Kambalda lateral”.

### **Analysis**

The Council takes a different view to the applicants of the meaning of the test of whether it is uneconomic to develop another pipeline. In its view, if existing pipelines can fully meet demand, then, from a social viewpoint, it would be wasteful for new pipelines to be built simply because the owners of existing pipelines refuse to provide access.

The Council notes the short length of these pipelines, in particular PLs 25, 26, and 28. However, this is not the determining factor of whether the pipelines exhibit natural monopoly characteristics.

The Council considers that PLs 25, 26, 27, and 28 exhibit characteristics of natural monopoly within the geographic regions served by them. They have considerable excess capacity to meet demand, and construction of other pipelines along the same routes would be socially wasteful in the sense that demand could be more cheaply met by the existing pipelines.

The Council notes SCP’s argument that seeking access to PL27 would require significant investment, and that it may be more effective to build a new pipeline to meet the requirements of the seawater pipeline scheme.

The Council does not accept this argument.

The Council is satisfied, in terms of social costs and benefits, that construction of a new pipeline would not be a more efficient way to meet the gas requirements of the seawater pipeline scheme. Typically looping or expansion of capacity through additional compressor stations is a cheaper way of providing additional capacity to the construction of a new pipeline.<sup>5</sup>

The Council concludes that PLs 25, 26, 27, and 28 meet criterion (b).

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<sup>5</sup> At some point, extra looping or compression is not possible and a new pipeline becomes the only alternative. Neither SCP or the Water Corporation suggested that the additional requirements associated with the seawater pipeline scheme would lead to this outcome in respect of PL27.

**Criterion (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.**

### **Background**

The rationale for this criterion is that the National Code should not be applied to pipelines where this may pose a legitimate risk to human health or safety.

### **Views Put to the Council**

The applications did not address this criterion.

The Water Corporation submitted that access to PL 27 would not pose undue health and safety risks and pointed out:

- the GGT pipeline system to Kalgoorlie is already operating as an open access pipeline, ... providing services to a number of shippers;
- WA-PL27 and the GGT pipeline are operated by the same management group, staffed by AGL personnel; and AGL has extensive experience in the operation of open access gas pipelines throughout Australia

SCP did not contest the Water Corporation's submission in its response.

### **Analysis**

Typically, third party access to gas pipelines does not pose undue risks to human health and safety where appropriate measures are taken by the operator. Third party access to gas pipelines has been permitted in relation to many pipelines in Australia without being considered to unduly compromise health and safety.

For these reasons, the Council considers that access to PL 27 would not pose undue risks to human health and safety.

The Council considers these reasons also apply in the case of PLs 25, 26, and 28.

The Council concludes that the relevant pipelines meet criterion (c).

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

### **Background**

In revocation matters, the Council will consider whether access to a pipeline is contrary to the public interest. This assessment will examine, among other matters, whether any benefits of access, such as cheaper prices and more efficient use of resources are outweighed by regulatory or compliance costs. The Council will also take into account factors such as the environment, regional development, and equity.

### **Views Put to the Council**

The applicants argue that regulating access to PLs 25, 26, 27 and 28 poses unnecessary regulatory costs on the owners/operators of the pipelines and on the regulator. If revocation is not granted, then the owners/operators will be required under the Code to prepare an access arrangement setting out the terms and conditions and prices on which access will be offered. In the view of the applicants:

Preparation of an Access Arrangement and Access Arrangement Information constitutes an unnecessary burden on the lateral owner, the Regulator, and the State.

The Water Corporation of Western Australia argued in respect of PL 27 and the GGT that:

the two pipelines are ... operated and managed by the same entity – as if it was a single system; and the same open access regime can be applied to the Kalgoorlie-Kambalda Gas Pipeline as to the GGT.

and the Australian Competition and Consumer Commission argued:

It would appear to be hard to justify requiring each owner to submit a separate access arrangement for each lateral, as the regulatory compliance costs would be likely to exceed the expected benefits.

However, taken collectively, the short laterals off the Goldfields pipeline are an integral component of the pipeline system. The fact that the laterals are operated by the operator of the Goldfields pipeline supports this.

The Code provides for an operator to submit an access arrangement for pipelines it doesn't own, for circumstances just such as this. Even though the laterals are not owned by the owner of the Goldfields pipeline, they are operated as part of an integrated transmission system. ...

The regulatory compliance cost in having the operator of the Goldfields pipeline submit an Access Arrangement that included proposed reference tariffs for the laterals should not be significantly more than one without the laterals.



In their written response to the Water Corporation submission and in a meeting with staff of the Council, SCP raised a number of further points in support of their application for revocation:

- requiring SCP to submit an access arrangement in respect of PL27 would impose excessive regulatory costs. Due to the separation in ownership between the GGT pipeline and PL27 and other reasons, SCP would not be able to rely on the access arrangement in respect of the GGT pipeline and would need to develop a special access arrangement in respect of PL27;
- it is not known if the seawater pipeline scheme being promoted by the water Corporation is commercially viable, and therefore the “need for regulated access [to PL27] is not pressing”;
- the seawater pipeline scheme would require major enhancements to the capacity of PL27, including additional metering equipment and possible compression facilities;<sup>6</sup>
- negotiated access would be preferable to regulated access;
- if the owners/operators of PL27 were required to submit an access arrangement, it would be difficult to prepare one to anticipate the possible types of services sought by access-seekers under the seawater pipeline scheme;
- it is in SCP’s own interests to encourage third party access, so regulated access is unnecessary;
- it would be more practical to permit revocation and consider re-coverage through the tests in section 1.9 of the National Code at the point in time when a third party was interested in seeking access. It was understood that a request for access in respect of the seawater pipeline scheme was some way off; and
- in the event of revocation, it is possible for third parties to seek access to the laterals under the *Goldfields Gas Pipeline Agreement Act 1994*, which makes provision for third party access to the GGT pipeline.

### **Analysis**

In determining where the public interest lies the Council has sought to quantify the respective costs and benefits of coverage.

The applicant has indicated that the major cost of coverage is the regulatory cost associated with preparing an access arrangement. The major benefit is the opportunity afforded to access-seekers to obtain information relating to access and to

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<sup>6</sup> Compression facilities compress gas as it is transported in a pipeline, thereby increasing the amount of gas that can flow down the pipeline.

negotiate with the owner/operator of the covered pipeline for access at a fair and reasonable price.

The Council considers that, in respect of PLs 25, 26, and 28, there is little evidence at this time that third parties are interested in seeking access. For this reason, it is likely that the regulatory costs entailed in submitting access arrangements for these laterals outweigh the benefits. The Council concludes that continued coverage of these laterals is not in the public interest.

However, in respect of PL27, there is the possibility that third parties will seek access to the lateral as part of the seawater pipeline scheme. Therefore it is appropriate to consider more fully the possible benefits and costs of continued coverage.

As stated above, the major benefit of continued coverage of PL27 is to provide third parties with a mechanism to negotiate access to PL27 at a fair and reasonable price either by adopting the reference tariff approved by the regulator or through commercial negotiations backed by the discipline of independent arbitration under the WA Gas Pipelines Act. This right ensures that interested parties are not required to pay monopoly prices when seeking access to PL27.

SCP submits that the seawater pipeline scheme promoted by the Water Corporation may not be commercially viable, and therefore access may not in the end be sought to PL27.

As it stated in its reasoning in relation to criterion (a), the Council is not in a position to predict with certainty whether the seawater pipeline scheme will eventuate. However, the Council considers that the scheme is sufficiently likely to eventuate that continued coverage of PL27 provides significant benefits.

The Council notes that the operator in respect of the GGT pipeline and PL27 is GGT Pty Ltd.

The ACCC suggests that GGT Pty Ltd would be likely to submit a single access arrangement in respect of the GGT pipeline and each of the laterals. This would to some extent streamline regulatory processes and save regulatory costs.

However, because of the different ownership of PL27 and the GGT pipeline, and the different characteristics of PL 27 compared to the GGT pipeline, it is possible GGT Pty Ltd may prefer to submit a separate access arrangement in respect of PL27. Even where a joint access arrangement is submitted, the Council accepts that there would be some additional regulatory costs resulting from the different ownership and other characteristics of the GGT pipeline compared to PL27.

On balance, the Council considers that the regulatory costs of access are not so significant that they outweigh the benefits of access. In particular, the Council considers that the owner/operator has a number of avenues to reduce its regulatory costs, such as attempting to put in place a joint access arrangement covering PL27 and the GGT pipeline, or using some of the same information as for the access arrangement in respect of the GGT pipeline where possible, such as adopting similar

terms and conditions to the terms and conditions developed for access to the GGT pipeline.

Many of the other arguments raised by SCP are less relevant to the consideration of the public interest. In particular:

- while the Council accepts that access to PL27 may require significant new investment (e.g. metering, additional compression stations), the National Code provides for this. It ensures that additional costs are reflected in costs of access;<sup>7</sup>
- the argument that SCP has incentives to encourage access overlooks the purpose of access regulation, which is to ensure that third parties can negotiate access without having to pay a monopoly price. While SCP would have incentives to encourage access even if PL27 was not covered, it may be able to charge monopoly tariffs for such access;
- while negotiated access may be preferable to regulated access under the WA Gas Pipelines Act and the National Code, the WA Gas Pipelines Act and the National Code make provision for negotiated access. They are designed as a backstop in case negotiations for access fail;
- granting revocation and permitting re-coverage at a future time would involve significant delay and regulatory cost. It may also deprive interested third parties of information on which to decide whether to pursue access;
- while the *Goldfields Gas Pipeline Agreement Act 1994* makes provision for access to the GGT, it is unclear that it makes provision for access to laterals such as PL27. In any case, the WA Gas Pipelines Act will supplant the access provisions of the *Goldfields Gas Pipeline Agreement Act 1994* on 1 January 2000.<sup>8</sup>

In summary, the Council considers that, in respect of PL 27, where there is a real prospect that a third party will seek access, the benefits of coverage outweigh the regulatory compliance costs.

The Council concludes that PL 27 meets criterion (d).

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<sup>7</sup> Sections 3.16, 8.16, 8.25, and 8.26 of the National Code.

<sup>8</sup> Section 97, WA Gas Pipelines Act.

***Appendix 1: Criteria for Coverage in Section 1.9 of National Code***

The Council must recommend revocation of coverage of a pipeline – either to the extent sought, or to a greater or lesser extent than sought in the application<sup>9</sup> – if the pipeline does *not* satisfy one or more of the criteria for coverage in section 1.9 of the National Code.

The criteria in section 1.9 are:

- 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;
- that it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the pipeline;
- 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
- that 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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<sup>9</sup> Taking account of any part of the pipeline that is necessary to provide services that potential users may seek access to (section 1.29).

***Appendix 2: Submissions received by Council***

The Council received submissions from the following organisations:

*Australian Competition and Consumer Commission*

*Normandy Power Pty Ltd*

*Southern Cross Pipelines Australia Pty Ltd*

*Water Corporation of Western Australia (two submissions)*