



Reference service and rebateable service definitions

Final rule determination 1 November 2012

The Australian Energy Market Commission has made a rule that better equips the Australian Energy Regulator (AER) to determine efficient prices for natural gas pipeline services. It gives the AER increased discretion in deciding which haulage services should attract reference tariffs. A new definition of reference service provides more flexibility in the National Gas Rules for the AER to respond to industry circumstances in its regulation of pipeline services.

Background

Gas pipelines that are fully regulated under the National Gas Law (NGL) are required to have arrangements that set out prices, and terms and conditions for access to these pipelines. Access arrangements are approved by the economic regulator and are in place for a set period (usually five years).

Access arrangements must specify the pipeline services offered by the service provider (the owner and/or operator of the pipeline) that are sought, or likely to be sought, by a significant part of the market. These services are known as reference services and are usually the main forward haulage services provided on the pipeline. In approving an access arrangement, the regulator determines the price (reference tariff) for these services. The reference tariff is set at a level that returns to the service provider at least the efficient cost of providing the reference service.

The service provider is not obliged to charge users the reference tariff but it can be used as a benchmark by an arbitrator if there is a dispute over access to the pipeline.

Other pipeline services may be included in an access arrangement. These services are considered as minor services (such as backhaul and interruptible) where demand and/or revenue generated from these services are uncertain. Because of difficulties in forecasting revenues and demand for these services, tariffs for them cannot be readily determined by the regulator. Therefore any revenue generated from these services can be rebated back to users of the reference service by a reduction in the reference tariff. Such a service is known as a rebateable service.

The AER's rule change request

On 5 August 2011 the Australian Energy Regulator (AER) submitted a rule change request to amend the definitions of reference service and rebateable service. The rule change request sought to allow more flexibility in the regulatory treatment of pipeline services in the NGR in order to better ensure that prices for regulated services are efficient and cost reflective.

The Commission has made a more preferable rule

The Commission has decided to make a final rule which is a more preferable rule to the AER's proposed rule. The final rule differs from the proposed rule in that it makes changes only to the reference service definition. It provides the regulator some discretion (limited by the revenue and pricing principles) in considering the appropriate regulatory treatment of pipeline services that are likely to be sought by a significant part of the market.

The final rule does not amend the rebateable service definition.

The final rule applies to all gas pipelines subject to economic regulation by the AER and the Economic Regulatory Authority (ERA) of Western Australia.

The new reference service definition will provide greater flexibility for regulators in determining the appropriate regulatory treatment of pipeline services.

Reasons for the Commission's decision

The Commission considered that the final rule will better promote:

- *the efficient use of and investment in pipeline services;*
When significant uncertainty exists as to the revenue and demand for a pipeline service the final rule reduces the likelihood that inefficient tariffs are set for that service.
- *the long term interests of consumers with respect to price and security of gas supply.*
As a result of the final rule, the regulator will not be required to set a tariff for a pipeline service which in certain circumstances may not be reflective of efficient costs.

This is because the final rule provides increased discretion to the regulator to enable it to accommodate the particular circumstances of a pipeline and the services it offers.

The final rule will allow the regulator to recognise that in some circumstances market mechanisms, rather than setting a reference tariff, may be better at determining the price for, and allocation of, a pipeline service that is likely to be sought by a significant part of the market.

As a result, the final rule will not increase investment risk on regulated pipelines. Instead, it may aid investment by providing service providers with relevant and appropriate pricing signals.

Conversely, the Commission considered that the proposed amendment to the rebateable service definition may lead to an increase in investment risk which could result in inefficient investment in pipeline services and may not be in the long term interests of consumers. For this reason, the proposed rebateable services definition has not been made.

For information contact:

AEMC Chief Executive, **Steven Graham** (02) 8296 7800

Media: Communication Manager, Prudence Anderson 0404 821 935 or (02) 8296 7817

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