



6 June 2013

Ms Natalie Naylor
Legal Counsel
Wagga Wagga revocation
National Competition Council
Level 21, 200 Queen St
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Submitted by email: gas@ncc.gov.au

Dear Ms Naylor

APPLICATION FOR REVOCATION OF COVERAGE OF THE WAGGA WAGGA NATURAL GAS DISTRIBUTION NETWORK - Response to NCC request for additional information

Further to the submission provided by Origin Energy (Origin) on 28 May 2013, and following the telephone conference between Origin and the National Competition Council (NCC) on 30 May 2013, Origin provides the following supplementary submission that addresses the issue of light regulation in relation to the Wagga Wagga natural gas distribution network (Wagga network).

In summary, Origin does not consider light regulation is the most appropriate form of regulation for gas distribution networks, like Wagga. We consider full coverage for this distribution network is the most effective means of promoting competition in the related markets, particularly given a distributor is a monopolist supplier with customers having limited access to alternative services. The consequence of a distributor's market position and the associated likelihood of disputes mean the costs associated with light regulation could be comparable to those of full coverage. If the cost of dispute was too high, that leaves network users with little alternative than to accept onerous terms and conditions to secure access. In either case, light regulation would be a less efficient regulatory option than full coverage.

Less upfront costs but scope for significant dispute costs

Light regulation is considered to be appropriate where the market power exercised by the provider is less substantial and there is the potential for contestability in services to emerge.¹ This is to say, light regulation is appropriate in circumstances where the supplier of pipeline services is unlikely to seek to impose onerous terms and conditions of access because network users and prospective users can access substitute services. We do not consider this to reflect the environment of distribution networks, like the Wagga network.

By definition, a light handed regulation regime imposes fewer requirements up front for the network owner. Under full coverage, the network owner must submit a full access arrangement containing terms and conditions of access, including tariffs; it need not do so under a light regulation regime. With respect to the Wagga network, Envestra would

¹ NCC, Light regulation of covered pipeline services, July 2011, paragraph 2.9, available at http://www.ncc.gov.au/images/uploads/Gas_Guide_Part_C_July_2011.pdf

not have a regulatory requirement to submit detailed financial and operational information in relation to the Wagga network in the absence of full coverage.

This means existing or prospective users of the network have less information up front to assess the appropriateness of the terms and conditions for network access. Light regulation also requires users to negotiate away from the distribution network's starting point. This creates an imbalance of negotiating power, with each party needing to make an individual decision on the merits and cost of dispute. Section 181 of the National Gas Law (NGL) enables users and prospective users of a network under light regulation to notify the AER of an access dispute about any aspect of access. However, it is conceivable that the cost of the disputes required to deliver an access arrangement equivalent to that available under full regulation could be around the cost of full regulation itself.

A less efficient and less effective form of regulation for the Wagga network

As outlined in our previous submission, Origin considers that a monopolist supplier of distribution services may function to stymie the development of competition in the retail gas market. Origin provided examples under other regulated access arrangements where the AER decided against terms and conditions initially proposed by the distributor that could be considered onerous and one-sided. This history makes it difficult to be confident in any starting point for access terms and conditions proposed by a monopolist service provider. This is likely to have an impact on the effectiveness of competition in the retail gas market.

That light regulation would be less well suited to the Wagga network is illustrated by considering the guidance provided by the NCC in relation to the form of regulation factors set out in section 16 of the NGL.² In fact, the NCC's Guide explicitly states that light regulation is less likely for '*Distribution pipelines (especially established distribution pipelines with a high market penetration)*'.³

In the event that an application was made for light regulation of the Wagga network, the NCC would be required to have regard to the costs associated with light regulation. Given there has historically been robust discussion and review of distributor network terms and conditions in the Access Arrangement process, it is likely that network users would have difficulty reaching commercial agreement. Disputes are likely. It would only take a handful of such disputes to occur within a regulatory period for the costs of light regulation to reach those of full coverage. It is therefore quite possible that costs associated with light regulation would not be significantly lower than full coverage. (In its application, we note that Envestra stated that the costs of light regulation are less certain and could potentially lie within a large range from 'somewhere between \$0.25 million up to and including the cost of full regulation'.⁴)

However, it is also possible that the expense associated with raising disputes could mean retailers may need to accept more onerous terms and conditions. As noted by Origin in its previous submission, to the extent that onerous terms and conditions function to transfer risk to parties that are less well placed to manage it, they result in market inefficiency

² NCC, Light regulation of covered pipeline services, July 2011, pp 51-53, available at http://www.ncc.gov.au/images/uploads/Gas_Guide_Part_C_July_2011.pdf

³ NCC, Application for a light regulation determination in respect of the covered portion of the Moomba to Sydney natural gas pipeline system, Final Decision and Statement of Reasons, 19 November 2008, Table 3.1, p.22

⁴ Envestra Ltd, Wagga Wagga Network Revocation Submission, Public version, 1 May 2003, paragraph 120, available at <http://www.ncc.gov.au/images/uploads/ReGaWWAp-001.pdf>

and higher prices for end users. It is therefore likely that, even if light regulation imposes less overall direct regulatory expense than full coverage, it will be significantly less effective.

Conclusion

Light regulation is best suited to circumstances where there is less likely to be significant commercial dispute between the supplier of pipeline services and network users. Given most distribution access arrangement processes focus significant time and effort on assessing and reviewing terms and conditions of access, we consider a commercial process is unlikely to deliver the best outcome to end use consumers. In the absence of effective commercial negotiation, light regulation of distribution networks more generally are likely to be inefficient and costly when compared with current arrangements. As such, Origin does not consider light regulation is the most appropriate form of regulation for gas distribution networks, like Wagga.

Should you have any questions or would like to discuss this submission further, please contact Hannah Heath (Manager, Wholesale Regulatory Policy) on (02) 9503 5500 or hannah.heath@originenergy.com.au.

Yours sincerely,



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