

**Wagga Wagga Network Revocation  
Response to National Competition Council  
Draft Recommendation**

Public Version

Envestra Ltd

15 July 2013



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## 1. Introduction

1. On 1 May 2013 Envestra submitted to the National Competition Council (NCC) an application to revoke coverage of the Wagga Wagga Gas Distribution Network (WWGDN). Envestra's application assessed the WWGDN against the four pipeline coverage criteria set out in section 15 of the National Gas Law (NGL) and concluded continued coverage of the WWGDN is not warranted as two of the criteria are not satisfied. The two criteria that are not satisfied are that:
  - access (or increased access) to the services provided by the pipeline would promote a material increase in competition in at least one other market (criterion (a)); and
  - access (or increased access) to the services provided by the pipeline would not be contrary to the public interest (criterion (d)).
2. On 17 June 2013 the NCC issued its draft recommendation that all four coverage criteria are satisfied and therefore coverage of the WWGDN should remain. The NCC found that coverage would promote a material increase in the dependent downstream market for gas sales in the area served by the WWGDN, and as such, criterion (a) is satisfied. As well as other factors, the NCC had regard to the following arguments when reaching its draft recommendation that criterion (a) is satisfied:
  - the removal of network coverage at this time may affect the scope for the removal of retail price regulation of gas sales in NSW, which would in-turn lead to greater retail gas competition in Wagga Wagga;
  - Envestra's market power is not constrained by the ability for consumers to switch from gas to electric appliances; and
  - Envestra may apply non-price access terms to transfer risk to retailers, which would further affect the prospects for competition in the gas sales market.
3. The NCC also found that the costs of full regulation of the WWGDN are unlikely to exceed the benefits of continued coverage, and as such, criterion (d) is satisfied.
4. The NCC noted in its draft recommendation that its decision was based on "the information available at this stage". This submission provides the additional information that addresses the issues raised by the NCC in its draft recommendation. Envestra contends that the available information does support the revocation of coverage of the WWGDN and not continued coverage as recommended by the NCC.
5. Section 2 of this report focuses on criterion (a) and explains why the available information shows that continued coverage will not promote a material increase in the downstream dependent market of gas sales in the area served by the WWGDN. This is for a range of reasons, including that:
  - the coverage status of a network has no bearing on the scope for the removal of retail gas price regulation or on retail gas competition more generally; and
  - any market power Envestra may possess is significantly constrained by the ability for consumers to readily (and at a low cost) switch from gas to electric appliances.
6. Envestra notes that its conclusion that criterion (a) is not satisfied is consistent with the independent expert views of Acil Allen Consulting, which advice has been provided with this submission.

7. Section 3 focuses on criterion (d), which demonstrates that the costs of regulation, which Envestra has estimated at \$2.8 million for each five year period, exceed the benefits of coverage, which Envestra estimates do not exist for the reasons set out in assessing criterion (d).
8. Envestra therefore submits that neither criterion (a) nor criterion (b) are satisfied, and as such, continued coverage of the WWGDN is not warranted. That is, continued coverage will not promote a material increase in competition in the market for gas sales in the area served by the WWGDN nor is coverage in the public interest.

## 2. Coverage Criterion (a): Promoting a material increase in competition in a dependent market

9. Criterion (a) is satisfied where access (or increased access) to the services provided by a pipeline would promote a material increase in competition in at least one other market if that pipeline were to be covered. The NCC agreed with Envestra's definition of the relevant downstream market as the market for gas sales in the Wagga Wagga and Uranquinty area and that this was the most relevant/appropriate market against which to assess whether criterion (a) was satisfied.
10. The NCC however made a draft recommendation that criterion (a) is satisfied in respect of the market for gas sales in the area serviced by the Wagga Wagga Gas Distribution Network (WWGDN).<sup>1</sup> In forming this view, the NCC had consideration to Envestra's application along with four submissions received to that application. The submissions were from the three major retailers in Australia and from the Energy Retailers Association of Australia (ERAA).
11. The key arguments relied upon by the NCC for finding that criterion (a) is satisfied was that a covered WWGDN is more likely to better promote competition in the market for gas sales than an uncovered WWGDN. More specifically, the NCC found in its draft recommendation that:
  - the removal of coverage at this time *might* affect the scope for the removal of price regulation of gas sales in NSW, and if this were to happen, the scope for additional competition in the area served by the WWGDN and more widely would be significantly reduced;<sup>2</sup>
  - the costs and risks of competing in the gas sales market in the area served by the WWGDN, especially for smaller second tier retailers, are *likely* to be lower if the conditions for access are known in advance;<sup>3</sup>
  - related to the above is a concern of the NCC that non-price access terms, and other measures to transfer risk between Envestra and other parties, *may* adversely affect the prospects for competition in the gas sales market;<sup>4</sup>
  - that gas and electricity are not sufficiently substitutable to constrain the use of market power as the costs of switching from gas to electric appliances are *likely* to be substantial;<sup>5</sup>
  - that while retailers can be expected to have some countervailing market power, the application of such power *may* be an inadequate response to constrain the use of market power given that, under current regulatory arrangements, distribution costs can be passed through to customers;<sup>6</sup> and
  - any initiatives to standardise transactional interfaces between Envestra and retailers are more likely to flourish within a regulatory environment than where a pipeline is uncovered.<sup>7</sup>

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<sup>1</sup> NCC Wagga Wagga Gas Distribution Network – Draft Recommendation (17 June 2013) paragraph 4.49

<sup>2</sup> Ibid. paragraphs 4.27, 4.28, 4.45 and 4.46

<sup>3</sup> Ibid. paragraphs 4.43

<sup>4</sup> Ibid. paragraphs 4.32

<sup>5</sup> Ibid. paragraphs 4.39 and 4.40

<sup>6</sup> Ibid. paragraph 4.42

<sup>7</sup> Ibid. paragraph 4.47

12. The NCC noted in its draft recommendation that its preliminary views were based on "the information available at this stage." This submission provides additional information, including factual evidence, that is relevant to test the above matters relied upon by the NCC in its draft recommendation to find that criterion (a) is satisfied. This additional information includes the following two independent expert reports:
- Acil Allen Consulting: "Revocation of Coverage, Wagga Wagga Gas Distribution Network – which report is focussed on an assessment of the arguments made by the NCC in relation to criterion (a); and
  - Core Energy Group: Competitive Assessment of Natural Gas – which report is focussed on an assessment of the competitiveness of natural gas and electricity in the area served by the WWGDN and the likely consumer behaviour given forecast changes in prices for both sectors.
13. Envestra's response to the views of the NCC as it applies to a consideration of whether criterion (a) is satisfied is to be read alongside the views set out in the above two independent expert reports. Envestra will however endeavour to refer to the views of the experts throughout this submission where relevant.

## 2.1. Relationship between network coverage and retail price (de)regulation

14. The NCC in its draft recommendation has created a link between the potential for retail price regulation to be removed with its decision in regard to the revocation of coverage of WWGDN. Specifically, the NCC has suggested, at this point in time, that revocation of coverage might affect the scope for the removal of retail price regulation, which would in turn significantly reduce competition in the downstream market for gas sales:

In addition to the issues canvassed in the application and submissions the Council is concerned that revocation of coverage at this time might affect the scope for removal of retail price regulation of gas sales in NSW.<sup>8</sup>

And:

The Council is aware that the AEMC is to report to the NSW Government on competition in electricity and gas markets in NSW including whether and how price caps should be removed. The AEMC has published a draft report (AEMC 2013) and is seeking additional submissions before making its final report and recommendations in September. The Council believes that were the revocation of coverage of the WWGDN (perhaps as a precursor to other revocation action) to discourage removal of retail price regulation the scope for additional competition in the area served by the WWGDN and more widely would be significantly reduced. In such circumstances continued coverage would materially promote competition including in the relevant dependent market.<sup>9</sup>

15. This section discusses the issues relevant to a decision as to whether retail price regulation should be removed in NSW, the potential for "other revocation action" in regards to Envestra's other gas distribution networks and what Envestra considers to be the key reasons explaining the low levels of retailer participation in regional markets.

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<sup>8</sup> Ibid paragraph 4.45

<sup>9</sup> Ibid paragraph 4.46

### 2.1.1. NSW retail price regulation

16. As noted by the NCC, the AEMC is currently undertaking a review into the effectiveness of competition in the NSW retail energy markets for small customers, including whether competition is promoting effective choices for customers at a price and with the quality of service that is consistent with competitive market outcomes. The AEMC has released its draft recommendation to the NSW Government, which states that:

While the gas market is providing less choice for gas customers, both in terms of gas retailer and product choice, the market is still providing efficient outcomes.<sup>10</sup>

And:

While competition is less effective in rural areas than urban areas, we consider competition to be sufficient to enable these customers to benefit from the removal of price caps. Retailers in NSW have customers across the state and the majority of retailers have market offers in rural areas. Amongst customers, the awareness of the ability to switch and switching rates are similar between urban and rural areas.<sup>11</sup>

This led to the following draft recommendation by the AEMC:

Price caps be removed for all customers at the same time so that all customers have an equal opportunity to benefit from increased competition and product choice.<sup>12</sup>

17. That is, despite low levels of retail competition/participation in rural areas, the AEMC draft recommendation is for retail price regulation to be removed for all customers in NSW. This decision was based purely on a consideration of the competitive outcomes currently observed by the AEMC in both rural and urban areas, which areas have a mix of both regulated and unregulated gas distribution networks.
18. A similar approach was also taken in considering whether to remove retail price regulation in Victoria, and more recently, in South Australia. In both states, the decision was made to remove retail price regulation for all customers despite the then (and current) low levels of retail competition/participation in rural areas (see section 2.1.3.2). The decisions were based on whether consumers were receiving efficient outcomes that were consistent with a competitive market.
19. Similar to the AEMC, the Independent Pricing and Regulatory Tribunal (IPART) in its recent decision on gas retail prices for 2013-16 concluded that:

Based on our analysis for this report, we consider it likely that competition in the market is now effective enough to provide sufficient protection to customers, as well as offering more choices and better price and service outcomes. Only 28% of small gas customers now remain on regulated prices in NSW, below the proportion of small electricity customers remaining on regulated prices (around

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<sup>10</sup> Australian Energy Market Commission (AEMC) *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales, Draft Report* 23 May 2013 Op. Cit. p85

<sup>11</sup> AEMC Op. Cit. pii-iii

<sup>12</sup> AEMC Op. Cit. pii



40%). We also consider that a competitive market is best placed to manage the uncertainties that are emerging in the wholesale gas market and note that other States have removed formal price regulation of retail gas.<sup>13</sup>

20. Acil Allen Consulting (AAC) in its report noted that the AEMC (and therefore presumably governments) consider a range of issues in deciding whether energy consumers are receiving efficient outcomes. These factors include the existence of barriers to retailer participation in the market, the conduct of market participants and whether outcomes are consistent with that expected from a competitive market. Importantly, and contrary to the NCC, the AEMC does not consider the approach to network regulation to be a relevant factor:

Any decision the NSW Government might make about removing retail price regulation would, we presume, be made based on the AEMC's final recommendation and the Government's view as to the best interests of NSW consumers. That is, and as reasoned by the AEMC, the relevant factors that will influence a decision by the NSW Government to remove retail price regulation is the extent of competition in the retail market and not how distribution networks are regulated (which matter was not considered to be a relevant factor for consideration by the AEMC).<sup>14</sup>

AAC went on to state that:

Given the draft recommendations of the AEMC, the Independent Pricing and Regulatory Tribunal's support for price deregulation, and the interests of NSW consumers more broadly, the Council's assertion that revocation of the WWGDN, which supplies a relatively small proportion of NSW consumers, would dissuade the NSW Government from removing retail price regulation is highly speculative. The Council's assertion would appear particularly speculative given that network regulation was not considered by the AEMC to be a relevant factor in making its draft recommendation to the Minister.<sup>15</sup>

21. Envestra agrees with AAC that the decision as to whether retail prices should be regulated in NSW will be based on the specific characteristics of the retail market, including customer outcomes, and not on whether the WWGDN continues to be covered. To this end, Envestra notes that it applied to the NCC for revocation of coverage around 3 weeks prior to the AEMC releasing its draft recommendation and met with IPART prior to the release of both its draft and final reports into retail gas prices.
22. While the decision as to whether to remove retail price regulation is independent of the NCC revocation decision, the NCC has expressed concern that, should retail price regulation be removed, revocation could impact "the scope for *additional* competition in the area served by the WWGDN". Envestra explains in section 2.1.3 of this submission that there are significant barriers to retailer participation in the smaller regional markets that are unrelated to coverage of the distribution network.

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<sup>13</sup> IPART, *Review of regulated retail prices and charges for gas*, June 2013, page 6

<sup>14</sup> ACIL Allen *Revocation of Coverage Wagga Wagga Gas Distribution Network* paragraph 30

<sup>15</sup> ACIL Allen Op. Cit. paragraph 32

### *2.1.2. Potential for further network revocation*

23. The NCC also intimated that the NSW Government's decision as to whether to remove price regulation might be influenced by a view that revocation of the WWGDN might precipitate further revocation action. As expressed below, the concern appears to be that such a potential for further revocation activity would discourage the removal of retail price regulation not only in Wagga Wagga but in those other (unknown) networks as well:

The council believes that were the revocation of coverage of the WWGDN (perhaps as a precursor to other revocation action) to discourage removal of retail price regulation the scope for additional competition in the area served by the WWGDN and more widely would be significantly reduced.<sup>16</sup>

24. AAC articulated this aspect of the NCC's reasoning in the following manner:

This suggests that the Council's true concern is that the NSW Government would not remove retail price regulation if more customers were connected to distribution pipelines that were not covered.<sup>17</sup>

25. AAC has stated that such a concern is "highly speculative"<sup>18</sup>. Envestra agrees with AAC. This is for the reasons set out in the previous section, including that the AEMC and/or IPART did not consider the potential for revocation of the WWGDN, or any other network in NSW, as being a relevant factor in deciding whether to remove retail price regulation. Envestra is also unaware of any other government citing this as a relevant consideration in its decision as to whether to remove retail price regulation. For example, the Victorian Government removed retail price regulation in that state despite the Mildura network being uncovered.

26. More importantly, Envestra considers that its application for revocation of the WWGDN should be considered on its own merits. This view is consistent with AAC, who noted that:

Each application for revocation of coverage of a pipeline for a particular market should be considered on its merits. The Council's decision on Envestra's application for revocation of coverage of the WWGDN should not be influenced by any further applications for revocation of other pipelines that may or may not occur.<sup>19</sup>

27. That aside, Envestra reiterates the point made in an earlier submission to the NCC that:

Envestra, as the owner of the Albury network, has no intention of seeking revocation of coverage of the Albury network (nor would such a matter impact on the merits of the case for Wagga Wagga in any event).<sup>20</sup>

28. This reflects that there are particular characteristics of the Wagga Wagga gas market that make it suitable for revocation, including the lack of a competitive price advantage of gas over electricity, the expected significant worsening of this position overtime, the strong incentive to increase throughput, the lack of an incentive and ability to influence the gas sales market (including through price

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<sup>16</sup> NCC Op. Cit. paragraph 4.46

<sup>17</sup> ACIL Allen Op. Cit. paragraph 33 -34

<sup>18</sup> ACIL Allen Op. Cit. paragraph 32

<sup>19</sup> ACIL Allen Op. Cit. paragraph 35

<sup>20</sup> Envestra (Letter the NCC responding to retailers' submissions) 5 June 2013 p6

discrimination among retailers) and the high regulatory costs relative to the expected benefit. Envestra notes that the costs of regulation for the WWGDN can not be shared with its other regulated networks, as in the case with our other review processes (this matter is discussed further in section 3.2).

### *2.1.3. Barriers to retailer participation in the Wagga Wagga gas market*

29. Gas retailer participation in Wagga Wagga is limited. There is one dominant retailer who has 98% of the customer base and one other retailer with the remaining share. This circumstance has persisted despite over a decade of Full Retail Contestability (FRC). It is worth noting that at the present moment it appears only the dominant retailer is actively offering gas contracts to residential and small business consumers.<sup>21</sup>

30. While this fact was accepted, the NCC expressed a view that this situation has arisen because of retail price regulation:

The Council is of the view that the limited competition seen in this (relatively small) market principally reflects the lack of incentives for new market entry or expansion given available margins and the difficulties of competing for new customers in the presence of retail price controls.<sup>22</sup>

31. This view was also set out in the retailer submissions as the key reason as to why there was limited competition in the Wagga Wagga market. The retailers also suggested that the market would become more competitive once retail price regulation was removed, which position was also accepted by the NCC:

The Council considers that it is likely that additional incentives for competition in gas supply will emerge in NSW (including in the area serviced by the WWGDN) in the short to medium term. In recent draft reports, both the Australian Energy Market Commission (AEMC) and the NSW regulator, the Independent Pricing and Regulatory Tribunal (IPART), have concluded that competition in gas supply in NSW is sufficiently effective to allow regulation of retail prices to be removed. Acknowledging the preliminary findings of these agencies, the Council agrees with Origin that competition is likely to become more vigorous when retail price regulation is removed and some improvement of margins is allowed. The Council recognises, however, that the development of further competition in the market for gas sales in the area serviced by the WWGDN (and more generally) may be limited by availability of gas supplies and increased gas prices (both in absolute terms and perhaps relative to electricity).<sup>23</sup>

32. Envestra notes that the NCC in the above has only sufficient certainty to state that "competition is *likely* to become more vigorous when retail price regulation is removed" and has noted certain caveats around this view, which importantly recognise issues relating to the availability of gas supplies and increased gas prices.

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<sup>21</sup> A review of the AER's [energymadeeasy.com.au](http://energymadeeasy.com.au) website yielded only one active gas retailer in Wagga Wagga. A review of the smaller retailer's website also suggested they were not actively offering contracts to new small customers.

<sup>22</sup> NCC Op. Cit. paragraph 4.26

<sup>23</sup> NCC Op. Cit. paragraph 4.27

33. Envestra notes that there are significant barriers to entry for retailer participation in the smaller regional markets that are unrelated to network coverage, which issues are discussed in the following section. Prior to this, Envestra addresses the impact of retail price competition on the market for gas sales in Wagga Wagga over the past 10 years of FRC.

#### *2.1.3.1. Impact of retail price regulation*

34. Envestra has reviewed Origin Energy's retail price proposal for the Wagga Wagga gas sales market and IPART's subsequent review of that proposal. Origin Energy proposed a retail price increase of CPI+4.9% to apply from 1 July 2013 while IPART determined that an increase of approximately CPI+20% would be more appropriate, which increase is largely driven by forecast changes in the wholesale cost of gas over the regulatory period.<sup>24</sup>
35. Origin Energy advised that it has elected not to increase prices to the extent permitted by IPART to avoid a price shock for consumers in the area served by the WWGDN.<sup>25</sup> Envestra finds the limited price increase applied by Origin Energy to be peculiar if previous levels of cost recovery were so low as to explain the lack of retailer participation in Wagga Wagga. Envestra notes that there was insufficient explanation in the Origin Energy submission or IPART decision to explain the reasons for the relatively small increase in retail prices.
36. Envestra has also reviewed the IPART retail price decision for the 2010/11 to 2012/13 period. Country Energy, the previous host retailer for Wagga Wagga (since sold to Origin Energy in March 2011), found the retail margin allowed by IPART to be sufficient.<sup>26</sup> Again, there is insufficient evidence in Origin Energy's submission, at least that Envestra is aware of, explaining why retail margins are now insufficient, if that is in fact the case, particularly in light of the significant economies of scale of the Origin Energy business.
37. Envestra does not however consider that there is evidence that there has been a history of regressive behaviour on the behalf of IPART to hold retail margins at levels that are insufficient to promote retailer participation in the Wagga Wagga market. At best, and again noting that Envestra can not test the veracity of the argument, margins may have been insufficient from March 2011 (i.e. when Origin Energy acquired the Country Energy retail business), which was 10 years after the period where FRC commenced in NSW. However, Envestra notes that there has been no retail competition in Wagga Wagga either pre or post Origin's interest in that gas sales market, including a period when Country Energy operated the business and considered that margins were adequate.

#### *2.1.3.2. Barriers to retailer participation in small regional markets*

38. Envestra disagrees with the NCC (and retailer) view that "competition is likely to become more vigorous when retail price regulation is removed and some improvement of margins is allowed"<sup>27</sup>. The issue of margins was discussed in the previous section. The key reason explaining the low level of retailer participation in Wagga Wagga reflects the high cost and risk of entering the small gas sales market relative to the low expected returns. This fact explains the low retailer participation not only in Wagga Wagga but in all other regional areas served by Envestra's networks.

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<sup>24</sup> IPART *Review of regulated retail prices and charges for gas, 2013 to 2016 – Draft Report* April 2013 p 38

<sup>25</sup> IPART Op. Cit. p 39

<sup>26</sup> Country Energy *Gas Draft Report - Review of Regulated Retail Tariffs and Charges 2010-2013* 14 May 2010 p 1

<sup>27</sup> NCC Op. Cit. paragraph 4.27

39. In its supplementary submission to the NCC, EnergyAustralia identified a large and diverse range of issues that need to be addressed by a retailer before entering a new gas market. These matters were listed by EnergyAustralia as including:

- Registration and certification with AEMO (Australian Energy Market Operator)
- Obtaining transmission haulage to the network receipt points
- Obtaining distribution system haulage
- Procuring suitable gas supply from producers
- Procuring/managing gas supply hedges to offset risks in the wholesale gas market
- Establishing the business to business protocols including new connections and other service orders
- Building suitable tariffs and tariff structures to manage distribution network tariffs and retail risks
- Building processes and protocols to manage network billing
- Establishing new connection processes
- Ensuring customer contracts and terms address regulatory obligations and distribution processes
- Educate operational staff on the market issues of each network including emergency management

40. Envestra also considers that significant expenditure would need to be incurred by retailers on marketing in order to attract new customers, especially for a new retailer that was is not active in the relevant gas sales market and needed to develop a brand presence to attract new customers. What is clear from the EnergyAustralia submission is that there are a large number of activities, costs and risks that are in addition to entering into a distribution supply contract that retailers need to undertake in order to enter the Wagga Wagga market.

41. Of the above list, the key material factors that carry the greatest cost/risk relate to access to wholesale gas and pipeline capacity.<sup>28</sup> The costs are exacerbated by the existence of the contract carriage model that applies in NSW, which requires retailers to enter into bilateral contracts with gas producers, which are typically on a take or pay basis and over a long term period. In contrast, the market carriage model that applies in Victoria allows retailers to access wholesale gas and pipeline capacity through a trading market administered by the Australian Energy Market Operator (AEMO).

42. The resultant high barriers to entry were recognised by Momentum Energy in its submission to the AEMC's review of the effectiveness of retail energy competition in NSW. Momentum Energy explained the higher costs associated with entering and operating under the contract carriage model in NSW versus the market carriage model utilised in Victoria:

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<sup>28</sup> AEMC Op. Cit. p155

While there may be rivalry between the big three retailers, the NSW retail gas market is in practice largely limited to just them. This absence of actively competing gas retailers is due to the barriers to entry being high. There are three principal reasons for this are:

- Procuring wholesale gas is more difficult in NSW than Victoria;
- There are less supply and transportation options in NSW, and;
- Gas retailers rely heavily on bi-lateral contracts rather than purchasing from the market.

Gas is now transacted through the STTM at the Sydney Hub, but this gas is primarily used for balancing purposes. When smaller retailers are seeking reliable longer term contracts, gas producers generally demand a higher price for gas from such a lower volume purchaser, combined with more onerous take or pay arrangements and less flexibility in daily cash flow arrangements. Consequently, for second tier retailers, price and volume are unlikely to be sufficiently certain to back the provision of gas to their retail customers.<sup>29</sup>

43. Envestra notes that Momentum Energy was referring to entering the Sydney gas sales market, a market of over 1 million customers, which is 50 times the size of the customer base served by the WWGDN. Envestra also notes that the barriers referred to by Momentum Energy did not include issues relating to entering into a gas distribution contract, including whether the network was regulated (or not).

44. These facts led AAC to state that:

Retailers thus need to take on significant cost and risk to enter new (including small) markets, most of which are not related to the distribution pipeline, with little potential benefit for entry to small retail markets such as the WWGDN area. While many of these costs and risks are common for entry to each electricity and gas market, there are significantly greater costs and risks associated with entry to small gas markets, particularly in NSW, Queensland and South Australia, which operate on a contract carriage model.<sup>30</sup>

45. These barriers to entry, particularly the market size and prevailing market structure (i.e. contract carriage model), has led to low levels of retailer participation on all regional networks that are served by Envestra's distribution networks. The following figures show the impact that the market size and structure has had on the market share of the host (or incumbent) retailer on Envestra's networks in South Australia (Figure 1) and Queensland (Figure 2), which operate on a contract carriage model and Victoria (Figure 3), which operate on a market carriage model.

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<sup>29</sup> Momentum Energy *Submission to the AEMC's Issues Paper on the Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales* 15 February 2013 p2

<sup>30</sup> ACIL Allen Op. Cit. paragraph 71

Figure 1: South Australian Host Retailer Market Share, 2003 to 2013

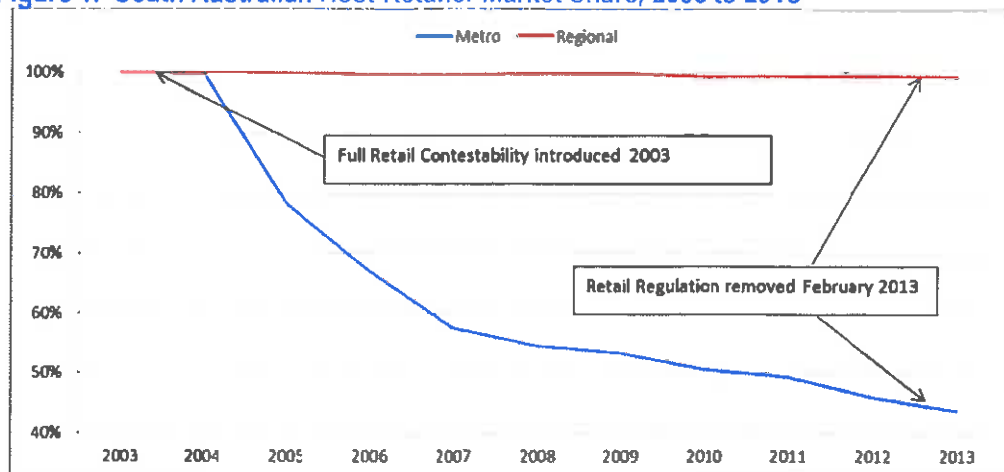


Figure 2: Queensland Host Retailer Market Share, 2004 to 2013

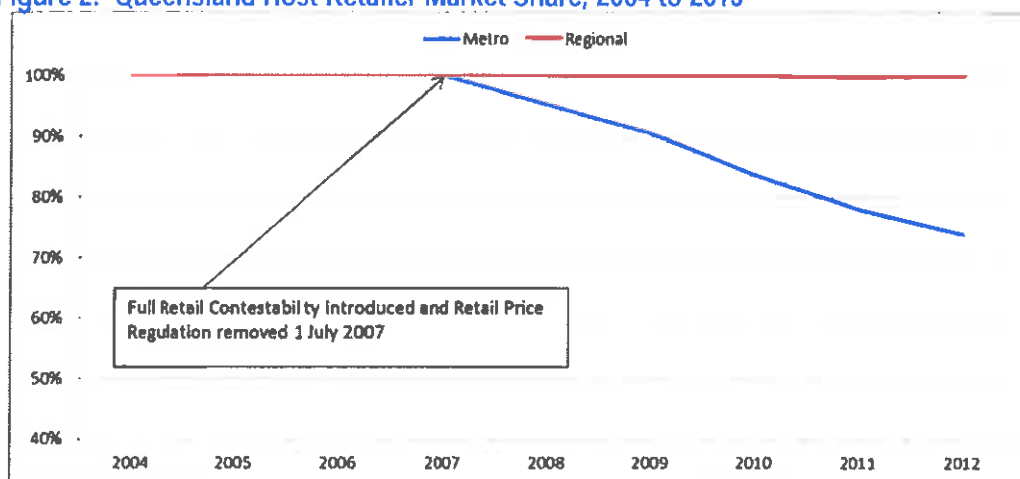
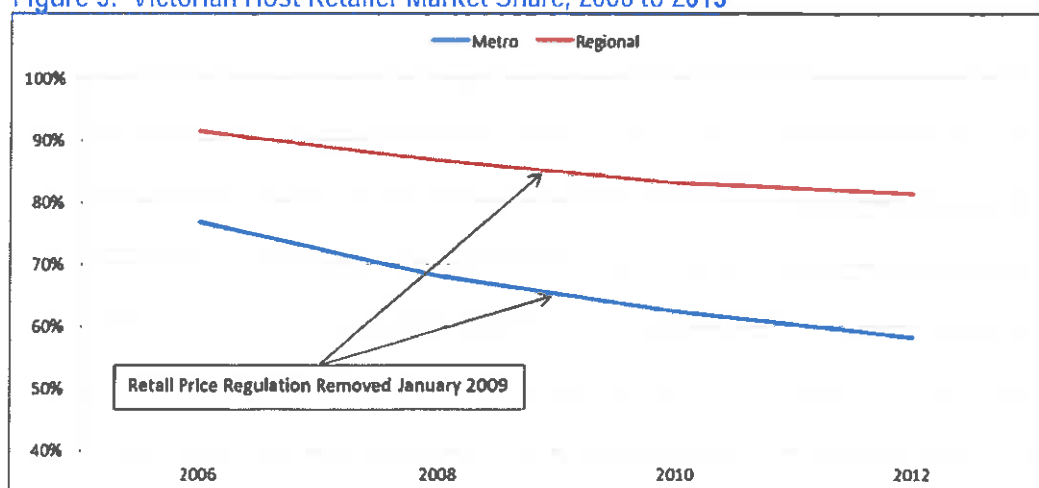


Figure 3: Victorian Host Retailer Market Share, 2006 to 2013



46. It is clear from the above that:

- retailer participation/competition is far stronger in metropolitan areas than in regional areas, irrespective of the wholesale gas market structure;

- retailer participation/competition is stronger in Victoria where a market carriage model exists relative to South Australia and Queensland where a contract carriage model exists;
- related to the above, and similar to in Wagga Wagga where a contract carriage model also exists, the host (or incumbent) retailer in regional South Australia and Queensland has either the entire or the great majority of the retail market share; and
- retailer competition/participation has not become "more vigorous when retail price regulation is removed", as evidence by the modest change in the market share of the host retailer post deregulation (which reflects that markets were already considered to be competitive prior to the removal of price regulation).

47. In relation to figures 1 to 3 above, AAC state that:

... the market share of the "host retailer" in those states operating under a contract carriage model, is higher than in Victoria (other than Mildura), which operates under a market carriage model. This is due to the additional costs and risks associated with negotiating the required wholesale gas contract and shipper contract under a contract carriage model. Retailers are required to enter into long term wholesale gas contracts and shipper contracts before winning new customers. The fixed costs under these contracts are incurred regardless of the actual customer base<sup>31</sup>.

And:

... the market share of the "host retailer" in regional areas is significantly higher than in metropolitan areas. This is due to the higher cost per customer relative to the potential benefits incurred by a new entrant retailer, particularly in the smaller regional areas, to address the issues identified by Energy Australia in paragraph 69 [of the AAC report], including to negotiate the required wholesale gas contract and shipper contract. That is, regional areas are associated with high costs and risk for little benefit, due to their small size, which facts have led to the observed low levels of competition across all regional retail markets in which Envestra operates.<sup>32</sup>

48. The matters referred to as identified by EnergyAustralia are those activities, costs and risks referred to in paragraph 39 of this submission.

49. Importantly, the facts demonstrated above are independent of whether the network is covered. For example, Envestra's uncovered Mildura network is supplied from South Australia under a contract carriage model rather than from Victoria under a market carriage model. Figure 4 shows that the host retailer in Mildura has a 100% market share. Moreover, this market share has not changed following the introduction of FRC, revocation of coverage of the network and the period following the removal of retail price regulation.

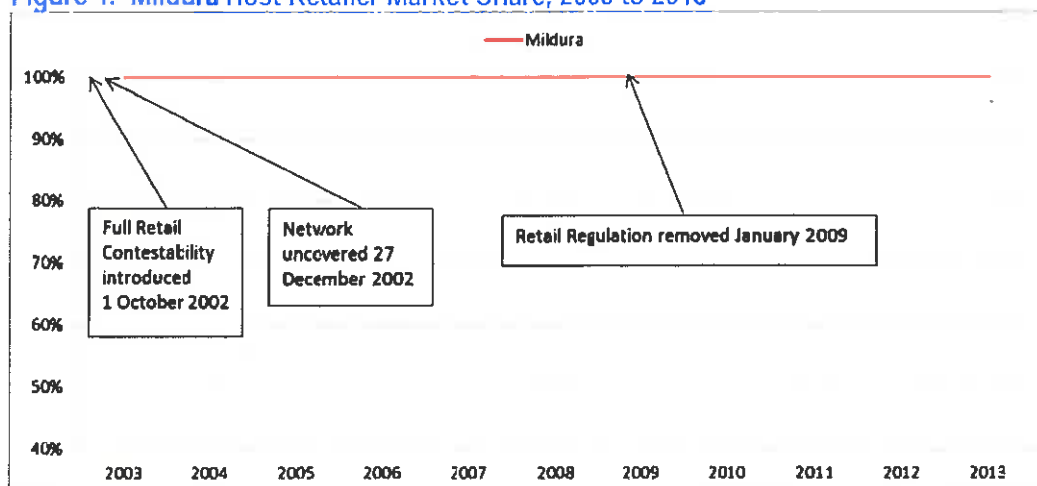
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<sup>31</sup> ACIL Allen Op. Cit. paragraph 81

<sup>32</sup> ACIL Allen Op. Cit. paragraph 82



Figure 4: Mildura Host Retailer Market Share, 2003 to 2013



50. To this end, EnergyAustralia in its supplementary submission<sup>33</sup> to the NCC attempted to draw a link between the coverage status of a network and the extent of retail competition within the area serviced by the network. The table, as presented by EnergyAustralia in its submission, showed that only covered networks had more than one retailer in the gas sales market while uncovered networks had only one retailer. Envestra submits that this table is misleading as it ignores the relative market shares of each retailer.

51. For example, and using Wagga Wagga as an example, the host retailer has 98% of the small customer market with the smaller retailer having the remainder (and appearing to no longer be offering contracts to new customers).<sup>34</sup> The story is the same for the regional markets in South Australia and Queensland. In regional South Australia there are four retailers present where the host retailer market share is 99%. In regional Queensland there are three retailers present where the host retailer again has a 99% market share.

52. The defining factor in each of these markets is not the coverage status of the network, but the small size of the markets and the related high costs/risk that must be taken on by retailers for relatively low potential benefits. This is in turn largely driven by the existence of the contract carriage model. These facts led AAC to conclude that:

The higher level of cost and risk associated with a contract carriage model, particularly in regional markets, vis a vis a market carriage model will be faced by new entrant retailers, regardless of whether the WWGDN is covered or not.<sup>35</sup>

53. That is, the decision to revoke coverage (or not) will not influence either the decision to remove retail price regulation in NSW or impact the level of retailer competition/participation in regional areas.

<sup>33</sup> EnergyAustralia Response to Envestra's Application for Revocation of Coverage – Wagga Wagga Gas Distribution System: Supplement 1 page 2 table 1

<sup>34</sup> Refer footnote 34 above

<sup>35</sup> ACIL Allen Op. Cit. paragraph 83

## 2.2. Terms and conditions for the WWGDN

54. The NCC has suggested that the costs and risks discussed in section 2.1.3.2 are likely to be lower for a covered network because this provides greater certainty to retailers over the terms and conditions of access to the network:

The Council also considers that the costs and risks of competing in the market for gas sales in the area serviced by the WWGDN, especially for smaller second tier gas retailers, are likely to be lower if the conditions for access to the WWGDN (and the basis for the determination of these in the future) are known in advance. The ex ante regulation associated with a covered pipeline seems more likely to allow this, and also provides some certainty to retailers in deciding to enter a new market, than would be the case for an uncovered pipeline (or indeed a pipeline subject to light regulation).<sup>36</sup>

55. As explained in section 2.1.3, the key barriers to entry, particularly for second tier retailers in regional areas, are the costs of negotiating bilateral gas supply and shipping contracts. Core Energy in its report (Attachment 2) also refer to the difficulties that retailers will experience in contracting gas for domestic supplies as a result of the growth of the LNG export industry. This matter will be compounded for retailers seeking to enter into long term contracts for small amounts of gas to supply Wagga Wagga.
56. Importantly, and as already explained, these barriers are not in anyway related to concerns over retailers entering into contracts for the haulage of gas across distribution networks.
57. That aside, the above matter appears to stem from concerns raised in the retailer submissions over the ability to negotiate fair and reasonable terms and conditions with Envestra if the network were to be uncovered. The retailer concerns regarding terms and conditions were summarised by the NCC as follows:

... that in the absence of coverage network users could be exposed to inefficient (monopoly) prices and non-price terms of access which would restrict the development of competition.<sup>37</sup>

And:

Envestra's retention of 'onerous' access terms for access to uncovered pipelines which have been disallowed in relation to covered pipelines illustrates the scope for imposition of terms and conditions of access that may restrict the development of further competition if coverage is not retained.<sup>38</sup>

58. Again, the NCC appears to have accepted the concerns raised by retailers in making its draft recommendation:

...the Council is concerned that non price access terms, and measures to transfer risk between a pipeline owner and other parties, may adversely affect

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<sup>36</sup> NCC Op. Cit. paragraph 4.43

<sup>37</sup> Ibid. paragraph 4.16

<sup>38</sup> Ibid.

the prospects for competition in the sale of gas in the area serviced by the WWGDN.<sup>39</sup>

59. Envestra has indicated in its initial application to the NCC, its subsequent submission that responded to the retailer submissions and during its consultation with the retailers prior to lodging its initial application that it intends to apply the most recent AER approved terms and condition to the Wagga Wagga network in the event coverage is revoked. This approach is consistent with current practice. For example, if a retailer sought the terms for Envestra's uncovered networks in the areas surrounding Wagga Wagga, Envestra would use the AER approved WWGDN terms as the basis for negotiation.
60. Envestra intends to continue with the process of developing, to the maximum extent possible, standard terms and conditions across all of its regulated and unregulated networks. This process has so far occurred in respect of the AER approved terms and conditions that apply in South Australia, Queensland, Victoria and Albury. Envestra will continue with this process for Wagga Wagga, regardless of whether or not revocation is granted.

61. On this matter, AAC notes that:

Nationally consistent terms and conditions across all Envestra pipelines would provide the level of certainty that the Council is of the view that new entrant retailers require. This is because a new entrant retailer could review the most recent terms and conditions approved by the AER for Envestra's regulated networks. It would be most likely that the potential retailer would operate in the other networks owned by Envestra, and as such, have a high level of familiarity with Envestra's terms and conditions.<sup>40</sup>

62. Despite this assurance, the NCC has noted:

While the Council has little reason to doubt the *bona fides* of Envestra's stated intentions to return some of the savings in regulatory costs to customers, limit future price increases and engage with retailers in relation to access terms, these intentions can only be given limited weight given difficulties that would arise in enforcing such promises in relation to an uncovered pipeline.<sup>41</sup>

63. Envestra notes that there would be significant reputation risk if it does not act in accordance with the intentions set out in its application, which fact was recognised by AAC in considering this matter. That aside, and as noted by AAC, any such concern could be easily overcome:

If the Council remains concerned that Envestra will not have sufficient incentive to use national consistent terms and conditions for the WWGDN, the Council could recommend that revocation of coverage of the WWGDN be subject to Envestra entering into an undertaking with the Minister or with the relevant retailers that national consistent terms and conditions be used for the WWGDN.<sup>42</sup>

64. Envestra would have no concern in entering into such an undertaking, either directly with the Minister or through its terms and conditions, to apply the national terms and conditions that apply to its other

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<sup>39</sup> Ibid. paragraph 4.32

<sup>40</sup> ACIL Allen Op. Cit. paragraph 87

<sup>41</sup> NCC Op. Cit. paragraph 4.35

<sup>42</sup> ACIL Allen Op. Cit. paragraph 92

regulated networks. Envestra however notes that such action is not necessary given its proposal set out in its application to the NCC to continue to publish terms and conditions in the event that coverage is revoked.

65. The terms and conditions to apply in respect of the Wagga Wagga networks was one of the key matters raised by retailers during our customer consultation process prior to lodging our application to the NCC. Envestra noted in its application in response to this concern that:

It is important to note Envestra's intention to continue to publish on its website the tariffs for access to the Wagga Wagga network if revocation of coverage is granted. This is consistent with Envestra's objective of not discriminating between retailers in an effort to promote competition in the dependent downstream market.<sup>43</sup>

Envestra intends to engage with retailers to determine a mutually agreeable set of terms to apply to the Wagga Wagga network in the event that coverage is revoked.<sup>44</sup>

66. Envestra therefore does not anticipate there to be any significant issue relating to the negotiation of access terms that would have a material impact on competition in the gas sales market. As noted by ACC, any concerns that might exist, despite Envestra's submission, can be easily overcome by recommending that Envestra enter into certain undertakings with the Minister (or retailers) as a condition of revocation being accepted.

#### *2.2.1. Other matters raised in retailer submissions*

67. Envestra considers that it would be instructive to address certain other matters raised in the retailer submissions regarding terms and conditions, despite these matters not being of central importance to considering whether criterion (a) is satisfied.
68. The first relates to the process for negotiating the terms and conditions for Envestra's regulated distribution networks. For example, EnergyAustralia noted in its submission on Envestra's application that:

Despite our experience and knowledge of the regulatory framework we have had very little success in our past negotiations in obtaining access to the pipeline on fair and reasonable terms and conditions.

By way of example, we refer to the recent review for the AER Victorian Envestra AA 2013-17 Draft Decision and draw your attention to the list of suggested changes to the terms and conditions. During the consultation process, retailers suggested thirty four changes to the terms and conditions and Envestra gave in principle support to only four of these proposed changes.<sup>45</sup>

69. Envestra notes that not one of the proposed changes suggested by EnergyAustralia was aimed at increasing competition in the Victorian gas sales market. As would be expected, many of the suggested changes were aimed at transferring risk from the retailer to the distributor. Ultimately, the AER has set terms and conditions that it considers provide for a fair, reasonable and efficient allocation of risk between distributors and retailers, having considered the retailer submissions.

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<sup>43</sup> Envestra *Wagga Wagga Network Revocation Submission* 1 May 2013 paragraph 142

<sup>44</sup> *Ibid.* paragraph 143

<sup>45</sup> EnergyAustralia *Application for Revocation of Coverage – Wagga Wagga Gas Distribution System* 27 May 2013 p2

70. A further (and related) issue that was also raised by EnergyAustralia in its submission is the prospect of negotiating fair and reasonable terms and conditions for an uncovered network:

Much of our experience in trying to negotiate access to this pipeline has been under the protection of a "covered" pipeline, where a regulator or market operator has also been involved. As such, the prospect of negotiating terms and conditions of access under an uncovered arrangement does not provide us with much confidence that future negotiations, under an uncovered arrangement will achieve fair and reasonable outcomes.<sup>46</sup>

71. Again, Envestra has sought to make it clear throughout all of its submissions on this matter that the Wagga Wagga terms and conditions will continue to be based on the AER approved terms for that region, as is current business practice.
72. Relevant to this point is that at no stage in our history has it been necessary for a retailer to resort to an arbitration of Envestra's terms in respect of either our covered or uncovered networks. Envestra also submits that at no stage has a retailer not gained access to an Envestra network, covered or uncovered, due to an issue with Envestra's terms.

### 2.3. Countervailing power of customers

73. A key argument in Envestra's application was that it did not have the ability to exercise any market power that it might have given that gas does not currently have a competitive price advantage over electricity in Wagga Wagga (unlike in our other networks). Envestra submitted that this competitive position is expected to worsen given the projected *increase* in retail gas prices for small customers of around 35% and *decreases* for electricity customers of 4% in Wagga Wagga over the 2013-16 period.
74. The Core Energy Group (CEG) in its report has estimated that the projected increase in gas prices could allow a customer to reduce costs by [REDACTED] if they choose to replace their gas appliances with the equivalent electric appliance <sup>47</sup>. Moreover, this saving will be made as early as 2014/15.
75. Such pricing outcomes are of considerable concern given that gas is a fuel of choice. Consistent with Envestra's application to the NCC, the AEMC identified that there is less regulatory intervention in gas than electricity as:

... it is feasible to substitute away from gas to electricity. While it is difficult to completely replace electricity with gas (for example electricity is required for lighting and the majority of appliances), it is possible to replace gas with electricity (although we note that this may be at some expense, for example if appliances needed to be replaced). This ability for customers to use an alternative fuel to gas has been viewed as a market mechanism for keeping some control on prices and hence to justify a lighter-handed form of regulation.<sup>48</sup>

The AEMC concluded that:

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<sup>46</sup> EnergyAustralia Op. Cit. p2

<sup>47</sup> Core Energy *Competitive Assessment of Natural Gas* July 2013 p7

<sup>48</sup> AEMC Op. Cit. p70

... customers' greater ability to switch away from gas to electricity ... provides pressure to keep gas retailers' prices and service quality similar to outcomes expected in a competitive market.<sup>49</sup>

76. Despite this, the NCC did not consider that the ability to substitute gas appliances for an electric equivalent placed an effective constraint on the potential for Envestra to exercise market power:

... while in principle the matters outlined above could be expected to constrain the ability of Envestra to use market power and thereby adversely impact on competition in the relevant dependent market, the feasibility of such matters must be taken into account. The purported alternatives for users are not without costs. Installing new appliances or machinery that use an alternative source of fuel to gas requires expenditure by the user. Similarly, assuming that it is even possible, configuring existing appliances or machinery to use an alternative fuel source also comes at a cost. The Council considers that in both the domestic and industrial contexts such costs are likely to be substantial, allowing exploitation of significant market power without triggering significant switching.<sup>50</sup>

77. As set out in the above, a key reason for the NCC not accepting Envestra's submission is its view that appliance switching costs "are likely to be substantial". Envestra engaged CEG to provide an independent and expert view of the competitiveness of natural gas and electricity as an energy source available to the residential segment in Wagga Wagga, the potential for switching from gas appliances to electric appliances and whether such costs are likely to present a barrier to that switching.

78. With regard to expected consumer behaviour, CEG states:

Core believes residential customers place the largest weight on appliance capital and operating cost over other factors at the time of considering replacement of space heating, water heating and cooking appliances. Significant differences in annual operating costs of gas versus electric appliance equivalents will provide incentive to encourage customers to change appliance type, either when the appliance has reached the end of its useful life or earlier.

In the event of end of life replacement, and contrary to the NCC view, Core believes that the costs of switching from a gas appliance to an electric equivalent appliance will be negligible given electricity is already supplied to the household. Core also considers that the cost of replacing an appliance prior to the end of its useful life is also likely to be negligible given the low likely residual value of the appliance at the time of replacement. Furthermore the value may be offset relatively quickly by the cost differential between fuel types shown in table 3.1 (and explaining the motivation for the early replacement).

Core therefore does not consider, for residential customers, that appliance switching costs "are likely to be substantial" as claimed by the NCC. To the contrary, and for residential customers, appliance switching costs are most likely to be negligible such that it would not provide a barrier to fuel switching.<sup>51</sup>

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<sup>49</sup> AEMC Op. Cit. paragraph 85

<sup>50</sup> NCC Op. Cit. paragraph 4.39

<sup>51</sup> Core Energy Op. Cit. p8

79. These views were also held by AAC:

An economically rational consumer will assess the lowest cost form of space and water heating and cooking. In response to changes in the price of electricity or gas, an economically rational consumer will consider the cost of switching fuels by considering the upfront cost to switch and the life time costs.<sup>52</sup>

80. CEG built an appliance turnover model to test a range of potential scenarios regarding the proportion of gas appliances that are due for replacement switching to an electric equivalent on the throughput of the WWGDN. This model made informed assumptions on the current stock of gas appliances in the residential market, the average consumption of those appliances and the appliance life. This showed that, by June 2019, "approximately 41 percent of total gas demand will be subject to change based on requirement for appliances to be replaced"<sup>53</sup>.

81. Based on this model, which has been provided to the NCC with this submission, CEG found that:

Core believes that there is a high probability that the level of annual gas usage will fall as a result of moderate substitution to electric appliances. For example, assuming a 25% substitution rate total usage would decline from around 827GJ per annum in 2013/14 to below 760TJ per annum by 2018/19, representing a CAGR of around -1.8 percent. This reflects the median of the range of scenarios depicted in Figure 8.1, [REDACTED]

- Core's analysis suggests the cost of gas will be over [REDACTED] higher than the equivalent cost of electricity in Wagga Wagga by as early as 2014/15 (Table 6.3).
- Core is of the view the costs of switching from a gas appliance to an electric equivalent will be negligible in the case of appliance replacement given electricity is already supplied to the household. Further, the above analysis does not include an accelerated appliance change over, whereby residential customers may seek to substitute gas appliances nearing the end of their useful life for electric equivalents appliances.
- the analysis does not take into account the potential repeal of the carbon tax following the next federal election, which would further decrease the cost of electricity relative to gas (hence resulting in a greater rate of appliance switching); and
- Core has not considered a number of long observed and accepted drivers of declining average gas demand, including:
  - ongoing improvements in appliance efficiency and/or improvements in the thermal efficiency of homes; and
  - the trend towards milder weather.<sup>54</sup>

82. The findings of both CEG and AAC therefore suggest that Envestra will be under significant pressure to retain its current market share given the considerable increase in gas prices relative to electricity prices forecast to occur over the immediate period. Moreover, both experts did not agree with the NCC that such switching costs are "likely to be substantial", but instead found that the costs would be negligible at the time an appliance is due for replacement.

<sup>52</sup> ACIL Allen *Revocation of Coverage Wagga Wagga Gas Distribution Network* July 2013 paragraph 111

<sup>53</sup> Core Energy Op. Cit. p13

<sup>54</sup> Core Energy Op. Cit. p9

83. At this time, CEG has demonstrated that it is reasonable to foresee a significant decrease in gas throughput due to the replacement of gas appliances with their electric equivalent. Envestra notes that the CEG report was based on a range of conservative assumptions, including that customers will not switch appliances before the end of their useful lives. Envestra estimates that the cumulative revenue impact of the lost (or replaced) throughput, based on a 25% rate of appliance substitution, would be around \$3 million by June 2019.
84. Envestra therefore submits that electricity is a readily available and highly credible substitute for gas, which matter is significantly compounded in this current environment of increasing gas retail prices, which are in-turn driven primarily by significant increases in wholesale gas costs as a result of the development of the LNG export industry in Australia. The dynamics of substitution of electric for gas appliances, as demonstrated by CEG, will place a strong incentive to ensure that prices reflect efficient costs. These competitive tensions were summarised by AAC as follows:

In conclusion, the future relativity between gas and electricity prices suggests that Envestra will be under significant pressure to retain customers and, given the long life of Envestra's assets and commitments, will act as a further constraint against increasing distribution prices, regardless of coverage of the WWGDN.<sup>55</sup>

#### 2.4. Countervailing power of retailers

85. The NCC has agreed with Envestra that retailers, due to their experience and knowledge of the gas sector, will possess countervailing power. The NCC has however considered that the incentive on retailers to exercise that countervailing power is limited by the fact *current* regulatory arrangements generally allow for network prices to be passed through.

The Council agrees that the two existing retailers, Origin and Energy Australia can be expected to have some countervailing power due to their experience and knowledge of the gas sector. Any new entrant retailer would also be likely to possess some countervailing power as it is more likely than not that it will be a retailer operating in some other energy market that can leverage off its knowledge and experience to negotiate with Envestra in order to start operating in the Wagga Wagga region. However, the strength of such countervailing power of any retailer cannot necessarily be expected to benefit end users and, in particular, households. Under current regulatory arrangements gas retailers are generally allowed to pass through distribution cost increases, which limits the incentive for retailers to resist such increases. As such the application of any countervailing power by a retailer may be an inadequate response to any possible anticompetitive conduct affecting end users.<sup>56</sup>

86. Interestingly, the NCC has referred to the incentives faced by retailers to "pass through" distribution tariffs under the "current regulatory arrangements", despite a focus of NCC reasoning elsewhere being prefaced on such regulatory arrangements changing as per the AEMC and IPART recommendations to remove retail price regulation in NSW. Envestra considers that, in the event retail price regulation is removed, the incentives facing the retailers will change considerably.

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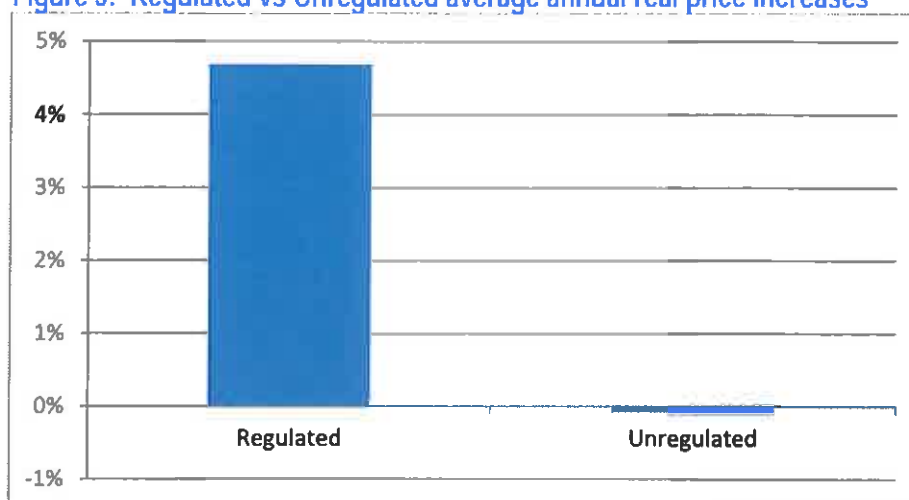
<sup>55</sup> ACIL Allen Op. Cit. paragraph 83

<sup>56</sup> NCC Op. Cit. paragraph 4.42



87. This is illustrated to an extent by Origin Energy's decision not to pass through to customers the full increase in retail gas tariffs allowed by IPART on the basis that Origin Energy is "very much aware of the cost of living pressures facing its customers". This behaviour suggests that, regardless of whether network coverage is revoked, Origin Energy will seek to protect the interests of its customers. Another example is that Origin Energy has not agreed to any price increase above the CPI in respect of Envestra's Mildura network (where Origin Energy is the sole retailer).
88. As per our initial application, Envestra considers that it is instructive to compare the price outcomes achieved on our regulated and unregulated networks (Figure 1). This shows that unregulated real annual price decreases (of 0.1%) have been 4.8% lower than for regulated networks (which increased by 4.7%). The unregulated tariffs are governed by bilateral agreements negotiated between Envestra and retailers. The regulated tariffs on the other hand reflect the outcome of full access arrangement reviews.

**Figure 5: Regulated vs Unregulated average annual real price increases**



89. Not only does figure 1 demonstrate the countervailing power of retailers in uncovered networks, it quite clearly demonstrates the overall ability of uncovered networks to deliver price stability to consumers, of which EnergyAustralia had regard for in its submission.<sup>57</sup> Envestra considers that this provides strong evidence of the ability for retailers to negotiate price outcomes that are in the long term interests of its consumers.
90. On a minor (but related) matter, Envestra notes the comment of EnergyAustralia that is set out by the NCC in its draft recommendation:

...querying whether gas distribution network prices should be falling as they are said to have done recently in Victoria (rather than rising in line with CPI).<sup>58</sup>

91. Envestra notes that the AER has approved price increases for its Victorian network totalling 24% over the 2013 to 2017 Access Arrangement period. Moreover, and consistent with the two other Victorian distributors, the AER has allowed Envestra to apply for additional capital expenditure over the regulatory period once it completes a defined threshold of mains replacement. Envestra expects to meet this threshold and apply for the additional capital expenditure in mid 2014. This will further increase allowed prices for Victoria.

<sup>57</sup> EnergyAustralia Application for Revocation of Coverage – Wagga Wagga Gas Distribution System 27 May 2013 p4

<sup>58</sup> NCC Op. Cit. paragraph 4.36

92. In terms of the other businesses, Envestra notes that certain parts of the AER Victorian decision are subject to an appeal. In respect of Multinet, the AER has recently conceded on an appeal ground relating to the appropriate approach to setting the opening regulatory asset base as at 1 January 2013, which is expected to provide that business with an additional \$45 million in revenue. The actual impact on tariffs had not been finalised by the AER at the time of providing this submission to the NCC.
93. Finally, Envestra submitted that Envestra is further constrained by the ability for any party, including retailers, to apply for revocation of the network. The NCC did not accept this position, noting that:

...reimposing coverage can be a costly exercise. In the Council's view, were coverage to be revoked as a result of this application, the prospect of the WWGDN being re-covered provides only a limited constraint on setting access prices and other terms in relation to the WWGDN, especially in the shorter term.<sup>59</sup>

94. Envestra does not accept this argument, particularly for a business the size of Origin Energy (or any other retailer for that matter). Origin Energy has a market capitalisation of around \$14 billion, which makes it some four times larger than Envestra. The cost of lodging an application for revocation is only \$7,500, which hardly presents a barrier for a company the size of Origin. As AAC note, even assuming such an application would cost \$0.1 million, this would only account for 0.001% of Origin's market capitalisation.
95. The costs of seeking revocation, as most likely intended by governments, is immaterial (particularly relative to a company the size of Origin Energy).

## 2.5. Standardisation of Transactional Interfaces

96. A final argument that was raised by the retailer submissions and agreed to be the NCC related to the potential for greater harmonisation of transactional interfaces, which is considered to be a barrier to entry for retailers, if the WWGDN were to remain covered. The NCC stated in its draft recommendation that:

Having regard to the submissions received that Council is also concerned that the costs associated with the transactional interfaces between gas retailers and distribution pipeline operators are significant. Unlike the electricity sector where most of these processes have been standardised and automated, in the gas sector many pipeline appears (sic) to have bespoke requirements and retailers have to interface with each different system. There appears to be significant scope for these costs to be reduced and for competition to be enhanced as a result. The Council understands that some initiative may be under way in this regard. However, it appears to the Council that any such initiatives, and positive developments in this regard more generally, are more likely to flourish within a regulated environment than where a pipeline is uncovered.<sup>60</sup>

97. The NCC is correct in stating there was "some initiative... under way in this regard". Indeed, AEMO commenced a review in 2010 to determine whether aligning the NSW/ACT transactional

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<sup>59</sup> NCC Op. Cit. paragraph 4.44

<sup>60</sup> NCC Op. Cit. paragraph 4.47

interfaces/processes with those in South Australia, Queensland and Victoria would deliver industry benefits. AEMO however ceased this review based on the outcome of a cost benefit analysis conducted in early 2013<sup>61</sup>. The cost benefit analysis identified:

- substantial costs to industry of the project of up to \$50 million;
- that there was no consensus from industry on the need for, and value of, the program to standardise systems; and
- the costs of the project exceed the benefits.

98. With regard to the last point, the National Gas Rules require that any expenditure of the nature described in this section (i.e. IT systems) can only be rolled into the regulatory asset base if, among other things, the benefits of the expenditure exceed the costs. Given the AEMO review, any expenditure incurred by Envestra in implementing standard transactional systems for a covered network would not be added to Envestra's asset base.

99. Envestra notes that covered and uncovered networks form part of the same NSW gas market. Therefore AEMO had no regard as to the coverage status of the networks when assessing the merits of the standardisation of transactional interfaces project. Envestra also notes if the project proceeds the standardisation will occur in all covered and uncovered networks.

100. Given the above two points, the NCC's assertion that "...it appears to the Council that any such initiatives, and positive developments in this regard more generally, are more likely to flourish within a regulated environment than where a pipeline is uncovered"<sup>62</sup> is without foundation.

## 2.6. Conclusion on Criterion (a)

101. In its draft recommendation the NCC concluded that criterion (a) is satisfied. In coming to this conclusion the NCC had regard to several factors, which in its view, led to the conclusion that continual coverage of the WWGDN would better promote competition in the market for gas sales. Those factors, and Envestra's response to those factors, is summarised as follows:

- the removal of coverage at this time might affect the scope for the removal of price regulation of gas sales in NSW – Envestra submits this is highly speculative as the AEMC (and IPART) have both formed the view that price regulation should be removed despite low levels of retail competition in rural areas;
- the costs and risks faced by retailers are likely to be lower if the conditions for access are known in advance – Envestra submits that the key costs and risks faced by retailers in regional areas is primarily explained by the small size of the market and the existence of the contract carriage model in NSW. This has led to low retail participation/competition in regional areas, which is consistent with actual experience with our other regional networks;
- that non-price access terms may adversely affect the prospects for competition in the gas sales market – Envestra submits that it will continue to apply the AER approved terms and conditions in Wagga Wagga in the event that coverage is revoked, which is consistent with current business practice;

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<sup>61</sup> Nours Group *NSW/ACT Gas Market Reform – Cost Benefit Analysis* 15 March 2013 p3

<sup>62</sup> NCC Op. Cit. paragraph 4.47

- that gas and electricity are not sufficiently substitutable to constrain the use of market power – Envestra submits that switching costs are not substantial and that, given the significant price increase in gas relative to electricity, electricity is a readily available and credible substitute for natural gas;
- the application of countervailing market power by retailers is likely to be inadequate – Envestra submits that Origin Energy has recently demonstrated that it will not necessarily pass through the full costs incurred in retailing gas to customers in the WWGDN area. Envestra also submits that its pricing outcomes for Envestra's unregulated networks have been lower and more stable than for regulated networks.
- any initiatives to standardise transactional interfaces are more likely to flourish within a regulatory environment – Envestra submits that this ignores the recent review by AEMO that the costs of standardising these transactional interfaces in NSW are unlikely to exceed the benefits (and therefore terminated its review into this matter).

102. Based on the above, including the facts referred to throughout this submission, Envestra considers that criterion (a) is not satisfied as continued coverage of the WWGDN will not promote a material increase in competition of the Wagga Wagga gas sales market. Envestra therefore submits that coverage of the network should be revoked.

103. Envestra notes that this view is consistent with the conclusion reached by AAC:

Indeed, such a conclusion [that criterion (a) is satisfied] is counter to the significant factual evidence set out in this report. This evidence shows low levels of retail competition in all markets with a contract carriage model (New South Wales, Queensland and South Australia), particularly in regional areas such as Wagga Wagga. In nearly all cases, the relevant regional gas distribution networks are covered. This strongly suggests that network coverage is not likely to, nor has it, promoted a material increase in competition in the dependent retail markets. Rather, the high cost and risks, particularly associated with the contract carriage model, relative to the potential benefits explain the limited competition in regional markets operating within a contract carriage model.<sup>63</sup>

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<sup>63</sup> ACIL Allen Op. Cit. paragraph 138

### 3. Coverage criterion (d) - Public interest test

104. Criterion (d) is satisfied where it can be shown that access (or increased access) to the pipeline services provided by means of the pipeline would not be contrary to the public interest. The NCC in its draft recommendation found that criterion (d) is satisfied.<sup>64</sup> Specifically, the NCC found that:

- Envestra's costs of \$2.3 million for preparing and gaining approval for an Access Arrangement to be excessive;<sup>65</sup>
- related to the above, that the costs of full regulation of the WWGDN are within Envestra's control, and as such, *should* be able to be reduced due to synergies that are *likely* to exist across Envestra's business;<sup>66</sup>
- the costs of negotiating terms and conditions of access to the WWGDN if it were to be uncovered *may* involve significant costs, which will erode the regulatory cost savings suggested by Envestra;<sup>67</sup> and
- the costs of full regulation of the WWGDN are "unremarkable" and *unlikely* to exceed the benefits that would flow from the promotion of competition due to continued access on fair and reasonable terms through continued coverage of the WWGDN.<sup>68</sup>

105. This section firstly comments on the matters raised by the NCC regarding the proper interpretation/application of criterion (d) before addressing the above reasons regarding the NCC decision that the costs of coverage are unlikely to exceed the benefits.

#### 3.1. Application of criterion (d)

106. The NCC has indicated, based on its interpretation of the High Court Pilbara Rail Decision<sup>69</sup>, its views regarding the manner by which criterion (d) is to be properly applied:

The Council considers that the preferable approach to coverage criterion (d) is to seek generally to identify any matter that could mean access (or increased access) might be contrary to the public interest and then assess whether the likelihood and consequences of that matter make access contrary to the public interest. The Council considers that this approach is more consistent with the Pilbara Rail decision in that it involves a judgment that the Council is well able to advise on, and a Minister is well placed to make, rather than a detailed technical examination of costs and benefits for which only partial information is likely to be available.

107. Envestra generally accepts the manner by which the NCC has interpreted its requirements under criterion (d). However, in exercising "a discretionary value judgement", Envestra considers that the following extracts from the High Court Pilbara Rail Decision are instructive::

... when a discretionary power of this kind is given, the power is "neither arbitrary nor completely unlimited" but is "unconfined except in so far as the subject matter

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<sup>64</sup> NCC Op. Cit. paragraph 5.43

<sup>65</sup> NCC Op. Cit. paragraph 5.34

<sup>66</sup> NCC Op. Cit. paragraph 5.36

<sup>67</sup> NCC Op. Cit. paragraph 5.37

<sup>68</sup> NCC Op. Cit. paragraph 5.41

<sup>69</sup> The Pilbara Infrastructure Pty Ltd v Australian Competition Tribunal (2012) 290 ALR 750.

and the scope and purpose of the statutory enactments may enable the Court to pronounce given reasons to be definitely extraneous to any objects the legislature could have had in view”.

108. Envestra interprets this as saying that the NCC (and Minister) do not have unfettered discretion in exercising any discretionary powers that are required in applying criterion (d). That is, the matters that the NCC could consider are “neither arbitrary nor completely unlimited”. This constrains the matters under consideration to those that are relevant to the statutory requirements. In addition, any exercise of judgement is to be reasonable having regard to the relevant facts/information before the decision maker.
109. In applying criterion (d), Envestra has sought to quantify the likely costs and benefits of continued coverage of the WWGDN. This consideration is based on several assumptions that have been informed by fact. Envestra believes that its assessment has considered all relevant matters that are relevant to a consideration of the public interest of continued coverage and that its analysis is reasonable.

### 3.2. Estimate of regulatory costs for Wagga Wagga

110. In the draft recommendation the NCC concluded:

The Council accepts that the costs of full regulation of the WWGDN are significant although it considers the quantum may be disputed. The Council notes that applications put to it for light regulation of covered pipelines put the costs savings from removing the requirement to have an access arrangement within the range \$400 000–1.5 million. While direct comparisons cannot be made the Council considers Envestra’s stated \$2.3 million cost for preparing and gaining approval for an access arrangement to be excessive.<sup>70</sup>

111. The retailers also expressed a view that Envestra’s estimated costs of regulation are high. The NCC accurately summarised the retailer positions in the draft recommendation as follows:

Origin states that based on its experience, a smaller network is likely to require a less onerous access arrangement. The ERAA also queries Envestra’s claims that the cost of an access arrangement is independent of the size of the network. Origin also notes the WWGDN is a less complex system and a smaller proportion of Envestra’s overall business, particularly when compared to Envestra’s South Australian and Queensland networks. Origin considers that developing an access arrangement for the WWGDN should be less onerous and costly.<sup>71</sup>

112. Envestra considers that the neither the NCC nor the retailers have given due consideration to the approach adopted by Envestra in developing the forecast regulatory cost for Wagga Wagga. Envestra has relied upon the most recent information on the actual costs of undertaking full access arrangement reviews in Victoria, South Australia and Queensland. These costs have then been adjusted to account for the small size of the WWGDN. The adjustments made were the:

- removal of all costs associated with developing operating and capital expenditure forecasts – which is reflected in a \$1.4 million reduction in internal labour costs when compared to Victoria;

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<sup>70</sup> NCC Op. Cit. paragraph 5.34

<sup>71</sup> NCC Ibid. paragraph 5.31

- removal of all legal costs – which is reflected in a \$0.4 million reduction when compared to Victoria; and
- removal of all appeal costs – which costs amounted to around \$0.4 million for both South Australia and Queensland.<sup>72</sup>

113. Envestra has therefore incorporated significant “synergies” and had due consideration to the different size (or scope) of a full access arrangement review in Wagga Wagga relative to our larger networks. For example, the forecast regulatory costs in Wagga Wagga are around 30% lower than the actual costs that were recently incurred in Victoria, 35% lower than actual costs incurred in Queensland and 45% lower than actual costs incurred in South Australia.

114. Further, in its submission to the NCC, Origin Energy also had regard for the fact that Envestra’s direct regulatory expense for the WWGDN of:

...\$2.3 million represents more than total capital expenditure on the network over the current regulated period, and over two thirds of the operational expenditure budget. It is hard to understand how it can be a commercial undertaking for Envestra to spend as much on the network’s five year capital outlay solely on one regulatory application.<sup>73</sup>

115. This is factually incorrect. As advised to the NCC in Envestra’s response to retailer submissions:

...Origin Energy’s submission has compared the regulatory costs to what it considered to be the capital expenditure and operating expenditures for Wagga Wagga over a five year period. The costs referred to in the Origin Energy submission were in fact for the year 2011-12 only.<sup>74</sup>

116. The NCC expressed a view in its draft recommendation that it “is of the view that some of the regulatory costs identified by Envestra may not evaporate if coverage is revoked”. Envestra however expects that the costs of administering price adjustments and non-price terms to be immaterial, and as such, unlikely to influence a decision as to whether criterion (d) is or is not satisfied. The material costs will relate to the operation, management and construction costs associated with running the network.

117. Envestra therefore considers that the retailer submissions were based on unsubstantiated assertions, ignore the facts set out in Envestra’s application regarding the nature and the quantum of costs or were otherwise based on errors. Envestra considers that its approach to forecasting regulatory costs for Wagga Wagga takes into consideration actual cost information relating to Envestra’s most recent review processes, incorporates aggressive assumptions regarding expected synergies/scope savings, and as such, reflects a best estimate arrived at on a reasonable basis.

### 3.3. Ongoing regulatory savings/synergies

118. Retailers have also suggested regulatory costs should diminish over time due to synergies across Envestra’s networks. Origin Energy stated in its submission:

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<sup>72</sup> Envestra Wagga Wagga Network Revocation Submission 1 May 2013 paragraph 113

<sup>73</sup> Origin Energy Op. Cit. p4

<sup>74</sup> Envestra (Letter to the NCC responding to retailer submissions) 5 June 2013 p 3



...we would expect to see synergies across Envestra's business units. The reviews relate to similar subject matter and Envestra could utilise overlapping advice from external advisors.<sup>75</sup>

119. The NCC agreed, stating in its draft recommendation:

Many of the costs to Envestra of full regulation of the WWGDN are within its control and should be able to be reduced due to synergies that are likely to exist across Envestra's business.<sup>76</sup>

120. Again, Envestra considers that the retailer submissions and NCC draft recommendation have not given due consideration to the factual information regarding the costs of undertaking a full access arrangement review set out in Envestra's application. For example, table 9 in Envestra's application showed actual costs incurred by Envestra for its three most recent regulatory review processes. This showed that regulatory costs have in fact increased overtime and not decreased due to, for example, past learnings as asserted in the retailer submissions.

121. As explained in our application, the reason why regulatory costs do not decrease over time is the continual evolution of regulatory debate and changes in regulatory requirements/expectations over time. The example provided in our application was the current AER Better Regulation program, which will result in changes to the methodology and information that the AER will require in assessing, for example, businesses expenditure proposals.

122. The AER has recently released a "Draft Consumer Engagement Guideline"<sup>77</sup>, which places additional requirements on Envestra to consult with stakeholders as part of an Access Arrangement review process. Importantly, these requirements will require Envestra to incur additional costs on customer consultation that were not incurred in previous regulatory review processes (including in our most recent Victorian review).

123. Envestra again notes the considerable synergies that have been factored into its forecast regulatory costs, as explained in the previous section.

### 3.4. Costs of negotiating terms and conditions

124. Regarding the costs of negotiating terms and conditions if the WWGDN were to be uncovered, the NCC notes:

Envestra and the existing and potential users of the WWGDN will need to negotiate the full range of access terms and conditions—a process which may involve significant costs. It may well be that the costs of negotiating access on a commercial basis will increase should coverage be revoked which will in turn erode the regulatory cost saving suggested by Envestra.<sup>78</sup>

125. As explained in response to criterion (a), Envestra does not expect the costs of negotiating terms and conditions for the uncovered WWGDN to be "significant" or any different from those incurred in a regulated network. This is because of Envestra's stated intention to apply the current AER approved Wagga Wagga terms and conditions until agreement is reached with the retailers to shift across to a

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<sup>75</sup> Origin Energy Op. Cit. p 4

<sup>76</sup> NCC Op. Cit. paragraph 5.36

<sup>77</sup> AER *Draft Consumer Engagement Guideline for Network Service Providers* July 2013

<sup>78</sup> NCC Op. Cit. paragraph 5.37



nationally consistent set of AER approved terms and conditions. Regardless, the terms that will apply to our uncovered networks will reflect the regulated terms approved by the AER, as is current business practice.

126. On the related matter of light regulation, Envestra noted in its submission that:

Envestra does not have any direct experience with light regulation. All else equal, Envestra would expect the costs of light regulation to be less than full regulation by virtue of the fact that a limited Access Arrangement proposal only requires the approval of non-price terms and conditions and certain other information. Envestra estimates, based on its experience with full regulation, that such an approval process would cost around \$0.25 million for both Envestra and the AER.<sup>79</sup>

Envestra in its application went on to state that it:

... considers that the costs of light regulation are less certain and could potentially lie within a large range. Envestra considers it reasonable to assume that the costs of light regulation could be somewhere between \$0.25 million up to and including the cost of full regulation set out in table 10.<sup>80</sup>

127. While there is the potential for costs to increase under light regulation, as suggested in the above, Envestra considers this to be highly unlikely given its approach of relying on AER approved terms and conditions for its unregulated networks. To this end, Envestra notes a point made earlier in this submission that at no stage in our history has it been necessary for a retailer to resort to an arbitration of Envestra's terms in respect of either our covered or uncovered networks.

128. Envestra therefore considers that its first characterisation of regulatory costs is most appropriate, being around \$0.25 million. This reflects the total costs to Envestra, the AER and other stakeholders of developing AER approved terms and conditions under a light handed form of regulation.

### 3.5. Conclusion on criterion (d)

129. Criterion (d) is satisfied where it can be shown that access (or increased access) to the pipeline services provided by means of the pipeline would not be contrary to the public interest. A measure of the public interest requires a reasonable comparison of the expected benefits of coverage relative to the expected costs of that coverage.

130. In terms of costs, Envestra for the reasons outlined in this section considers that its estimate of regulatory costs for a full access arrangement review for the WWGDN of \$2.8 million, as set out in its initial application, to reflect a best estimate arrived at on a reasonable basis. The estimate is based on recent actual information of similar costs and incorporates aggressive assumptions of expected synergies/scope savings.

131. In terms of benefits, the NCC did not seek to quantify the actual benefits of continual coverage. This most likely reflects the NCC's view that it only needs "to seek generally to identify any matter that could mean access (or increased access) might be contrary to the public interest." Envestra on the other hand considered that there are no (or zero) benefits of continual coverage for the reasons set out in its assessment of criterion (a).

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<sup>79</sup> Envestra *Wagga Wagga Network Revocation Submission* 1 May 2013 paragraph 116

<sup>80</sup> Ibid. paragraph 120

132. Envestra notes the key conclusion of the NCC that:

... in relation to the WWGDN these [regulatory] costs are unremarkable and unlikely to exceed the benefits which would flow from the promotion of competition due to continued access on fair and reasonable terms through continued coverage of the WWGDN.

133. Envestra notes that the characterisation of regulatory costs as being "unremarkable" is in contrast to its earlier consideration that the "Council accepts that the costs of full regulation of the WWGDN are significant". The difference in characterisation might reflect the views expressed by the NCC in paragraph 5.35 that such costs are unlikely to evaporate.

134. That aside, Envestra has reaffirmed in this submission its view that there are no benefits of continued coverage. Envestra has explained in its consideration of criterion (a) that coverage has not so far promoted material retailer participation/competition in the gas sales market served by the WWGDN. Envestra has also explained that any assertion that retail competition will increase if retail price regulation is removed and coverage is retained is highly speculative and inconsistent with a proper assessment of:

- the actual barriers to retailer participation in the smaller regional markets – which reflects the high costs and risk of entering these regional markets relative to the small potential benefit, which matter is made worse in NSW as a result of the contract carriage model that exists;
- the actual data supporting the above demonstrating that the limited actual levels of retailer participation/competition in all regional networks served by Envestra's networks, particularly where a contract carriage model is in place; and
- that actual observations of retailer participation/competition explained in the previous point do not improve to a material extent following the removal of retail price regulation. (and that this position does not change following.

135. Envestra is therefore of the view, as per its initial application to the NCC, that the costs of continual coverage will exceed the benefits, and as such, criterion (d) is not satisfied.

## 4. Conclusion

136. The WWGDN can only remain covered if it can be demonstrated that all four pipeline coverage criteria set out in section 15 of the NGL are satisfied. The four criteria are:

- access (or increased access) to the services provided by the pipeline would promote a material increase in competition in at least one other market (criterion (a));
- it would be uneconomic to develop another pipeline to provide the services supplied by the pipeline (criterion (b));
- access (or increased access) to the services provided by the pipeline can be provided without undue risk to human health or safety (criterion (c)); and
- access (or increased access) to the services provided by the pipeline would not be contrary to the public interest (criterion (d)).

137. In its revocation application submitted to the NCC on 1 May 2013, Envestra contended that continued coverage of the WWGDN is not warranted as neither criterion (a) nor criterion (d) are satisfied.

138. In its draft recommendation of 17 June 2013 the NCC came to a contrary conclusion. The NCC's preliminary view was that continued coverage of the WWGDN is warranted as it:

- will promote a material increase in competition in the downstream gas sales market in the area served by the WWGDN, and as such, criterion (a) is satisfied; and
- is in the public interest as the costs of continued coverage is outweighed by the benefits, and as such, criterion (d) is satisfied.

139. In coming to its conclusion, the NCC had regard to several factors, which in its view, have the potential to limit competition if coverage of the WWGDN was revoked. Envestra has assessed those arguments put by the NCC in support of maintaining coverage against the available information. Envestra considers the available information supports a conclusion that criterion (a) and criterion (d) are not satisfied and therefore coverage of the WWGDN should be revoked.

140. With regards criterion (a), Envestra does not consider the criterion satisfied as:

- the removal of coverage of the WWGDN will have no affect on the scope for the removal of price regulation of gas sales in NSW. Both the AEMC in its draft recommendation into retail energy competition and IPART in its review of retail gas prices for 2013 to 2016 found the NSW retail energy market sufficiently competitive to allow the removal of retail price regulation. Coverage of the gas distribution network was not considered by either the AEMC or IPART as a relevant factor in influencing the effectiveness of retail competition and therefore deciding whether retail price regulation should be removed;
- it is the small size of the WWGDN offering little benefit to offset the costs and risks of the contract carriage model that acts as the most significant barrier to retailer entry, not the access terms to the WWGDN. A retailer must enter into long term bilateral contacts for wholesale gas and pipeline capacity regardless of whether the WWGDN is covered. The high costs/risk and low expected benefits explains the empirical evidence that, irrespective of the coverage status of a network, retailer competition is lower in regional gas sales

markets that operate on a contract carriage model (New South Wales, Queensland and South Australia) rather than a market carriage model (Victoria);

- Envestra has committed to apply the AER approved terms and conditions if coverage of the WWGDN is revoked, which is consistent with Envestra's current business practice. There is a reputational risk if Envestra does not act in accordance with these commitments and any party can apply for the WWGDN to be covered again. Further, and as suggested by AAC, Envestra is willing to enter into an undertaking with the Minister or contract with the retailers to provide any further certainty that might be required on this issue;
- gas is sufficiently substitutable by electricity, which as recognised by the AEMC, works as a market mechanism to control gas (including network) prices. CEG has estimated that a residential gas bill will be around [REDACTED] than an electricity bill for the equivalent appliances in Wagga Wagga. This will place Envestra under significant pressure to retain customers and therefore act as a further constraint on distribution prices given the long life of Envestra's assets;
- retailers possess and use their countervailing market power. The pricing outcomes for Envestra's unregulated tariffs have been lower and more stable than for regulated tariffs. Unregulated tariffs are set bilaterally with the retailers which confirms, if the WWGDN was revoked, that retailers would utilise their market power to influence price; and
- AEMO recently ceased the initiative to standardise transactional interfaces in NSW that the NCC had regard to on the basis that the costs of this initiative outweighed the benefits. Such inefficient investment in the case of small regulated network would not be permitted under the National Gas Rules in any event.

141. With regards criterion (d), Envestra does not consider the criterion satisfied as:

- in terms of costs, the estimate of regulatory costs for a full access arrangement review for the WWGDN of \$2.8 million reflects the best estimate arrived at on a reasonable basis. The estimate is based on recent actual information of similar costs and incorporates assumptions of expected synergies/scope savings, and as such is not excessive;
- in terms of benefits, Envestra has the view that there are no benefits of continued coverage. Envestra has explained in its consideration of criterion (a) that coverage will not promote material (or any additional) retailer participation/competition in the gas sales market served by the WWGDN.

142. Based on the above, Envestra considers both criterion (a) and criterion (d) are not satisfied. Continued coverage of the WWGDN will not promote a material increase in competition of the Wagga Wagga gas sales market and nor is it in the public interest as the costs of regulation exceed the benefit. Coverage of the WWGDN should therefore be revoked.

143. Envestra notes the independent expert advice from AAC reached a similar:

... ACIL Allen is of the view that the Council has not demonstrated that pipeline coverage criteria (a) has been satisfied. That is, the Council has not demonstrated that access (or increased access) to pipeline services provided by means of the WWGDN would promote a material increase in competition in at

least one market (whether or not in Australia), other than the market for the pipeline services provided by means of the WWGDN.<sup>81</sup>

And:

Indeed, such a conclusion is counter to the significant factual evidence set out in this report. This evidence shows low levels of retail competition in all markets with a contract coverage model (New South Wales, Queensland and South Australia), particularly in regional areas such as Wagga Wagga. In nearly all each cases, the relevant regional gas distribution networks are covered. This strongly suggests that network coverage is not likely to, nor has it, promoted a material increase in competition in the dependent retail markets. Rather, the high cost and risks, particularly associated with the contract carriage model, relative to the potential benefits explain the limited competition in regional markets operating within a contract carriage model.<sup>82</sup>

Envestra therefore submits, for the reasons outlined in this submission, that coverage of the WWGDN should be revoked.

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<sup>81</sup> ACIL Allen Op. Cit. paragraph 137

<sup>82</sup> Ibid. paragraph 138