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Mr Peter Hallahan
Secretary
Senate Economics Legislation Committee
Suite SG.64
Parliament House
CANBERRA ACT 2600

Dear Mr Hallahan

**AGL Submission to Senate Economics Legislation Committee
Inquiry:
Trade Practices Amendment (National Access Regime) Bill 2005**

1. Introduction

The Australian Gas Light Company (AGL) is pleased to make this submission to the Senate Economics Legislation Committee.

AGL is a major owner/investor in energy infrastructure in the gas and electricity industries in Australia, and is a committed supporter of the ongoing Ministerial Council of Energy (MCE) energy reform process.

AGL was part of a broad industry group that made submissions to the Productivity Commission's (PC) review of the National Access Regime (Part IIIA of the Trade Practices Act) in 2001. More recently, AGL has made submissions to the Commission's review of the Gas Access Regime. Several of the Commission's key Part IIIA recommendations have been recommended for the gas regime (2004). For reasons discussed in this submission, AGL sees it as vital that the Bill before the Committee fully incorporates the Government's response to the Productivity Commission's Part IIIA review.

2. Importance of the Part IIIA recommendations

Part IIIA of the Trade Practices Act together with the Competition Principles Agreement comprises the framework for regulation of essential infrastructure services in Australia.

As noted by the Productivity Commission, the focus of the National Access Regime is on infrastructure services that are essential inputs to final (downstream) or upstream services, and involve a 'natural monopoly'

technology. This technology means that it is unlikely to be profitable for more than one firm to provide the essential service. Society gains from this 'single supplier' arrangement because it potentially provides a lower cost service than the competitive market model with multiple suppliers.

However, a single supplier is in a position to use market power. A common solution to this problem is to impose some form of 'access' framework, often including price regulation, whereby potential users can gain access to the service on reasonable terms and conditions. Nevertheless, as the Productivity Commission has noted in several of its reviews, access regulation is not without its own costs, the chief one being the potential to deter investment in essential infrastructure:

Any such impacts on investment are a cause for concern. This is because the costs of failing to invest in essential infrastructure are likely to be larger than the costs of monopoly pricing of the services it provides. Hence, it is crucial that access regulation gives proper regard to incentives to invest.¹

In its review of Part IIIA, the Commission identified 'significant deficiencies' in the regime, including:

- The lack of an overarching objective and pricing principles to guide access seekers, service providers and regulators;
- An emphasis on 'promoting competition' rather than efficiency.

To remedy these deficiencies, the Commission's recommendations included:

- An objects clause for Part IIIA with a clear emphasis on economic efficiency (including a statement that the clause would provide a framework and guiding principles for industry-specific regimes);
- A set of specific pricing principles designed to promote the efficient use of essential infrastructure without detracting from efficient investment incentives.²

From the above outline, there can be no doubt that the PC saw its recommendations as improving the capacity of the National Access Regime to deliver economically efficient outcomes through efficient and timely investment. The PC also recognised that an amended Part IIIA would provide an important model for industry-specific regimes (such the gas and electricity regimes) thus establishing a basis for consistent access regulation across jurisdictions.

The recent report of the Prime Minister's Exports and Infrastructure Task Force drew attention to the need for transparent and predictable regulatory settings to encourage efficient commercial investment. AGL considers that implementation of the Part IIIA recommendations will strongly support this objective.

¹ Productivity Commission (2001) Review of the National Access Regime, *Position Paper*, p xii

² *Ibid*, p 199

3. Lack of pricing principles in the current Bill

Given the Government's response to the PC of February 2004, AGL had understood that the Productivity Commission's pricing recommendations (as agreed by the Government) would be established within the legislation. In AGL's view, inclusion of these pricing principles is crucial to the Treasurer's Second Reading Speech objectives of:

- Clarifying the regime's objectives and scope;
- encouraging efficient investment in new infrastructure in Australia;
- strengthening incentives for commercial negotiation; and
- improving the certainty, transparency and accountability of regulatory processes.

The Government's February 2004 response said that the establishment of statutory pricing principles would:

Provide guidance for pricing decisions and contribute to consistent and transparent regulatory outcomes over time. They will also help to provide certainty for investors and access seekers alike and facilitate commercial negotiations between parties.

AGL completely supports the Government's reasons for establishing statutory pricing principles, and is therefore puzzled and concerned with their omission from the Bill before the Committee. No explanation is offered in the Explanatory Memorandum or Second Reading Speech for this omission. Instead, Section 44ZZCA of the Bill simply delegates to the Commonwealth Minister the discretion to determine pricing principles by legislative instrument at a future time. There are a number of immediate issues arising from this discretion:

- There is no timeframe in which the Minister must introduce the pricing principles;
- There is no indication as to whether these principles will be the same as those agreed in the Government's response; and
- Omission of the agreed principles is likely to significantly diminish the benefits of the amendments now before the Committee by creating uncertainty as to the Government's immediate and long term intentions for infrastructure regulation (See section 4 below).

AGL believes that omission of pricing principles in the current Bill does not meet the criterion of fully incorporating the Government's own responses to the Productivity Commission in its legislation. In its interim response (2002) the Government indicated that it would accept the Commission's recommended pricing principles (with minor amendments). Following consultation with the States and Territories, the Government's final response (2004) confirmed that it accepted the amended principles and that they would be included in legislation amending Part IIIA. This has clearly not occurred.

Another concerning aspect of the omitted principles is the length of time since they were first committed to and the lack of signals as to the

Government's intentions. It is now approaching three years since the Government's original acceptance of the pricing principles. In the interim, there has been no indication that the principles would be other than as agreed to by the Government, and (most importantly) that they would *not* be introduced by the same legislation that incorporated all the other agreed amendments to Part IIIA. This long silence on the legislative introduction of the pricing principles can only serve to exacerbate the significant concerns of infrastructure investors outlined below.

4. Concerns arising from legislative instrument

As indicated by the previous discussion, a Ministerially determined legislative instrument to establish the key pricing principles of Part IIIA was not anticipated by infrastructure investors.

This unanticipated action on the Government's part leads to significant concerns for investors about the Ministerial potential to vary the Government-agreed pricing principles unilaterally, both upon their introduction by the Minister and at some future stage. These concerns could be immediately allayed if the agreed pricing principles were incorporated into the amending Bill.

The Productivity Commission has recently confirmed its support for the Government's agreed Part IIIA pricing principles by recommending the same principles in its 2004 review of the Gas Access Regime. This supports the observation in section 2 above, that the Part IIIA principles provide a firm model for similar principles in other access regimes. By omitting one of the most important elements of the Part IIIA model from the legislation, the Government has unnecessarily engendered concerns about whether the Government's agreed pricing principles will be included in Part IIIA at all.

AGL believes that it is vital that the pricing principles as agreed by the Government be included in the legislation, in order to attain the objectives of:

- the Productivity Commission, by establishing statutory pricing principles specifically designed to promote the efficient use of essential infrastructure;
- the Government itself as expressed in its response to the PC, by providing guidance for pricing decisions and contributing to consistent and transparent regulatory outcomes over time.

Nevertheless, even if the pricing principles introduced by a Ministerially determined legislative instrument were those agreed to by the Government, there would still be major unresolved concerns because:

- The mechanism for changing the pricing principles is uncertain, and there is a significant possibility that further changes could be made

without appropriate consultation with the States and Territories and industry; and

- It is contrary to the principle of separation of powers that such a significant change should be made by a Minister without the full involvement of Parliament.

5. Amendments to the Bill

AGL strongly supports inclusion of the pricing principles set out in the Government's response to the Part IIIA review through amendment to the current Bill. The principles should also be extended to the Competition Principles Agreement.

There is a counter-view to the above position, which suggests that administrative flexibility might be attained by using a legislative instrument, rather than incorporating pricing principles into legislation directly. This would enable the principles to be changed in the future without full parliamentary debate and approval as would be necessary with amended legislation. There are several reasons why flexibility of this kind is neither desirable nor needed:

- The pricing principles agreed to by the Government are supported by the Productivity Commission's investigations into both the national and gas access regimes. These investigations involved wide-ranging public consultation and debate. The Commission has established the soundness of the principles from economic and policy viewpoints, and the Government has formally agreed to them. There is no discernible reason why these principles would need to be changed in the future;
- The need for investment certainty clearly outweighs any perceived need for administrative flexibility or convenience. Flexibility of the kind introduced in current Bill is costly, since it engenders investment uncertainty with adverse economic results.

However, if this view were to prevail that it is appropriate to amend the pricing principles without Parliament's full review, then AGL considers that the following provisions are essential in the Bill:

- The legislation should contain the Government's agreed pricing principles;
- Before any revision of the initial pricing principles, the Minister must consult with the States and Territories and with industry on the proposed revisions;
- Any proposed revisions to the pricing principles must be consistent with the objectives clause of the Part IIIA national regime (this clause is included in the current Bill); and

- The Minister must be satisfied that the operation of Part IIIA will be enhanced consistent with its objectives and give reasons as to why the principles should be revised.

6. Note on other submissions

AGL is aware that several industry associations representing infrastructure investors (notably APIA, ENA and AusCID) have made submissions to the Committee on the current Bill and have highlighted the omission of the Part IIIA pricing principles, with recommendations that the Government-agreed principles be included in the Bill. AGL supports these positions and encourages the Committee to further discuss this very important issue with those associations.

Yours faithfully

Robert Wiles
General Manager Regulation and Policy