
Regulatory issues

Electricity

Dispute resolution—National Electricity Code change

In July 2000 the National Electricity Code Administrator (NECA) lodged applications with the Commission for authorisation of amendments to the National Electricity Code. The proposed amendments deal with the code dispute resolution arrangements.

On 13 March 2002 the Commission issued its determination. It decided to grant authorisation, on the condition that several amendments were made to the proposed code changes. The Commission's determination outlines its analysis and views. The full determination can be found on the ACCC website at <<http://www.accc.gov.au>> and a summary in ACCC Journal no. 38. Subject to the conditions imposed, the Commission considers the code changes an improvement on the existing code dispute resolution mechanism as they provide a clearer, more streamlined framework in which market participants can actively resolve disputes.

Gas

Tender for the supply of gas to the Loddon Murray region of Victoria

On 1 November 2001 the Commission released its decision to approve an application lodged by the Loddon Murray Gas Supply Group (LMGSG) to conduct a competitive tender. This tender was to determine a preferred supplier of gas for the Loddon Murray Region of Victoria and allows the successful bidder to construct both a transmission and distribution pipeline to the area. The Victorian Office of the Regulator General (now the Essential Services Commission) released its decision approving the distribution components of the tender at the same time.

Under the access arrangement approval process, proposed tariffs for covered pipelines are submitted

to the Commission for assessment. Alternatively, for new pipelines, the gas code allows tariff-related aspects to be established through a competitive tender process. The Commission's role would be to ensure that the tender rules allow tariffs to be determined by competitive forces. When the tender has been conducted in accordance with the approved tender rules, the tariffs are 'locked in' for the initial access arrangement period.

After the Commission's approval of the LMGSG's request, the group conducted the tender and bidding closed on 15 March 2002.

On 9 April 2002 the Commission was advised by the LMGSG that no formal bids had been received. Despite this, some companies expressed an interest in the project and LMGSG indicated its intention to approach them for further information with the aim of facilitating the venture.

GasNet and VENCORP access arrangement revisions

The Commission has begun the first scheduled review of the GasNet Australia (Operations) Pty Ltd (GasNet) and the Victorian Energy Networks Corporation (VENCORP) gas transmission access arrangements which it approved in 1998. GasNet and VENCORP lodged revisions with the Commission on 28 March 2002 to come into effect on 1 January 2003.

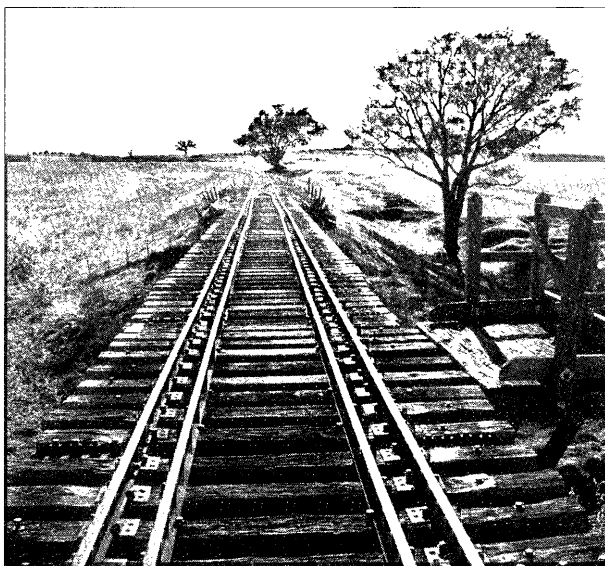
Under the market carriage capacity management system operating in Victoria, users pay tariffs to both the system owner, GasNet, and the independent system operator, VENCORP. About 85 per cent of the combined tariff is paid to GasNet.

Matters being considered by the Commission include:

- the relationship between the two service providers and between their access arrangements, in particular a proposal by GasNet that it not make any services available
- GasNet's proposal to 'reopen' the capital base, increasing the 1 January 1998 value by \$35.8 million

- GasNet's proposal to include the cost of the south-west pipeline under the gas code's economic feasibility test
- the proposed merger of the GasNet principal transmission system and western transmission system access arrangements
- GasNet's proposed real tariff increase of more than 10 per cent over the second access arrangement period
- the proposed introduction of prudent discounts
- GasNet's proposed tariff restructure whereby injection charges would be levied on the 10 peak days (rather than five) and the withdrawal charge would be solely levied on total volume (rather than one charge on peak and another on total volume)
- VENCorp's expected real tariff reduction of about 10 per cent for metering charges and about 4 per cent for commodity charges over the second access arrangement period
- VENCorp's proposal to move from annual to five-yearly budget approval for registration and commodity tariffs.

The Commission has asked for submissions from interested parties on the proposals and released an issues paper. The Commission is currently considering these submissions and expects to issue its draft decision shortly. It will then hold a public forum on the issues raised in that decision and the Commission's proposed approach. After considering further submissions, the Commission will issue its final decision.



Rail

Australian Rail Track Corporation access undertaking accepted by the Commission

On 1 May 2002 the Commission reached its first decision on a rail track access undertaking under Part IIIA of the Trade Practices Act. The undertaking was lodged with the Commission by the Australian Rail Track Corporation (ARTC).

ARTC is a public company, owned by the Commonwealth of Australia, and was established in 1998 to manage the infrastructure and access to the standard gauge rail network connecting the mainland capital cities between Brisbane and Perth. That part of the network which is subject to the undertaking (network) comprises track that links:

- Kalgoorlie in Western Australia
- Adelaide, Wolseley and Crystal Brook in South Australia
- Broken Hill in New South Wales
- Melbourne and Wodonga in Victoria.

The proposal for an access undertaking was submitted to the Commission under s. 44ZZA of the Act. An access undertaking is a legally binding commitment, given by an owner of a nationally significant facility which sets the terms under which access to the facility will be granted. If there is no undertaking in place, access seekers have the option under Part IIIA of the Act of seeking declaration of rail track services. Declaration gives users the right to negotiate terms of access and, if the negotiations prove unsuccessful, the opportunity to have the Commission arbitrate the access dispute.

The undertaking provides a framework for negotiations between ARTC and train service operators who want to access the network. In making the undertaking, ARTC aims to stimulate customer confidence and market growth in the rail industry. The undertaking implements ARTC's policy of equity and transparency as key elements of its procedures for determining access, prices and terms and conditions of agreements. Specifically, the undertaking covers the process of negotiation for access, pricing principles, quality and performance indicators and various network management issues. It also includes an indicative access agreement (IAA) that forms a basis for an agreement between ARTC and an operator.

As required under the Act, the Commission's decision to accept the undertaking followed an extensive process of public consultation, negotiation with ARTC, revisions to the proposal and assessment on the basis of the statutory criteria set out in subsection 44ZZA(3). These criteria impose an obligation on the Commission to ensure that the undertaking, among other things, achieves an appropriate balance between the interests of the infrastructure owner and access seekers and the public interest. The Commission formulated some principles to help the assessment process. These address three broad issues of:

- pricing for access to ARTC's rail track that focuses on efficient outcomes
- processes for gaining access including negotiation and dispute resolution provisions that provide for timely, commercially negotiated outcomes
- providing clear conditions that allow enforceability of the undertaking.

It is the first time this process was followed and resulted in ARTC adopting some significant changes to its original proposal.

The Commission also recognised that, while ARTC is assumed to operate as a commercial, profit-maximising business, the interstate rail network has many of the characteristics common to natural monopolies:

- investment in specialised assets which is, to a large extent, irreversible
- correspondingly high-sunk, fixed costs leading to economies of scale
- network effects.¹

Some of ARTC's customers have significant sunk investments in infrastructure, which could potentially provide ARTC with leverage in commercial negotiations.

There may be some limits to ARTC being able to take advantage of any consequent market power when the nature of the markets in which its customers operate is considered. The majority of

ARTC's revenues, earned from the interstate transport of freight, are earned in markets that are subject to a substantial degree of competition from non-rail sectors, predominantly road and sea. Similarly, prices set by ARTC result in revenues significantly below those needed for an adequate long-term economic rate of return. These factors, together with the fact that ARTC is not vertically integrated, appear to provide an incentive to drive greater productivity from the asset and ensure that the physical asset is maintained to increase rail's relative competitiveness.

Provisions in the undertaking also act as constraints to the misuse of market power. These include ARTC's intention to commit to ongoing reductions in real prices charged to users and a proposed curb on price discrimination. The conditions underscore dependence on growing the amount of traffic on the network and on greater operating and cost efficiency to ensure future profitability. These features include the following.

Floor and ceiling limits to access charges

Access charges will fall between a floor limit and a ceiling limit. The floor limit is defined as the charge for access to a segment which would generate revenue sufficient for ARTC to cover the incremental cost of that segment. The incremental cost excludes depreciation and a return on investment. The ceiling limit would generate revenue sufficient to cover the total economic cost of that segment.

No discrimination between access seekers

In formulating charges, ARTC will not discriminate between alike services where access seekers are operating in the same market.

Indicative access charges

The undertaking includes indicative access charges for access to segments of the network. The way in which these charges may be varied is also specified. Increases are limited to the greater of either the CPI minus 2 per cent or two-thirds of the CPI.

Flexibility enables negotiation

The undertaking, which includes an IAA, is the basis for negotiation between parties to an access agreement and ARTC can only depart from the provisions of the IAA if that is agreed by both parties. This allows for negotiation of aspects of an agreement including access charges and gives access flexibility to assume certain risks or costs itself.

¹ A network effect occurs when users of an infrastructure service benefit from other users deciding to use that infrastructure. In ARTC's case this may include, for example, the ability to connect with other users, the availability of complementary products or reduced network access costs.

However, constraints on ARTC's non-price conduct may be less effective. Clauses in an earlier version of the undertaking, particularly those dealing with negotiation processes, capacity management, network extensions and capacity additions, gave ARTC broad scope in its dealings with access seekers and the Commission considered that they did not satisfy the legislative criteria in Part IIIA.

The Commission made recommendations on these provisions in the draft decision. Subsequently, ARTC amended some provisions to impose more stringent obligations on itself and/or greater safeguards for access seekers. The undertaking thus achieves a more appropriate balance between the interests of the infrastructure owner and access seekers.

The most significant of the modified provisions affecting ARTC's non-price conduct are as follows.

Information on capacity

ARTC has committed itself to providing a significant amount of information on capacity which will enable operators to independently assess the extent of spare capacity on the network.

Conflict resolution

Under the proposal, the Commission was given the role of arbitrator with arbitration being the final step in the conflict resolution process. The Commission accepted this role but made recommendations in the draft decision on the conflict resolution process.

One of these recommendations was that a conflict manager be appointed as a compulsory part of the dispute resolution process. The final undertaking allows for the appointment of a conflict manager if agreed by both parties.

Also arising from the Commission's recommendations, the undertaking contains modifications in respect of dispute resolution allowing the publication of arbitration decisions (subject to consideration of commercial confidentiality) and allowing joint hearings of arbitration where appropriate.

Quality and performance standards

The undertaking requires ARTC to maintain the network in a fit for purpose condition. This, together with provisions in the IAA make ARTC strictly liable for any loss or damage to the track to the extent that it caused or contributed to that loss. These provisions would preclude or deter ARTC, despite its monopoly position from running down the network

to maximise profits. The provisions provide an inbuilt incentive for ARTC and the operators to minimise foreseeable and unforeseeable losses by maintaining and using the network at a high standard. They also ensure that the network is used at an economically efficient level.

The undertaking also requires ARTC to publish performance indicators that can be used by operators and others to monitor performance. The IAA provides for a process whereby specific performance indicators, including financial incentives or penalties pertaining to the achievement of these indicators, can be negotiated between ARTC and individual operators.

The Commission's decision is that, although particular outcomes are not prescribed, the provisions in the undertaking and IAA impose an appropriate obligation on ARTC to discuss and negotiate on service levels.

The undertaking represents an important step towards improving interstate rail access for train operators and can be used, together with the Commission's detailed analysis, as a guide for further access undertakings covering other parts of the interstate rail network. The final decision is now available from the Commission's website at <<http://www.accc.gov.au>>.