



Reference service and rebateable service definitions

Draft rule determination 15 March 2012

The Australian Energy Market Commission has made a draft rule that changes the definition of reference service in the National Gas Rules (NGR). The key purpose of this change is to allow more flexibility in the regulatory treatment of pipeline services by giving the regulator limited discretion to determine which services can be classified as reference services.

Background

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

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

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

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

The AER's rule change request

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

The Commission intends to make a more preferable rule

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

The draft rule does not amend the current rebateable service definition.

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

Reasons for the Commission's decision

The Commission considered that the draft rule will better promote:

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

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

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

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

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

Submissions

The Commission invites stakeholder submissions to its draft rule determination and draft rule. The closing date for submissions is **26 April 2012**.

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