

# Queensland Gas Pipelines

Applications to Revoke Coverage of  
Certain Transmission Pipelines under the  
Queensland Gas Access Regime

## Recommendations

November 2000

National Competition Council

# Contents

<b>1</b>	<b>RECOMMENDATIONS .....</b>	<b>2</b>
<b>2</b>	<b>BACKGROUND.....</b>	<b>4</b>
2.1	THE QUEENSLAND GAS ACCESS REGIME .....	4
2.2	COVERAGE OF PIPELINES UNDER THE QUEENSLAND REGIME .....	4
2.3	REVOCAION OF COVERAGE OF A PIPELINE.....	5
2.4	THE APPLICATIONS.....	6
<b>3</b>	<b>APPLYING THE REVOCATION CRITERIA.....</b>	<b>8</b>
3.1	THE REVOCATION CRITERIA .....	8
3.2	GUIDANCE IN INTERPRETING THE CRITERIA .....	8
3.3	THE RELEVANT PIPELINES AND THE SERVICES PROVIDED BY THOSE PIPELINES.....	9
3.4	THE MARKETS IN WHICH THE PIPELINES PROVIDE SERVICES .....	11
3.5	MEANING OF THE TERM “MARKET” .....	11
3.6	DIMENSIONS OF MARKETS.....	12
3.7	CRITERION BY CRITERION ASSESSMENT.....	13
	<b>APPENDIX 1: THE COUNCIL’S PROCESS.....</b>	<b>34</b>
	<b>APPENDIX 2: SUBMISSIONS RECEIVED BY THE COUNCIL.....</b>	<b>35</b>

# 1 Recommendations

In August 2000, the National Competition Council (**the Council**) received applications to revoke coverage under the Queensland Gas Pipelines Access Regime (**Queensland Regime**) of three transmission pipelines, as listed in Table 1 below.

**TABLE 1 Pipelines Subject to Revocation Applications**

<b>Pipeline Licence</b>	<b>Pipeline Owner</b>	<b>Pipeline Operator</b>	<b>Location/Route</b>	<b>Length (km)</b>	<b>Diameter (mm)</b>
Qld:PPL 3	Oil Company of Australia Limited	Oil Company of Australia Limited	<i>Kincora to Wallumbilla</i>	53	219.1
Qld:PPL 26	Oil Company of Australia (Moura) Transmissions Pty Limited	Oil Company of Australia (Moura) Transmissions Pty Limited	<i>Dawson Valley to Duke Queensland Gas Pipeline</i>	47	168.3
Qld:PPL 61 (formerly Qld2:ML 80032)	Peabody Moura Investments Pty Limited and Peabody Moura Mining Pty Limited	Peabody Moura Mining Pty Limited	<i>Moura Mine to Duke Queensland Gas Pipeline</i>	23	219.1

The effect of revocation is to remove a pipeline from regulation under the National Third Party Access Code for Natural Gas Pipeline Systems (**National Code**). In effect, the owner of the pipeline is relieved of any obligation under the National Code to grant access to third parties.

The Council hereby releases its recommendations that coverage of each pipeline be revoked. The Council's reasons are set out in section 3 of this document. In essence, the Council is not satisfied that regulated access to the pipelines would promote competition in another market or confer net public interest benefits.<sup>1</sup> The Council's recommendations take into account arguments raised by the applicants, submissions lodged by interested parties and discussions with a range of stakeholders.

The applications will now be decided by Senator, The Hon. Nick Minchin, Minister for Industry, Science and Resources. Under the National Code, the Minister has 21 days to decide the matter.

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<sup>1</sup> These issues are raised under coverage criteria (a) and (d). See Section 3 of this paper.

### ***The Council's process***

While the Council considered each application separately, the Council ran joint public consultation processes and presents its recommendations in a single report. The Council regards this as an efficient approach, especially given the overlapping issues raised by two of the pipelines; and common ownership of two pipelines. Further information on process matters is provided at Appendix 1 of this document.

A list of submissions received by the Council regarding the applications is provided at Appendix 2. All submissions were taken into account by the Council in formulating its Draft Recommendations, released in October 2000. The Council called for further submissions upon release of the drafts, but none were received. As no additional issues came to light, the Council's final recommendations mirror its draft positions.

Copies of the applications, the Council's Recommendations and Draft Recommendations are available to interested parties on the Council's web page at [www.ncc.gov.au](http://www.ncc.gov.au)

## 2 Background

### 2.1 The Queensland Gas Access Regime

Queensland has enacted a gas pipeline access regime to provide parties with a method for seeking access to certain gas transmission and distribution pipelines located in Queensland. The regime is contained in the Queensland Gas Pipelines Act, which applies the Gas Pipelines Access Law which includes the National Code<sup>2</sup>.

A copy of the National Code can be found on the Code Registrar's website at [www.coderegistrar.sa.gov.au](http://www.coderegistrar.sa.gov.au).

The regime assists parties wishing to transport gas through gas transmission and distribution pipelines in Queensland to contract on competitive terms for transport with pipeline owner/operators. For example, a mining company may wish to buy gas from a gas producer at a particular production site and transport it to a gas-fired power station at its mining site. Under the Queensland regime, it has the opportunity to negotiate a contract for transport of the gas with the owners/operators of pipelines covered by the regime in accordance with the rules laid down by the regime. In the absence of the Queensland regime, the owners/operators of pipelines might, by virtue of any monopoly powers over the transport of gas between the particular geographic regions, refuse to transport gas or demand a monopoly price for the transport of gas.

The revocation process is designed to determine whether it is appropriate for particular pipelines to continue to be covered by the Queensland regime. The regime provides that applications for revocation must be examined against four coverage criteria. The coverage criteria look at such matters as whether the pipeline confers monopoly power, and whether access to the pipeline would promote competition in another market.

### 2.2 Coverage of Pipelines under the Queensland Regime

The three pipelines for which revocation of coverage is sought became covered by the Queensland gas access regime when they were listed in Schedule A to the National Code. Pipelines listed in Schedule A were covered from the commencement of the Queensland gas access regime.

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<sup>2</sup> The Gas Pipelines Access Law is contained in Schedule 1 to the *Gas Pipelines Access (South Australia) Act 1997* (SA) (the **SA Gas Pipelines Act**) and the National Code, which is contained in Schedule 2 to the SA Gas Pipelines Act.

Where pipelines are covered, the owners/operators of the relevant pipelines must comply with certain obligations under the Gas Pipelines Access Law (including the National Code). These obligations include rules covering such matters as:

- the content and operation of Access Arrangements (Access Arrangements specify the terms, conditions, and prices on which owners/operators offer access);
- the information to be provided by owner/operators to parties interested in obtaining access;
- dispute resolution mechanisms; and
- pricing principles (how the prices in the Access Arrangement are derived).

## 2.3 Revocation of Coverage of a Pipeline

The National Code permits any party to seek revocation of coverage of a pipeline. The party must apply to the Council asking the Council to recommend to the relevant Minister that coverage of a pipeline be revoked. On receipt of the Council's recommendation, the relevant Minister must then decide the matter. For each of the pipelines for which revocation of coverage is sought, the relevant Minister is Senator, The Hon. Nick Minchin, Minister for Industry, Science and Resources.

In reaching a recommendation, the Council is required by section 1.31 of the National Code to consider the criteria for coverage in section 1.9 of the National Code. The Council's assessment of the Applications against these criteria is contained in Section 3 of this document.

Where revocation is granted, the owner/operator of the pipeline is released from its obligations under the Gas Pipelines Access Law (including the National Code). The owner and operator are no longer required by the National Code to submit an access arrangement for the pipeline to the regulator, or to respond to access requests by third parties.

The Queensland Gas Pipeline Act includes a process for administrative (merits based) appeals against a decision to revoke coverage. The process is set out in section 38 of the Gas Pipeline Access Law. In Queensland, administrative appeals from revocation decisions concerning transmission pipelines are heard by the Australian Competition Tribunal (**Tribunal**).

## 2.4 The Applications

The revocation applications relate to three gas pipelines listed in Schedule A of the National Code. The pipelines for which revocation of coverage is sought are listed in Table 1 at the front of this document.

### *Peabody-Mitsui Pipeline*

Peabody Moura Mining Pty Limited (**Peabody Moura**) is the applicant in respect of the Peabody-Mitsui Pipeline. The Peabody-Mitsui Pipeline carries gas from the Moura Mine gas drainage operation to the Duke Queensland Pipeline (formerly the PG&E Queensland Gas Pipeline). Peabody Moura Investments Pty Ltd and Mitsui Investment Pty Ltd (**Moura Joint Venture**) are the joint venture owners of the pipeline, and Peabody Moura is the operator.

The Peabody-Mitsui Pipeline is routed within the Moura Mine mining leases and within the road easement of Three Chain Road and Theodore-Baralaba Road. The pipeline passes approximately 6 km to the east of the township of Moura. The Moura Joint Venture acquired the pipeline from BHP Mitsui Coal Pty Limited in 1999. The pipeline first carried gas in 1996.

The pipeline currently carries gas to:

- (a) the inlet on the Duke Queensland pipeline; and
- (b) the service line inlet for a plant operated by Queensland Nitrates Pty Limited (**QN Plant**).

The gas from the Moura Mine is sold by Moura Sales Pty Limited as agent for the Moura Joint Venture.

The pipeline is also used by Energex to backhaul gas from the Duke Queensland pipeline to the service line inlet for the QN Plant.

The Dawson Valley Pipeline is in the vicinity of the Peabody-Mitsui Pipeline. The two pipelines run parallel for part of their length in a south-easterly direction from the inlet valve on the Duke Queensland Pipeline for approximately 12 km before the Dawson Valley Pipeline deviates south while the Peabody-Mitsui Pipeline continues in a south-easterly direction. The inlet valve of the QN Plant is past this point of deviation. Peabody Moura understands that the owner of the Dawson Valley Pipeline intends to extend its pipeline to include a service line to the QN Plant.

The Peabody-Mitsui Pipeline currently has substantial unused capacity as it is currently only operating at approximately 20% of its nominal capacity of 50 TJ per day.

### *Dawson Valley Pipeline*

Oil Company of Australia Ltd (**OCA**) is the applicant in respect of the Dawson Valley Pipeline (PPL 26). The Dawson Valley transmission pipeline transports gas 47 km from the Dawson Valley gas fields in the Bowen Basin to the Duke Queensland Pipeline.

The pipeline was constructed in 1996 by Conoco Australia as part of its development of the Dawson Valley coal seam methane (**CSM**) gas fields. The pipeline together with the associated gas fields was acquired by OCA in 1998.

As noted above, for 12 km of the length of the Dawson Valley Pipeline it runs alongside the Peabody-Mitsui Pipeline (the pipelines are only 20 metres apart).

The major customers of the gas transported in the pipeline are Origin Energy (which supplies the Boyne Island smelter), Tigor Chemical Company in Gladstone, and Energex (which supplies the QN Plant near Moura).

The Dawson Valley Pipeline only carries gas from the Dawson Valley CSM gas fields. The maximum capacity of the pipeline is 20 TJ per day, and OCA states that it is currently operating at only 35% of this maximum capacity, although OCA expects this figure will rise to 70% of the maximum capacity within 2 years.

### *Kincora Pipeline*

OCA is also the applicant in respect of the Kincora to Wallumbilla pipeline (PPL 3). The Kincora to Wallumbilla Pipeline transports gas 53 km from the Kincora gas processing plant in the Surat Basin to ML1A on the Roma to Brisbane pipeline. The gas transported in the pipeline is sold to Origin Energy, which on-sells it to customers in southeast Queensland.

Hartogen Limited constructed the pipeline in 1977 as part of the development of the western Surat gas fields. OCA acquired the pipeline together with the Surat gas fields and the Kincora gas processing plant in 1990.

Throughput in the year ending June 2000 was 2.7 PJ. This level of throughput is expected to continue for another year, and then decline to 1 – 1.5 PJ per year until recoverable reserves are depleted.

The maximum capacity of the pipeline is 30 TJ per day and OCA states that it is currently operating at no more than 50% of its maximum capacity.



### 3 Applying the Revocation Criteria

This section outlines the criteria in the National Code against which the revocation applications must be assessed, and the reasons underlying the Council's recommendations.

#### 3.1 The Revocation criteria

In reaching its recommendations, the Council is required by section 1.31 of the National Code to consider the criteria for coverage in section 1.9 of the National Code. Where the Council is not affirmatively satisfied that a pipeline meets each of the criteria in section 1.9, the Council must recommend revocation of coverage of that pipeline.

The criteria set out in section 1.9 of the National Code are:

- (a) that access (or increased access) to Services provided by means of the Pipeline would promote competition in at least one market (whether or not in Australia), other than the market for the Services provided by means of the Pipeline;
- (b) that it would be uneconomic for anyone to develop another Pipeline to provide Services provided by means of the Pipeline;
- (c) that access (or increased access) to the Services provided by means of the Pipeline can be provided without undue risk to human health or safety; and
- (d) that access (or increased access) to the Services provided by means of the Pipeline would not be contrary to the public interest.

In considering these criteria, the Council has taken into account the views of the applicants, and of parties that made written submissions as well as other interested parties with whom discussions were held. A list of the parties that made written submissions is at Appendix 2.

#### 3.2 Guidance in Interpreting the Criteria

In interpreting the coverage criteria under section 1.9 of the National Code, the Council has used general principles of statutory interpretation. The Council has had regard to the following specific matters.

First, the Council has had regard to the purpose sought to be achieved in enacting the Queensland gas access regime.<sup>3</sup> Reference has been had to the preamble to the Queensland Gas Pipelines Act to determine this purpose.

Second, pursuant to section 10.5 of the National Code, the Council has had regard to the introduction and overview to section 1 of the National Code:

- where the meaning of the provision in section 1 appeared clear, to confirm the ordinary meaning conveyed by the text of the provision; or
- where the Council considered the provision was ambiguous or obscure, or the ordinary meaning would lead to a manifestly absurd or unreasonable result, to determine the meaning of the provision.

Third, the Council has had regard to decisions of the Tribunal in relation to applications for declaration under Part IIIA of the TPA. This is because in relevant respects the words of the declaration criteria in sections 44G(2) and section 44H(4) of the TPA raise for consideration the same issues as those raised by the criteria set out in section 1.9 of the National Code. The declaration criteria under the TPA have been considered by the Tribunal in the *Australian Union of Students decision* and the *Sydney Airports decision*.<sup>4</sup>

### 3.3 The Relevant Pipelines and the Services Provided by those Pipelines

Each of the criteria in section 1.9 of the National Code requires consideration of whether either the pipeline under consideration or the services provided by it satisfy certain tests. The Council therefore considers it useful to begin by identifying the relevant pipelines and the services provided by them before considering the individual criteria in detail.

‘Service’ is defined broadly in the National Code to mean a service provided by means of a pipeline including (without limitation) haulage services (such as firm haulage, interruptible

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<sup>3</sup> Section 14A, *Acts Interpretation Act, 1954* (Queensland).

<sup>4</sup> *Re Application for review of the decision by the Commonwealth Treasurer & published on 14 August 1996 not to declare the “Austudy Payroll Deduction Service” under Part IIIA of the Trade Practices Act 1974; by the Australian Union of Students* [1997] ACompT 1 (28 July 1997); (1997) 19 ATPR 41-573 and *Re Application for Review of the Declaration by the Commonwealth Treasurer Published on 30 June 1997 of Certain Freight Handling Services Provided by the Federal Airports Corporation at Sydney International Airport* (2000) ATPR 41-754.

haulage, spot haulage and backhaul), the right to interconnect with the pipeline and ancillary services.<sup>5</sup>

The Council considers that for the purposes of considering the applications for revocation of coverage, it is not necessary to define every possible type of gas transportation service.

The definition of service in the National Code says nothing about the geographic scope of the service provided by a pipeline, in other words whether the transportation service is one which is a point to point service, or a more broadly defined service of transporting gas to a particular destination or region.

The essence of a pipeline is that it transports gas between two points. Those two points may be the origin and destination of the pipeline itself. Alternatively, the points may be the origin and some other point along the route.

From the perspective of a gas producer, a transportation service must originate at the relevant gas field. This may occur either by a pipeline having its origin there or a spur line or interconnect being developed to link in with an existing pipeline. A pipeline which transports gas from another field to the same destination point as that to which the first producer wishes to transport gas is of no use to the first producer.

As outlined by the Council in its Final Recommendation in relation to the Eastern Gas Pipeline (**EGP Final Recommendation**) and its Final Recommendation in relation to the Moomba to Sydney Pipeline System (**Moomba Final Recommendation**), there are two possible approaches to service definition. The first involves defining the relevant service in terms of both the start and end points (or regions) of the service. In the case of the three pipelines for which revocation is sought, such an approach would involve the transport of gas from the starting point to all points served by the respective pipelines along their respective routes.

This point to point approach focuses on the key nature of the service provided by pipelines as being a transportation service which is sensitive to both origin and destination.

An alternative approach would be to consider the service to be defined by reference to the destination or the market it serves. The reasoning behind this approach is that since one of the prime objectives of the National Code is to promote competition in relevant upstream and downstream markets, the service definition should focus on the areas of actual and potential competition.

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<sup>5</sup> Section 10.8, National Code

The Council considers that a point to point approach to service definition is more consistent with the language of the Code and the approach to service definition more generally under Part IIIA of the TPA. It also reflects the fact that service definition is concerned with the particular facility at issue.

The Council concludes that, consistent with this approach, the services of the three pipelines for which revocation has been sought may be described as follows:

- the Peabody-Mitsui Pipeline provides gas transport services from the Moura Mine to the Duke Queensland Pipeline as well as to points in between including the service line inlet for the QN Plant;
- the Dawson Valley Pipeline provides gas transport services from the OCA gas fields in Dawson Valley and the Duke Queensland Pipeline as well as to points in between; and
- the Kincora to Wallumbilla Pipeline provides gas transport services from Kincora to ML1A on the Roma to Brisbane Pipeline as well as to points in between.

### 3.4 The Markets in which the Pipelines Provide Services

Having identified the relevant services or products as being the point to point gas transportation services identified above, ordinary market analysis must be used to determine, in the case of each separate product, what market it is in. In other words, for each separate transportation service, it must be determined whether there are any other transportation services competitive with that service.

### 3.5 Meaning of the Term “Market”

In considering the questions of market definition, the Council is guided by the work of the Federal Court, the Tribunal, and the Australian Competition and Consumer Commission in their consideration of market for the purposes of Part IV, as well as the Tribunal's and the Court's consideration of Part IIIA.

The Tribunal has defined ‘market’ in the following way:

*A market is the area of close competition between firms, or putting it a little differently, the field of rivalry between them (if there is no close competition there is of course a monopolistic market). Within the bounds of a market there is substitution – substitution between one*

*product and another, and between one source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive. Re Queensland Co-operative Milling Association Ltd (1976) 25 FLR 169 at 190*

This view of market definition has been accepted by the High Court in the *Queensland Wire* case<sup>6</sup> and was adopted by the Tribunal in the context of Part IIIA of the TPA in the *Sydney Airports decision*.

### 3.6 Dimensions of Markets

The relevant dimensions of markets include the following.

- The product market, that is the types of goods and services in a market. Product markets can be considered separate if their respective products are not substitutable in demand or supply. Products are substitutable in demand (and therefore in the same product market) if consumers will substitute one product for the other following a small but significant change in their relative prices. Substitution in supply occurs when a producer can readily switch its assets from producing one product to another.
- The functional market. Functional market definition focuses on the different steps in a production process. In defining functional markets, the Council has had regard to the Tribunal's approach to functional market delineation in the *Sydney Airports decision* which is consistent with the approach used by the High Court in *Queensland Wire* and developed by Professor Maureen Brunt<sup>7</sup> and Professor Henry Ergas.<sup>8</sup> The Council considers that the two following conditions must be satisfied before markets can be regarded as functionally separate:
  - ◆ The layers at issue must be separable from an economic point of view (economically separable). This involves an assessment as to whether the transaction costs in the separate provision of the good or service at the two layers are so large as to prevent such separate provision from being feasible. In effect, to be in different markets, vertical integration must not be inevitable.

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<sup>6</sup> *Queensland Wire Industries Pty Ltd v The Broken Hill Proprietary Ltd and Another* (1989) 167 CLR 177

<sup>7</sup> Brunt, Maureen (1990), *Market Definition Issues in Australian and New Zealand Trade Practices Law*, 18 *Australian Business Law Review*, 86.

<sup>8</sup> Ergas, Henry (1997), *Submission to the NCC in support of an Application by Carpentaria Transport Pty Ltd*, pp. 1-3.

- ◆ Each layer must use assets sufficiently specific and distinct to that layer such that the assets cannot readily produce the output of the other layer (*economically distinct*). In effect, supply side substitution must not be so readily achievable as to unify the field of rivalry between the two layers.

Markets may be functionally separate even though there is a *one for one* relationship, that is to say, perfect supply and demand side complementarity. A good example of this is rail track and train operations. However, where complementarity is associated with economies of joint production or consumption such that separate provision or consumption was not economically feasible, the services will not be in functionally separate markets.

- The geographic dimension of the market. This refers to the area covered by the market such as national, intrastate or regional markets. The reference to ‘other markets’ in criterion (a) includes markets outside Australia.
- The temporal dimension of the market. This refers to whether the size and scope of the market is likely to change over time. The temporal dimension is particularly relevant where production technologies are continually changing. In order to determine the temporal parameters of markets, the Council generally has regard to long-run rather than short-run substitution possibilities.

### 3.7 Criterion by criterion assessment

**Criterion (a) that access (or increased access) to services provided by means of the pipeline would promote competition in at least one market (whether or not in Australia), other than the market for the services provided by means of the pipeline.**

#### ***Background***

The rationale for this criterion is that access regulation is only warranted where access is likely to create better conditions or a better environment for competition in at least one market other than the market for the services of the gas pipeline. For example, providing access may promote competition in upstream (gas exploration and production) and/or downstream (gas sales) markets.

Before it concludes that a pipeline meets this criterion, the Council must be satisfied that:

- the service to which access is sought is not in the same market as the market or markets in which competition is promoted; and
- access would actually promote a more competitive environment in that other market.

The Council's approach is to:

- verify that the market or markets in which competition is said to be promoted is separate from the market for the service; and, if so, then
- determine if access (or increased access) would promote competition in this separate market or markets.

It is not necessary to define precisely the boundaries of all the possible markets, only to determine whether there are distinct markets.

In order to determine whether the services provided by the three pipelines for which revocation is sought are in the same or different markets from the market or markets in which competition is likely to be promoted, the Council applies the test outlined earlier under the discussion of market definition.

First, the Council must consider the market or markets in which each of the pipelines provides its services.

In relation to the Peabody-Mitsui Pipeline and Dawson Valley Pipeline, both applicants contended that the other pipeline provided services which competed with the services provided by its pipeline. The applicants noted that the pipelines ran alongside one another for part of their length.

As noted above, the Council considers that the services provided by these two pipelines are point to point services.

The Council notes that while the pipelines run side by side for approximately 12 km, there is currently no gas consumer located in proximity to the pipelines in the area where they run side by side and therefore there is currently no person to whom they might provide competing services. The QN Plant is currently connected to the Peabody-Mitsui Pipeline to the south of the area where the two pipelines run in parallel. Peabody Moura informed the Council that OCA intends to build a spur to connect the Dawson Valley Pipeline to the QN Plant. While this spur is not yet completed, the Council considers that once completed, the spur will enable the QN Plant to obtain natural gas either from the Peabody-Mitsui Pipeline or the Dawson Valley Pipeline.

However, the Council notes that while the two pipelines share a common destination and run side by side for approximately 12 km, the two pipelines have different origins. For a natural gas consumer obtaining gas from the OCA gas fields, the Peabody-Mitsui Pipeline does not provide a competing service to the Dawson Valley Pipeline. Nor does the Dawson Valley Pipeline provide a competing service for anyone who wants to obtain natural gas from the Moura Mine. The Council notes that a gas user's ability to switch between suppliers of both gas and gas transportation services are limited by contractual arrangements, which often include medium to long term obligations as well as take or pay components. Accordingly, while the services provided by one of the pipelines may be an effective substitute for the services provided by the other pipeline for some users, the Council does not consider that the ability to switch between the two producers of natural gas is sufficiently easy to integrate the field of rivalry for the services provided by the two pipelines.

Therefore the Council does not consider that the Dawson Valley Pipeline provides services which compete with those provide by the Peabody-Mitsui Pipeline. The Council considers that the two pipelines provide services in separate markets.

In relation to the Kincora Pipeline, OCA stated that the Silver Springs to Wallumbilla pipeline (**Silver Springs Pipeline**) was relatively close to the Kincora Pipeline and could provide all of the services provided by the Kincora Pipeline.

The Council notes that although the Kincora Pipeline and Silver Springs Pipeline share a common destination, the two pipelines have different origins. While both pipelines terminate at Wallumbilla on the Roma to Brisbane Pipeline, the Kincora Pipeline connects to the OCA gas processing plant in Kincora which is south west of Wallumbilla, whereas the Silver Spring Pipeline travels close to due south from Wallumbilla. At Kincora, the two pipelines are over 35 km apart.

In addition, the Council understands that the Silver Springs Pipeline is a raw gas pipeline – it does not transport sales specification natural gas. While some of the gas transported by the Silver Springs pipeline has undergone some processing before being transported, gas transported by the Silver Springs Pipeline requires further processing before it is injected into the Roma to Brisbane Pipeline. The Council understands that, by contrast, the gas transported by the Kincora Pipeline is processed to sales specification at a processing plant in Kincora which is operated by OCA and does not require further processing.

Therefore, the Council does not consider that the Silver Springs Pipeline provides services which compete with the services provided by the Kincora Pipeline.

The Council considers that the primary markets served by each of the pipelines are:



- in relation to the Peabody-Mitsui Pipeline, the market for gas transport services from the Moura Mine to the Duke Queensland Pipeline as well as points in between, including the service line inlet for the QN Plant;
- in relation to the Dawson Valley Pipeline, the market for gas transport services from the OCA gas fields in Dawson Valley and the Duke Queensland Pipeline as well as points in between; and
- in relation to the Kincora Pipeline, the market for gas transport services from Kincora to ML1A on the Roma to Brisbane Pipeline as well as points in between.

The Council must next consider the market or markets in which competition may be promoted. There are a number of potential markets that may be affected by a decision to revoke coverage of the three pipelines, in particular, the markets encompassing the activities of gas exploration, production, processing, reticulation, wholesaling and retailing.

The most likely market in which access (or increased access) to the services of the three pipelines for which revocation is sought may promote competition is the market within which gas sales take place.

In defining the relevant market in which sales of natural gas take place, the Council examined:

- whether the relevant market was a natural gas sales market or an energy sales market;
- whether there are a number of functional levels within which sales of natural gas occur (e.g., wholesale, retail); and
- the geographic extent of this market (e.g., whether it encompasses just the Surat Basin in relation to the Kincora Pipeline, or just the Dawson Valley area in relation to the Peabody-Mitsui Pipeline and the Dawson Valley Pipeline or whether it extends to Southern and Central Queensland for all three pipelines).

#### *Electricity or LPG as a Substitute for Natural Gas*

In the *AGL Cooper Basin decision*, the Tribunal examined the extent of substitution between electricity and gas in defining the nature of the market within which natural gas existed. The Tribunal considered gas and electricity were not substitutes (though to some extent the demand for gas related to the demand for electricity) and that a separate natural gas market existed with competition from other forms of energy at the margins.

The Tribunal considered that over time gas and electricity markets were likely to converge, resulting in the eventual creation of a broader energy market.<sup>9</sup>

While neither the applicants in respect of the three pipelines for which revocation of coverage is sought nor any other interested party has made submissions to the Council on this issue, the Council examined this issue at length in the Moomba Final Recommendation and the EGP Final Recommendation.

The price of electricity affects the price of gas on a number of levels. First, when users are making decisions about asset purchases, the relative competitiveness of gas and electricity are considerations in determining what appliances or plant should be purchased. Second, because one of the uses of gas is as an input for electricity production, its price continues to be constrained by the price of electricity to some degree even after these investments are made.

The Council considered that the evidence before it in the Moomba Final Recommendation and the EGP Final Recommendation lead it to the view that gas and electricity remain in separate markets. The Council considers that that view is equally applicable in relation to the three applications for revocation which it is currently considering. While the Council considers that electricity can be a substitute for gas in some circumstances and it can also provide some constraints on the price of gas, the Council does not consider that the field of rivalry is so close as to put them in the same market.

The Council considers that the position of LPG may be similar to that of electricity. The Council considers that natural gas and LPG may be viable substitutes for some users, however the Council does not currently have sufficient information to conclude that the field of rivalry is so close as to put them in the same market. None of the applicants or other interested parties made any detailed submission to the Council about substitutability between natural gas and LPG, although the Council notes that a current user of LPG who is located in proximity to the Dawson Valley Pipeline has stated that it is considering switching from LPG to natural gas.

For the reason discussed below, the Council considers that it is unnecessary for it to come to a final view on whether the market in which natural gas sales take place also encompasses sales of LPG.

#### *Relevant Functional Levels within the Natural Gas Industry*

The Tribunal in the *AGL Cooper Basin decision* considered that there were a number of functional levels to be considered in defining the natural gas market: exploration, production and processing and distribution. The Council agrees with this analysis. In using the term

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<sup>9</sup> *Re AGL Cooper Basin Natural Gas Supply Arrangements* (1997) ATPR 41-593 at 44,197-44,199.

‘distribution’ in this context the Tribunal meant gas sales, rather than carriage of gas through distribution pipelines.

In examining the distribution dimensions, there is a question whether there are separate functional markets for wholesale sales of natural gas and for retail sales of natural gas.

For the reasons set out in the Moomba Final Recommendation, the Council considers that it is not possible, at this time, for the Council to be sufficiently certain that there are separate functional markets for wholesaling and retailing of gas. For the purposes of its consideration of the criteria under section 1.9 of the National Code, the Council considers the market to be the supply and sale of natural gas, what the Tribunal referred to as the distribution functional dimension of the natural gas market.

#### *Geographic Dimension of Gas Sales Market*

Currently, through a system of interconnected transmission pipelines, the producers in the Cooper Basin and other producers in Queensland are connected to Brisbane, Mt Isa, Gladstone, Rockhampton, Barcaldine and various other regional centres in Queensland. The Council estimates there is approximately 2700 km of transmission pipelines in Queensland.<sup>10</sup> The major transmission pipelines which form the backbone of this system in Queensland are:

- the Ballera to Wallumbilla pipeline;
- the Roma to Gladstone/Rockhampton pipeline (the Duke Queensland Pipeline);
- the Roma to Brisbane pipeline; and
- the Ballera to Mount Isa pipeline.

The Council understands that it is also proposed to construct a major transmission pipeline which would run from gas fields in Kutubu in Papua New Guinea down the east coast of Queensland and connect to the transmission pipeline system in Southern and Central Queensland (**Chevron Pipeline**).

The Council considers that the existing pipeline network gives the gas sales market a geographic dimension that encompasses Southern and Central Queensland. This geographic dimension relies on the assumption that producers and users have access to the network of pipelines described above, on reasonable terms and conditions. Access has been, or will be, provided either because:

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<sup>10</sup> See the Issues Paper prepared by the Council in April 1999 titled “*Queensland Access Regime for Gas Pipeline Services: Consideration of effectiveness under s 44M(2) of the Trade Practices Act 1974*”

- regulation of third party access to monopoly pipelines is now in place in Queensland; or
- the pipelines would provide appropriate access of their own accord.

The Council considers that it is possible that the proposed construction of the Chevron Pipeline broadens the geographic dimension of the gas sales market in Queensland from Southern and Central Queensland to encompass the whole of the State of Queensland. However, the Council notes that construction on the Chevron Pipeline has not yet commenced, and that it is not anticipated that the Chevron Pipeline will be completed and operational in the near future.

The Council does not consider that, for the purposes of making its recommendations on these applications, it is necessary to come to a final view on whether the gas sales market in Queensland extends beyond Southern and Central Queensland. The Council will refer to the market within Queensland where gas sales take place as the Queensland Gas Sales Market.

#### *Temporal Dimension of Gas Sales Market*

The Council considers that there are no particular issues going to the temporal dimension of the Queensland Gas Sales Market on which consideration of this criterion is likely to turn. However, as noted above, the Council recognises that relevant considerations include the possible future convergence of energy markets and the possible construction of other pipelines that will have an impact on this market.

The Council considers the markets in which the services provided by the three pipelines for which revocation is sought exist are separate from the Queensland Gas Sales Market.

#### *Meaning of the Term “Promote Competition”*

The Council has been assisted by the consideration given to this term by a recent decision of the Tribunal in the *Sydney Airports decision*.<sup>11</sup>

The notion of promoting competition in criterion (a) involves the idea of creating the conditions or environment for improving the state of competition compared with that which would otherwise exist. Put another way, the Council must examine whether the opportunities and environment for competition with access to each of the three pipelines for which revocation is sought are better than they would be without access.

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<sup>11</sup> *Re Application for Review of the Declaration by the Commonwealth Treasurer Published on 30 June 1997 of Certain Freight Handling Services Provided by the Federal Airports Corporation at Sydney International Airport* (2000) ATPR 41-754 at 40,775)

In applying the with and without test endorsed by the Tribunal, the Council compares the market conditions which would prevail if the pipeline were not covered under the National Code with those that would prevail if it were covered under the National Code.

### ***Views Put to the Council***

#### *Peabody-Mitsui Pipeline*

Peabody Moura submitted that access would be unlikely to promote competition in either upstream or downstream markets.

Peabody Moura stated that there are no prospective gas producers in the Moura area who would be interested in seeking access to the pipeline. It stated:

*The only current gas producers in the region are the Moura Joint Venture and OCA. There are no other known natural gas deposits in the area, to date no third party gas producers have sought access or indicated a desire to seek access to the Pipeline, and the Applicant is not aware of any gas exploration plans by any third party.*

Peabody Moura stated that OCA holds the authority to prospect over the entire coal bearing region around the pipeline, and noted that OCA has already constructed a pipeline to serve OCA's needs (the Dawson Valley Pipeline).

Peabody Moura stated that, apart from the current third party user (Queensland Nitrates Pty Ltd), there are only two prospective local third party users of gas - Queensland Cotton Corporation Limited (**Queensland Cotton**) and a granary. These two parties currently use LPG but could switch to natural gas. The applicant understands that OCA intends to link these two parties to its Dawson Valley Pipeline. Queensland Nitrates Pty Ltd uses gas from the Peabody-Mitsui Pipeline but also plans to link to the Dawson Valley Pipeline.

Peabody Moura stated that it understood that the local township of Moura (population 2000) had no plans to reticulate gas.

Peabody Moura stated that access to the pipeline would not promote competition in the broader south-east Queensland gas market because the gas transported through the pipeline represents only about 2 percent of the total volume of gas consumed in that market.

Queensland Cotton objected to the revocation of coverage of both the Peabody-Mitsui Pipeline and the Dawson Valley Pipeline. Queensland Cotton considered that revocation of coverage under the National Code would limit the commercial options for potential users of gas in the region. Queensland Cotton currently operates a cotton gin approximately 4 km south of the

township of Moura adjacent to the Dawson Valley Pipeline. The cotton currently uses LPG but Queensland Cotton has stated that it is considering switching to natural gas. Although Queensland Cotton has not made any estimates of the amount of gas that this cotton gin might consume annually, from information supplied by Queensland Cotton, the Council considers it unlikely that the cotton gin would consume more than 15 000 GJ of natural gas annually.

Queensland Cotton has stated that only Origin Energy (the majority owner of OCA) has approached Queensland Cotton with an offer to supply it with natural gas. Queensland Cotton does not have any present intention to seek access to either the Dawson Valley Pipeline or the Peabody-Mitsui Pipeline itself.

While the Queensland Cotton gin is located very close to the Dawson Valley Pipeline, the gin is located approximately 5 km west of the Peabody-Mitsui Pipeline.

#### *Dawson Valley Pipeline*

The applicant argued that no third party had expressed an interest to date in seeking access to the Dawson Valley Pipeline.

The applicant argued the Dawson Valley Pipeline only transports gas from the Dawson Valley fields to the Duke Queensland Pipeline, and that no other fields in the area require the use of the pipeline. It argued the Peabody-Mitsui Pipeline could provide all the services of the Dawson Valley Pipeline.

As discussed above, Queensland Cotton has objected to the application for revocation of coverage of the Dawson Valley Pipeline.

#### *Kincora Pipeline*

The applicant argued that no third party had expressed an interest to date in seeking access to the Kincora Pipeline.

OCA argued the Kincora Pipeline services a number of mature gas fields with declining reserves and a limited remaining field life. It also considered the Silver Springs Pipeline could provide all the services of the Kincora Pipeline.

Mosaic Oil NL (**Mosaic**) made a submission to the Council objecting to the application for revocation of coverage of the Kincora Pipeline, stating that third parties may want access to the Kincora Pipeline in order to transport gas from the western region of the Surat Basin to Wallumbilla in order to obtain access to the Roma to Brisbane Pipeline. Mosaic has stated that

the Surat Basin is not as depleted as some industry participants believe and that significant quantities of gas remain to be discovered and exploited.<sup>12</sup>

## ***Analysis***

Submissions to the Council did not precisely identify any particular markets in which access might promote competition.

However, the most likely market in which access *might* promote competition is the Queensland Gas Sales Market. As noted above, the Council considers that this market is separate from the markets in which the each of the pipelines provides its services.

The next issue is whether access (or increased access) to the pipelines would promote competition in the Queensland Gas Sales Market.

### *Dawson Valley Pipeline*

In relation to the Dawson Valley Pipeline, the Council understands that there is no other known deposit of natural gas in the Dawson Valley area in relation to which any producer would require access to the pipeline.

Through discussions with the Queensland Department of Minerals and Energy (**Queensland DME**), the Council has been informed that:

- there is an authority to prospect (**ATP**) west of the Dawson Valley Pipeline (ATP 606P) which is held by Tristar Petroleum; and
- there are other ATPs for areas south and west of the Dawson Valley and Peabody-Mitsui pipelines which the Queensland government is currently in the process of auctioning to prospectors. The Queensland DME expects these ATPs to be granted in February 2001.

In relation to the ATP held by Tristar Petroleum, since the Duke Queensland Pipeline runs roughly east-west through this area, if gas were to be produced in this ATP, it may be more efficient to connect directly to the Duke Queensland Pipeline than to either the Dawson Valley Pipeline or the Peabody-Mitsui Pipeline. While Tristar Petroleum has been contacted by the Council in relation to the applications for revocation, it has not made any submission in response to the applications.

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<sup>12</sup> The information provided to the Council by Mosaic included a short written submission as well as additional information provided by Mosaic in discussions with representatives of the Council's secretariat.

In relation to the other ATPs which are due to be auctioned, the Council understands that it may be possible to develop any deposit found within these other ATPs within a relatively short time of discovery. Since a number of these ATPs are in areas which lie to the south or south west of the Dawson Valley Pipeline (which runs roughly north to south), it is possible that the most commercially viable way for a producer who discovered a deposit in one of these ATPs to transport gas to the Duke Queensland Pipeline for sale in the Queensland Gas Sales Market would be for that producer to seek to interconnect its pipeline to the Dawson Valley Pipeline or the Peabody-Mitsui Pipeline.

However, the Council has not received any submissions from any gas explorer or prospective gas producer indicating that they may seek to interconnect or otherwise seek access to either the Dawson Valley Pipeline or the Peabody-Mitsui Pipeline were they to be successful in the auction of the ATPs and subsequently discover any natural gas.

The Council considers that the promotion of production of gas in the Dawson Valley area may promote competition in the Queensland Gas Sales Market. However, the Council considers that at present there is not a strong enough likelihood of a producer seeking third party access to the Dawson Valley Pipeline for the Council to be affirmatively satisfied that access (or improved access) to the Dawson Valley Pipeline will promote competition in a market other than the market in which the Dawson Valley Pipeline provides its services.

The Council has also considered whether a third party request for access is likely in the medium term from a gas user or a gas retailer or aggregator. The Dawson Valley Pipeline currently only carries gas from the Dawson Valley CSM gas fields (owned by OCA) to the Duke Queensland Pipeline. No third party has expressed an interest in obtaining access to the Dawson Valley Pipeline. There is currently only one gas user in the Dawson Valley area and the Council understands that this user, the QN Plant, has entered into a long term contract for the supply of delivered gas and therefore would not obtain any benefit from coverage of the Dawson Valley Pipeline for over 5 years.

The Queensland Cotton gin is a potential user of gas from the Dawson Valley Pipeline. However, the Council notes that the gin is currently using LPG rather than natural gas. The Council notes that Queensland Cotton has not yet indicated that it will definitely convert from LPG to natural gas. The only company which has approached Queensland Cotton with an offer to supply it with natural gas is Origin Energy, which itself is the majority owner of OCA. Origin has not objected to OCA's application for revocation of the Dawson Valley Pipeline.

In these circumstances, the Council is not currently satisfied, on the evidence available to it, that access (or increased access) to the Dawson Valley Pipeline would promote competition in any other market. Therefore the Council considers that the Dawson Valley Pipeline does not meet criterion (a).



The Council notes that if a third party does require access to the Dawson Valley Pipeline in the future (for example if commercial quantities of gas are discovered in the Dawson Valley area), then the National Code allows any person to apply to the Council for the Dawson Valley Pipeline to be covered again under the National Code.

#### *Peabody-Mitsui Pipeline*

Despite the auction being conducted for ATPs in the area to the south and west of the Peabody-Mitsui Pipeline, no prospective explorer for gas or producer of gas has indicated any intention that they might seek to interconnect with or otherwise gain access to the Peabody-Mitsui Pipeline.

Apart from the QN Plant, which is currently supplied with gas from the Peabody-Mitsui Pipeline under a long term contract, the only other prospective user of gas in the area is the cotton gin operated by Queensland Cotton. The Council considers that while it would be technically feasible to connect this cotton gin to the Peabody-Mitsui Pipeline so that gas could be delivered to the cotton gin (either from the Moura Mine or from the Duke Queensland Pipeline), the relatively small amount of gas that would be consumed by the cotton gin were it to switch from LPG to natural gas may render it commercially unviable to construct the lateral of over 5 km in length which would be necessary to connect the gin to the Peabody-Mitsui Pipeline.

The Council has therefore come to the view, on the evidence available to it, that the Peabody-Mitsui Pipeline does not satisfy criterion (a).

As with the Dawson Valley Pipeline, the Council notes that the National Code allows for any person to apply to the Council for the Peabody-Mitsui Pipeline to be covered once again should the relevant circumstances change in the future.

#### *Kincora Pipeline*

The applicant in respect of the Kincora Pipeline, OCA, stated that it was unaware of any material gas reserves adjacent to the Kincora Pipeline that would require its use. Mosaic has submitted that coverage should not be revoked because other parties may seek access to the Kincora Pipeline in the future to transport gas to the Roma to Brisbane Pipeline.

The Council understands that the gas fields and the ATPs in the vicinity of the Kincora Pipeline are held by either OCA (including OCA in joint ventures with others) or by Santos Limited (who has stated that it does not object to revocation of coverage of the Kincora Pipeline).

OCA stated in its application that the OCA Joint Venture gas fields which are served by the Kincora Pipeline are mature and have rapidly declining lives. Mosaic stated that it considers that

the reserves in the western area of the Surat Basin are larger than others in the gas industry consider them to be.

Mosaic has stated that access to the Kincora Pipeline will still be important for other producers or prospective producers in the western area of the Surat basin because:

- OCA is currently engaged in offering to farm out various sections of the ATPs which it holds in areas in the vicinity of the Kincora Pipeline; and
- under the conditions of the ATPs issued by the Queensland Government, holders of ATPs are required to relinquish areas under an ATP if they do not engage in adequate exploration activity in that ATP.

In relation to the farm out of ATPs by OCA, Mosaic stated that it did not consider that access to the Kincora Pipeline would necessarily be part of the agreement (or set of agreements) under which OCA would farm out the relevant section of an ATP. Mosaic stated that regulated access to the Kincora Pipeline would still assist those persons who entered into farming out agreements with OCA. However, OCA has informed the Council that it has only entered into one farm out agreement in relation to the ATPs that it holds in proximity to the Kincora Pipeline and that access to the Kincora Pipeline was addressed in that agreement. OCA has informed the Council that it does not currently have any intention to enter into any further farm out agreements in relation to ATPs it holds in proximity to the Kincora Pipeline.

In relation to the relinquishment obligation, the Council understands that exploration activity must be reported to the Queensland DME every 6 months, and these reports are used as the basis for determining when insufficient exploration has taken place. Further, the Council understands that legislation is proposed in Queensland which will impose an obligation on holders of ATPs in Queensland to relinquish a certain percentage of an ATP area every 4 years regardless of exploration activity.

Mosaic therefore submits that while the ATPs in areas in the vicinity of the Kincora Pipeline are currently held either by interests associated with OCA or by Santos who does not object to revocation, this situation may change if either of these parties are required to relinquish sections of their ATPs due to insufficient exploration activity. Mosaic contends that regulated access to the Kincora Pipeline may be an important factor to encourage producers to develop any gas reserves which they might find in the vicinity of the Kincora Pipeline.

OCA has informed the Council that it is not aware of any obligation which would require it to relinquish any areas of the ATPs which it holds in proximity to the Kincora Pipeline in the short term. The Council understands that upon an obligation to relinquish, before requiring access to the Kincora Pipeline, a prospective producer would have to:

- engage in exploration activity within the ATP and discover natural gas in a commercially exploitable quantity; and
- exploit the gas through drilling wells.

In addition, it is likely that a prospective producer would also need to construct a short lateral or feeder line to connect the well head to the Kincora Pipeline as well as make arrangements for the gas to be processed (if necessary) to sales specification. The Council understands that if gas is not sales specification, then the only way in which this gas can be injected into a natural gas pipeline such as the Kincora Pipeline is for that producer to find a producer who has a drier gas with which the first producer could match the unprocessed, wetter gas in order to keep the gas in the pipeline at sales specification. The Council understands that there are limits to the amount of gas which could be matched in this fashion, and it would not be possible to transport all of the gas from a significant deposit in this manner.

The Council considers that the promotion of production of gas in the Surat Basin may promote competition in the Queensland Gas Sales Market. However, the Council considers that at present there is not a strong enough likelihood of a producer seeking third party access to the Kincora Pipeline for the Council to be affirmatively satisfied that access (or improved access) to the Kincora Pipeline will promote competition in a market other than the market in which the Kincora Pipeline provides its services.

Therefore the Council has come to the view that the Kincora Pipeline does not meet criterion (a).

The Council notes that if a third party does require access to the Kincora Pipeline in the future (for example if commercial quantities of gas are discovered in the western area of the Surat Basin), then the National Code allows any person to apply to the Council for the Kincora Pipeline to be covered again under the National Code.

*In relation to each of the pipelines for which revocation has been sought, the Council has come to the view that it is not satisfied that competition will be promoted in the Queensland Gas Sales Market on the basis that the relevant product dimension of this market is natural gas. Therefore the Council does not consider it necessary to come to a concluded view on whether the relevant product dimension may be wider than this and also include LPG.*

**Criterion (b)                    that it would be uneconomic for anyone to develop another pipeline to provide the services provided by means of the pipeline.**

## **Background**

Criterion (b) would appear to be designed to identify potential coverage of pipelines where the development of competing pipelines would be inefficient.<sup>13</sup> The intent is that competitive infrastructure (whether in actual or potential terms) should not be covered under the National Code. In other words, access regulation should be limited to infrastructure where competing facilities are not economically viable.

As such, access regulation should normally be confined to infrastructure exhibiting natural monopoly characteristics – that is, where a single facility can meet market demand at less cost than two or more facilities. Such a facility is normally characterised by large up-front investment costs and low operating costs, resulting in economies of scale or scope across a broad range of output. In other words, as output from a natural monopoly facility increases, average costs per unit of output continue to decrease across the range of output sought by the market.

This approach is consistent with that of the Tribunal in the *Sydney Airports decision*. The Tribunal held that ‘another’ facility must be one capable of providing services competitive with those provided by the relevant facility. Services which are merely complementary to those provided by the relevant facility should not be regarded as competing services for the purposes of this criterion.

The Council therefore considers the reference in criterion (b) to ‘services’ should be interpreted as involving a consideration of whether it is uneconomic to develop another pipeline to provide competing services.

Legislative restrictions may also sometimes be pertinent in considering whether it is economic to build another pipeline to provide the services provided by the pipeline in question. For example, the feasibility of developing another pipeline may be questionable in some cases due to environmental or planning regulations.

In considering whether it is economic to build another pipeline, the Council adopts a social test rather than a private test. While a private test would consider whether it is viable for an individual to invest in a new facility, a social test considers whether building a new facility represents an efficient use of resources from the viewpoint of the community.

The Council considers that the objectives of the legislative scheme are best met by having regard to the provision of competing services by another existing pipeline rather than limiting its consideration to the development of new pipelines.

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<sup>13</sup> *Re Application for Review of the Declaration by the Commonwealth Treasurer Published on 30 June 1997 of Certain Freight Handling Services Provided by the Federal Airports Corporation at Sydney International Airport* (2000) ATPR 41-754 at 40,791-40,793.

## **Views Put to the Council**

### *Peabody-Mitsui Pipeline*

The applicant argues it would not be uneconomic to develop another pipeline to provide the services of the pipeline because: (i) it is relatively short (23 km); (ii) there is no difficult terrain in the area to hinder construction; and (iii) the Dawson Valley Pipeline runs parallel to the pipeline for a significant part of its length. The Dawson Valley Pipeline was constructed after the Peabody-Mitsui Pipeline.

### *Dawson Valley Pipeline and Kincora to Wallumbilla Pipeline*

The applicant in respect of these two pipelines argues that the existence of the Silver Springs Pipeline (in relation to the Kincora to Wallumbilla Pipeline) and the Peabody-Mitsui Pipeline (in relation to the Dawson Valley Pipeline) proves that it is economic to build pipelines to provide the services of the Kincora to Wallumbilla and the Dawson Valley pipelines.

## **Analysis**

In considering whether it would be uneconomic to develop another pipeline to provide these services, the Council notes that gas pipelines typically have high construction costs and low operating costs, making the marginal cost of reticulating a unit of gas very low. Moreover, up to the point of fully expanded capacity, average costs of reticulation per unit of gas decline. These features are indicative of natural monopoly characteristics. In lay terms, it is almost always cheaper to transport gas through existing pipelines (if spare capacity exists or can be added) than it is to build another pipeline to transport gas.

Moreover, investment in new pipelines is, in economic language, 'sunk'. That is, the investment is fixed or committed, and if the investment is a failure, little or none of it can be retrieved. This means that entry and exit costs to provide these services are high, and that incremental or gradual entry – a common form of entry in other industries – is not feasible in the gas transportation industry.

Finally, it is not uncommon for existing pipelines to have spare capacity. From a pipeline company's point of view, it is often prudent to cater to the unpredictability of future requirements by building a larger capacity pipeline. This is because the costs of laying a new pipeline rise slowly compared with increases in the capacity of that pipeline. In other words, it is much less expensive – per unit of capacity – to lay a large capacity pipeline than a small capacity pipeline.

In summary, therefore, it is generally not economic to develop another pipeline where an existing pipeline has existing spare capacity (or can develop it through a relatively inexpensive upgrade of

the network). Having said this, the Council recognises it will always be necessary to consider the facts of particular pipelines.

In relation to whether any existing pipelines provide services which are competitive with the services provided by the pipelines for which revocation of coverage is sought, the Council notes that, for the reasons discussed above:

- in relation to the Peabody-Mitsui Pipeline, the Council considers that the services provided by this pipeline do not compete with the services provided by the Dawson Valley Pipeline;
- in relation to the Dawson Valley Pipeline, the Council considers that the services provided by this pipeline do not compete with the services provided by the Peabody-Mitsui Pipeline;
- in relation to the Kincora Pipeline, the Council considers that the services provided by this pipeline do not compete with the services provided by the Silver Springs Pipeline;

#### *Peabody Mitsui Pipeline and Dawson Valley Pipeline*

In relation to the Peabody-Mitsui Pipeline and the Dawson Valley Pipeline, both applicants have submitted that the fact that the two pipelines are located close together, and indeed run parallel to each other only 20 metres apart for 12 km, demonstrates that it is economic to duplicate both of these pipelines.

The Council does not consider that the mere existence of another pipeline which runs over essentially the same route (or part of the same route) as the first pipeline demonstrates that the two pipelines do not satisfy this criterion. The Council notes that the test to be considered is a social test not a private test – it involves consideration of whether a new pipeline represents an efficient use of resources from the perspective of the community as a whole.

The Council notes that under section 1.29 of the National Code, the Council is entitled to recommend that coverage be revoked over part only of a covered pipeline and that the Council may recommend revocation to a greater or lesser extent than has been requested by an applicant.

Therefore, under section 1.29 of the National Code, the Council is entitled to consider whether particular parts of pipelines satisfy criterion (b). The Council considers that while the two pipelines do not provide competing services for a large part of their length, the two pipelines do provide services which compete with each other for that distance of 12 km over which the two pipelines are only 20 metres apart.

In relation to the sections of the pipelines which do not offer competing services, the Council considers that, due to the unused capacity on both of these pipelines, it would be uneconomic for anyone to develop another pipeline to provide the services provided by either pipeline.

In relation to the sections of the pipelines where they do offer competing services, the Council notes that the applicant in relation to the Peabody-Mitsui Pipeline stated that the Peabody-Mitsui Pipeline was constructed before the Dawson Valley Pipeline. The applicant stated that, while OCA investigated the possibility of using the Peabody-Mitsui Pipeline, it decided to construct its own pipeline instead.

The Council considers that there are a number of reasons why someone in OCA's position might have chosen to build its own pipeline side by side with the Peabody-Mitsui Pipeline even though it is uneconomic to do so. For example:

- OCA might have been unable to negotiate what it considered to be a reasonable agreement for access to this section of the Peabody-Mitsui Pipeline; or
- OCA may have considered that, for strategic reasons, it was worth constructing the additional length of pipeline (which represents only approximately a quarter of the total length of the Dawson Valley Pipeline) to avoid having to rely on access to a pipeline which was owned by a party related to a competing gas producer.

The Council notes that the Peabody-Mitsui Pipeline, which was constructed prior to the Dawson Valley Pipeline, has excess capacity which exceeds the total maximum capacity of the Dawson Valley Pipeline.

In these circumstances, the Council has come to the view that the Peabody-Mitsui Pipeline and the Dawson Valley Pipeline satisfy criterion (b).

#### *Kincora Pipeline*

As noted above, the Council does not consider that the Silver Springs Pipeline (PPL 4) provides services which compete with the services offered by the Kincora Pipeline.

The Council also notes that while the maximum capacity of the Kincora Pipeline is 30 TJ per day, it is currently only transporting no more than 15 TJ per day, and that OCA expects that the load carried by the Kincora Pipeline will fall to only half this amount next year.

The Council has therefore come to the view that the Kincora Pipeline satisfies criterion (b).

**Criterion (c)**                    **that access (or increased access) to the services provided by means of the pipeline can be provided without undue risk to human health or safety.**

### ***Background***

The rationale for this criterion is that the National Code should not be applied to pipelines where access might pose an undue risk to human health or safety.

### ***Views Put to the Council***

#### *Peabody-Mitsui Pipeline*

The applicant stated in relation to this criterion that:

*“There is no reason to believe that either Coverage or revocation would have any impact on the risk to human health and safety.”*

None of the submissions received by the Council in relation to the application for the Peabody-Mitsui Pipeline addressed this issue.

#### *Dawson Valley Pipeline and the Kincora Pipeline*

The application by OCA stated that it included reasons why coverage of these two pipelines should be revoked. The application did not address this criterion.

None of the submissions received by the Council in relation to the applications for these two pipelines addressed this issue.

### ***Analysis***

The Council considers that typically, third party access to gas pipelines does not pose undue risks to human health and safety where appropriate measures are taken by the operator. Third party access to gas pipelines has been permitted in relation to many pipelines in Australia without being considered to unduly compromise human health or safety.

For these reasons, the Council considers that all three pipelines satisfy criterion (c).



**Criterion (d)**                    **that access (or increased access) to the services provided by means of the pipeline would not be contrary to the public interest.**

### ***Background***

One matter of public interest is whether any benefits of access, such as cheaper prices and more efficient use of resources, are outweighed by regulatory or compliance costs. Other matters of public interest include environment considerations, regional development, and equity.

### ***Views Put to Council***

#### *Peabody-Mitsui Pipeline*

Peabody Moura argued that regulated access under the National Code would be costly and would provide few benefits and therefore access was contrary to the public interest.

While Peabody Moura did not provide any monetary estimate of the amount of cost involved in preparing an access arrangement for the pipeline, it did note that this cost would bear little relationship to the length and capacity of the pipeline to which it relates. The applicant also noted that these regulatory costs would be passed on to users, and argued that in view of the small user base and modest volume of usage, these costs would swamp any benefits of access.

No submissions received by the Council addressed this issue.

#### *Kincora to Wallumbilla Pipeline and Dawson Valley Pipeline*

OCA estimated that the regulatory and compliance costs associated with regulated access would be about \$100,000 to \$150,000 in respect of each pipeline, and similar costs would be borne by the regulator and the Queensland Government. It noted that both pipelines have relatively low throughput and few customers, and these customers would have to bear the regulatory costs.

It suggested that in light of the lack of interest in third party access, the costs of regulation outweighed the benefits.

No submissions received by the Council addressed this criterion.

### ***Analysis***

The Council accepts that there are regulatory and compliance costs associated with coverage under the National Code.

Given that the Council is not satisfied that regulated access to either the Dawson Valley Pipeline, the Peabody-Mitsui Pipeline or the Kincora Pipeline would promote competition in another market, the Council cannot identify any relevant benefits which might offset the regulatory and compliance costs associated with regulated access in relation to these three pipelines.

Accordingly, the Council has come to the view that the Dawson Valley Pipeline, the Peabody-Mitsui Pipeline and the Kincora Pipeline do not meet criterion (d).

## Appendix 1: The Council's Process

In determining its final recommendations, the Council followed the process set out in the National Code. Under this process the Council:

- acknowledged receipt of the applications and advised the owners and operators of the pipelines and the Queensland Department of Mines and Energy;
- advertised receipt of the applications in the *Australian Financial Review* and the *Courier-Mail* on 1 September 2000;
- prepared and released an Issues Paper in relation to the applications and called for public submissions;
- wrote to a large number of parties whose interests may be affected by the applications and also conducted discussions with several interested parties in relation to the applications;
- released Draft Recommendations on the applications and called for further submissions.

The Council's final recommendation will now be forwarded to Senator The Hon. Nick Minchin, Minister for Industry, Science and Resources. The Minister must make a decision on revocation of coverage on the basis of the same criteria applied by the Council. The Minister has 21 days to decide the matter.

The Minister's decision may be appealed to the Relevant Appeals Body (in this case, the Australian Competition Tribunal).

## Appendix 2: Submissions Received by the Council

The Council received submissions from the following organisations:

- Energex Retail Limited
- Mosaic Oil NL
- Oil Company of Australia Limited
- Peabody Moura Mining Pty Limited
- Queensland Nitrates Pty Ltd
- Santos Limited