

Submission in response to Consultation Paper on MCE Review of Decision-Making in the Gas and Electricity Regulatory Frameworks

1. Introduction

AGL welcomes the opportunity to participate in the SCO's consultation process on merits reviews for gas and electricity economic regulatory decisions. The issue of appropriate merits review is an important component of the MCE's Energy Market Reform program. Merits review and judicial review are an integral feature of administrative law within the Australian legal system. Merits review and judicial review have been part of the Gas Access Regime (GAR) since its inception in 1998, and it is appropriate that the strong track record of merits review in the GAR be applied to improving the quality of access regulation in the energy market.

AGL has participated actively in energy market reform processes during the 1990s that led to the implementation of the GAR and the National Electricity Market (NEM). It also participated in the subsequent reviews by the Parer Committee on Energy Market Reform and the Productivity Commission's reviews of the National Access Regime (NAR) and the GAR. AGL has been able to bring significant experience because it has been privately owned since its establishment, and has probably the longest experience with utility regulation in Australia. AGL has consistently argued for the accountability and balance, which are provided by both merits and judicial review, in order for regulation to be robust and for all participants to have confidence in regulatory processes and outcomes. AGL remains persuaded of the need for review of regulatory decisions, not only on matters of procedure and law (which is a given), but also on matters of the merits and reasonableness of decisions.

This submission does not seek to respond to all of the large number of issues raised in the SCO's discussion paper, either in terms of arguments raised or in terms of all of the details of implementation. It is appropriate at this time that the debate focuses on the overall benefits of merits review of economic regulatory decisions. AGL submits that it is essential that industry be provided with the opportunity for further involvement in consultation on the detail of implementation, when the MCE has made its decision about the key elements of merits review arrangements.

2. General Comments on Approach

2.1. The need for and benefits of merits review

The discussion paper identifies the need for transparent, fair and reasonable decision-making that produces economically efficient outcomes and highlights a number of essential components that lead to this result. The paper further identifies that one of those components is review mechanisms which deliver regulatory accountability.

AGL agrees with this reasoning and is of the view that the role of appropriate review mechanisms is significant in the maintenance and ongoing development of a strong national energy market where there is continued investment. All participants in regulatory processes need to have confidence in the regulatory decisions that will result from them. However, this is most particularly the case for infrastructure service providers and investors, because of the considerable

impact of an inappropriate or incorrect decision on their businesses and the ongoing incentive to invest. The availability of adequate and appropriate merits review (in addition to judicial review) in a regulatory regime is one of the key elements which can provide this confidence. The NCC drew similar conclusions in its recommendation on the effectiveness of the GAR in 1997¹.

This confidence results from:

- Awareness and accountability of regulators that provide an environment for disciplined in decision-making in the first instance;
- Review mechanisms that are clearly defined, efficient and effective;
- Elimination of errors in decision making when they do occur;
- Provision of consistency in decision-making through an authoritative body of precedent; and
- Ensuring that regulatory decisions remain consistent with policy intent.

The discussion paper identifies seven criteria (or objectives) of an appropriate review scheme and two possible models for review. It is AGL's view that the criteria will be best met through a limited form of merits review of the kind embodied in Model A (with judicial review as a given) as explained in detail below. AGL submits that Model B on its own will not meet many of these criteria.

The range of possible forms of review that are available is broad, with varying levels of constraint or limitation, ranging from simple judicial review at one end through to unconstrained *de novo* merits review at the other end. The discussion paper largely focuses on two of the many possible models of review. Both models are at the constrained end of the possible range and only brief consideration has been given to fuller forms of review. While AGL accepts the need for reviews of regulatory decisions to be streamlined, efficient and effective – and this will of necessity lead to some limitations in the appropriate model - it is important to note that even the less constrained proposal (Model A) is at the highly constrained end of a possible spectrum.

2.2. Merits review under the Gas Access Regime

The discussion paper refers to a number of examples of regulatory regimes with merits review and these provide useful experience. However, AGL submits that the most relevant experience is available from the GAR. A number of lessons arise from experience of merits reviews under the GAR:

- Regulatory errors that should be corrected can occur;
- The timeframes for limited merits review are not protracted²;
- Precedents resulting from merits review have been useful in subsequent regulatory reviews of access arrangements;
- The ACT has the appropriate expertise to handle review of economic decisions.

This experience demonstrates that merits review of economic regulatory decisions related to energy access under the GAR have met the criteria as specified in the discussion paper for an effective review scheme. It is notable, however, that the Productivity Commission recommended strengthening merits review arrangements in the GAR by removing the need for grounds of review, even

¹ Page 5, *Recommendation to the Gas Implementation Group on the National Third Party Access Regime for Natural Gas Pipelines*, National Competition Council, September 1997

² It should be noted that the timeframes for the reviews for the Moomba - Adelaide Pipeline and the GasNet Primary Transmission System were delayed as a result of an oversight in relation to the administration of the ACT.

though the experience of merits reviews had identified and corrected errors³. This indicates the PC's concern about the need for increased review rights to enhance the effectiveness of and confidence in the gas regime.

The National Access Regime, as the template for access legislation, also provides an important relevant reference point, with merits review being provided for decisions on declaration - analogous to coverage decisions - and undertaking decisions⁴ - analogous to an access arrangement in gas or revenue/pricing decisions in electricity. It should also be noted that in these cases reviews under Part IIIA of the Trade Practices Act would be substantially less constrained than under the Gas Pipelines Access Law (GPAL) or under the discussion paper's Model A.

It is essential that the SCO and MCE recognise and preserve the rights of review that are currently available to participants under the GAR. Any material reduction to the merits review arrangements currently available under the GPAL would represent a substantial loss of rights to participants for which there should be a demonstrable offsetting benefit and should be supported by strong policy reasoning. This is of particular importance in the case of gas transmission and distribution businesses for which merits review rights in the GAR are a significant protection against loss of property rights.

In this regard AGL notes that Model A is broadly similar to merits review as provided for in gas, except for decisions that are reviewed under section 38 of the GPAL (principally coverage). Merits reviews under section 38 do not involve a limitation on grounds for review and not limit the material before the ACT to what was before the NCC and the Minister. In addition to this reduction in rights in relation to reviews under section 38, Model A may reduce the rights compared to section 39 of the GPAL in particular in respect of grounds for review. Our analysis in section 4 below provides AGL's detailed comments about the each of the elements of Model A.

2.3. *Misconceptions about merits review*

AGL is of the view that there are a number of misconceptions about merits review which have been raised in debate on the topic over the past year that need to be corrected. These are largely addressed in our discussion of the two models of review proposed in the paper below. Two other misconceptions not addressed as part of the discussion of the two models below are:

- that applicants for merits review "cherry pick" regulator's decisions, only seeking review of selected matters, whereas the regulator would be able to show that a decision was correct in its totality; and
- that regulatory error can be avoided and accountability increased by other mechanisms such as increased regulator resourcing.

Both these suggestions do not withstand scrutiny. Firstly, the concept of "cherry picking" suggests that where a participant believes that the regulator has made an error in its decision, it is appropriate to open up all aspects of the decision, including those over which there is no dispute. This would seem to be unnecessary and inefficient. It is appropriate that only those matters that are disputed should be reviewed.

³ These were the merits reviews of ACCC's decisions on the Moomba-Adelaide Pipeline and the GasNet Primary Transmission System.

⁴ It is assumed that Trade Practices (National Access Regime) Bill will be passed.

Secondly, while additional resources may provide some potential to enhance the quality of decisions, additional resources will not increase regulator awareness and accountability, will not provide a body of precedent and will not correct errors when they occur. Moreover, given the resources currently available to regulators any improvement in decision quality of regulators is likely to be marginal.

3. Preferred Model

In section 2 above, AGL expressed its strong in principle support for merits review generally, in order to achieve accountability and balance in regulatory decisions; and specifically for a limited form of merits review to apply to economic regulatory decisions of the Australian Energy Regulator (AER). Overall, AGL favours an approach which is consistent with the current GPAL arrangements. In this regard we note that the discussion paper's Model A is similar. AGL supports Model A on the basis that the appropriate options for the elements of Model A (which are discussed in section 4 below) are chosen.

As explained below, AGL has major concerns with Model B being presented as a substitute for merits review. The discussion paper has not adequately balanced the shortcomings of Model B against the positive features of Model A (with judicial review as a given). Moreover, the presumed disadvantages of Model A outlined in the paper either cannot or are unlikely to occur in practice, and certainly do not lead to the conclusion that Model B should substitute for Model A. Rather, Model A and Model B should be understood as complements.

In addition, it is proposed that only judicial review will apply to Ministerial decisions that are currently subject to merits review under s 38 of the GPAL (on the premise that such decisions are essentially policy and therefore merits review by an administrative tribunal is not appropriate).⁵

3.1. What does Model B offer over and above judicial review?

The discussion paper presents Model B as an "augmented" form of judicial review. The apparent additional dimension which is intended to augment Model B beyond judicial review is the specific requirements exemplified in ss 16, 35 and 36 of the NEL. However, there is no empirical evidence to demonstrate how this model would work in practice to increase the scope for correction of regulatory error.

In general none of the NEL requirements contained in ss 16, 35 & 36 is remarkable in providing particular constraint on a regulators discretion⁶. Broad requirements such as these are normally included within economic regulation. Suggesting that their existence increases the opportunity to "augment" judicial review extends their value beyond what has previously been recognised. Such obligations as these are already contained within the GAR and clearly do not add anything to a regime that already incorporates wide regulatory discretion.

In summary, Model B presents an apparent form of "augmented" judicial review. It does this by simply recognising the procedural obligations that are normally followed by a regulator. These obligations are relatively broad and while they may allow for judicial review of some decisions on the basis of procedural *ultra vires*, they would also permit a very wide range of decisions, including decisions which are unreasonable and/or contain particular types of error. These adverse outcomes are likely to either (a) not be detected at all by a reviewing court, or

⁵ SCO para. 2.37

⁶ The relevance of ss 35 & 36 in the context of constraining the AER is uncertain since they apply to the AEMC not the AER.

(b) even if they were detected, will still be considered consistent with the legislative obligations.

Model B presents no significant advance over the existing bases for judicial review. However, as identified in the discussion paper, judicial review remains an appropriate “given”, to ensure that regular’s decisions are made properly within the powers that are delegated to them.

3.2. Is Model B a substitute for Merits Review?

AGL fully concurs with the initial assessment of Model A in the discussion paper⁷ that merits review provides a more extensive type of review than judicial review, and enables correction of a greater range of regulatory errors that might have significant adverse consequences on participants. Legal authorities⁸ have stressed that merits review in an administrative appeals tribunal differs substantially from court judicial review, the latter being more concerned with the lawfulness of a decision rather than its correctness. As noted in section 3.1 above, judicial review cannot adequately address major sources of error which are most likely in complex economic decision-making, such as errors of fact and errors in use of regulatory discretion. The discussion paper itself provides a good example of one of the limitations of judicial review:

In judicial review, courts will only interfere with the findings of fact of the original decision-maker where an error of law occurs – for example, where that person or body has made a decision based on “no evidence” at all for the finding of fact. But if there is some cogent evidence, the court will not go further to determine whether they are the “correct” facts.⁹

More generally, the discussion paper notes that the courts will not be able to intervene where judicial review grounds are not made out, regardless of adverse economic effects on the regulated entities and end users.¹⁰ This inability to adequately address the correctness or reasonableness of decisions is the major limitation of judicial reviews in the economic regulatory context.

This inability is illustrated in the following brief examination of the requirements of ss16, 35, 36 of the NEL (as summarised in the discussion paper), which shows that the extent to which the merits of a decision can be tested through the Model B judicial review process is limited, if not non-existent.

- *The national energy market objective must be taken account of;*

This requirement is very broad and general, and leaves the regulator very wide discretion about how to take account of the market objective. A regulator may demonstrate that it has had regard to the objective and there is therefore no ground for judicial review. However it may do so incorrectly or unreasonably. While correction would not be available under Model B it would be under a limited merits review model such as Model A or the GPAL.

- *Registered participants in the NEM must be informed of material issues and given a reasonable opportunity to make submissions;*

⁷ SCO para 2.23

⁸ Examples: Hon Justice Garry Downes AM. *Tribunal in Australia: their roles and responsibilities* – www.aat.gov.au/corporatepublications/speeches/downes/pdf.tribunals.pdfs

⁹ SCO para 2.9

¹⁰ SCO para 2.25

This requirement is one that would normally be required as a matter of procedural fairness and accordingly non-compliance by the regulator would be judicially reviewable. It is difficult to see how it is pertinent to the merits of, or errors in, a regulator's decision once due process has been followed.

- *A regulated transmission system operator must be provided with a reasonable opportunity to recover its efficient costs of complying with regulatory obligations.*

Judicial review would be able to determine whether the revenues allowed were sufficient to meet the costs it had assessed, as such matters will be transparent. However, it is unlikely to provide an ability to test whether the regulator's assessment of efficient costs is reasonable or whether the transmission operator has a reasonable opportunity to recover the costs. These are significant matters which the Court is unlikely to be inclined to consider.

- *Effective incentives must be provided to promote economic efficiency, including efficient investments and efficient service provision;*

Similarly, while the court would be able to determine whether a regulator may provide incentives under the Model B review it is unlikely to have to consider if the incentives will in fact be effective in promoting economic efficiency.

- *The value of assets must be allowed for and regard had to any existing valuation.*

While the regulator may allow for the value of assets and have regard to any existing valuation, the appropriateness of how the broad discretion is applied is unlikely to be able to be considered by the Court.

Regulatory discretion

In successful applications for merit reviews of regulatory decisions to date, the incorrect or unreasonable use of regulatory discretion has been a major issue. There is a line of reasoning in the discussion paper which suggests that the need for merits review can be significantly reduced if the legislation or rules governing the decision-maker are made more explicit:

If the decision involves the exercise of significant discretion, and the factors guiding that discretion are expressly set out and well structured in the governing rules... arguably there is less need for merits review, and judicial review would be an adequate review mechanism¹¹

While this may be valid as a high level concept, the analysis above indicates it is not relevant, either to existing gas legislation or the new NEL and Rules, which require regulators to exercise very high levels of discretion in applying broad regulatory principles, particularly in sensitive areas such as pricing. One reason for the Productivity Commission's recommendation to retain (and strengthen) provision for merits review in the GAR was recognition of the "imperfect" nature of regulatory instruments in an environment where there was high potential for regulatory error:

The prospect of exposure to imperfect regulatory instruments means that there is a strong case for a merits review¹²

¹¹ SCO para 5.3

It is clear from the discussion paper that Model B was developed on the premise that the new NEL is highly prescriptive in the way the regulator must carry out its functions.¹³ However, the level of prescription contained in ss 16, 35, 36 is, in AGL's view, a very long way from the amount of prescriptive detail that would be needed in order to imply that regulatory discretion had been minimised to the extent that merits review was no longer appropriate.

Conclusion

Both traditional judicial review and Model B are unable to adequately address major sources of error, which impact the correctness or reasonableness of regulatory decisions. For this reason, Model B cannot be considered a meaningful or valid substitute for merits review.

3.3. The Arguments for and against Models A and B

The discussion paper raises a number of arguments for and against the two models, but lacks balance as no arguments are presented against Model B. Further, AGL has serious concerns that the paper's arguments for Model B and against Model A are based on misconceptions. These concerns are described below. AGL believes that once the misconceptions are corrected the clear conclusion is that limited merits review (ie Model A or a version of it) is the appropriate model for a review of decision making in both the gas and electricity frameworks.

3.3.1. Arguments for Model B

Higher accountability for the AER

The discussion paper argues that Model B will enhance the AER's accountability because:

- the AER will be subject to the discipline of the specific requirements set out in the energy legislation; and
- since the Federal Court can remit the matter to the AER, this is an incentive for the decision-maker to make a correct initial decision.¹⁴

It is difficult in the light of the discussion in sections 3.1 and 3.2 to see how Model B will enhance the AER's accountability beyond what is already provided by judicial review. Overall, the new NEL obligations do not impose any enhanced accountability on decision-makers so long as their decisions are subject to judicial review alone.

The second accountability argument relies on the proposition that, as the Federal Court lacks the power to substitute its own decision for that of the decision-maker (as an administrative tribunal might do) it would therefore remit the decision back, and that this increases the incentive to make a correct initial decision:

The incentive will be high if the decision-maker knows that the decision will be returned to it for remaking. In particular, any inclination on the

¹² Productivity Commission *Review of the Gas Access Regime*, June 2004, p.498. See also comments on p 109 re regulatory error.

¹³ SCO para 2.33

¹⁴ SCO paras 2.51-2.53

*part of the decision-maker to act in the expectation of having its decisions substituted by a review body will be avoided.*¹⁵

The logic of this argument is illusory. A regulator is likely to have greater incentive to ensure correct and appropriate decisions, if its decisions could be substituted (or varied) by the review body than if its decisions could only be remitted back to it to be remade. This incentive arises because it will lose all say in the final outcome. However, that said, this distinction is not likely to be as significant, as the main incentive for a decision-maker to make correct decisions arises from the potential for a review to find an error.

In addition, there are objective grounds to suggest that incentives to make a correct decision under Model A are considerably stronger, because the grounds go beyond simply complying with the requirements of the law to the quality of the decision in terms of factual correctness and reasonableness.

Little incentive for "gaming" by regulated entities

There is an implication in the discussion paper that, because "a review body [has the option of] making a new decision" under Model A there is an "incentive [for an applicant] to hold back critical information"¹⁶. The logic of this argument is also unclear. AGL can see no connection.

Firstly, under Model A, the review body would only be able to have regard for information before the AER. Whether, in the event of an error being found, the review body substitutes its own decision or remits it to the AER, would be irrelevant. The important thing for the applicant will be that an error is identified and that can only be done if all the relevant material is before the regulator.

Secondly, while the business may prefer the review body to substitute its own decision rather than have it remitted to the AER (and this is by no means certain), its far greater concern will be that an error identified by the review body is corrected, whether by the review body or the original decision-maker.

Moreover, if there was genuine potential for "gaming" the process by withholding information, it could only occur with Model B because under this model new material may be introduced.

There is no advantage in review by a specialist tribunal

The discussion paper argues:

*While various ACT decisions may be cited by some as proof of the need for merits review in the energy sector, the Federal Court has dealt competently with complex economic issues in that sector. Therefore, there is no particular advantage in having review by a specialist tribunal.*¹⁷

AGL makes the following comments:

- While the Federal Court has dealt with complex economic issues this is not the normal focus of its decision making. Accordingly in order to make decisions on complex economic issues the Court must employ significantly more elaborate processes, including drawing on expert economic evidence which is both costly and time consuming.

¹⁵ SCO paragraph 2.53

¹⁶ SCO paragraph 2.54

¹⁷ SCO paragraph 2.55

- The use of an expert tribunal, such as the ACT, which is well versed in complex economic matters, obviates the need for expert witnesses, and will therefore be involve considerably less cost.
- Limited merits review along the lines of model A is therefore much more likely to be simple and streamlined than Model B, particularly where matters to be reviewed are of a complex economic nature.

Avoiding multiple actions in respect of the same matter

The discussion paper argues:

*The right to judicial review is a given. If merits review by a tribunal applies as well, the potential will exist for multiple actions in different forums in respect of the same AER decisions. This will be avoided under Model B.*¹⁸

and,

*Model B will locate all review of AER economic regulatory decision-making in the Federal Court. This will substantially streamline regulatory processes consistent with the MCE's reform objectives, promoting further confidence in the regulatory regime.*¹⁹

AGL questions whether there will be a streamlining of process associated with all review decisions being made by the Federal Court. If aggrieved participants are denied the opportunity of genuine merits review (albeit limited), there is a real likelihood of a greater number of judicial reviews being sought. If this were to be the case, this will involve more time, legal expertise and cost than would have been the case if merits review had been available. Thus, the potential for the restrictive Model B to reduce the time and costs involved in reviews is overstated.

While placing the review of AER economic regulatory decision-making in the one body has superficial appeal as a matter of administrative convenience, it ignores the matters of greater significance, namely that participants must have confidence that in the event that regulators make errors, these can be corrected. AGL cannot see how "confidence in the regulatory regime" will be promoted if the form of review (ie Model B) leaves important significant errors uncorrected.

Minimising costs and time delays – maximising regulatory certainty

The discussion paper argues:

*Reducing the potential for multiple actions in respect of the same AER decisions will also assist in minimising costs and time delays associated with reviews and maximising regulatory certainty. If review is limited, there will be greater certainty around economic decision-making. All parties would be able to appeal to one forum where all their issues concerning the decisions could be raised.*²⁰

AGL makes the following comments:

- Given that merits review has room to deal with some errors of law the potential for an applicant to seek both merits and judicial review is not high.

¹⁸ SCO paragraph 2.56

¹⁹ SCO paragraph 2.57

²⁰ SCO paragraph 2.58

Experience has shown that in the small number of cases where there has been both a judicial review and a merits review, the value of both forms of review has been demonstrated.

- Removal of merits review is by no means a guarantee that regulatory processes will be streamlined.
- Applicants are very aware of the costs and time involved in reviews and would have every incentive to seek the most cost-effective form of review given the nature of the particular regulatory decision;
- Experience to date clearly shows that merits reviews have involved substantially shorter time periods (and therefore costs) than judicial reviews;
- AGL does not support the contention that if review is limited to an “augmented” judicial review, there will be greater certainty around economic decision-making. In fact it would seem self-evident that the opposite is true, as there is much greater uncertainty that the regulator’s errors can be corrected.

The discussion paper also argues that:

*the AER’s decision-making process will involve an extensive inquiry process that would be both time-consuming and costly to repeat on review. The Administrative Review Council (ARC) guidelines indicate that, where a decision involves an extensive inquiry process, merits review may not be justified.*²¹

This argument includes a number of considerations that are not relevant or incorrect as follows:

- Neither Model A nor model B involves repeating of a process on review; and
- The full quote from the ARC’s guidelines relating to “factors that may justify exclusion of merits review” is: “Decisions involving extensive inquiry processes and decisions which have such limited impact that costs of review cannot be justified”. The underlined part of the quote has been omitted in the discussion paper. Clearly economic regulatory decisions of the type taken by the AER in relation to gas and electricity access cannot be classified as being of such limited impact that the costs of review are not justified. Merits reviews that have demonstrated error to date have been associated with very significant amounts of money.

On this basis, exclusion of merits review cannot genuinely be portrayed as being supported by the ARC’s guidelines. Again, the opposite is true. When the whole of the ARC’s guidelines are considered they point very strongly to the need for merits review in the case of economic regulatory decisions on energy access.

3.3.2. Arguments against Model A

The discussion paper puts the view that:

*A commonly expressed concern with merits review is that it is highly likely to result in gaming and forum shopping by (rational and self-interested) energy providers.*²²

²¹ SCO paragraph 2.59

²² SCO paragraph 2.50

Such concerns are essentially based on misconceptions about the actual provisions for and practice of merits review, particularly under the GPAL.

Resources needed by the review body

The discussion paper questions the reviewing body's competence to identify error if it does not have the same resources as the original decision-maker. This position indicates a misconception about the process undertaken in a limited merits review, such as model A²³. In particular:

- The discussion paper's implication that the review body must have the full resources of the decision-maker does not reflect current practice in merits review. An expert review body such as the ACT, generally relies on evidence before the original decision-maker and arguments about it put by the decision-maker and the applicant. It is well equipped to evaluate and draw conclusions about this material. This well-understood process delivers high quality decisions effectively and efficiently; and
- This is demonstrated by merits reviews by the ACT under the GPAL, which have uncovered significant regulatory error in reviews. There is no conceptual or practical reason why merits review bodies, as currently resourced, cannot continue to function effectively.

The interests of the range of stakeholders

The suggestion that, the interests of particular stakeholders will be overlooked if the merits review body does not duplicate the investigative and consultative process used by the regulator, is not sustainable because:

- The discussion paper acknowledges that Australian regulators follow "a thorough consultative process and public scrutiny"²⁴. This gives all parties the opportunity to present their views. This information then becomes part of the material before the merits review body;
- The discussion paper envisages that under neither Model A nor Model B will a *de novo* review be available²⁵. Thus, neither the ACT nor the Federal Court will be able to conduct "a comparable investigative and consultative process to that which is used by the regulator" and therefore it is not contemplated that stakeholder consultation will be duplicated; and
- In summary, a duplication of the regulator's "investigative and consultative process" is neither contemplated nor warranted, and the absence of such duplication is not an argument against a Model A merits review – and is certainly not an argument for Model B.

The time and cost of conducting merits reviews

Experience to date demonstrates that merits reviews under the GAR have involved substantially shorter time periods (and therefore costs) than judicial reviews. There are a number reasons for this:

- Appellants are only going to seek review of matters over which there is dispute. This will limit the material to be considered;

²³ It also suggests a simplistic view of the requirements of a judicial review.

²⁴ SCO Discussion Paper, para 3.12

²⁵ SCO Discussion Paper, para 2.1

- The GPAL requires the continuation of the regulator’s decision pending the outcome of the review (and subsequent implementation of the review body’s determination). That is, it is not stayed. This means that the applicant has nothing to gain from prolonging an appeal, because there will be no benefit if error is not found; and
- The GPAL requires a limitation of 90 days for the review body’s determination. While the ACT may extend the time to make its decision by 30 day periods under defined circumstances, both the defined constraint in the GPAL and the Tribunal’s obligation to be prudent with its own time mean that the decision will be made in the shortest possible time.

Including similar requirements under Model A could be expected to deliver streamlined and efficient merits reviews as have been experienced under the GAR.

3.4. *The appropriate applications for Model A and Model B*

It is clear from the foregoing analysis that Model B provides little, if any, more scope for review than current judicial review. The discussion paper’s main argument appears to be that Model B’s main advantage is that it eliminates the right to merits review. This offers the possibility of reducing administrative costs, but to the extent that the assumption about costs is correct, this does not take into account far greater economic costs of uncorrected regulatory error and reduced confidence in the regulatory regime. AGL submits that the potential level of cost reduction is questionable, because the absence of merits reviews is likely to lead to an increased number of judicial reviews, and these reviews with extensive process and evidentiary requirements may prove to be at least as costly overall.

As noted in section 3.1 and 3.2 above, there are implications in the paper that Model B, as an enhanced version of judicial review, might substitute for Model A merits review. AGL submits that such a view is not sustainable on the evidence and indeed Model B is a complement to rather than a substitute for Model A.

Once misconceptions about both Model A and Model B are corrected, it can be seen that Model A (with judicial review as a given) will meet the policy criteria for review. That is, limited merits review (Model A) and judicial review (Model B) are not alternatives which invite a choice, but complements. The availability of each type of review allows the full spectrum of regulatory error to be addressed in a manner which maximises confidence in the regulatory regime and meets the criteria set out in section 1.10 of the discussion paper, while at the same time delivering reviews at the lowest total administrative and economic cost.

4. Merits Review – Appropriate characteristics for Model A

AGL broadly supports Model A as set out in the discussion paper. Further comment on the various elements of Model A is provided below.

4.1. *Review body*

AGL agrees that the ACT’s experience, knowledge, structure and independent position make it the most appropriate appeals body to conduct merits appeals for regulatory decisions. The ACT’s role under the Trade Practices Act generally makes it eminently suited to the role of reviewing economic regulatory decisions. In particular, having responsibility for review of decisions in the overlapping

arenas of competition regulation and access regulation brings strength to its decision making.

Given the breadth of ACT roles and the common core elements in economic regulation for gas and electricity, the distinction between decisions for these two energy forms is unlikely to be relevant. However, the ACT can only be strengthened by inclusion of non-judicial members with expertise in electricity and gas matters.

4.2. *Standing to commence merits review proceedings*

On the questions of access to the review process and other related matters, AGL largely supports the criteria put forward in the discussion paper, and believes that service and network providers and affected users who meet a high threshold or "materiality" test should have standing to commence proceedings. AGL questions the inclusion of the regulator in the list of parties to have standing as the regulator is the decision-maker and therefore would not appeal its own decisions.

AGL sees little reason for interveners aside from the appellant and the respondent. The benefits of allowing others to join merits review proceedings are likely to be minimal and would be outweighed by the associated costs and complications. Energy consumer interests are already adequately represented in such proceedings, as the regulator will be required to take their interests into account, both as part of their charter and by the objectives of the NEL and NGL. However, AGL accepts that such decisions should properly be left with the appeals body.

For coverage decisions, AGL supports providing the right to merits appeal to all parties affected by such decisions.

4.3. *Grounds for review*

The Productivity Commission's (PC) review of the GAR recommended the removal of limitations on the grounds of appeal for merits review to allow full merits review on access arrangements drafted and approved by the regulator (and consistent with the grounds of merits review for coverage decisions)²⁶. This recommendation was made in recognition of the need to appropriately protect property rights. While AGL supports the PC's findings, AGL accepts that for efficient merits review, that - other than for coverage decisions and other non-access arrangement decisions - the development of a clear set of grounds is appropriate for regulator's decisions.

AGL notes that the grounds currently contained in section 39(2) of the GPAL have proven to provide an appropriate balance between preserving participants rights and delivering streamlined reviews and provide a sound basis for the grounds of review for a limited merits review model.

The discussion paper proposes a more restricted grounds of review for Model A by excluding the third ground, namely that the occasion for exercising the discretion did not arise. While AGL sees no reason to move the third ground, it accepts that the second ground effectively encompasses it and is not opposed to its removal.

The discussion paper suggests a possible replacement of the second ground to where the exercise of discretion by the regulators was "manifestly" unreasonable.

²⁶ *Review of the Gas Access Regime*, Productivity Commission Inquiry Report, June 2004, Recommendation 11.4

Such a change would render Model A merits review pointless as it would potentially raise the bar on merits review to one that is even higher than would apply in judicial review. Accordingly the test should simply be for reasonableness in all the circumstances.

Under the GPAL for merits review of coverage decisions (and also non-access arrangement decisions), there is currently no limitation on grounds. AGL submits that the nature of this decision – where the decision-maker must be ‘affirmatively satisfied’ about a number of matters in order to decide that a pipeline should be regulated can be made – means it is unlikely that appropriate grounds can be developed. Moreover, AGL submits that the Model A grounds would be unworkable for the purpose of coverage decisions (and probably the other non-access arrangement decisions).

4.4. *Appropriate types of decisions*

AGL broadly agrees with the appropriate types of decisions set forth in chapter 5 of the discussion paper. However, AGL is opposed to a reduction in participant rights. Consequently it is necessary to review whether the proposed appropriate types of decisions for Model A would be narrower in scope than those currently available under the GPAL. This outcome would be undesirable and would require a revisiting of the criteria for meeting the requirements of Model A.

With regard to electricity, AGL is of the view that the availability of merits review should not be limited to pricing and access decisions. Availability should be extended to decisions regarding ringfencing (as for gas).

4.5. *Powers and remedies*

AGL supports the powers and remedies for Model A proposed in the discussion paper. The ACT should have the discretion to make its own decision in place of the regulator’s or remit the matter to the regulator for reconsideration in accordance with its directions. AGL notes that the powers and remedies put forward for Model A in the discussion paper are largely consistent with those currently available under the GPAL and that these have proven to be practical and efficient.

4.6. *Admissible materials*

The scope of evidence to be considered by the ACT should be linked to evidence that was formally before the regulator leading up to the final decision. This approach allows the merits appeal body to properly step into the shoes of the decision-maker and limits the likelihood of time delays associated with gathering additional evidence.

AGL is of the view that as a general rule for economic regulatory decisions such as decisions about access arrangements for gas and revenue/pricing, it is unnecessary for new material to be submitted during a merits review hearing even where an error of fact or discretion is found. Importantly, it is likely that allowing new material at the point of finding of error will substantially and unnecessarily add to the time that appeals will take, with little benefit. This would largely be because the ACT would first have to find error and then provide participants in the review the opportunity to gather new evidence and then deliver it before the Tribunal. Producing new evidence will also involve more protracted processes than material that is already before the regulator.

While AGL is of the view that the general rule should preclude new material, there is a case for the ACT to have limited discretion to introduce new material. This would be limited to (a) where there has been a material change in circumstance or (b) where the regulator has relied on material that was not subject to public/industry consultation.

Under the GPAL, for merits reviews of coverage decisions there is currently no limitation on materials that may be entered into evidence. AGL submits that the nature of this decision – is such that effectively a ‘go/no go’ decision on whether a pipeline should be regulated – there are sound reasons for broader material to be included than that considered by the National Competition Council (NCC) and the Minister. There is no incentive for an applicant to withhold information during the process leading to the Minister’s decision. The introduction of new material may actually focus and streamline the merits review.

4.7. Costs

AGL cannot see any valid reason to fetter the ACT’s discretion in relation to costs and believes that the wide discretion currently allowed by GPAL should be carried over to the new merits review model. Allowing the ACT wider discretion to make decisions on costs provides for a more flexible approach and for such decisions to be made on a case-by-case basis as appropriate.

It would be shortsighted to set barriers to parties legitimately seeking review of regulatory decisions in order to discourage potentially (and unlikely) trivial or vexatious actions being brought. The ACT may refuse to hear matters of such a nature under the GPAL and it is assumed such a provision will be part of Model A.

4.8. Scope of review

Issues that can be considered by the merits appeal body should be restricted to the matters of contention raised by the applicant. This will focus the review to the matters of contention, thereby increasing the efficiency and timeliness of merits review.

5. Merits review for gas and electricity

Earlier in this submission, AGL identified that a limited form of merits review of the kind embodied in Model A is an appropriate model for review of energy access decisions. AGL has also identified that the GAR provides limited merits review rights similar to Model A and that any material reduction in merits review rights would substantially reduce gas participant rights. Without the support of a demonstrated offsetting benefit to participants and strong policy reasoning this outcome would be totally inappropriate.

The discussion paper raises several questions about whether it is appropriate to provide merits review for electricity. AGL has in its submission on the Statement of Approach for the Gas Legislative Framework identified differences between the gas and electricity regimes and argued that there should not be an automatic presumption that they should be treated in the same manner. However, the differences identified related to the focus for the legislative frameworks for the two regimes; the focus for the electricity regime being the market in electricity itself while for gas it is access to infrastructure. The context for the MCE’s consideration of merits review relates to economic regulatory decisions on access matters that have been made by the same regulatory bodies and following similar processes. Accordingly differences identified by AGL are not relevant to the need for review of economic regulatory decisions about access. Furthermore, in the

making of such decisions, the levels of discretion available to the regulator in electricity are no less than those available in gas, so it is logical that merits review, as applied in the gas access regime, should be made available to electricity access regime.

AGL notes that the discussion paper suggests that the need for merits review for electricity would need to be assessed should the nature of electricity revenue and pricing determinations become much less discretionary.²⁷ AGL is puzzled at this statement as under both the NER and individual state-based regimes electricity decisions have considerably more discretion available than gas decisions. There would have to be a significant lessening of discretion in both the gas and electricity regimes before such a reassessment is warranted.

Another comment made in the discussion paper is that the introduction of merits review for electricity would need to be justified on substantial grounds and would not be warranted, for example, simply to achieve consistency between gas and electricity.²⁸ As outlined in section 2 of this submission, the availability of merits review for gas has enhanced the gas regime and is a key element in maintaining confidence in it. AGL submits that there are strong reasons to maintain the review regime for gas, and there is much to be gained by enhancing the electricity regime by providing recourse to merits review. It is not a question of simply achieving consistency between gas and electricity, but of applying the same compelling logic to the access regimes for both energy forms and reaching the same conclusions in both cases.

A further comment made in the discussion paper is that the non-inclusion of merits review under the old NEL does not appear to have lessened the quality of decisions made by economic regulators²⁹. This comment is not sustainable as there is no counterfactual. That is the lack of availability of merits review means that participants had no forum to test the quality of the regulator's decisions. In any event, it does not logically follow that the availability of merits review will not improve the quality of economic regulatory decisions in electricity. Moreover, the facts do not support the contention, as there have been merits reviews of electricity decisions in both Victoria and SA, and in both cases the regulator's decisions were varied.

In conclusion, AGL is strongly opposed to gas merits review rights being downgraded as this would not only lead to a substantial loss of rights for gas participants, but would also lead to reduction in the quality of regulatory decision making and erode confidence in the system. Extending merits review rights to electricity would allow that regime to gain from increased quality of and confidence in decision making.

²⁷ Paragraph 5.14

²⁸ Paragraph 2.60

²⁹ Paragraph 2.60. The reasons for merits review not being previously available for economic regulatory decisions in electricity is probably historical, relating to the traditional government ownership of utility assets.

Answers to Specific Questions

Question 1: Do you prefer Model A or Model B?

AGL does not believe that Model B provides a valid alternative to Model A merits review. In fact, presenting the two models as alternatives is misleading and they should properly be considered as complementary. That is, Model B has a valid role as judicial review which complements Model A merits review. Refer to section 3.4 of this response for a detailed explanation of AGL's position.

As to Model A

Question 2(a): Do you agree with subjecting the following decisions to Model A merits review:

- AER decisions to draft and approve access arrangements or revisions to access arrangements in gas;
- Ring fencing decisions by the AER, including decisions not to approve associate contracts, in gas;
- Ministerial decisions in relation to coverage of gas pipelines; and
- For electricity, the AER's determinations on revenue caps for transmission network services, and ultimately distribution network services?

At a minimum the above types of decisions should be open to merits review. Some decisions (such as those relating to coverage) may warrant a wider type of merits review than that prescribed in Model A. Further, as outlined in section 4.4 of this submission there are additional types of decisions which should be subject to merits review.

Question 2(b): Who do you consider should be able to commence Model A merits review in respect of:

- Ministerial decisions on coverage in gas, and
- the specified AER economic regulatory decisions?

See section 4.2 of this submission for a detailed response to this question.

Question 2(c): Who should be able to join Model A merits review proceedings once they have been commenced and what issues should intervenors be able to raise with a decision?

There is no reason for any intervenors aside from the appellant and the respondent. The benefits of allowing others to join merits review proceedings are minimal and would be outweighed by the associated costs and complications. Energy consumer interests are already adequately represented in such proceedings as the regulator acts on their behalf. However, this matter can reasonably be left in the hands of the appeals body (presumably the ACT) as is the case in the GPAL.

Question 2(d): SCO seeks comments from stakeholders as to the suggested grounds of review set out in Model A, in respect of both:

- Ministerial decisions on coverage in gas, and
- the specified AER economic regulatory decisions.

See section 4.3 of this submission for a detailed response to this question.

Question 2(e): Do you agree with the restriction on evidence proposed for Model A merits review in paragraph 6.60? Do you agree with the suggestion set out at paragraph 6.64?

For the reasons outlined above in section 4.6 of this submission, AGL believes that as a general rule it is unnecessary for new material to be submitted during a merits review hearing.

In respect of the proposed AER guidelines AGL does not see any particular benefit from these. To the extent that these are relevant, they would be taken into account when considering whether the regulator's discretion was "reasonable in all of the circumstances".

AGL is concerned about the possible development of guidelines by the regulator that effectively amounted to it making its own rules. An essential rationale in establishing the AEMC and the AER has been to separate the roles of rule making and regulating. In the light of the importance of the principle of separation of powers, the making of such guidelines by the regulator would be inappropriate (and possibly beyond its powers). Importantly, if the review body was required to take these into account the ACT would have to assess the reasonableness of the guidelines, so that it was not prevented from finding a ground for review simply because the regulator had published its own guideline.

Question 2(f): Do you agree with the proposal for awarding costs for Model A merits review in paragraph 6.67 or have any other views as to the costs of the review process?

As outlined above in section 4.7 of this submission, AGL favours the approach to costs currently contained in the GPAL and considers it unhelpful to fetter the ACT's discretion in this regard.

As to Model B

Question 3(a): Comment is sought on the central proposition of Model B: namely, that the usual basis for judicial review should be augmented by specific legislative requirements to define the decision-making process and make explicit the basis for decision-making.

Comment on this proposition could be directed to the requirements now set out in ss.16, 35 and 36 of the NEL (in relation to transmission determinations) – eg are those requirements appropriate to form the basis for judicial review of the kind proposed in Model B? Comments might also be made on what requirements would be appropriate for that purpose in the case of distribution determinations under the NEL and economic regulatory decisions under the NGL.

For the reasons given in section 3.1 and 3.2 AGL does not believe that "augmented" judicial review embodied in Model B provides a capacity to review decisions which is materially greater than ordinary ADJR judicial review rights. In addition, the Model B approach does not provide any review of the merits of a regulator's decision.

Question 3(b): Do you agree with the approach proposed in respect of Ministerial decisions on coverage in gas?

AGL believes that the approach of only applying judicial review to ministerial decisions on coverage is incorrect. The reason coverage decisions reside with the Minister is to separate the decision to regulate from the regulatory body. Ministerial decisions on gas coverage matters are largely competition-related decisions rather than policy decisions and are analogous to declaration decisions under the National Access Regime³⁰. As full merits review is available for declaration decisions Model A merits review of such decisions (with no grounds for review) should be available.

Question 3(c): Comments are invited on other aspects of Model B.

As a general comment, Model B provides little/no extra review on top of the judicial review which would ordinarily be available under the ADJR Act. Further, it does not go to the merits of a decision and would therefore not lead to increased quality in regulatory decision making. AGL's view is that Model B (as judicial review) is essentially a complement to Model A, which should not be presented as an alternative.

³⁰ Part IIIA of the Trade Practices Act