

ECONOMIC REGULATION AUTHORITY SUBMISSION TO THE

Ministerial Council on Energy Expert Panel Draft Report on Review of Revenue and Network Pricing Across the Energy Market

INTRODUCTION

The Western Australian Economic Regulation Authority (“Authority”) is pleased to make this submission to the Expert Panel (“Panel”) on its Draft Report.

The Authority as the relevant regulator under the *National Third Party Access Code for Natural Gas Pipeline Systems* (“National Gas Code”) will be directly affected by the recommendations of the Panel, although its economic regulation of access to electricity transmission and distribution services, which is undertaken under a State-based regime, may not be affected immediately.

The Authority believes that the Panel has produced a balanced assessment of the issues and broadly agrees with the findings and recommendations. In this submission the Authority has addressed the following broad areas.

1. The Legal and Regulatory Framework.
2. Objectives for the Energy Access Regime.
3. Framework for Regulatory Decision Making.
4. Guidance on the Application of Price Control.
5. Information Requirements.

In discussing the five areas listed above, the Authority has given particular attention to the possible impact that the Ministerial Council on Energy’s recommendations may have on the future development of State based regulatory regimes in Western Australia.

THE LEGAL AND REGULATORY FRAMEWORK

The Authority concurs with the Panel’s view that there is a need to achieve a common approach to energy sector regulation in electricity and gas. A common legislative approach would provide high level principles that define (and constrain) the scope of Rule making and regulatory discretion.

The Authority also agrees with the Panel’s view regarding the degree of detail to be included in the Law and that the principles in the Law should be cast at a level so that they can be expressed in similar terms across transmission and distribution facilities in both the electricity and gas markets. This allows scope for differences in the application of the common principles, in order to account for different market and technical characteristics, being reflected in the Rules and regulatory decision making.

With respect to the level of prescription in the Rules, the Authority agrees with the Panel’s reasoning for concluding that due to the nature of the conflicting objectives¹ there is unlikely to be any meaningful general legislative principle that would provide guidance on the appropriate level of prescription within the Rules. The Authority believes, however, that in considering the conflicting objectives that the existing regime should be seen as a point of

¹ That is, prescription to achieve certainty/stability of regulatory outcomes versus being able to accommodate the particular circumstance of individual market participants in regulatory decisions.

reference, given that there is evidence that the balance is about right and there is an absence of evidence to the contrary.

OBJECTIVES FOR THE ENERGY ACCESS REGIME

The Authority agrees with the Panel's assessment of the differences between the objects clauses in the National Electricity Law (NEL) and the National Gas Law (NGL) and considers that there is merit in ensuring that the clauses are consistent. The Authority therefore supports the two recommended objects clauses for the NEL and the NGL and the suggested explanatory statement to be included in the Explanatory Memorandum and Second Readings speech for the Bill.

FRAMEWORK FOR REGULATORY DECISION MAKING

The Authority (and its predecessor the Western Australian Independent Gas Pipelines Access Regulator) has had substantial experience in approvals under section 2 of the National Gas Code and supports the process under the National Gas Code for assessment and approval of access arrangements. The Authority considers that the process of draft and final decisions, and opportunities for consultation that this provides, is consistent with broad requirements for procedural fairness in the making of regulatory determinations. The process under the National Gas Code has become known and accepted by stakeholders in regulatory determinations.

In considering the establishment of a maximum time period for a regulatory determination the consideration should be given to the following:

- where a service provider or other relevant party withholds information that the regulator may require for the making of a determination, significant delays in the process may occur where the regulator has to resort to compulsory powers of information acquisition, particularly in circumstances where a service provider or other party has a right of appeal over the exercise of these powers or over a decision by the regulator to publicly release information;
- where, after an initial submission of a revenue proposal, a service provider submits changes to its proposal or further information, the AER may find it necessary to extend periods of consultation to allow interested parties to make submissions on the relevant changes or further information; and
- where new information becomes available to the regulator during the course of a determination, particularly subsequent to a draft decision and related submissions, which would cause the regulator to make a significant alteration of its determination and, for reasons of procedural fairness, may require the regulator to engage in further consultation with either the service provider or other stakeholders that would be affected by the alteration.

The Authority therefore submits that, if a maximum time for a determination is established, that consideration be given to the problems that this might create for obtaining information relevant to the determination and for procedural fairness. In particular, the Authority considers that those responsible for establishing the rules should give consideration to:

- providing explicit guidance to the regulator as to the process, functions and powers in the making of a determination in circumstances where the service provider fails to provide adequate supporting information in support of certain elements of the service provider's proposal;
- the circumstances in which it may be necessary or desirable to suspend the timing of a determination, and the process by which such a suspension may be implemented.

GUIDANCE ON THE APPLICATION OF PRICE CONTROL

The Authority notes that the Panel has given considerable attention to the presumption of accepting a proposal from a service provider in the context of considering the broad “model” of regulation. The Panel has taken the view that these requirements are consistent with a “propose-respond” model of regulation similar to that established under the WA Electricity Code (explicitly) and the National Gas Code (as the Gas Code has been interpreted since 2003). The Authority also notes that the Panel has taken the view that this model of regulation establishes a presumption in favour of accepting a service provider’s proposal and may lead to a systematic increase in the returns to service providers relative to a conventional “consider-decide” model of regulation.²

To the extent that the existing regulatory schemes for gas and electricity infrastructure may potentially give rise to regulatory risk for service providers, the Authority agrees with the Panel’s conclusion that there are more appropriate mechanisms for addressing the potential for regulatory risk. In particular:

- requiring that the regulator accord weight to the service providers proposal in making a determination, but not establishing the presumption in favour of approving the service provider’s proposal; and
- ensuring that there exists a well-designed process for merits review of regulatory determinations.⁵

The Authority suggests that the revision of regulatory frameworks is itself a potential source of regulatory risk and that the need for change should be rigorously demonstrated. The prospect of revisions to regulatory frameworks and the impact that this has on regulatory risk is an issue that the Authority has raised in submissions in the past. The Authority considers that the grounds for proposing revisions to regulatory frameworks need to be well founded in order to avoid impacting on regulatory risk unnecessarily.⁶

² Expert Panel on Energy Access Pricing, March 2006, Draft Report to the Ministerial Council on Energy, pp 68, 69.

⁵ *Ibid.* p 77.

⁶ The following submissions by the Authority (available on the ERA website at <http://www.era.wa.gov.au/publications.cfm>) make reference to the impact on regulatory risk of proposing changes to the regulatory framework:

- Inquiry Into the Provisions of the Trade Practices Amendment (National Access Regime) Bill 2005, 29 July 2005, ERA submission to the Senate Economics Legislation Committee Inquiry into National Access Regime amendments.
- Utility Regulators Forum Joint Paper to the Ministerial Council on Energy - 7 April 2005
- Australian Institute of Energy – Perth Branch, June 1, 2004, Lyndon Rowe, Chairman Economic Regulation Authority.
- “Future Energy Developments in Western Australia: Issues in Economic Regulation”, 17 November, 2004, Lyndon G. Rowe, Chairman, Economic Regulation Authority, Sixth Energy in Western Australia Conference 2004.
- ERA submission to the Infrastructure Taskforce discussion paper on exports and infrastructure, 29 April 2005.
- ERA follow-up submission to the Infrastructure Taskforce discussion paper on exports and infrastructure, 16 May 2005.

The Authority agrees with the Panel's recommendation that, if the approach that is being taken by the AEMC in its draft Electricity Rule proposal for determinations on cost forecasts were to be maintained and more broadly applied in access regulation, consideration should be given to mechanisms to reduce the options for 'gaming' the decision making process.⁷

INFORMATION REQUIREMENTS

The Authority strongly agrees with the Panel's assessment, findings and recommendations regarding the information requirements as an essential input into the regulatory functions of the regulator. It also recognises that the form of regulation will dictate the level of information that the regulator will need to effectively discharge its obligations.

CLOSING REMARKS

The Authority has previously made a number of submissions⁸ which cover a number of the matters addressed above including the objectives for the energy access regime, the framework for regulatory decision making, information requirements and the form of regulation. The Authority would encourage the Panel to review these if it desires further perspectives on the matters discussed in this submission.

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⁷ Expert Panel, *op.cit.*, p 82.

⁸ These submissions are referenced at footnote 6 above.