



15 November 2005

Merits Review
c/- MCE Market Reform
Department of Industry, Tourism and Resources
GPO Box 9839
Canberra ACT 2601

Review of Decision-Making in the Gas and Electricity Regulatory Frameworks

esaa welcomes the opportunity to comment on the Standing Committee of Officials' (SCO) consultation paper on Review of Decision-Making in the Gas and Electricity Regulatory Frameworks (the Paper). esaa represents the Chief Executives of Australia's 45 electricity and downstream natural gas companies. These companies include network businesses, as well as network users, and esaa is therefore well placed to comment on an appropriate, balanced model for the review of decision-making in the gas and electricity regulatory frameworks.

esaa has a clear position on the need for merits review. We strongly contend that economic regulatory decisions related to access arrangements for energy networks should be subject to merit and judicial review and once concluded be enduring, given the long-lived nature of the assets involved

Form of the Regulatory Framework Unclear

In seeking to provide detailed comments on the paper, however, an unfortunate aspect of this consultation process is that the form and nature of the regulatory framework itself is still in question. The Ministerial Council on Energy has announced the formation of an Expert Panel to consider, among other matters, fundamental questions about the nature and scope of the regulator's discretion in the energy access regime. The Paper even recognises that the design of an appropriate review regime is dependent on the "larger framework" and that this is to be settled over the "coming months". Therefore, the industry can only consider the two proposed review models in the context of the existing regulatory regimes – which are highly discretionary, technically complex and particularly wanting when it comes to a "body of rules designed to structure and guide the exercise of regulatory discretion".

The existing regulatory frameworks for gas and electricity both give the regulator a broad discretion to make highly technical and complex decisions that have a significant economic impact on the viability of a business. The basic principle behind merits review is that where a regulator/administrative decision maker exercises a significant degree of discretion and this discretion has a large impact on the economic viability of a business there should be the opportunity to review the exercise of this discretion. Notwithstanding the inclusion of Sections 16, 35 and 36 of the new NEL, the electricity regulatory regime continues to be highly discretionary and, one could argue, even more discretionary than gas.

esaa Supports Model A

On this basis, the esaa supports the Paper's proposed 'Model A' – where the Australian Competition Tribunal (ACT) would undertake a limited form of merits review of the economic regulatory decisions of the Australian Energy Regulator (AER) in the case of gas and electricity, and of relevant Ministers in the case of coverage decisions. Indeed, esaa considers that an expansion of Model A may be warranted to cover the types of decisions that would be subjected to merits review. Should the Ministerial Council on Energy decide to implement the SCO's proposed model for price monitoring in the Gas Access Regime, then the esaa considers that the AER's decision over the form of regulation (price regulation or price monitoring) should be subjected to merits review too. In addition, the Expert Panel has been tasked with considering whether a 'coverage' type decision should be warranted in electricity distribution. If a 'coverage' decision was to apply to electricity distribution networks then the Minister's decision should be subjected to merits review - as is the case with gas networks. Similarly, should the Expert Panel recommend a 'propose and respond' model for electricity network regulation, then the AER's decisions to draft and approve access arrangements or revisions to access arrangements in electricity should also be subjected to merits review.

esaa does not accept the Paper's assertion that 'Model B' could be a possible alternative model for an appropriate review scheme. To suggest that 'Model B' is more than the judicial review rights that are afforded to a business by the Constitution and Commonwealth law is, we contend, erroneous. Further, the right to judicial review already exists and to suggest that the National Electricity Law (NEL) is now sufficiently prescriptive that the regulator's discretion is curtailed to the point where judicial review is a reasonable alternative to merits review is rejected. In fact, the legal advice esaa received from Gilbert & Tobin when the new NEL was being drafted stated that the move to a single market objective actually **reduced** the scope for judicial review because the new, single market objective is broader than the multiple objectives that previously existed and it therefore could be more difficult to prove that the regulator acted outside its remit. This is a fundamentally different question to the merits of a particular position settled on by a regulator in areas where they have discretion.

Arguments Against Model A Not Compelling

The considerable benefits that a merits review mechanism affords are well known and well articulated by industry participants, policy makers, regulators and the judiciary alike. The Paper itself makes a series of compelling arguments in favour of 'Model A' and there is no need to re-state those arguments in this submission. Conversely, in our view the Paper's arguments against 'Model A' and in favour of 'Model B' are not compelling.

'Model A' is not a *de novo* review mechanism but has been specifically designed as a limited form of merits review to address the very issues the Paper lists as potential weaknesses. As set out in other submissions, 'Model A' contains a number of procedural restrictions which ensures that the review process is low cost, targeted to the issues in contention, does not delay the entry into effect of the decision, and is not subject to potential gaming by parties.

On the other hand, the Paper puts forward 'Model B' as a viable alternative, despite the fact that judicial review is a fundamentally different type of review process designed to ensure the law has been correctly interpreted and followed. It does not test the validity of the judgements and assumptions made by regulators in areas where they have quite broadly bounded discretion.

Adding to the problems of relying solely on a judicial review process through the Federal Court is that this is often a much lengthier and more costly process than a merits review hearing by an independent tribunal and, as the Paper states, "has the potential to leave in place regulatory errors that may have adverse economic effects."

Further Benefits from Merits Review

There is, however, a further significant benefit from a merits review mechanism that is not articulated in the Paper. As the energy industry moves toward a single, national energy regulator, the opportunity to benchmark regulatory performance significantly reduces. While the esaa does not support the continued existence of multiple energy sector regulators, it should be recognised that the existence of a number of similar regulatory agencies, performing very similar functions, provides an external point of comparison and applies an additional discipline on any individual regulator.

Merits review decisions in a new single regulator environment should be seen as an important component of developing the application of the regulatory framework. Together with the regulator's decisions, the body of merits review decisions will provide precedents that will yield greater clarity and assistance to the regulator and companies alike in an environment where there will be little, if any, opportunity to consider regulatory approaches in the context of peer decisions.

Consistent Treatment of Gas and Electricity Needed

The Paper states that there is a need to mount a case for the application of merits review in electricity (as opposed to gas) but this is reliant on the belief that 'Model B' is actually feasible as an alternative to merits review. Dr John Tamblyn, while he was still Chair of the Essential Services Commission and regulating both electricity and gas distribution assets, made the statement that:

“There is no obvious reason why owners of electricity transmission and distribution assets should have inferior rights to appeal than owners of comparable gas network assets, and the presence of such differentiation raises concerns about whether the pattern of investment may be distorted between the industries, as well as raising basic questions about fairness and natural justice.” (*Administrative Law Meets the Regulatory Agencies: Tournament of the Incompatible?*)

esaa concurs with Dr Tamblyn's observation.

We consider that the availability of merits review for economic regulatory decisions in gas and electricity is a critical component of an effective regulatory regime. We encourage the SCO to recommend to Ministers that they adopt 'Model A' as the appropriate review regime for the energy market.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Brad Page', with a stylized flourish at the end.

Brad Page
Chief Executive Officer