

7 November 2005

Ref.

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

Emailed to: MCEMarketReform@industry.gov.au

Dear Sir/Madam

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

Thank you for the opportunity to present Enertrade's views on the Standing Committee of Officials' consultation paper on possible review schemes in the gas and electricity regulatory frameworks.

Enertrade owns and operates the North Queensland Gas Pipeline, a gas-fired power station at Barcaldine, and purchases electricity from privately-owned power stations through Power Purchase Agreements, which it trades into the National Electricity Market.

Enertrade strongly supports the retention of the current appeals rights contained in the Gas Access Regime. It also supports the extension of these rights to the electricity industry.

In addition to its own submission, Enertrade supports the submission made by the Australian Pipeline Industry Association.

The right to merits review

Merits review is available for a broad cross-section of administrative decisions ranging from decisions by the Australian Film Commission on the exhibition of short films to decisions subjecting hundreds of millions of dollars of privately owned infrastructure to regulation under the National Access Regime.

This reflects a presumption of the right to merits review when an administrative decision is likely to impact on an individual's legitimate interests.

This raises the question why merits review should not be available in respect of energy regulation? Decisions made under the Gas Access Regime and the National Electricity

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Rules have the potential to substantially and adversely impact on the finances and commercial operations of users and service providers.

Enertrade strongly submits that judicial review alone is inadequate to protect the legitimate interests of service providers and users. While access to judicial review ensures the Regulator is held accountable for following the correct procedures in reaching its decision, access to merits review is required to ensure that the correct and preferable decision is reached:

A decision made under the Gas Access Regime involves both procedural and judgemental elements. That is, when the correct procedures and processes are followed, the decision maker still exercises an element of judgment. There is a risk that an error will be made.¹

Further, decisions under both regimes are long-lived – generally five years for access arrangements and an indefinite period for coverage – and have the potential to cost affected parties millions of dollars. These decisions also have a wider impact on the economy. Unchecked regulatory error will undermine ongoing investment in a critical industry.

The sale of utility assets to private investors has imposed a high hurdle for both the transparency of the regulatory process, and for checks and balances in the process – The degree of confidence investors have in the regulatory framework and decision-making under which prices are determined will be a driver of willingness to continue to invest.²

The significance of the errors on the interests of individuals highlights the value of a system of comprehensive appeal rights. These appeal rights are particularly important in the energy sector given the size of the investments and the consequential impact an erroneous decision can have on an affected party.

The history of merits review in gas

While there have been relatively few appeals, the cases before the Australian Competition Tribunal under the Gas Access Regime have demonstrated that errors have occurred and that they have had a significant impact upon the businesses.

In the Duke Eastern Gas Pipeline case³ the Tribunal found that the case for coverage had not been made out on the facts noting that a decision to cover a pipeline can have major commercial implications for the owner or operator of the pipe.

Tribunal decisions on access arrangements have also revealed regulatory errors that had significant implications for the pipeline owner. In the Epic Energy case⁴ the Tribunal found the approach adopted by the ACCC of choosing the lowest indicative

¹ Productivity Commission, *Review of the Gas Access Regime*, 2004, p 488.

² John Tamblin, *Administrative Law meets the Regulatory Agencies: Tournament of the Incompatible?*, papers from the 2004 Public Law Weekend Administrative Law Conference.

³ *Duke Eastern Gas Pipeline Pty Ltd* [2001] A CompT 2 (4 May 2001)

⁴ *Application by Epic Energy South Australia Pty Ltd* [2003] A CompT 5 (10 December 2003)



prices for line pipe in calculating the initial capital base was not reasonable. This was particularly significant given the importance of line pipe costs in the calculation of Epic's costs. The Tribunal also found that the decision to include the expansion as part of the covered pipeline was unreasonable.⁵

GasNet applied to the Tribunal⁶ for review on the grounds related to the determination of the reference tariff. The Tribunal noted the adverse impact on GasNet's revenue caused by the ACCC's rejection of GasNet's estimations of the Capital Asset Pricing Model parameters and of the non-capital costs.

The decisions of the Tribunal form a significant body of precedent which will assist Regulators, users and service providers alike on the application of the Gas Code going forward. This provides greater certainty to parties and may lead to even fewer appeals.

Model A styled merits review has not been justified

Enertrade believes that the right to merits review in respect of energy regulation is indisputable. The principal question for the Ministerial Council on Energy to resolve is the appropriate form of merits review.

Merits review is available under the Gas Code for decision on coverage, ring fencing obligations, contracts between service providers and affiliates and imposition of an access arrangement by the regulator.

The right to merits review is limited in terms of the parties that can apply for review (those affected by a decision), the timeframes for the appeal body to make a decision (90 days) and the powers of the appeals body. In respect of decisions relating to coverage, ring fencing obligations and associate contracts there are no limitations on the grounds for appeal.

In the case of decisions on access arrangements, appeals are allowed in respect of three grounds only:

- (i) of an error in the relevant Regulator's finding of facts; or
- (ii) that the exercise of the relevant Regulator's discretion was incorrect or was unreasonable having regard to all the circumstances; or
- (iii) that the occasion for exercising the discretion did not arise.

Merits review avenues are further limited by the information that can be included in the application and the matters to which the appeal body can refer in making a decision.

Model A seeks to impose a more limited form of merits review on these decisions. It seeks to limit the grounds of appeal to grounds similar to (i) and (ii) above. This removes one ground of appeal currently available to gas industry participants in respect of access arrangements. It substantially changes the rights available to industry participants in respect of decisions on coverage, ring fencing and associate

⁵ Ibid at paragraph 120

⁶ *Application by GasNet Australia (Operations) Pty Ltd* [2003] ACompT 6 (23 December 2003)



contracts in respect of the grounds of appeal and the information that the appeal body can consider.

The discussion paper fails to argue in any detail why Model A offers a more robust or effective framework of appeal rights compared with the existing rights under the Gas Access Regime.

The majority of arguments presented in favour of Model A apply broadly to merits review. The paper, however, does argue that limited merits review balances the competing interests of not revisiting regulatory decisions reached after lengthy and expensive consultative processes and taking into account the interests of network and service providers whose economic viability may depend upon the decision. It also argues that a merits review scheme limited in significant respects will lessen the incentive of regulated entities to 'game' the regulatory process such as withholding information.

In respect of the balancing of interests, this exercise was conducted at the advent of the Gas Access Regime. The current merits review framework is limited in a number of significant respects.

In respect of gaming, the paper fails to provide any evidence that this has been a problem to date, or that it has even occurred. In fact, appeals under section 39 of the Gas Pipelines Access Law do not delay the Regulator's Access Arrangement from taking effect. Moreover, in respect of timeliness of decision-making, appeals on merits have taken significantly less time than decisions by the Regulator or judicial review decisions.

Conclusion

Enertrade believes that access to merits review for decisions under the Gas Access Regime and the National Electricity Rules is a fundamental and indisputable right. The need for merits review has been demonstrated through the cases before the Tribunal.

Model A is a significant departure from the existing merits review framework, particularly in respect to decisions on coverage, ring fencing and associate contracts. Enertrade is strongly of the view that the removal of these existing rights has not been justified and therefore these rights should be retained.

Yours sincerely

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