

**REVIEW OF DECISION-MAKING IN THE GAS  
AND ELECTRICITY REGULATORY FRAMEWORKS**

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**DECISION**

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**Ministerial Council on Energy**

**May 2006**

## **1. Overview**

This document sets out the Ministerial Council of Energy's (MCE) policy position in relation to an appropriate scheme for review of decision-making in the gas and electricity regulatory frameworks.

This paper is organised as follows:

Section 2 refers to some objectives of the MCE in choosing an appropriate review scheme for the gas and electricity sectors.

Section 3 summarises the option chosen by the MCE, that is, a limited merits review scheme in respect of specified economic regulatory decisions in gas and electricity. Reference is also made to the MCE review into the effectiveness of the model adopted to be undertaken in the first seven years of commencement.

Section 4 sets out some background, including the different types of review (judicial review and merits review) currently available in gas and electricity. This section also outlines the two models put forward by the MCE's Standing Committee of Officials (SCO) in the discussion paper entitled "Review of Decision-Making in the Gas and Electricity Regulatory Frameworks" issued on 10 October 2005 for consultation with stakeholders (hereafter described as "the discussion paper").

Section 5 discusses briefly the MCE's choice of an appropriate review scheme for the specified economic regulatory decisions, noting that the MCE prefers a limited merits review scheme, as opposed to judicial review alone. Reference is made to the more significant issues raised by stakeholders in their submissions.

Section 6 then discusses the main features of the review scheme, referring to submissions received from stakeholders, and noting the MCE's response to certain key policy issues raised in the context of an appropriate review scheme. This section deals with features of the review scheme as follows:

- What decisions should be open to review
- Appropriate review body
- Who may seek review, and once proceedings are commenced, who may intervene in proceedings
- Grounds of review
- Powers and remedies
- Admissible material before review body
- Costs and procedure generally.

## **2. Objectives of review scheme**

Two forms of review are available for decisions made in the electricity and gas sectors. The first, which applies to all decisions, is judicial review, whereby an assessment of the process undertaken is made to ensure due process has been followed and the decision is within the legal bounds proscribed by law. In addition, some decisions could be subject to merits (or administrative) review, where the relative merits of the decision are assessed and a preferred decision arrived at.

As noted in the Regulatory Impact Statement on the Models for Review of Decision-Making in the Gas and Electricity Regulatory Frameworks issued on 6 December 2005, there is a need to provide a regulatory framework that promotes the efficient investment in and use of energy infrastructure, such that economic regulatory decisions provide a balanced outcome between competing interests and protect the property rights of all stakeholders. An important part of balancing this is allowing parties affected by decisions appropriate recourse to have decisions reviewed. The current system of review in the electricity and gas sectors does not provide a consistent framework to support the efficient investment in and use of energy infrastructure.

The appropriate review mechanisms should aim for the optimal decisions possible within a framework where the benefits of the review outweigh the costs to stakeholders.

Some criteria relevant to developing an appropriate review scheme are:

- Maximising accountability;
- Maximising regulatory certainty;
- Maximising the conditions for the decision-maker to make a correct initial decision;
- Achieving the best decisions possible;
- Ensuring that all stakeholders' interests are taken into account, including those of service and network providers, and consumers;
- Minimising the risk of "gaming"; and
- Minimising time delays and cost.

### **3. Summary of review model adopted**

The MCE considers that the objectives noted above are best met by the adoption of a limited merits review scheme, designed to balance the various competing interests involved, in relation to certain key regulatory decisions in gas and electricity. In addition, the MCE will cause a review to be undertaken into the effective operation of the merits review provisions within the first seven years of their commencement.

#### **Key features of model adopted**

##### **Decisions subject to merits review**

The following decisions will be subject to merits review:

- Ministerial decisions in relation to coverage of gas pipelines (including binding no-coverage determinations);
- Decisions by the Australian Energy Market Commission (AEMC) on the form of regulation to apply in gas;
- Australian Energy Regulator (AER)<sup>1</sup> decisions to draft and approve (or revise) gas access arrangements;
- AER ring fencing decisions, including non-approval or voiding of associate contracts, in gas;
- AER pricing and revenue determinations for transmission and distribution in electricity (including application of regulatory test);

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<sup>1</sup> The MCE notes that, for the AER decisions specified in this paper, in the case of Western Australia, the relevant decision-maker is that State's Economic Regulation Authority (ERA).

- AER decisions not to exempt entities from ring fencing guidelines or impose additional ring fencing requirements, in electricity.<sup>2</sup>

The particular regulatory decisions subject to merits review will be prescribed by regulation.

### **Appropriate review body**

The merits review body will be the Australian Competition Tribunal (ACT), as an already existing administrative tribunal specialising in economic regulatory and competition matters with a Federal Court judge presiding in all matters determined by it.

### **Standing to seek, and participate in, review**

*Standing to commence review:* The persons able to commence a review will be:

- (i) service and network providers,
- (ii) users who are materially affected by the original decision, and
- (iii) user and consumer groups.

In the case of coverage, there will be a wider standing test as presently found in the current gas access regime, that is, “a person adversely affected” by the decision will be able to commence a review.

To control the number and scope of reviews, it is proposed that a leave requirement be added as follows:

1. A requirement that the applicant seek leave from the ACT to bring a review; and
2. No leave to be granted unless:
  - a. The application is brought within 10 business days of a final decision; and
  - b. The ACT is satisfied that, where an economic regulatory decision is involved, the amount at issue exceeds \$5 million or 2% of the annual regulated revenue of the applicant whichever is the lesser, alternatively if quantification is not readily possible, that the amount in issue is material in terms of the regulated revenue. In all other cases (ie. ‘non-revenue’ errors), the ACT is satisfied that the error is a material one; and
  - c. The ACT is satisfied there is a serious question to be tried.
3. In addition, leave may be refused if the ACT is satisfied that the applicant:
  - a. without reasonable excuse failed to comply with any requests for information made by the regulator in the primary regulatory proceedings; or
  - b. without reasonable excuse failed to comply with any other requests or directions made by the regulator in those proceedings; or
  - c. without reasonable excuse conducted itself in those proceedings so as to delay the making of the economic regulatory decision sought to be reviewed; or
  - d. misled or attempted to mislead the regulator in those proceedings.

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<sup>2</sup>It is noted that, in the Northern Territory and Western Australia, the model applies to gas access matters. Electricity decision references relate to the National Electricity Market.

*Intervention in review, once commenced:* The persons able to intervene in review proceedings, once commenced, will be:

- (i) persons with a “sufficient interest” in the original decision,
- (ii) jurisdictions, and
- (iii) user and consumer groups with leave of the ACT.

In determining whether to grant leave to user and consumer groups, the ACT is to have regard to whether:

- (i) groups seek to raise matters not raised by an existing party to the review, in which case leave should be granted; or
- (ii) the interests of the group or its members are adversely affected, in which case again leave should be granted.

To further ensure that user and consumer groups intervention is not needlessly opposed, there will be legislative provisions to the effect that the interests of a group are taken to be affected if a determination relates to an object or purpose of the group and to provide that leave should not be refused on the basis only that the interests of a group or its members with respect to the matter are not wholly coincident with that of the network or service provider<sup>3</sup>, or on the basis that the interests of the group or its members could be represented by the regulator. Further, leave should also be granted where the evidence the group wishes to lead and the submissions it wishes to make are better presented directly rather than indirectly through any existing party to the proceedings.

Intervenors will be able to raise new grounds of review, that is, review would not be limited to only those grounds that the network or service provider, or user and consumer group (if the latter initiate a review), advance. They may be required to pay other parties’ costs if they fail to make out such additional ground(s) of review but the presumption will be that costs would not be awarded against user and consumer groups unless the ACT is satisfied that they have conducted their case in the review regardless of cost, time and the arguments of the applicant.

There will be an additional requirement imposed– only parties who have participated in the original decision-making process (eg made submissions) will be able to either seek review, or intervene in review proceedings once commenced.

*Standing of original decision-makers:* Once proceedings are commenced, the original decision-maker will become a party to proceedings. The original decision-maker will be able to raise new grounds of review – that is, review will not be limited to only those grounds that the network or service provider advances. Subject to the usual control of the ACT over its own proceedings, the original decision-maker will also be able to provide its views to the ACT on appropriate remedies once a ground of review has been made out.

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<sup>3</sup> In other words, leave would be refused where the interests of a group or its members (such as a representative group) wholly coincide with the interests of the relevant network or service provider. Thus organisations representing the interests of such entities can be excluded from intervening in a decision relating to one of their members under the formulation “user and consumer groups” in heading (iii). The interests of these groups will usually line up with those of network/service providers, who can instead intervene under heading (i) “persons with a sufficient interest”. Where such groups have interests that do not wholly coincide with the provider, there would still be scope for intervention by the groups.

## **Grounds for review**

The grounds for review will be as follows:

- (i) that the decision-maker made an error of fact and that fact was material to the decision;
- (ii) that the exercise of the decision-maker's discretion was incorrect having regard to all the circumstances;
- (iii) that the decision-maker's decision was unreasonable having regard to all the circumstances.

These grounds will provide a limited merits review that enables correction of errors.

## **Powers and remedies**

The ACT will be able to affirm or vary the original decision, or set aside the decision and either substitute a new decision; or remit to the AER, AEMC or Minister for reconsideration in accordance with the ACT's directions or recommendations. In addition, there will be some guidance set out in the legislative provisions to suggest when the ACT should consider remitting the matter back to the original decision-maker for re-determination in accordance with directions or recommendations, such as in circumstances where the matter before the ACT is particularly complex or inter-related with the regulatory decision as a whole.

## **Admissible evidence**

*Evidence restrictions:* In determining grounds for review, only the material that was before the original decision-maker can be considered. However, once a ground(s) of review has been made out, the ACT may allow the introduction of new evidence where the Tribunal would be assisted by the introduction of such evidence, provided that the material was not unreasonably withheld from the original decision-maker.

*Other material before the review body:* The ACT will be obliged to "have regard to" the policies (if any) of the AER or AEMC providing guidance as to how to exercise its discretion in making the specified economic regulatory decisions. However, the ACT will not be bound by any such policies.

## **Costs and procedure**

*Cost recovery mechanisms:* There should be a presumption that costs will be awarded on an indemnity basis unless the ACT orders otherwise. This is on the basis of the normal rule that costs follow the event. There should be two exceptions to that general rule. There will be legislative presumptions that costs are not to be awarded against:

- the AER or AEMC save where the AER or AEMC conducts its case regardless of cost, time and the arguments of the applicant; and
- intervenor user or consumer group save where that group conducts its case regardless of cost, time and the arguments of the applicant. For other types of intervenor, the ACT will have a discretion to award costs against such intervenor (for avoidance of doubt).

*Strict indicative time limits:* An applicant will have 10 business days to bring an application for review, and the ACT will have 65 business days to determine the review, with the

possibility of extension(s) for further period(s) of 20 business days, if it considers that the matter cannot be dealt with properly without an extension, either because of its complexity or because of other special circumstances. Where the ACT extends these time limits, it will be required to give reasons publicly for the extension.

*Decisions that remain in effect during a review:* AER pricing and revenue determinations in electricity transmission/distribution, AER decisions on drafting of gas access arrangements, and AER decisions involving non-approval or voiding of associate contracts, will all remain in effect during a review.

AER ring-fencing decisions (other than non-approval or voiding of associate contracts) in gas, AER decisions to exempt entities from ring fencing guidelines or impose additional ring fencing requirements in electricity, Ministerial decisions on coverage of gas pipelines, and AEMC decisions about the form of regulation in gas, will be suspended (or “stayed”), unless the ACT determines otherwise in its discretion, taking into account all the circumstances.

### **MCE review into effectiveness of scheme**

The MCE will cause a review into the effectiveness of the intended merits review scheme to be undertaken within the first seven years of commencement of the relevant merits review provisions. The review will be public and will be carried out by a person nominated by the MCE. The purpose of the review will be to assess how the merits review scheme has operated since commencement. The MCE will specify how the review is to be carried out. It is expected that issues such as the following would be examined:

- whether merits review has favoured any particular parties and there is evidence of ‘gaming’ by any parties;
- the costs implications for governments and parties;
- whether information disclosure and evidence restrictions have been effective;
- to what extent energy users and consumers have been able to participate;
- whether the ACT has acknowledged the expert knowledge developed by the primary decision-makers by remitting appropriate matters back to them;
- whether additional modifications are necessary to achieve the MCE’s objectives in light of future developments in the structure of the regulatory decisions themselves;
- whether the legislative framework for the merits review model could be improved; and
- whether the merits review scheme could be abolished, so that only judicial review would remain available to challenge the regulators’ decisions.

It is expected that the fact that such a MCE review is to occur will focus service and network providers, as well as other types of participants, on only bringing (or intervening in) merits review proceedings where they consider that a significant error has been made by the regulator.

The review will be given legislative recognition in the proposed National Gas Law (NGL) and in the National Electricity Law (NEL).

At this stage there is no intention on the part of the MCE to include a ‘sunsetting’ provision in the NGL or NEL (ie statutory provisions which provide that the merits review scheme ceases to apply on a certain date, or a date prescribed by regulation, or similar). However, the regulatory decisions subject to merits review will be prescribed in regulations made by the South Australian Minister. Such regulation(s) can be varied at a later stage to delete particular regulatory decision from the merits review scheme, for example, if the MCE review indicated that the merits review scheme was not operating effectively in relation to some, or all, reviewable decisions.

## **4. Background**

### **Current system of reviews within the NEM and the National Gas Access Regime**

The AER and the AEMC are subject to judicial review in relation to decisions or conduct in both the National Electricity Market (NEM) and in the National Gas Access Regime going forward. The National Electricity Market Management Company Ltd (NEMMCO) is also subject to judicial review of its decisions and conduct under the NEL and its decisions and conduct under the National Electricity Rules (NE Rules). Decisions of the relevant Minister in relation to coverage of gas pipelines are also subject to judicial review.

#### **Gas**

Decisions of the relevant Minister in relation to coverage of gas pipelines are subject to merits review. The regulator is also subject to a limited form of merits review in relation to decisions on pipeline access arrangements.

The Gas Pipelines Access Regime currently includes two merits review rights each relating to different types of decisions, and each with different grounds of review available (see Gas Pipelines Access Law (GPAL) ss.38 & 39). The decisions, which are presently subject to some type of merits review in gas, are:

- Decisions of a Regulator to draft and approve an access arrangement or revisions to an access arrangement (focus most often on the reference tariffs set out in those arrangements);
- Ring fencing decisions (that can impose obligations relating to business structures to deal with vertical separation of related businesses, including decisions not to approve associate contracts); and
- Decisions of Ministers in relation to coverage of pipelines (these are decisions on whether a pipeline owner or operator is to be subject to a regulatory regime rather than being able to operate in a competitive market environment).

In relation to decisions to which it applies, s.38 provides a wide type of merits review (although there are some restrictions on a s.38 review). In relation to decisions to which it applies, s.39 provides a more limited merits review restricted to correction of error.

Both the merits review provisions in the GPAL restrict the scope of the review in a number of ways. For example, only specific categories of persons have standing to seek review; the types of decisions that may be reviewed are limited; and the available grounds of review are limited particularly in relation to access arrangements (s.39). In the case of review of decisions about coverage and ring fencing under s.38, the ACT has, as a matter of practice,

not seen its task as a true *de novo* hearing but rather one restricted to the matters raised in submissions by the parties. Similarly, the ACT cannot admit new information as a matter of law under s.39 and has insisted on relevant information as a matter of practice in reviews under s.38.

## **Electricity**

Sections 16, 35 and 36 of the new NEL, by defining the AER's decision-making process and making explicit the basis for its decision-making, have arguably increased the scope for judicial review of economic regulatory decisions under the NEL and NE Rules. These sections set out key principles in relation to how the AER must exercise its economic regulatory functions. Failure to comply with these requirements will be an error of law and subject to judicial review by the Federal Court pursuant to the *Administrative Decisions (Judicial Review) Act (ADJR Act)*. There is currently no system of merits review of AER economic regulatory decisions in transmission regulation.

It should be noted that the current system of review for electricity distribution regulation cannot be maintained as it is different in each State and Territory and is in the process of being transferred to a national framework. However, some of those electricity distribution decisions are subject to merits review.

SCO has publicly indicated that it will review the position relating to merits review in the electricity and gas sectors in the development of a response to the Productivity Commission's Review of the Gas Access Regime. On 10 October 2005 SCO released a detailed discussion paper entitled "Review of Decision-Making in the Gas and Electricity Regulatory Frameworks", outlining two review options for the electricity and gas regimes.

### **Two review models put forward for public consultation**

In the discussion paper, SCO suggested that the following types of regulatory decisions (described as 'economic regulatory decisions') are suitable for review: decisions by the AER and Ministerial decisions in relation to gas which are currently subject to review under ss.38 and 39 of the GPAL; and in electricity, AER decisions relating to determinations on revenue caps for transmission network services and, ultimately, distribution network services.

SCO then identified two possible models for an appropriate review scheme:

- Model A: an option for limited merits review by the ACT;
- Model B: an option for judicial review by the Federal Court of the economic regulatory decision-making of the AER.

It should be noted that *de novo* review was not proposed by SCO in the discussion paper under either model. *De novo* review involves the reviewing decision-maker starting from the beginning and fully reproducing the administrative processes to make a truly "fresh" decision.

#### **Option A: limited merits review by the Australian Competition Tribunal**

Under this option, the ACT would undertake a limited form of merits review of the economic regulatory decisions of the AER in the case of gas and electricity, and of relevant Ministers in the case of coverage of gas pipelines. These decisions have a substantial impact on the economic viability of network and service providers. In addition, the decision-making power

involves the exercise of significant amounts of discretion, so that judicial review is arguably not sufficient and a form of merits review may be justified on policy grounds.

Merits (or administrative) review involves consideration of more than just whether a decision contains an error of law. Generally merits review considers whether the decision under review is the “correct and preferable” decision. The review can be of all of the aspects of the decision: the facts, the policy, the reasoning and the law. The reviewer “stands in the shoes” of the original decision-maker and makes the decision again. However, merits review can be more limited and can look simply at some aspects of a decision.

There are many models of statutory merits review, but they tend to fall into two groups:

1. Full merits review - on any grounds, and where the review body “stands in the shoes” of the original decision-maker, and is given all the powers of the original decision-maker. The review body can make a fresh decision, can take into account fresh information and in all aspects, the review body is the decision-maker.
2. Limited merits review – where key aspects of the review rights available are constrained by placing limits on any or all of:
  - *The types of decisions (or parts of decisions)* that are to be subject to review;
  - *Those who may apply for review* so that persons must satisfy a threshold to seek review, eg those who have previously participated and/or are “adversely affected” or “aggrieved”; versus “any person” which is in effect a full third party appeal right;
  - *The grounds of review* so that only specific grounds are available that focus on key aspects of decision-making where unchecked regulatory error has significant adverse impacts;
  - *The powers and remedies* available to a review body to correct regulatory error but also to safeguard against the high costs of unjustified or unwarranted review applications;
  - *The evidence* that the review body may take into account.

A merits review scheme with certain limitations was put forward by SCO for consultation with stakeholders, in order to balance the costs and delays involved in merits review, and the fact that the relevant regulatory decisions have usually been reached after extensive public and consultative processes.

Model A involved a limited merits review by the ACT, where the grounds of review would be limited to a consideration as to whether there was regulatory error on the facts or on the exercise of the discretion of the original decision-maker (similar, but not identical, grounds to the limited merits review presently found in s.39 of the GPAL). The ACT would have all the powers of the original decision-maker and be able, if it chooses, to substitute the correct or preferable decision. The ACT would be able to consider all the material that the original decision-maker had before it at the time of the decision, and an applicant would not be able to introduce new evidence to establish the grounds of review, although new evidence may be admissible in certain circumstances.

As to who should be able to seek review, a suggested formulation was that standing to commence proceedings be restricted to service and network providers, affected users meeting some “materiality” test, as well as the original decision-maker. However, once proceedings

had been commenced, a wider range of persons could be permitted to intervene to put their views, such as consumer advocacy groups. SCO raised the possibility that a different standing test may be appropriate in respect of gas coverage decisions, as coverage decisions directly and significantly affect persons other than network providers, for example, access seekers.

### **Option B: judicial review by the Federal Court of the economic regulatory decision-making of the AER**

An alternative option was described in SCO's discussion paper at Model B – instead of merits review, this option involved judicial review by the Federal Court of the economic regulatory decision-making of the AER in the context of specific requirements set out in the new NEL and the proposed NGL. Model B is based on the example of sections 16, 35 and 36 of the NEL in relation to electricity transmission determinations - these sections define the AER's decision-making process and make explicit the basis for that decision-making. Failure to comply with these requirements would be an error of law and subject to judicial review by the Federal Court. Under Model B, the same approach would be taken for distribution determinations to be provided for in the NEL, and economic regulatory decision-making by the AER under the NGL. Gas coverage decisions would be subject to judicial review, and not merits review as is presently the case under s.38 of the GPAL.

On Model B, the test for standing would be that of a “person aggrieved by a decision”, as is the case for current Federal Court judicial review of AER decisions under the *ADJR Act* scheme, and “a person interested in a decision” would be able to be a party to the proceedings.

The grounds of review would be those set out in the *ADJR Act*. The Court would also have the powers and remedies available under that Act: in particular, the Court would be able to suspend the operation of a decision pending the judicial review; and the orders available to the Court would be to quash or set aside the decision in whole or in part; to refer the matter back to the AER for further consideration in accordance with the Court's directions; and declaration, mandamus or injunction. Federal Court rules about admissibility of material as evidence in the proceedings would apply – the Court would be able to allow additional material to be adduced that, in the Court's opinion, would assist it to deal with the matter.

## **5. Proposal for an appropriate review scheme**

A total of twenty-eight submissions, plus three additional legal opinions, were received in relation to the issues raised in the discussion paper from a broad range of stakeholders, including network and service providers, users of gas and electricity, industry associations and user groups, consumer groups, and interested persons or bodies including the National Competition Council, the Administrative Review Council, the Law Council of Australia (Trade Practices Committee), the Public Interest and Advocacy Centre, and the Total Environment Centre.

### **Support for a merits review scheme**

The overwhelming majority of the submissions received by the MCE Secretariat during the consultation period support some form of merits review in the gas and electricity sectors, in addition to judicial review of AER and Ministerial decisions already available. Many

submissions pointed to the different and complementary roles of merits review and judicial review, and emphasised that judicial review and merits review are not substitutes for each other.

There is acknowledgement in the most of the submissions that a greater range of regulatory errors could be corrected by merits review than would be the case under judicial review alone. Further reasons put to support some form of merits review for the economic regulatory decisions specified in the discussion paper include:

- there is high risk of regulatory error occurring in the decision-making process, and the potential for regulatory error to result in considerable financial losses or under-investment or inefficient use of infrastructure is considerable;
- these decisions impact significantly on the property rights and financial interests of many affected parties and such interests warrant the protections afforded by merits review;
- merits review is likely to ensure that regulators pay close attention to the detail of the decision-making and hence may help to ensure that the most correct or preferable decisions are made;
- the introduction of a new national regulatory body, the AER, centralises regulatory power in the energy industry on one body, and that in order for the participants and users in the energy industry to have confidence in the AER's decisions, the AER needs to be transparent in, and accountable for, its decision-making; and
- merits review will help to encourage investment in both the gas and electricity sectors, and across those sectors, by promoting confidence that correct regulatory decisions will be made.

Most submissions express a preference for a limited type of merits review, along the lines put forward in Model A in the discussion paper, over Model B judicial review. However, a significant number of stakeholders advocate a wider type of merits review than proposed in Model A, for example, a merits review scheme with unlimited grounds of review, or a merits review for both gas and electricity which replicates that currently found in the GPAL for gas access.

### **Support for judicial review model, with no merits review**

In those submissions that favour Model B judicial review (totalling four), some stakeholders argue that there is such an information and resource asymmetry that consumers and small users (even larger users) cannot effectively participate in merits review, even if standing to commence proceedings, or to intervene in proceedings, were to be specifically granted. On this basis, some groups argue that consumers and users are best served by no merits review process in gas and electricity, so that service providers cannot seek review and then pass on appeal costs ultimately to consumers and end users through price/revenue re-sets. It is argued that the discipline on network service providers to appropriately consider whether there are legitimate grounds for review are diminished, if providers know that they can run a merits appeal (regardless of the strength of their case) and re-coup these costs. Some stakeholders who favour Model B judicial review also argue that regulatory error is considerably minimised as a result of the new regulatory frameworks, and they are concerned that Model A

will encourage unnecessary appeals by providers, result in delays, create regulatory uncertainty and disadvantage consumers' interests.

Some stakeholders supporting Model B judicial review nonetheless argue that, if a limited merits review scheme were to be adopted by the MCE, there should be wide standing so that users and representative groups can participate meaningfully in the process, and/or that they should be able to raise new grounds of review as intervenors so that they can do more than react to other parties' grounds of review. There are also arguments put that the review body should only have the power to remit matters back to the regulator, for re-determination.

### **Consistent review arrangements in electricity and gas**

In a number of the submissions it is argued that there are no justifiable reasons to fail to apply a merits review scheme consistently across electricity and gas. The discussion paper suggests at para. [5.15] that there is a heavier burden for justifying Model A in the case of economic regulatory decisions in electricity, as compared with economic regulatory decisions in gas. However, it is argued, for example, in response that it does not follow from the premise that the availability of judicial review has not reduced the quality of electricity regulatory decisions, that the availability of merits review would not improve the quality of such decision-making. Other reasons include distortion of investment across gas and electricity if the same merits review is not available for pricing/revenue determinations in both sectors. One consumer group notes in its submission that, from the point of view of consumers, there are even more compelling reasons to have merits review in electricity than in gas, given that pricing decisions in electricity have a large impact on all consumers (unlike gas).

### **MCE choice of a merits review model**

After consideration of the submissions received and debate about the issues involved, the MCE is of the view that a limited merits review scheme in both the gas and electricity sectors will best facilitate the correction of a range of regulatory errors with significant adverse consequences, encourage the making of the best administrative decisions in all the circumstances, and will encourage investment in gas and electricity and across those sectors by promoting confidence in the regulatory process. The MCE considers that a form of merits review of the economic regulatory decisions of the AER, and of Ministers in relation to gas coverage, is justified on policy grounds. Judicial review, without a complementary merits review scheme in place, is not considered to be sufficient to achieve the MCE's objectives.

As SCO states in the discussion paper, a merits review scheme will provide a more extensive type of review than judicial review, and enable correction of a far greater range of regulatory errors that may have significant adverse consequences on participants, including network and service providers, than judicial review. Further, while there is no constitutional or other legal obligation to provide merits review of administrative decisions, it is generally accepted that the availability of administrative (or merits) review leads to improved accountability in regulatory decision-making, for example, by encouraging increased awareness among decision-makers about the exercise of decision-making power within the terms of the authorising legislation, promoting the consistent application of the law by decisions-makers, and leading to improvements in the quality of primary decision-making. It is expected that the provision of limited merits review for the regulatory decisions earlier specified will reduce the risk to both businesses and the community of regulatory error and failure, that such review scheme will clarify and inform the operation of legal frameworks through the development of

precedents which will provide greater predictability in future decision-making, and will underpin private sector decisions to invest in new and long-lived capital assets.

In addition, the MCE favours merits review in electricity for the same sort of decisions that are presently reviewable on the merits in gas. The MCE supports consistency between the electricity and gas regimes, where feasible and appropriate, and considers that there are compelling reasons to implement a limited merits review scheme in both sectors in the present context.

## **6. Key features of merits review model proposed**

The MCE considers that a merits review scheme with certain limitations is appropriate, in order to balance the costs and delays involved in merits review, and the fact that the relevant regulatory decisions have usually been reached after extensive public and consultative processes. This section outlines the MCE's response to certain key policy issues raised in the context of deciding upon the major features of the review scheme. Reference is made in general terms to the most significant issues raised in the submissions received from stakeholders during the consultation process.

### **Decisions subject to limited merits review**

As noted earlier, SCO proposed in the discussion paper that the following types of regulatory decisions (described as 'economic regulatory decisions') are suitable for limited merits review: decisions by the AER and Ministerial decisions in relation to gas which are currently subject to review under ss.38 and 39 of the GPAL; and, in electricity, AER decisions relating to determinations on revenue caps for transmission network services and, ultimately, distribution network services.

Amongst those stakeholders who support some form of merits review, there is support for these economic regulatory decisions to be subjected to merits review. Reasons mentioned include that these decisions involve the exercise of a high level of discretion by the regulators, and there is a substantial risk of regulatory error occurring in the decision-making process.

Some stakeholders consider that additional regulatory decisions should also be subjected to merits review. It is argued that electricity ring fencing decisions should be included in any merits review model on the basis that there is little difference between the way ring fencing is treated in the NEL and in the Gas Law. The MCE notes that electricity ring fencing decisions presently involve a different decision-making process than in gas. Regulators' decisions are made under guidelines, and these guidelines can be seen as quasi-legislative in nature (being similar to a set of rules). SCO noted in its discussion paper that rule-making functions and powers that involve legislative-type decisions are generally not viewed as suitable for merits review. It is also worth noting that ring fencing guidelines for electricity are currently managed differently by the various jurisdictional regulators and in the majority of jurisdictions this is not in a way considered suitable for merits review. On the other hand, ring fencing decisions in gas, for example relating to legal separation of parts of businesses, are administrative decisions made in individual circumstances and are directed at particular service providers (unlike the electricity guidelines). The MCE does not consider that electricity ring fencing guidelines, and their application to entities, are generally suitable for merits review.

However, the MCE does consider that there is a strong case for subjecting *certain* administrative decisions involved in the electricity ring fencing process to merits review. These administrative decisions are those made to exempt entities from ring fencing guidelines or impose additional ring fencing requirements. This is because these particular administrative decisions (to be made by the AER) will be directed to individual network providers, and will involve the exercise of a significant enough discretion to warrant a merits review process.

As a general principle, the MCE remains of the view that arbitration decisions (such as those to be carried out by the AER in the gas regime and the Dispute Resolution Panel in electricity) should not be subject to merits review. Judicial review is an effective accountability mechanism for these types of decisions.

One stakeholder stated that more of the reviewable decisions under the old NEL and NE Code should be subjected to merits review. However, the MCE does not consider that the reviewable decisions (these are referred to in SCO's discussion paper and set out at Annexure B to that paper) meet the criteria that relevant decisions have both a substantial impact on the economic viability of network and service providers, and that the decision-making power involves the exercise of significant amounts of discretion. Accordingly, the MCE does not agree that the previously reviewable decisions under the old NEL and NE Code should be subjected to merits review.

Another stakeholder expressed the view that merits review should be available for decisions over the form of regulation (price regulation or price monitoring). These decisions will be made by the AEMC. The 'net benefit' test to be included in the new NGL will involve a significant enough discretion to warrant a merits review process. However, the AEMC rule changes, as a legislative function, should not be subject to a merits review process.

The MCE's policy position is that the decisions to be subjected to limited merits review are:

- Ministerial decisions in relation to coverage of gas pipelines (including binding no-coverage determinations);
- Decisions by the AEMC on the form of regulation (price regulation or price monitoring) to apply in gas;
- AER decisions to draft and approve (or revise) gas access arrangements;
- AER ring fencing decisions, including non-approval or voiding of associate contracts, in gas;
- AER pricing and revenue determinations for transmission and distribution in electricity (including the application of the regulatory test); and
- AER decisions to exempt entities from ring fencing guidelines or impose additional ring fencing requirements, in electricity.

All of these decisions have both a substantial impact on the economic viability of network and service providers, and the decision-making power involves the exercise of significant amounts of discretion, such that judicial review alone is not sufficient and a form of merits review is warranted.

The MCE has decided, in light of the need to review these provisions within seven years and the changing nature of how the decisions are structured, that the appropriate mechanism for listing which decisions in the NEL, NGL and associated Rules should be reviewable is for

such decisions to be prescribed by the regulations. The MCE will ordinarily consult with stakeholders before making any material change to the list of decisions subject to merits review.

### **Appropriate review body**

In the discussion paper, SCO proposed the ACT as an appropriate specialist administrative review body to undertake the Model A limited merits review. The ACT is an already existing administrative tribunal specialising in economic regulatory and competition matters, with a Federal Court judge presiding in all matters determined by the Tribunal. In the course of undertaking limited merits review, the ACT will be able to identify and review for errors of law in the original process, and correct these (the presidential member, a Federal Court judge, alone determines questions of law). The discussion paper noted that, for legal reasons, at the federal level it is unlikely that merits review can be undertaken by a court, since this would be giving the court an executive function, however this is likely to be possible at the State level. While that paper contained a detailed discussion about the advantages and disadvantages of the State and Territory Supreme Courts as merits review bodies, there was no comment in the submissions about this possible option by stakeholders.

In those submissions favouring some form of merits review, the ACT received overwhelming support as the most appropriate body to carry out merits review in the gas and electricity sectors. Comments were made to the effect that the ACT has long experience of, and significant expertise in, economic regulatory matters and merits review given its role under the *Trade Practices Act*, and that its structure and independent position make it the most appropriate merits review body. Having responsibility for review of decisions in the overlapping arenas of competition regulation and access regulation was also said to bring strength to the ACT's decision-making. In so far as the ACT may be considered to lack expertise or experience in relation to gas and electricity, the view was put that the best solution would be to make some additional appointments to the ACT.

For the reasons set out by SCO in the discussion paper, and informed by the submissions received, the MCE considers that the ACT is the most suitable body to carry out merits review of the limited type described in this paper.

### **Who may seek, and participate in, review: standing issues**

The discussion paper issued by SCO considered, in some detail, various arguments in relation to who should have standing to seek review of a decision, and who should be able to intervene in any proceedings, once commenced. There is a broad range of interests to consider when devising standing formulations in any merits review scheme.

For the AER's economic regulatory decisions in gas and electricity (excluding coverage decisions by relevant Ministers in the case of gas pipelines), SCO proposed that standing to commence proceedings be restricted to service and network providers, the regulator, and affected users who meet some type of high threshold or "materiality" test. However, once proceedings have been commenced in relation to a particular regulatory decision, then a wider range of persons could be permitted to intervene in the proceedings to put their views, such as persons "adversely affected" and/or those with a "sufficient interest" in the matter. There could be specific provision to allow for consumer advocacy groups to intervene in a matter.

SCO left open the role that these parties may have in alleging that the original decision was in error on grounds other than those already raised.

SCO also noted that a different standing test may be appropriate in respect of gas coverage decisions as coverage decisions directly and significantly affect persons other than network providers, for example, access seekers.

The submissions received from stakeholders canvassed a broad range of views. At the one end, some agreed with the proposal put in the discussion paper and further argued that intervenors should not be permitted to raise any new grounds of review. However, other stakeholders argued strongly for a wider standing test so that users (whether small, medium or large) and representative groups could both commence proceedings, or at the very least, intervene in proceedings once commenced. Some argued that intervenors should be able to raise new grounds of review, as otherwise users and representative groups would be restricted to “reacting” to grounds of review raised by service and network providers, rather than being able to participate in a more “proactive” manner by raising additional grounds of review.

The MCE has attempted to address some of the concerns raised by user groups. Model A originally proposed that users who are materially affected by a decision would be able to commence a review process, which is likely in many cases to cater for large energy users. However, the MCE considers that a widening of standing to commence a review is justified, to allow energy users, for example as part of a representative association, to commence a merits review process. It is not intended that small consumers could individually seek a review. Rather, user and consumer groups will be permitted to commence a review. In addition, there will also be a relatively wide scope for certain persons and user and consumer groups to intervene in proceedings, once commenced, and intervenors will be able to raise new grounds of review.

### **Commencement of review**

The MCE’s policy position is that, other than for Ministerial gas coverage decisions, the persons who will be able to commence a review will be:

- (i) service and network providers,
- (ii) users who are materially affected by the decision, and
- (iii) user and consumer groups (as defined).

In the case of coverage, there will be a wider standing test as presently found in the current gas access regime, that is, “a person adversely affected” by the decision will be able to commence a review.

To control the number and scope of reviews, it is proposed that a leave requirement be added as follows:

1. A requirement that the applicant seek leave from the ACT to bring a review; and
2. No leave to be granted unless:
  - a. The application is brought within 10 business days of a final decision; and

- b. The ACT is satisfied that, where an economic regulatory decision is involved, the amount at issue exceeds \$5 million or 2% of the annual regulated revenue of the applicant whichever is the lesser<sup>4</sup>, alternatively if quantification is not readily possible, that the amount in issue is material in terms of the regulated revenue<sup>5</sup>. In all other cases (ie. ‘non-revenue’ errors), the ACT is satisfied that the error is a material one; and
- c. The ACT is satisfied there is a serious question to be tried.

The restrictions on the grant of leave are designed to ensure that:

- applications are brought in a timely fashion;
- only final (not draft) decisions<sup>6</sup> are reviewed (thus ensuring that there are not multiple reviews in the ACT in the course of economic regulatory decision-making);
- only significant claims are reviewed; and
- trivial or vexatious claims are prevented.

The intention is to prevent the bringing of merits review claims where any regulatory errors made are relatively small, or where the error does not affect in a meaningful way the totality of the original regulatory decision. For ‘revenue’ errors, the figure put forward of \$5 million or 2% of the applicant’s annual regulated revenue (whichever is the lesser) is put forward on the basis that to date all reviews have involved at least \$2 million.<sup>7</sup>

As to “serious question to be tried”, this formulation is designed not only to exclude frivolous and vexatious claims but also to ensure that, even if the threshold amount test is met, only matters that raise serious issues go to the ACT. The criteria is aimed at preventing frivolous, vexatious or unmeritorious actions from proceeding.<sup>8</sup>

Further, leave may be refused if the ACT is satisfied that the applicant, without reasonable excuse, failed to comply with any requests for information (or other requests or directions) made by the regulator in the primary regulatory proceedings; or where the applicant conducted itself in those proceedings so as to delay the making of the economic regulatory decision sought to be reviewed (without reasonable excuse); or misled or attempted to mislead the regulator in those proceedings. This formulation replaces the “good faith” requirements in the merits review model proposed in Model A in SCO’s discussion paper. The MCE considers that the proposed formulation more precisely captures its intent.

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<sup>4</sup> There is a provision in s.39(4) of the GPAL which is to similar effect, although it does not specify actual dollar figures but instead simply refers to “the amount of money involved”. This gives a broad discretion to the ACT that smaller claims might be considered. It would seem better, in the context of dissuading “gaming”, to remove the opportunity for applicants to bring merits review for relatively small claims, by having as a starting point a fixed dollar or percentage requirement.

<sup>5</sup> It is not always possible to quantify precisely the monetary amounts at stake, as such a residual materiality test is required.

<sup>6</sup> Draft decisions would still be open for judicial review in the Federal Court: see *Re Dr Ken Michael AM; Ex parte Epic Energy (WA) Nominees Pty Ltd* (2002) ATPR 41-886.

<sup>7</sup> See Table 1, ENA submission.

<sup>8</sup> The formulation “serious question to be tried” is used in existing legislation as a threshold requirement to the bringing of certain proceedings: for example, see s.237(1)(d) of the *Corporations Act 2001* (Cth).

As to the right of users and consumers to commence merits review proceedings, after consideration of submissions received during the public consultation process, the MCE supports the right of groups representing users and consumers to commence review proceedings, subject to meeting the threshold requirements above described. The MCE is aware that problems could emerge if user and consumer groups are effectively exempt from any risk of adverse costs orders awards where they initiate reviews, and that such a situation could operate as a type of incentive for them to initiate reviews almost invariably and regardless of the merits of the particular case. As a disincentive to such groups needlessly initiating reviews, there needs to be a risk of substantial adverse costs orders – see further below for discussion of indemnity costs orders.

## **Intervenors**

The persons who will be able to intervene in review proceedings, once commenced, will be:

- (i) persons with a “sufficient interest” in the decision,
- (ii) jurisdictions, and
- (iii) user and consumer groups with leave of the ACT.

As to (i), persons with a “sufficient interest” in a decision will invariably include service providers, and may include large energy users depending on the particular circumstances. The ACT has commented that persons who have “sufficient interest” include those whose business interests or prospects could be adversely affected by the regulatory decisions, and noted that this test is not an unduly high one.<sup>9</sup>

As to (ii), jurisdictions will have an absolute right to intervene in, and be heard on, any review. The MCE considers that this measure may operate as a disincentive to “gaming”, along with other measures set out in this paper, if only because it means that jurisdictions can hear the arguments and then, if necessary, consider what amendments to the NEL or NGL or respective Rules are required to defeat unwanted policy outcomes arising from whatever decisions the ACT makes.

As to (iii), user and consumer groups are to be given the right to intervene in proceedings already commenced (in addition to the right to commence merits review proceedings), and may seek review on grounds other than those raised by an applicant network or service provider (or other applicant). However some restrictions on this right are required, in particular to avoid a plethora of groups seeking to intervene to raise irrelevant issues or to raise, to no additional benefit, the same issues as raised by the regulator and the service or network provider, thus unnecessarily prolonging the review and increasing its cost.

The MCE is of the view that user and consumer groups should only be allowed to intervene in proceedings already commenced with the leave of the ACT. In determining whether to grant leave to such groups, the ACT is to have regard to whether:

- (i) groups seek to raise matters not raised by an existing party to the review, in which case leave should be granted<sup>10</sup>; or
- (ii) the interests of the group or its members are adversely affected, in which case again leave should be granted<sup>11</sup>.

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<sup>9</sup> See para [6.16] of SCO discussion paper.

<sup>10</sup> Restricting the right to intervene to matters not already raised is consistent with the decisions of the ACT in *Qantas Airways Ltd* (2003) ATPR 410972 and *Application by Services Sydney Pty Ltd* (2005) ATPR 42-061.

To further ensure that user and consumer groups intervention is not needlessly opposed it is considered sensible to include provisions to the effect that the interests of a group are taken to be affected if a determination relates to an object or purpose of the group<sup>12</sup>, and to provide that leave should not be refused on the basis only that the interests of a group or its members with respect to the matter are not wholly coincident with that of the network or service provider<sup>13</sup>, or on the basis that the interests of the group or its members could be represented by the AER. Further, leave should also be granted where the evidence the group wishes to lead and the submissions it wishes to make are better presented directly rather than indirectly through any existing party to the proceedings<sup>14</sup>.

Intervenors will be able to raise new grounds of review with the leave of the ACT – so review will not be limited to only those grounds that the network or service provider, or user and consumer group (if the latter initiate a review), advance. Intervenors may be required to pay other parties' costs if they fail to make out any such additional ground(s) of review but the presumption will be that costs would not be awarded against user and consumer groups unless the ACT is satisfied that they have conducted their case in the review regardless of cost, time and arguments of the applicant.

There will be an additional requirement imposed – only parties who have participated in the original decision-making process (eg made submissions) will be able to either seek review, or intervene in review proceedings once commenced.

### **Role of original decision-maker**

Once proceedings are commenced, the original decision-maker will become a party to proceedings. The original decision-maker will be able to raise new grounds of review, that is, review will not be limited to only those grounds advanced by the applicant. This measure allows an application for review to operate as a broad “re-opener” if the original decision-maker so elects, notwithstanding limited grounds of review put forward by the applicant.

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<sup>11</sup> This will have the effect of overturning the ACT's decision in *Application by Orica IC Assets; re Moomba to Sydney Gas Pipeline (No 2)* (2004) ATPR 41-991 insofar as it was there held that, because the Energy Users Association of Australia (EUAA) and Energy Action Group (EAG) were incorporated associations, regard could not be had to the interests of their members as the groups as corporations were legally separate from their members.

<sup>12</sup> See *Philips v Department of Transport* (1978) 23 ALR 314. This case was distinguished by the ACT in *Application by Orica IC Assets: re Moomba to Sydney Gas Pipeline (No 2)* (2004) ATPR 410991 at para 10. As such this will represent a further overturning of that ACT decision.

<sup>13</sup> As noted earlier in this paper, leave would be refused where the interests of a group or its members (such as a representative group) wholly coincide with the interests of the relevant network or service provider. Thus organisations representing the interests of these entities can be excluded from intervening in a decision relating to one of their members under the formulation “user and consumer groups” in heading (iii). The interests of these groups will usually line up with those of network and service providers, who can instead intervene under heading (i) “persons with a sufficient interest”. Where such groups have interests that do not wholly coincide with a provider, there would still be scope for intervention by the groups.

This is similar to the test the National Electricity Tribunal applied to allow the NSW Minister for Energy to intervene in the *SNI Appeal (Murraylink Transmission Company Pty Ltd v NEMMCO)* – see decision dated 19 April 2002. In essence it allows the group to argue, as the NSW Minister did, that the interests of their members are not coincident with those of the regulator or the network/service provider, and as such they should be heard.

<sup>14</sup> This reflects the approach of the ACT in *Qantas Airways Ltd* (2003) ATPR 41-972.

In matters under the GPAL, the ACT has held that, on a review, it is only the matters that are the subject of the review (ie in respect of which the applicant service provider alleges error) that are to be dealt with.<sup>15</sup> The ACT has held that it cannot re-open any other matter in the regulatory decision being reviewed. A consequence is that an applicant service provider can choose only those matters where there are obvious errors and the ACT (and the regulator) are prevented from saying that those errors are ‘compensated for’ by assumptions or decisions benefiting a provider made elsewhere in the regulatory decision.

The ACT has further held that, after a review hearing, and in giving effect to its decision in terms of the orders to be made, it is not open to the regulator to re-open matters that were not raised in the review hearing itself.<sup>16</sup> This has the effect of precluding a regulator, once the full implications of the ACT’s decision are appreciated, from re-opening those parts of the economic regulatory decision that are necessarily and consequentially affected by what the ACT has decided.<sup>17</sup>

What is required is a provision to the effect that, if a review is brought by a network or service provider, then the regulator may, in its absolute discretion, seek a review by the ACT of other parts thereof, or of the entire decision, and the review would proceed on that basis, not only on the (limited) grounds of review that the network or service provider advances. This would then enable the regulator to argue such things as: ‘yes there was an error but we compensated for it by an adjustment we made elsewhere’.

The MCE notes that this need not entail a review of the entire decision, but only those *additional* aspects that the AER says warrant review having regard to the grounds of review advanced by the network or service provider. Allowing for a part re-hearing as well as a comprehensive review limits concerns that the review process could become needlessly expensive without detracting from the overall point that an error should be looked at in context.

Subject to the usual control of the ACT over its own proceedings, the original decision-maker would also be able to provide its views to the ACT on appropriate remedies once a ground of review has been made out.

## **Grounds of review**

In the discussion paper, the proposed merits review set out in Model A for the specified economic regulatory decisions is restricted in its grounds of review. This differs from the Productivity Commission’s review recommendations, which recommended a removal of the restrictions on grounds of appeal under s.39 of the GPAL, such that the review scheme would be a full merits review format. In Model A outlined in the discussion paper, SCO proposed that the grounds of review be limited to:

- a) error of the fact-finding by the decision-maker; and
- b) that the exercise of the decision-maker’s discretion was incorrect or was unreasonable having regard to all the circumstances (described as “error in exercise of discretion”).

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<sup>15</sup> See *Application by Epic Energy South Australia Pty Ltd* (2003) ATPR 41-932 at para 15 and *Application by GasNet Australia (Operations) Pty Ltd* (2004) ATPR 41-978 at paras 17, 31.

<sup>16</sup> See *Application by East Australian Pipeline Ltd* (2005) ATPR 42-047.

<sup>17</sup> See *ibid.*

These grounds are similar (but not identical) to the existing grounds of review in s.39(2) of the GPAL.

SCO stated in the discussion paper that these grounds of review, combined with a power to correct regulatory error by substituting the correct or preferable decisions, would allow the ACT to do more than a court can do under judicial review, but limits the administrative review to something less than a full re-exercise of the power to make the decision. The proposed grounds are related to traditional judicial review grounds, but with a less onerous hurdle to be satisfied.

*(a) First proposed ground of review: error of fact-finding*

The ACT may intervene where it considers that there has been an error in the findings of fact. The fact-finding task of an administrative decision-making body is fundamental to good quality decision-making, and if the facts upon which a decision is based are incorrect, or material facts are not available to the decision-maker, when the decision is made, the rational basis for the decision is in doubt.

SCO noted that, 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. However, the limited merits review proposed would permit a much greater level of scrutiny by the review body around the fact-finding task, and places the review body in the shoes, as it were, of the original decision-maker.

Importantly, SCO did not suggest that an applicant for review should be able to introduce new information before the review body in order to establish an error in the findings of fact. The ACT would make this assessment based on the information that was before the original decision-maker.

*(b) Second proposed ground of review: error in exercise of discretion*

SCO noted in the discussion paper that the specified economic regulatory decisions involve the exercise of broad discretions by the regulator in arriving at its determinations.

Judicial review allows only a very limited type of review in relation to the exercise of such broad discretions. Judicial review by a court to ensure that an administrative decision-maker has not abused a discretionary power conferred by law includes grounds such as the need to consider relevant considerations in the exercise of the power, not to make a decision for improper purposes taking into account the statutory scheme, and the test of *Wednesbury* unreasonableness. Each of these judicial review grounds is intended to allow a large degree of deference to the original decision-maker in the exercise of the discretionary power. So, for example, a court can only intervene on grounds of unreasonableness where the decision by the AER, for example, is so unreasonable that no reasonable person could have come to the decision. A court cannot and does not stand in the shoes of the original decision-maker.

This proposed merits review ground would instead allow the ACT to scrutinise the discretion exercised by the decision-maker, taking into account a wider range of circumstances than

judicial review would allow. The ACT could decide whether, in all the circumstances, it agrees with the reasoning, judgments and choices made by the original decision-maker. If the ACT considers it made an error, or the decision was unreasonable in a less onerous sense than the judicial review *Wednesbury* sense, then the ACT would have the power to re-exercise the power to the extent necessary to address the error, and to this extent has all the powers of the original decision-maker. But rather than being directed towards an examination at large, this merits review ground would allow the ACT to focus on those matters that it considers being of sufficient weight and importance to make out the specified ground of review.

The proposed grounds of review in Model A set out by SCO in the discussion paper attracted a substantial amount of comment in the submissions, and the views expressed by stakeholders were varied.

*Unrestricted grounds:* Some stakeholders argued for unrestricted grounds of review, or what they described as “full merits review”. While accepting that there are arguments against adopting full merits review such as the risk of ‘gaming’, the likely time and cost of conducting such a merits review and the complexity of the decision-making, some consider that given the importance of the decisions being made and the consequences of the decisions to the operation of the energy market and its participants, such cost and time is justified to ensure that preferable decisions are made. There is some concern that the limited version of merits review proposed in Model A may not adequately meet the needs of the participants and users in the energy market, nor adequately ensure that the administrative decisions made are correct or preferable. One submission advocating full merits review, stated that a limited merits review assumes that regulators get it right in some areas but not in others. It is also argued that potential ‘gaming’ arising from a full merits review scheme could be addressed by safeguards, for example, giving the ACT sufficient powers of discretion such that it is able to award costs, for example, against a party where there is evidence it is ‘gaming’ the process.

A further argument put to support unlimited grounds of merits review is to the effect that the National Access Regime provides full merits review and the same merit review standards afforded other infrastructure sectors by the National Access Regime should be afforded to electricity and gas infrastructure. Full merits review is currently available for declaration and revocation of coverage by the Minister, determination of the “effectiveness” of State and Territory access regimes by the Minister, and arbitrations on access terms and conditions by the ACCC. Further, the *Trade Practices Amendments (National Access Regime) Bill 2005* currently before the Commonwealth Parliament also seeks to extend full merit appeal rights to a range of decisions the ACCC may make in relation to access undertakings and codes, and competitive tendering processes.

There is also some support for unrestricted grounds of review in the case of gas coverage decisions (presently there are no restrictions on the grounds of merits review in respect of gas coverage decisions in the GPAL).

*Restricted grounds of review:* A number of submissions generally support the limited grounds of review proposed in Model A in the discussion paper, with some modifications suggested. Various stakeholders expressed the view that the form of limited review offered by Model A represents a workable model, and is a model appropriately balanced between the positions of judicial review (Model B) and full merits review, which was originally recommended by the Productivity Commission in its June 2004 final report on the *Review of the Gas Access Regime*.

The National Competition Council (NCC) agreed with SCO's proposal to limit the grounds of review of a decision of the AER and Ministers, but suggested a further restriction. From its experience in Part IIIA of the *Trade Practices Act* and Gas Code matters, while agreeing that the review body's jurisdiction should be focused on detecting errors of fact and errors of discretion by the primary decision maker, the NCC suggested that, in this context, there should be an onus of proof on the applicant to show that the primary decision-maker erred in a material way.

In those submissions that favour Model A over Model B judicial review, there is some criticism of the proposed removal of the 3<sup>rd</sup> ground of review currently set out in s.39(2)(a) of the GPAL (ie "that the occasion for exercising the discretion did not arise"). Some consider that the case for change has not been made out. On the other hand, some legal advice provided is to the effect that this removal does not involve any loss of review rights, given the relatively broad scope for review under the other proposed grounds of review. To the extent that the removal of the 3<sup>rd</sup> ground of review currently found in s.39(2) of the GPAL involves any lessening of review rights (and it is not clear that it does), the MCE considers that judicial review is the more appropriate avenue for raising such issues.

After consideration of relevant issues raised in the submissions, including legal opinions provided by several stakeholders, the MCE considers that the two grounds of review proposed in Model A as set out in the discussion paper are generally appropriate, but with modifications as explained below. The MCE does not consider that the 3<sup>rd</sup> ground of review currently set out in s.39(2) of the GPAL should be included in the grounds of merits review in the NGL and NEL (and Gas and NE Rules respectively) going forward.

As to the first ground of review proposed in the discussion paper relating to error of fact-finding, the MCE considers that this ground of review should have a limitation of "materiality" added. This would mean that a finding of fact by the original decision-maker would need to be a fact which is material to the decision, before a challenge to the regulatory decision could be made on this ground of review.

As to the second ground of review proposed in the discussion paper (error in the exercise of discretion), legal opinions commissioned by several stakeholders argue that the second ground should be recast, along the following lines: "that the decision is incorrect or is unreasonable having regard to all the circumstances". This is because the statute authorising the decision may or may not confer a discretion in the legal sense, and arguments about this issue are best avoided in a merits review process. There might be situations where the AER or other decision-maker misconceived or misapplied a statutory test that does not involve exercise of a statutory discretion, and if so, this would not be covered by the existing wording found in s.39(2)(a)(ii) of the GPAL. The MCE considers that there are valid reasons to recast the second ground of review proposed by SCO in the discussion paper, and intends to split that ground into two as follows: "that the exercise of the decision-maker's discretion was incorrect having regard to all the circumstances", and "that the decision-maker's decision was unreasonable having regard to all the circumstances.

On a further point, the MCE does not consider that gas coverage decisions should remain the subject of a merits review unlimited in its grounds of review, when the other decisions to be subjected to merits review will be limited in their grounds of review. The MCE does not see

a special case for gas coverage decisions, such that they should be the only class of regulatory decisions with unrestricted grounds of review.

The MCE's policy position is that the grounds for review, in respect of each of the economic regulatory decisions specified in this paper, will be as follows:

- (i) that the decision-maker made an error of fact and that fact was material to the decision;
- (ii) that the exercise of the decision-maker's discretion was incorrect having regard to all the circumstances;
- (iii) that the decision-maker's decision was unreasonable having regard to all the circumstances.

## **Powers and remedies**

In the discussion paper in relation to Model A (limited merits review option), SCO proposed that the ACT would have all the powers of the original decision-maker in order to enable the ACT to review on the facts and on the discretion and, if it chooses, to substitute the correct or preferable decision. To this extent, the ACT would "stand in the shoes" of the decision-maker, but this does not equate to a requirement to re-do any or all of the process leading to the original decision. The ACT would be able to:

- Affirm the decision of the AER, AEMC or Minister that is under review;
- Vary the decision that is under review;
- Set aside the decision that is under review and either:
  - make a decision in substitution for the decision set aside; or
  - remit the matter to the AER, AEMC or Minister for reconsideration in accordance with any directions or recommendations.

SCO did not specifically pose a question for consultation about the powers and remedies for the proposed merits review body.

Several stakeholders (who favour Model B judicial review) argued that, if a merits review model were adopted by the MCE, the ACT should not have power to substitute the AER's decision, but rather should be limited to remitting matters back to the AER for re-determination with specific directions. The AER or other relevant decision-maker should be obliged to revisit the "error" identified by the ACT and produce a new determination. This argument is based on the view that appeal mechanisms work best when matters are remitted back to the "experts" for re-determination - it is said, for example, that appeal bodies take too long and lack the technical expertise to undertake complex energy, economic, technical, engineering and financial matters, particularly when changing one element can have an impact on another apparently unrelated part of the regulatory decision.

On the other hand, another stakeholder (the National Competition Council) in its submission argued that the ACT should be allowed to make a decision, but in doing so, that review body should show that the first instance decision is wrong in principle, and specify the error(s) it considers warrants an alternative decision. This is on the basis that this would avoid costs and delays associated with sending the decision back to the primary decision-maker.

After consideration of the various issues involved, the MCE considers that the ACT should have all the powers and remedies available to it as set out in Model A in the discussion paper,

on the basis that these powers are desirable for the ACT to possess in order that it can carry out merits review efficiently and effectively. If the ACT were obliged to send every matter back to the AER, AEMC or relevant Minister for re-determination, additional costs would be incurred by all parties and unnecessary delays caused, with the increased regulatory uncertainty that such delays involve. This would be so particularly where the “errors” to be corrected are relatively small, and the ACT is of the view that it is well suited and able to correct that “error” by substituting a new decision.

However, the MCE considers that there may be some benefit in providing legislative guidance to the ACT to assist that body in exercising its powers to substitute the correct or preferable decision as at the time of the review. Therefore, the MCE has decided that, in addition to the ACT being empowered to “step in the regulator’s shoes” to substitute a new decision, there will be some guidance set out in the legislative provisions to suggest when the ACT should consider remitting the matter back to the original decision-maker for re-determination in accordance with directions or recommendations, such as in circumstances where the matter before the ACT is particularly complex or inter-related with the regulatory decision as a whole.

### **Admissible evidence**

In the discussion paper as set out in Model A (limited merits review option), SCO proposed that the ACT would be able to consider all the material that the original decision-maker had before it at the time of the decision. An applicant would not be able to introduce new information, issues or matters before the ACT to establish the grounds of review. This is in line with the Productivity Commission’s recommendations and paragraph 2.4(c) of the Competition and Infrastructure Reform Agreement signed by the Council of Australian Governments on 10 February 2006. However, SCO further proposed that if the ACT decides on the same material that was before the decision-maker that there is regulatory error of fact or discretion according to the grounds of review, then new material may be submitted (in certain circumstances) and taken into account by the ACT in reaching the correct or preferred decision as at the date of the review body’s decision. Legislative criteria could set out the circumstances in which the ACT may admit new evidence. For example, new evidence could be admitted where, in the opinion of the ACT, it would be unreasonable not to admit the evidence taking into account all the circumstances, including where the evidence was not available or not known at the time of the original decision and could not reasonably have been made available or known. SCO’s proposal that the ACT be able to admit and consider new or fresh material in certain limited circumstances recognises that there may be indeed be fresh facts or other material which would materially assist the ACT in reaching a correct or preferable decision.

SCO’s proposals relating to admissible evidence were favourably received in those submissions from stakeholders supporting some form of merits review. Comments were made to the effect that such approach would assist in reducing the risk of ‘gaming’. There was general support for the notion that strict limitations should be placed on the ACT’s ability to admit new material. Different formulations were suggested, for example, the ACT should have the discretion to admit new material only where the material was not available or known at the time of the original decision, and is critical to the decision. The ACT should also have discretion to accept or reject the information if it appears to have been deliberately withheld from the initial decision-maker.

The MCE's policy position is that, in determining grounds of review, only the material that was before the original decision-maker can be considered. However, once a ground(s) of review has been made out, the ACT will have discretion to allow new evidence where the Tribunal would be assisted by the introduction of such evidence, provided that the material was not unreasonably withheld from the original decision-maker.

The ACT will also have supporting powers to make directions to exclude irrelevant material generally and these powers would similarly apply to any proposed new evidence.

### **Other material before the review body**

In its discussion paper SCO raised the question as to whether specific regard should be given by the ACT to AER policy documents. Legislation could impose an obligation on the ACT to have regard to relevant AER policy documentation providing guidance as to how to exercise its discretion in making the specified economic regulatory decisions.

Some stakeholders made the point that the review body would, in any event, have before it any AER policy documents that were before the initial decision-maker, as the review body would have all the material that was before that decision-maker. Several stakeholders argued that the ACT should only be required to have regard to AER policy documents, but should not be bound by any such documents as the AER policy documents may themselves be in error.

The MCE considers that the ACT should be obliged to have regard to AER or AEMC policy documentation (where relevant), but the ACT will not be bound by such documentation.

### **Costs and procedure generally**

#### **Costs**

As pointed out in the discussion paper, currently reviews by the ACT are mostly conducted on the basis that each party bears their own costs, in recognition that merits review is not an adversarial court process but more a formal administrative mechanism to reconsider and correct that decision. However, other approaches are available, and some merits review bodies have an ability to make orders as to costs as is currently the case with s.38(10) of the GPAL. That sub-section provides that the relevant appeals body may make such orders (if any) as to costs in respect of a proceeding as it thinks fit.

In the discussion paper, SCO raised the idea that there be a discretion for the ACT to award costs against an applicant who has not succeeded in making out any ground of review, on the basis that an applicant may force a considerable number of parties (including the decision-maker) to great expense over a decision. For example, where an industry participant brings proceedings and fails to make out any ground of review, SCO stated that it may be appropriate that, as a general rule, that participant meet the costs of the other parties, save in exceptional circumstances. However, where a ground of review has been made out, all parties would bear their own costs.

There is support in the submissions for the ACT to have a general discretion to award costs against applicants where it considers it to be appropriate in the circumstances, along the lines of that currently found in s.38(10) of the GPAL. However, there is no agreement on how that discretion should be exercised as a general rule. One view expressed is that costs should

follow the event (ie you lose, you pay), and another view expressed is that each party should come to the proceedings with an expectation that it will bear its own costs. There is some agreement with the proposition that where an industry participant commences proceedings and fails to make out any ground of review, that participant should generally meet the costs of the other parties, including the costs of the original decision-maker. At least one stakeholder also commented that if intervening parties are permitted to raise additional grounds for review, there should be some scope for costs to be awarded against those parties if they fail to make out their additional grounds of review.

The MCE's policy position is that the ACT should have a discretion to make indemnity costs orders against applicants who are unsuccessful in making out their grounds of review, following the usual rule that costs follow the event. However, there will be no orders for costs against the AER and AEMC except where the AER or AEMC conducts its case regardless of cost, time and the arguments of the applicant. There would also be a presumption that there will be no costs orders against an intervenor user or consumer group except where that group conducts its case regardless of cost, time and the arguments of the applicant. As this would be a legislative presumption only, there would still be scope for the ACT to award costs against, for example, a large user or consumer group or association intervenor. The MCE notes that, for other types of intervenor, the ACT would have discretion to award costs against such intervenor (for avoidance of doubt).

Although the risk of costs orders is unlikely to operate as a disincentive to a network or service provider when large sums of money are at stake, it may operate as a disincentive with smaller sums, even with a minimum threshold for claims in place. Usually costs are awarded on a "party and party" basis which usually equates to approximately 60% of actual costs. To improve the 'disincentive' effect of costs orders, it seems sensible to provide that, where costs are awarded, they shall be awarded on an indemnity basis unless the ACT orders otherwise. This is likely to have the effect, if a network or service provider fails in a review and in default of a contrary order by the ACT, of increasing the costs it may have to pay.

This raises an issue in terms of user and consumer groups. The possibility of indemnity costs may operate against their intervention in reviews already commenced. To limit that disincentive it is proposed that a provision be enacted to the effect that costs shall not be awarded against intervenors unless the ACT is satisfied that they have conducted their case in the review regardless of cost, time and the arguments of the applicant. However it is not proposed that the same restriction apply where a user or consumer group *initiates* a review. As noted earlier, if user and consumer groups are effectively exempt from any risk of adverse costs awards where they initiate reviews, this could potentially operate as a perverse incentive for them to initiate reviews almost invariably and regardless of merits. A disincentive to needlessly initiating reviews is required and that will be the risk of indemnity costs orders being awarded against applicant user and consumer groups.

As to the AER and AEMC, these bodies will perform the necessary and proper rule of contradictor, and accordingly it seems inappropriate to make the AER or AEMC liable for costs except where the ACT determines otherwise. There will be a legislative presumption against the awarding of costs against the AER or AEMC even where an applicant network or service provider succeeds, other than in the limited situation where the AER or AEMC conducts its case regardless of cost, time and the arguments of the applicant. This is similar to the present position the ACT has taken in terms of costs orders being made against the

ACCC<sup>18</sup>: however the proposal now is that the legislation makes clear that costs are to be determined on that basis.<sup>19</sup>

## Stays

One area of ‘gaming’ risk is that parties may seek to delay implementation of an unfavourable decision, and procedural safeguards need to be in place to minimise such risk. The review process should reduce the incentives for network and service providers to delay finalisation of the merits review. At para. [2.15] of the discussion paper, SCO stated that, in any merits review scheme, if the NEL or NGL so allows, the ACT will be able to suspend the operation of a relevant regulatory decision pending a merits review.

In the current gas access regime, for access arrangements (and revisions to access arrangements) drafted by the relevant regulator, and for non-approval of associate contracts, an application for review does **not** operate to stay the decision (see s.38(6) of the GPAL). The decision of the relevant regulator will continue to apply unless that decision is re-made by the relevant appeals body or returned to that regulator for re-making. As the Productivity Commission points out, the currently available procedural safeguards in the gas access regime means that a service provider cannot frustrate access where there is no stay on the decisions for a s.39 GPAL access arrangement and s.38 associate contract merits reviews.<sup>20</sup>

On the other hand, decisions reviewed under s.38 of the GPAL relating to coverage, as well as decisions reviewed under s.38 dealing with ring-fencing (other than non-approval of associate contracts), **do** have the effect of staying the decisions, although the relevant appeals body has a discretion to determine otherwise. That body can determine whether staying a decision is in the best interest of all the parties. For coverage decisions, incentives to a delayed decision may change depending on whether the decision is to cover or to revoke coverage of the pipeline, and whether the applicant is the service provider or an access seeker. Important in these approaches is that merits review is only available once there is a decision in place that can apply while the review is undertaken. Merits review, available only after a final decision is in place, coupled with appropriate rules of whether review has the effect of staying a decision, does not provide incentives to delayed decision-making through review processes.

The MCE’s policy position is that the following AER decisions should remain in effect (that is, no “stay” on decisions) during any merits review:

- electricity transmission or distribution pricing or revenue determinations,
- gas access arrangements drafted or revised by the regulator, and
- non-approval or voiding of associate contracts in gas.

In relation to the above mentioned decisions, there would be no backdating of the effect of a review decision – this is likely to be the case in any event, but this would be made clear in the legislation.<sup>21</sup>

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<sup>18</sup> See *Application by East Australian Pipeline Ltd* (2005) ATPR 42-047 at paras 17-19.

<sup>19</sup> Presently it does not: see s.38(10) of the GPAL.

<sup>20</sup> *Report on Gas Access Regime*, 2004, p.492.

<sup>21</sup> In *Application by East Australian Pipeline Ltd* (2005) ATPR 42-062, the service provider sought a backdating of the increased tariffs that resulted from the decision of the ACT to the commencement of the relevant access arrangement period. The ACT refused on the basis that it interpreted the GPAL and Gas Access Code as not permitting such. However, there is no express provision in either the GPAL or Code to that effect, and it would appear sensible to put the matter beyond doubt.

The MCE further considers that, for

- gas coverage decisions by relevant Ministers,
- decisions about the form of regulation in gas by the AEMC,
- gas ring fencing decisions by the AER (other than non-approval or voiding of associate contracts), and
- electricity ring fencing decisions by the AER exempting individual providers from compliance with relevant guidelines or imposing additional ring fencing requirements,

the legislative provisions should confer a discretion on the ACT to decide whether to “stay” the regulatory decision, taking into account all the circumstances.

### **Time limits**

Consideration has been given to appropriate time limits that should be in place in the merits review process. Lengthy or delayed processes can increase costs for all parties to a merits review, and also create uncertainty over future regulatory arrangements. Time limits on how long a party has to launch a review, as well as how long the ACT has to consider a review, provide benefits to all parties to a review, as well as the community more generally.

The GPAL currently includes time limits on the amount of time a party has to launch a merits appeal following a regulatory or coverage decision, as well as some limitations on the time available to the review body in considering a review case. At present, an applicant for review has 14 days to make an application for merits review, from the day the relevant decision is made public: s.38(2). The review body then must make a determination within 90 days after receipt of the application for review: s.38(3), however the review body may extend this timeline by 30 day periods, if it considers that the matter cannot be dealt with properly without the extensions(s) either because of its complexity or because of other special circumstances: see s.38(4). Where it does so, the review body must notify the applicant and give reasons for the extension(s): s.38(5).

The MCE considers that 10 business days is a reasonable period of time in which an applicant for review may lodge a review application. The MCE also considers that the imposition of strict indicative time limits on the ACT is appropriate, given that the Tribunal will be determining the matter principally on material presented to the initial decision-maker. There would be risks in imposing an unduly short time frame on the ACT. The MCE thinks that a 65 business day time limit on the ACT would be a reasonable indicative time limit, with the ACT having the discretion to extend this timeline by period(s) of 20 business days, as it considers necessary.

The MCE’s policy position is that an applicant will have 10 business days to lodge a review application. The ACT will then have 65 business days to make its determination on the review, but may extend this period by period(s) of 20 business days, where the ACT considers that such extension(s) are considered necessary because of the complexity of the matter or because of other special circumstances. The ACT will be required to give reasons publicly in respect of any such extension(s).

### **Trivial and vexatious applications**

Several of the submissions received from stakeholders emphasised the need for the ACT to have a discretion to dismiss an application for review where it is trivial or vexatious. In

relation to the current gas access regime, s.38(11) of the GPAL provides that the review body may refuse to review a decision if it considers that the application for review is trivial or vexatious.

The MCE considers that there is no need for an express power in these terms to be conferred on the ACT. As a threshold issue, the ACT will not be permitted to grant leave to an applicant to commence a merits review unless the ACT is satisfied that, amongst other things, there is a serious question to be tried. An application for review which is in essence trivial or vexatious will fail to meet the requirement that there be “a serious question to be tried”.

### **Other procedure**

In the current gas access regime, there is provision in s.38(7) of the GPAL for the merits review body to conduct hearings in the absence of the public, on the application of a party to the proceedings brought under ss.38 or 39. Consideration is currently being given to whether a similar provision should be put in place for the merits review proposed in relation to the specified economic regulatory decisions both in gas and electricity. Any such provision would need to be consistent with other provisions both in the NEL and NE Rules, and in the proposed NGL and Gas Rules, about confidential information, including material that may be commercial-in-confidence.

The MCE considers that there should also be an obligation on the regulator to provide information and assistance to the ACT. At present, the GPAL provides that the relevant appeals body may require the regulator to give information and other assistance, and to make reports, as specified by the appeals body (s.38(8)). The MCE can see no reason why such a provision should not be included in the merits review scheme proposed for the gas and electricity regulatory frameworks, and accordingly the AER, AEMC and relevant Ministers (as the case may be) will be under an obligation to provide information and assistance to the ACT in any merits review application.