

# REVIEW OF DECISION-MAKING IN THE GAS AND ELECTRICITY REGULATORY FRAMEWORK

## SUBMISSION BY GASNET

### 1 INTRODUCTION

#### 1.1 Purpose

On 10 October 2005, the Ministerial Council on Energy's Standing Committee of Officials ("**SCO**") released a discussion paper on the role of a review scheme in the energy regulatory framework ("**Discussion Paper**").

The Discussion Paper looks at different types of review schemes and some of the key considerations relating to each scheme.

The SCO has invited comments from all stakeholders on the matters addressed by the Discussion Paper. This submission sets out GasNet's comments.

#### 1.2 Scope

This submission addresses GasNet's views on the key areas for consultation, being:

- (a) the preferred review scheme;
- (b) type of decisions that can be reviewed;
- (c) standing to commence and involvement in review proceedings;
- (d) grounds of review;
- (e) admissible evidence; and
- (f) awarding of costs.

Each of these issues are addressed in turn below, with a particular focus on preferred review schemes in the context of the Gas Pipelines Access Law.<sup>1</sup>

### 2 PREFERRED APPROACH

#### 2.1 Merits review preferred

GasNet considers that there is a strong case for retaining a limited form of merits review in the energy regulatory framework, consistent with the review processes currently allowed under the Gas Access Regime. GasNet considers that a limited merits review scheme, in combination with the existing judicial review regime, best balances the protection of service providers' property rights and freedoms against the need for regulatory efficiency and effectiveness.

Merits review and judicial review are complementary processes, and should not be viewed as competing alternatives. The two processes allow review of quite

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<sup>1</sup>Refers to the law established by Schedules 1 and 2 of the Gas Pipelines Access (South Australia) Act 1997 (SA).

different forms of error. Judicial review is aimed at correcting procedural defects, whereas merits review goes to the substance, or merits, of a decision.

GasNet considers that judicial review alone fails to guarantee that service providers' property rights are properly protected, and that both review processes are needed.

## 2.2 Protection of property rights the primary consideration

The Australian legal system establishes certain rights that should not be disturbed without a compelling reason. Certain decisions in the gas and electricity regulatory regimes have the potential to seriously impact upon a service provider's fundamental rights, particularly its abilities to contract freely and exercise basic property rights.

The Productivity Commission, when it examined the national access regime in 2001,<sup>2</sup> emphasised that "*appropriate protection for property rights must be the pre-eminent consideration in formulating a system of appeal rights for access regimes.*" It continues to support the need for merits review under the gas access regime on this basis, despite the fact that appeal processes might take considerable time and expend considerable resources.<sup>3</sup>

GasNet considers that protection of property rights should continue to be the primary consideration informing further policy developments in this area. The availability of merits review for decisions affecting property rights is critical to maintaining investment certainty and fostering stakeholders' confidence in the regulatory regime.

## 2.3 Other advantages of merits review

In addition to the considerations above, there are a number of other reasons why a form of merits review should be adopted, including:

- (a) **(Reviewer can correct error)**. A merits review process allows the review body to substitute the correct and preferable decision for the erroneous one, rather than merely remitting the decision to the original decision-maker for reconsideration. This saves time and money, as it avoids the original decision-maker having to re-examine the facts in light of the appeal decision.
- (b) **(Guidance to decision-makers)**. A body of appeal tribunal decisions will give primary decision-makers guidance on the proper operation and administration of the law. This in turn promotes predictability and quality of primary decision-making. This is particularly important where the relevant statute gives considerable discretion to the decision-maker.<sup>4</sup>
- (c) **(Accountability)**. The existence of a merits review scheme increases the accountability of decision-makers. Although judicial review also acts as an

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<sup>2</sup> Productivity Commission, *Review of the National Access Regime, Inquiry Report No 17*, 28 September 2001, p 396.

<sup>3</sup> Productivity Commission, *Review of the Gas Access Regime, Inquiry Report No. 31*, 11 June 2004 ("**PC Report**"), p 498.

<sup>4</sup> *PC Report*, p 488.

incentive to ensure correct decision-making, merits review provides an additional process for the scrutiny of regulatory decisions.

(d) (**Appropriateness of forum**). A merits review process often provides a more feasible avenue than a court-based appeal. Depending on the appeal tribunal process, the time delay and costs of merit review can be significantly less than for the judicial process. Having a merits review process also ensures that aggrieved parties will bring actions before appropriately qualified bodies, being:

- (i) for legal/judicial matters, judges with extensive legal knowledge; and
- (ii) for factual/merits matters, experts in the relevant fields.

## 2.4 Arguments against merits review are misplaced

The Discussion Paper identifies four considerations which may factor against merits review for economic regulatory decisions:

- (a) merits review may result in gaming and forum-shopping by energy providers;
- (b) merits review may actually increase the risk of regulatory error, rather than reduce it, if review bodies are not sufficiently resourced with expertise;
- (c) the review body may not properly take into account the interests of all stakeholders if it is not required to undertake consultative processes comparable to those undertaken by the original decision-maker; and
- (d) merits review processes can be costly and time-consuming.<sup>5</sup>

As for consideration (a), GasNet considers that merits review will not lead to “forum- shopping”, as that term is normally used. Rather, it gives energy providers access to a separate review process designed to provide redress for errors not covered by judicial review. The concern about “forum-shopping” is based on the incorrect assumption that merits review and judicial review provide alternate, or substitutable, fora. As identified in the Discussion Paper, “*not all the issues and aspects of a decision that individuals might regard as “incorrect” could be addressed by [either of] these processes [alone].*”<sup>6</sup> The availability of both merits review and judicial review protects against a fuller range of regulatory errors, and in individual cases allows an energy provider to select whichever forum has been established to deal with the specific error made.

As for consideration (b), GasNet agrees that any review body must have sufficient expertise to deal with the often complex economic and technical issues which arise. The Australian Competition Tribunal (“**ACT**”) has already shown competency in dealing with complex regulatory decisions in gas. GasNet sees no reason why it could not continue to do this, provided that it remains appropriately resourced and has access to experts where necessary. In fact, a well-resourced expert tribunal arguably provides a better forum than a court for dealing with

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<sup>5</sup> Discussion Paper, pp 27-8.

<sup>6</sup> Discussion Paper, p 28.

errors of substance concerning economic or technical matters, and strengthens the case for a merits review mechanism.

GasNet considers that imposing comparable public consultation obligations on a review body is not required to ensure that the body properly considers the wider impacts of its decision (consideration (c)). This is because even a limited merits review process will require the review body to fully consider all the material that was put before the original decision-maker, including the material from the public consultation process. It is this material - rather than the consultation process itself - which ensures that the review body considers all stakeholders' interests.

Finally, GasNet submits that, while re-hearings on their merits can sometimes be costly, the Productivity Commission correctly identifies that these costs do not outweigh the need for merits review for decisions which affect fundamental rights (see section 2.2 above). Further, the absence of a merits review process is likely to increase the costs of judicial review (see section 8.4 below).

## 2.5 Limitations

GasNet acknowledges that merits review has some disadvantages. As already noted, re-hearings can be time-consuming and costly. For this reason, GasNet generally agrees with the SCO that a more limited form of merits review is appropriate. However, GasNet considers that some of the limitations proposed by the SCO go unnecessarily further than the limitations on the existing merits review mechanism in the gas regulatory regime. In particular, GasNet considers that the third ground of review in the Gas Pipelines Access Law (that the occasion for exercising the discretion did not arise)<sup>7</sup> should continue to be available under a Model A type merits review scheme (see section 5 below).

GasNet set outs the limitations it considers appropriate in sections 3 to 6 below.

## 3 DECISIONS SUBJECT TO REVIEW

### 3.1 Decisions by energy regulators

The Discussion Paper identifies a range of regulatory decisions which could be made subject to merits review:

- (a) AER decisions to approve or revise access arrangements ("**Access Decisions**");
- (b) ring fencing decisions and decisions not to approve associate contracts ("**Ring-fencing Decisions**");
- (c) Ministerial decisions in relation to coverage of gas pipelines ("**Coverage Decisions**"); and
- (d) revenue cap determinations in relation to electricity transmission and distribution services ("**Revenue Cap Determinations**").

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<sup>7</sup> Section 39(2)(a)(iii), Schedule 1 of the Gas Pipelines Access (South Australia) Act 1997 (SA).

### 3.2 Decisions that should be covered

GasNet considers that, at a minimum, merits review should be available in relation to Access Decisions, Coverage Decisions and Revenue Cap Determinations.

Each of these decisions restricts the contractual freedoms and property rights that a private entity would ordinarily enjoy in our legal system. Access Decisions and Revenue Cap Determinations directly require the owners of facilities (ie pipeline and electricity transmission assets) to make those facilities available to others on terms and prices determined by an independent regulator, not by their owners. Coverage Decisions ultimately have this same effect. As discussed above, merits review ensures that these fundamental rights can only be abrogated after careful consideration and in limited circumstances.

In addition, these types of decisions generally involve the exercise of considerable discretion by the decision-maker. In these circumstances, judicial review is generally considered to be insufficient and some form of review mechanism is justified. This is recognised in section 5 of the Discussion Paper.<sup>8</sup>

For example, GasNet considers that judicial review alone would provide an inadequate check on the regulator's tariff-setting decisions in the National Third Party Access Code for Natural Gas Pipeline Systems ("**Gas Code**"). The Gas Code's non-prescriptive approach gives considerable flexibility to the regulator in this area. The Gas Code merely sets out broad tariff design principles and leaves the detailed determination to the regulator. This inevitably means that the regulator exercises an element of judgment, even where it follows the correct processes. This in turn increases the risk of the regulator making an error which, although it may adversely affect the rights and interests of the service-provider, falls outside the scope of judicial review.

### 3.3 Decisions involving public consultation

The Discussion Paper observes that merits review might not be appropriate for review of decisions which have been the subject of extensive public consultation.<sup>9</sup>

This is because a full merits review process would require the review body to undertake a similarly extensive investigative process, which would be overly costly and time-consuming.<sup>10</sup> GasNet considers that this concern is avoided by limiting the merits review mechanism so that the review body does not undertake fresh public consultations. Rather, the review body would simply consider the material submitted in the public consultation process for the original decision (see discussion in section 6 of this submission).

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<sup>8</sup> Ministerial Council on Energy - Standing Committee on Officials, *Review of Decision-making in the Gas and Electricity Regulatory Frameworks - Discussion Paper*, p 22 ("**Discussion Paper**").

<sup>9</sup> *Discussion Paper*, p 22.

<sup>10</sup> Administrative Review Council, *What Decisions Should be Subject to a Merit Review?*, <[http://www.ag.gov.au/agd/WWW/arcHome.nsf/Page/Publications\\_Reports\\_Downloads\\_What\\_decisions\\_should\\_be\\_subject\\_to\\_merit\\_review](http://www.ag.gov.au/agd/WWW/arcHome.nsf/Page/Publications_Reports_Downloads_What_decisions_should_be_subject_to_merit_review)> (accessed 7 November 2005), cited in *PC Report*, p 493.

## **4 STANDING TO COMMENCE AND INTERVENE IN REVIEW PROCEEDINGS**

### **4.1 Decisions on access arrangements**

The SCO has flagged the possibility of introducing a more “open” standing test to broaden the classes of people who can seek merits review of decisions relating to access arrangements. It has also suggested that there could be specific provision to allow consumer advocacy groups or other particular groups the right to intervene in a matter once it has been initiated.

GasNet considers that a broadening of the standing test is not appropriate in the context of regulatory decisions on access arrangements. The gas and electricity regulatory models are essentially aimed at protecting the rights of end users, not the rights of service providers. On this basis, the rights of end users are adequately represented by the regulator itself and through the extensive public consultation process conducted under the Gas Code.

This was recognised by the Productivity Commission in its 2004 review of the gas access regime, where it recommended that for access arrangements drafted and approved by the regulator, it is appropriate only for service providers to have the right of appeal on the basis that “*the regulatory intervention is on behalf of the wider economy, including users*”.<sup>11</sup>

Ultimately, it is the service provider who is most directly and significantly affected by the decisions of the regulator. Opening up the merits review process to entities who are not directly and materially affected by the decision has the potential to impose an unfair burden on service providers who will be forced to spend additional time and money, either:

- (a) “defending” regulatory decisions which are challenged by end users; or
- (b) accommodating third party involvement in its own review applications.

### **4.2 Decisions on coverage**

GasNet agrees that it may be appropriate to allow a broader category of persons to appeal decisions in relation to pipeline coverage on the basis that such decisions may have a more direct and material impact on other parties (eg the access seeker). However, GasNet considers that it should not be an open-ended test, and that the existing, narrow tests should be retained. In particular, it considers that the appeal rights should be limited to those who can demonstrate a direct interest in the decision.

## **5 GROUNDS OF REVIEW**

The Discussion Paper proposes that the grounds of review be limited to:

- (a) fact-finding errors by the decision-maker; and
- (b) errors in the exercise of the decision-maker’s discretion.

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<sup>11</sup> PC Report, p 499.

GasNet notes that these grounds do not include the third ground of review available under the Gas Pipelines Access Law, which provides that an applicant can seek review on the basis that “*the occasion for exercising the discretion did not arise.*”<sup>12</sup>

The existing review mechanism for gas regulatory decisions is already a limited review process and is intended to balance efficiency considerations against the need to preserve the essential feature of merits review. GasNet considers that the Discussion Paper advances no basis for further limiting the merits review scheme by removing this third ground of review.

Subject to the third ground of review being reinstated, GasNet considers that the proposed limitations are appropriate, in that they will allow a review body to stand in the shoes of the primary decision-maker to correct substantive regulatory errors.

## **6 EVIDENCE**

GasNet agrees with the restriction on evidence proposed in paragraph 6.60 of the Discussion Paper, on the basis that the merits review process should not be a full “de novo” hearing. That is, no new information, issues or matters should be raised before the review body in order to establish the grounds of review themselves.

It should only be in circumstances where the review body has already decided on the basis of the original material that there is an error of fact or discretion that new information may be submitted and taken into account by the review body in reaching the correct or preferred decision. This restriction on new evidence encourages parties to put forward all relevant information at the first instance, resulting in a more efficient and fairer decision-making process.

The issue of whether there should be legislative criteria setting out circumstances in which new evidence could be admitted by the review body (for example, if it would be unreasonable not to admit the evidence taking into account all the circumstances) should be carefully considered. While there is an argument that new evidence should be able to be submitted where there has been a nonsensical or materially unjust decision because evidence was not available or known at the time, any criteria for allowing new evidence must be narrow.

Paragraph 6.64 of the Discussion Paper proposes that the review body should be required to take into account the AER’s policy documents to assist in its review. While this may assist in certain circumstances by ensuring regulatory consistency, it should be clear that:

- (a) legislated requirements and considerations will always prevail over policy documents and administrative guidelines; and
- (b) the review body is free to depart from these policy documents in appropriate cases.

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<sup>12</sup> Section 39(2)(a)(iii) of the Gas Pipelines Access (South Australia) Act 1997 (SA).

## **7 COSTS**

GasNet considers that parties should bear their own costs in all proceedings before the review body. It is usual that parties bears their own costs in administrative reviews, such as those conducted by the Australian Competition Tribunal. As stated in the Discussion Paper, this recognises that a merits review is not an adversarial court process, but merely a formal administrative mechanism to reconsider and correct decisions.<sup>13</sup>

There is no evidence that the merits review avenue has been used vexatiously or frivolously in the past. The information provided in Annexure D of the Discussion Paper in fact shows that only a small percentage of gas and electricity regulatory decisions have been appealed on the merits.<sup>14</sup>

## **8 JUDICIAL REVIEW**

### **8.1 Overview**

The Discussion Paper identifies judicial review of certain regulatory decisions as a possible model for an appropriate review scheme.

This section sets out GasNet's comments on the availability of a judicial review mechanism in relation to decisions by energy regulators.

### **8.2 Preferred approach**

As already indicated, GasNet's preference is for the limited merits review mechanism consistent with the review processes under the current Gas Access Regime. However, for the reasons below, it sees no reason why judicial review should not continue to be available as well.

GasNet considers that, at a minimum, existing rights to judicial review in the energy context should be retained. GasNet also supports the SCO's proposal in Model B to improve the judicial review process by providing decision-makers with greater guidance on how to make their decisions. However, it does not consider that such a proposal should substitute for the more thorough appeal rights created by Model A.

### **8.3 Judicial review should continue to provide minimum level of review**

Judicial review is the minimum level of review that applies to almost all decisions made under statute, provided certain criteria are established (such as a final decision being made).

Judicial review provides individuals with fundamental protections against the improper and arbitrary exercise of executive power. It is intended to ensure that decision-makers avoid error of law and abide by the rules of natural justice. While, in rare cases, legislation has attempted to remove the ability to seek

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<sup>13</sup> Discussion Paper, pp 6-7.

<sup>14</sup> Discussion Paper, p 56.

judicial review, there does not appear to be any convincing reason to remove these basic rights in respect of regulatory decisions in the energy sector.

#### 8.4 Disadvantages of exclusive reliance on judicial review

Although judicial review provides basic and important protections for individuals, there are significant disadvantages of relying on this mechanism exclusively:

- (a) **(Judicial review limited to errors in law)**. Judicial review is limited to decisions involving errors in law<sup>15</sup> and can often involve extremely complex, technical arguments. Even if the improvements suggested by “Model B” were to be implemented (therefore enhancing guidance and improving consistency in decision making), regulatory errors will still go unchallenged unless they can be characterised as errors of law.
- (b) **(Judicial review is administered by a court)**. Secondly, judicial review requires an application to a court. Court actions tend to be extremely time-consuming and costly and can delay the implementation of the appropriate decision. This is exacerbated by the fact that, as mentioned in the Discussion Paper,<sup>16</sup> the court’s power are limited to:
  - (i) making an order to set aside or quash the original decision;
  - (ii) remitting the decision to the original decision maker for reconsideration; and
  - (iii) making declarations and directions.
- (c) **(Expertise)**. Thirdly, although the court is not making a decision on facts, it may lack expertise on the specific regulatory issues that arise in review applications.
- (d) **(Absence of merits review causes unnecessary complexity)**. Finally, where there is no merits review process, parties may attempt to “dress up” substantive errors as errors of law. This unnecessarily complicates review applications, requires courts to deal with areas outside their expertise, and can become extremely costly and time-consuming.

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<sup>15</sup> See *Discussion Paper*, paragraph 2.43.

<sup>16</sup> *Discussion Paper*, paragraph 2.46.