

Electricity Transmission Network Owners

**Initial Response to Exposure Draft
of the National Electricity Law**

**Submission to the Ministerial Council on Energy
Standing Committee of Officials**

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ElectraNet ♦ *Powerlink* ♦ *SPI PowerNet* ♦ *Transend* ♦ *TransGrid*

Initial Transmission Network Services Provider Submission on Draft National Electricity Law

This is a submission made on behalf of Electranet Pty Limited, Powerlink Queensland, SPI Powernet Pty Limited, Transend Networks Pty Ltd and TransGrid (the "TNSPs").

The TNSPs are the owners and operators of the high voltage transmission networks in the National Electricity Market or, in the case of Transend, will be the owner and operator of such a network once Tasmania joins the National Electricity Market.

In the time available, the TNSPs have not had an opportunity to fully analyse the exposure draft of the new National Electricity Law (the "**draft NEL**") and, as a result, this submission sets out their initial views only.

The TNSPs acknowledge that a key driver to the reforms is the separation of the "rule-making" function in the National Electricity Market from the enforcement of those rules. The TNSPs understand and support the rationale for this approach and recognise the progress made by jurisdictions in achieving that structure. However, the TNSPs believe that, as discussed below, the structure adopted for the draft NEL requires further clarity to clearly and consistently achieve that objective.

The TNSPs have a number of concerns regarding the draft NEL which are discussed in more detail below. In broad terms, major areas of concern for the TNSPs are:

- (a) the broad discretions granted to the AEMC, the AER and NEMMCO in the context of a move from merits based review rights to traditional judicial review;
- (b) the breadth of services potentially subject to access regulation under the proposed NEL and the lack of certainty as to the access framework;
- (c) the broad discretions granted to the AEMC in making Rules concerning transmission revenues and pricing and the similar lack of certainty concerning the manner in which the AER performs economic regulatory functions and powers;
- (d) uncertainties in the rule-making process; and
- (e) a number of more minor matters of a drafting nature.

1. Discretions and Judicial Review

The effect of the draft NEL is to replace a number of rights under the Code, the existing NEL and related legislation, such as the *Trade Practices Act*, to seek merits review of decisions taken under the Code with rights of judicial review.

At present, these rights arise in a number of ways:

- (a) through the relevant decision being a "reviewable decision" with recourse to the National Electricity Tribunal; and
- (b) through the ability to dispute the decision under chapter 8 of the Code (such as occurred in the context of the "Participant Fees Dispute").

The TNSPs understand that under the revised regulatory structure documented in the draft NEL, the initial approach will be that existing merits review rights will be replaced with rights to seek judicial review of decisions taken by the AER, the AEMC and NEMMCO. The TNSPs understand that this approach will be reviewed as part of the formulation of a response by the MCE to the Productivity Commission's "Review of the Gas Access Regime". Given this, the TNSPs have prepared this submission on the basis that the appropriateness of merits or judicial review is outside the framework of this consultation.

However, the TNSPs note that the comments set out below should not be taken as indicating that they support the removal of the right to seek a merits review of particular decisions. The TNSPs in general support the availability of a right of merits review, particularly in the context of transmission determinations. In the proposed interim framework, where judicial review is the only review option, the TNSPs wish to ensure that the right of judicial review granted is not abrogated through a series of extremely broad discretions being allowed to decision makers. Such broad discretions have the effect that review of any decision becomes very difficult.

On a general level, the TNSPs are concerned that the manner in which various provisions of the draft NEL have been formulated means that it will be extremely difficult to review decisions taken under it. Examples of this include:

- (a) the provisions relating to transmission revenue and pricing rules in section 91 and the similar provisions relating to the functions and powers of the AER under section 15;
- (b) the ability of the AEMC to determine the weight it gives particular aspects of the national electricity market objective under section 87(2); and
- (c) the lack of any requirement on the AEMC to have regard to submissions received in relation to rule change and proposals under part 7.

While each of these matters is discussed below, at a general level, the TNSPs note that the discretions granted are extremely broad. Vesting a broad or wide discretion in decision making bodies may, from a policy point of view, be able to be justified as being appropriate if there is an associated safeguard of a related merit review process. In these circumstances, in any specific case, the body undertaking the merits review can scrutinise with an appropriate level of accountability the exercise of any broad or wide discretion at first instance.

However, where the basis for appeal or review is restricted to judicial review then, to ensure that there is appropriate accountability and transparency, greater care must be taken in drafting the relevant discretionary provisions. This means that general or wide discretions should be avoided in favour of statutory provisions which identify relevant considerations against which the exercise of the particular discretion can be assessed.

Such an approach is necessarily the counterpoint to the adoption of an approach which abandons merits review in favour of only judicial review. In essence, there is then a greater need to ensure that specific discretions contain sufficient detail in terms of identifying relevant considerations. Otherwise, the judicial review processes in practice may provide only a limited check on the broad discretionary powers. This would appear inconsistent with one of the stated aims of the reform process, namely, the achievement of greater accountability and transparency in the regulatory process.

The TNSPs note that similar issues arise in relation to the discretions granted to the AEMC under sections 34, 35(3)(c), 35(3)(1), 35(3)(n), 94 and 96 of the draft NEL. This is expected to be addressed in the TNSPs' more comprehensive submission.

2. Services for Which Access can be Sought

At the consultation forum held in Sydney on 10 December 2004, it was noted that the provisions of the Rules relating to access were not in a final form as a number of policy decisions relating to access regulation had yet to be taken.

The TNSPs are concerned that, while significant aspects of the policy framework remain outstanding, the legislative basis for the regulation of access pricing are being finalised through the NEL amendments.

The TNSPs consider that it is difficult to comment meaningfully on the draft NEL provisions until it is clear how access will be regulated under the Rules. For example, if the policy decision is taken that the Rules will not be approved as an effective access regime or accepted by the ACCC as an industry access code (assuming that this were possible in respect of the Rules) under Part IIIA of the *Trade Practices Act*

then, in the absence of further legislative change, the services provided by the TNSPs would potentially remain subject to declaration under Part IIIA of the *Trade Practices Act*. If such a declaration were to occur, the TNSPs would potentially be subject to conflicting legal duties under Part IIIA and the Rules and NEL.

In these circumstances, the TNSPs consider that the need to finalise the NEL should not outweigh the need to develop a complete and coherent regulatory structure prior to legislating for part of that structure.

The TNSPs consider that the lack of a finalised regulatory structure creates significant uncertainty as to the application of the draft NEL. A major example of this are the services in respect of which the Rules will set out the basis on which access can be sought. At present, Item 13 of Schedule 1 of the NEL provides that Rules can be made in relation to:

"access to services provided by means of transmission systems and distribution systems".

From the manner in which the Rule is drafted, it appears that this would allow Rules to be made in relation to access to any service provided by a transmission or distribution system. This is a fundamental change from the regime currently provided for under the Code where the access undertaking given by Network Service Providers as set out in Schedule 5.8 of the Code relates to "network services". Chapter 10 of the Code defines a "network service" as a:

"transmission service or distribution service associated with the conveyance, and controlling the conveyance, of electricity through the network".

Item 13 is not restricted to services the pricing of which is regulated by the AER nor even to network services. For example, it would appear that a Rule could be made requiring access to telecommunications services which a network service provider's network may be capable of providing.

The TNSPs consider that Item 13 should be amended such that it only applies to services which are regulated by the AER or to which access can otherwise be gained under any relevant jurisdictional legislation. These services should be clearly defined in the draft NEL.

The TNSPs also note that section 91(3) which sets out the basis on which the AEMC is required to make Rules for the pricing of transmission revenues does not refer to Item 13 of Schedule 1 but only to Items 15 to 24. The TNSPs consider that the Rules relating to access to the services provided by transmission networks must be consistent with the basis on which those services are priced.

As a result, the TNSPs consider that section 91(3) should, in the context of the making of Rules concerning access to transmission networks, refer to Item 13 of Schedule 1.

3. The Regulation of Transmission Pricing

The TNSPs also have a number of concerns relating to the manner in which the draft NEL provides for the AEMC to make Rules in respect of transmission regulation and the functions of the AER in respect of economic regulation.

These concerns fall into 2 main categories, namely:

- (a) the difficulty of ensuring accountability of the AEMC and AER given the range of the discretions granted to them; and
- (b) the lack of clarity as to the relationship between the provisions of Schedule 1 and the provisions of the main body of the draft NEL.

Section 91 of the draft NEL sets out the matters the AEMC must take into account in making Rules for transmission regulation. These are in substance the same as the matters which the AER must have regard to in performing economic regulatory functions or powers under section 15(2). The TNSPs consider that the broad discretions granted to the AEMC and the AER will make it extremely difficult to successfully review any decision of the AEMC and AER for the reasons set out in section 1 above. The TNSPs wish

to have clarified whether the draft NEL is intended to allow for a move to price regulation in addition to or in place of the current revenue cap approach.

For example, section 91(3)(a) and section 15(2)(a) provides that the AEMC or AER, as the case may be, must ensure that the Rule or exercise of power:

"provide[s] an opportunity for a regulated transmission system operator to recover the efficient costs of complying with a regulatory obligation".

The use of the word "opportunity" creates substantial uncertainty as to what the Rule or decision must ensure. It can be read as requiring no more than that there is some possibility that the regulated transmission system operator could recover those costs. The TNSPs believe that if a regulatory obligation is imposed on them, they should have an entitlement to recover the efficient costs of complying with that obligation. The proposed wording of section 91(3) and section 15(2)(a) does not do this.

Similarly, section 91(3)(c) and section 15(2)(c) require only that the Rule or decision "makes allowance" for the value of network assets. No guidance is given as to the basis on which such allowance must be made or that the allowance should enable the recovery of the costs of prudent investment. The TNSPs are concerned that there is potential for a move away from the current framework for asset valuation with little guidance given as to what the preferred approach is.

The TNSPs believe it is an essential part of the "regulatory compact" to which they are subject that, if they are to be required to give access to their networks (and to augment those networks to a standard necessary to maintain appropriate service levels), they have a clear right to recover costs efficiently and prudently incurred. At present, the drafting of section 91 and section 15 means that it would be extremely difficult for the TNSPs to challenge any regulatory decision given that the discretion granted to the AEMC and AER is very broad (and hence it would be hard to challenge any exercise of that discretion on traditional judicial review grounds).

This difficulty is increased through a lack of clarity as to the relationship between the main body of the draft NEL and the provisions of Schedule 1. At present, section 15 of the draft NEL, which sets out how the AER performs its economic regulatory functions and powers, only refers to Schedule 1 in a procedural sense through section 15(1)(b) requiring that the AER must consult with regulated transmission system operators and affected Registered participants (in the manner provided for in the Rules) or in relation to the services which are the subject of regulation (in section 15(2)(b)). However, items 15 to 24 of Schedule 1 provide for the AER to make determinations on matters which are not set out in section 15 or provide for these matters to be addressed on a potentially different basis than is set out in section 15. The TNSPs consider that the matters set out in Schedule 1 are integral to the regulation of transmission revenue. As a result, it is essential that sections 15 and 91 reflect these.

For example, item 19 provides for the Rules to set out the economic framework and methodologies to be applied by the AER for the purposes of the AER's assessment of investments in transmission systems under items 18. There is no requirement that these Rules be consistent with the matters set out in section 15.

Further, item 22 provides that the AER must determine:

- (a) depreciation;
- (b) operating costs; and
- (c) an allowable rate of return.

However, there is no express reference to any of these matters in section 15 or section 91. The TNSPs consider that not only should there be consistency between Schedule 1 and sections 15 and 91, but also that they should have a clear right to recover efficient costs and the recovery of a rate of return which supports the achievement of the national electricity market objective.

The TNSPs also note that they have some concern about the difference between the overall objectives placed on the AER under section 15(1)(a) and the national electricity market objective in section 6. In the TNSPs' experience, a Court will generally assume that the use of different language into statutory provision indicates a parliamentary intention that the provisions be interpreted differently. Not only are the TNSPs not aware of any reason why there need be such a distinction drawn in these circumstances, they are also concerned that the difference in wording gives rise to significant uncertainty as to how a Court would interpret section 15(1).

4. Uncertainties in the Rule-Making Process

Under section 87(1) the AEMC is required to only make a proposed Rule if it is satisfied that the Rule "will or is likely to contribute to the achievement of the national electricity market objective".

However, it is not clear how the AEMC addresses matters which are raised in submissions made to it and the AEMC appears to have an almost unlimited discretion as to the actions it takes in considering a proposed Rule change.

Section 99(3) and 103(3) make it clear that the rule as approved by the AEMC need not be the rule which was originally proposed to the AEMC and, in the case of section 103(3), need not be the Rule which was foreshadowed in the draft Rule determination. No limitation is placed on the changes which may be made to a proposed Rule change or to the Rule change proposed in the draft Rule determination.

The discretion granted to the AEMC in this regard appears to only be constrained by the overall requirement in section 87 that the AEMC only make a Rule if it is satisfied that it will or is likely to contribute to the achievement of the national electricity market objective.

However, the test imposed by section 87 is one which requires only that the AEMC be satisfied that the Rule it proposes to make will contribute or is likely to contribute to the national electricity market objective. The AEMC is not required to determine that the proposed rule is the most appropriate way of achieving the national electricity market objective in the relevant area but only that the rule will "contribute" to that. This broad discretion gives rise to substantial difficulty in relation to the treatment of submissions made by interested parties on a proposed Rule change and allows a broad discretion to the AEMC to alter proposed Rule changes after the consultation process. Part 7 of the draft NEL does not impose any express requirement on the AEMC to take into account submissions received and it appears that the Rule change adopted by the AEMC could differ materially from that which was consulted on.

If the AEMC were to not adopt a submission which would make a proposed Rule more consistent with the national electricity market objective then it would appear that, so long as the Rule actually made satisfied the test in section 87, it would be very difficult to judicially review the AEMC's decision. Further, it would appear difficult to challenge an AEMC decision where the final Rule adopted was substantively different from the Rule consulted on.

To overcome these deficiencies, the TNSPs consider that the AEMC should be under an express duty to:

- (a) consider submissions received and to adopt those submissions if they were to aid or would be likely to aid in the achievement of the national electricity market objective (having regard to any relevant MCE statement of policy principles); and
- (b) not substantively alter proposed Rule changes between the draft and final determinations.

The TNSPs are also concerned that the broad discretion granted to the AEMC under section 87(2) to decide on what weight to give particular aspects of the national electricity market objective will increase the difficulty of reviewing decisions of the AEMC in relation to Rule changes. As discussed in section 1 above, the breadth of this discretion means that it is likely that a decision of the AEMC would only be reviewable if that decision were perverse or could otherwise be said to be unreasonable in a traditional review sense.

The TNSPs believe that imposing such a high barrier to the review of AEMC decisions will make it difficult to ensure the accountability of the AEMC in performing its Rule-making function.

5. Other Matters

(a) Definition of "*national electricity system*"

Section 2 of the draft NEL defines the "national electricity system" as:

- "(a) the generating systems and other facilities owned, controlled or operating in the participating jurisdictions connecting to the interconnected transmission and distribution system referred to in paragraph (b); and
- (b) the interconnected transmission and distribution system in the participating jurisdictions used to convey and control the conveyance of electricity that connects -
 - (i) the generating systems and other facilities referred to in paragraph (a); and
 - (ii) loads settled through the wholesale exchange operated and administered by NEMMCO under this Law and the Rules."

The TNSPs note that the manner in which load supplied by "local retailers" are settled under the Code and the draft Rules means that it is not clear whether distribution system assets which are used to supply customers which purchase electricity from the local retailer fall within subparagraph (b). This is because, in the wholesale market, the purchase of electricity for supply to these customers is settled at the point where the relevant distribution systems joins the relevant transmission network. As a result, those parts of the distribution system which supply such customers would not be used to convey electricity to a load settled through the wholesale exchange.

(b) Definition of "*national electricity market*"

Section 2 of the draft NEL defines the "national electricity market" as the national electricity system together with the "wholesale exchange operated and administered by NEMMCO under this Law and the Rules".

Given that the national electricity system is defined as the physical assets underlying the generation, transmission and supply of electricity, there appears to be some doubt as to whether the definition of "national electricity market" include matters which are not directly part of the wholesale exchange but which are necessary for the supply of electricity.

Examples of matters which could fall under this category are the procurement of ancillary services (particularly non-market ancillary services) and functions undertaken in relation to matters such as retail contestability.

(c) The relationship between definitions of "*national electricity market*" and "*national electricity system*"

As discussed above, the definition of "national electricity system" refers to the physical assets used for the generation, transmission and supply of electricity and the "national electricity market" is defined as the national electricity system plus the wholesale exchange operated and administered by NEMMCO.

Leaving aside the difficulties noted above which the reference to the "wholesale exchange" creates, the use of these 2 terms creates some difficulty in determining the functions and powers of certain Code or Rule bodies. For example, under section 37(2) the Reliability Panel is given certain functions relating to the national electricity system.

Given the definition of "national electricity system" and "national electricity market" it is unclear the extent to which the Reliability Panel can enquire into matters which relate to the "wholesale exchange" but which affect power system security and reliability. For example, matters such as the acquisition of ancillary services or the setting or reserve levels may impact significantly on power system security.

However, given that these matters do not relate to the "national electricity system" it is unclear to what extent the Reliability Panel can enquire into them.