Standing Committee of Officials of the

Ministerial Council on Energy

Statement of Scope

A National Legislative Framework for Gas and Electricity

July 2006

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Glossary of abbreviations and publications referred to in the Statement of Scope

Abbreviations

ACCC	Australian Competition and Consumer Commission
ACT	Australian Competition Tribunal
AEMA	Australian Energy Market Agreement - the intergovernmental agreement between the Commonwealth and all of the States and Territories first made in 2004 and amended in 2006
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
COAG	Council of Australian Governments
Expert Panel	Panel established by MCE in December 2005 to advise on a model to achieve a common approach to transmission and distribution revenue and network pricing across electricity and gas (Final Report delivered April 2006)
GPAL	Gas Pipelines Access Law – Schedules 1 and 2 to the *Gas Pipelines Access (South Australia) Act 1997*, including "Third party access to natural gas pipelines" (Schedule 1) and the National Third Party Access Code for Natural Gas Pipeline Systems (the Gas Code – Schedule 2)
MCE	Ministerial Council on Energy
NCC	National Competition Council
NEL	National Electricity Law, Schedule to the *National Electricity (South Australia) Act 1996*
NEMMCO	National Electricity Market Management Company
NER	National Electricity Rules – Statutory Rules made under Part 7 of the *National Electricity (South Australia) Act 1996*
NGL	National Gas Law, Schedule to the new *National Gas (South Australia) Act 2007*
NGR	National Gas Rules – Statutory Rules made under Chapter 6 of the new National Gas Law
RPWG	Retail Policy Working Group established under MCE SCO

SCO Standing Committee of Officials reporting to MCE

Relevant MCE Publications

MCE Statement of Approach – A New Legislative Framework for Gas, September 2005 (Statement of Approach)
http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=51EB99E6-FE2A-8D19-FF72A7C97121A7AD

MCE "Response to Key Issues Raised in Submissions to the Statement of Approach to the Development of the New National Gas Laws and Rules"
http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=409F0422-D257-A8DF-34E3098CCCE679B4

Productivity Commission Review of the Gas Access Regime, June 2004
http://www.pc.gov.au/inquiry/gas/finalreport/index.html

MCE Response to the Productivity Review of the Gas Access Regime, May 2006 (PC Response)
http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=1657B707-AD38-B43A-5CE8B8C11AFBE8E2

MCE Decision on Review of Decision-Making in the Gas and Electricity Regulatory Frameworks, June 2006
http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=839F2DC1-AE13-142E-8425FEF5F2E8C822

Final Report of the MCE Expert Panel on Energy Access Pricing, April 2006
http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=B0F3AD4C-A1C6-28DB-CB9CC594D2B88090

MCE Arrangements for Consumer Advocacy in the Energy Sector, December 2005
http://www.mce.gov.au/index.cfm?event=object.showContent&objectID=2CB6A5A9-EDA6-E716-FD118AA822DD7665

1. Purpose of Paper

This paper seeks to assist stakeholders by outlining details of future national legislative arrangements for gas and electricity markets and clarifying the scope of the proposed legislative packages to progress the MCE Energy Market Reform Agenda. The paper revisits and updates the MCE Statement of Approach of September 2005.

The legislative packages will give effect to the requirements of the Council of Australian Governments' (COAG) Australian Energy Market Agreement (AEMA) as amended and endorsed by COAG in June 2006.

Consultation with stakeholders on exposure drafts of the laws and rules will be an integral part of the process. While an exposure draft of the 2006 Legislative Package is expected to be released in the near future, the MCE is currently reviewing the timelines for that package and will announce its decision shortly.

Public consultation on the exposure draft will entail information sessions where stakeholders can ask questions and raise issues.

Full details of the exposure draft and public consultation will be announced through MCE Energy Market Reform Bulletins and placed on the MCE website at www.mce.gov.au when available.

2. Policy Background

2.1 The Ministerial Council on Energy's Reform Agenda

The current set of reforms arose out of the MCE's December 2003 report to COAG, *Reform of Energy Markets*,[1] which identified a number of specific objectives for the reform program, the most relevant to the current reform agenda being to:

- strengthen the quality, timeliness and national character of **governance** of the energy markets, to improve the climate for investment;
- streamline and improve the quality of **economic regulation** across energy markets, to lower the cost and complexity of regulation facing investors, enhance regulatory certainty and lower barriers to competition; and
- further increase the penetration of **natural gas**, to lower energy costs and improve energy services, particularly in regional Australia, and reduce greenhouse emissions.

The MCE's December 2003 report contained specific reforms to the governance arrangements for the energy sector, and recommended further activities for the achievement of the other objectives, including an in-principle agreement to develop a national approach to energy access under the *Trade Practices Act 1974*, covering electricity and gas transmission and distribution.

The MCE's report, including the objectives set out above and the specific recommendations, was endorsed by First Ministers and formed the basis for the AEMA on 30 June 2004.[2] This inter-governmental agreement set out the timetable for the progressive introduction of the new governance arrangements for the gas sector[3]. In broad terms, the new governance arrangements will comprise:

- *The MCE*, the national policy and governance body for the Australian energy market including for electricity and gas, with a power to direct reviews by the AEMC with respect to rule-making and market development;
- *The Australian Energy Market Commission (AEMC)*, responsible for rule-making and market development functions in respect of electricity and natural gas transmission and distribution networks and retail markets (other than retail pricing); and
- *The Australian Energy Regulator (AER)*, responsible for enforcement and economic regulation of electricity and gas transmission and distribution networks and retail markets.

Amendments to the AEMA were endorsed by COAG in June 2006 to provide for:

- transfer of retail and distribution regulation (other than retail pricing) to a national framework in an agreed timeframe;
- agreement to implement national distribution and retail functions in new national rules by 1 January 2008;

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[1] Ministerial Council on Energy Report to the Council of Australian Government, *Reform of Energy Markets*, 11 December 2003.

[2] Council of Australian Governments, Intergovernmental Agreement on an Australian Energy Market, 30 June 2004.

[3] Under the Agreement, WA is not committed to transferring functions to the AER related to gas, and to the AER and AEMC relating to electricity. WA is committed to conferring functions to the AEMC relating to the making of Gas Access Rules.

- agreement of the longer term funding arrangements for the national energy institutions;
- a process for providing advice to jurisdictions on the effectiveness of competition in retail markets; and
- arrangements for the certification of energy access regimes on a nationally consistent basis.

Consistent with the change in the governance arrangements for economic regulation in the industry, a new legal structure has also been agreed to. In particular, the legal framework for economic regulation in both electricity and gas is being modified to consist of:

- the law (National Electricity Law (NEL) and National Gas Law (NGL)), to be modified by Parliaments, consistent with the processes set out in the AEMA;
- statutory rules (National Electricity Rules (NER) and National Gas Rules(NGR)) initially made by the South Australian Energy Minister on the recommendation of the MCE, with the AEMC being responsible for the Rules and the amendment process in accordance with the procedures set out in the NEL and NGL;
- regulations under the NEL and NGL, limited to minor process and procedural matters in the NEL and NGL and the prescription of civil penalties;
- statements of policy principle from the MCE to the AEMC, subject to the procedures set out in the NEL and NGL.

The access related parts of these instruments will then be submitted for certification under the Part IIIA of the *Trade Practices Act 1974* through coordinated and concurrent State and Territory applications.

The discussion in this paper presumes a broad understanding of the current electricity and gas regulatory frameworks. Readers unfamiliar with these frameworks would be advised to read the broad summary of the legislative structure in Part 2 of the Expert Panel on Energy Access Pricing's final report (pp 16-30) available on the MCE website.

3. The 2006 Legislative Package

3.1 Overview

The 2006 Legislative Package includes the new NGL, Regulations and Rules, and amendments to the NEL and Rules. The legislative package is designed to deliver fairer, more effective access regimes for both gas and electricity, achieving commonality where appropriate, and focusing on economically efficient outcomes that are in the long term interests of consumers.

The AEMA sets a clear framework for MCE to further these goals. This package involves significant legislative changes to achieve the following objectives:

- Transfer the governance and institutional arrangements for the gas regime to the national framework, with the AER as the independent industry regulator and the AEMC as the rule-maker and market development body;
- Implement policy changes to the gas regime developed from the MCE's Response to the Productivity Commission's Review of the Gas Access Regime (PC Response), released on 9 May 2006, including light-handed regulatory approaches, a common objects clause and incentives for greenfields pipelines;
- Implement a limited merits review model for economic regulatory decisions in the gas and electricity regimes consistent with the MCE decision of 2 June 2006;
- Implement a common framework for revenue and network pricing across the energy market, building on the advice of an MCE-established Expert Panel on Energy Access Pricing (Expert Panel); and
- Strengthen consumer advocacy arrangements consistent with the MCE decision of November 2005 to establish a long-term consumer advocacy funding model for advocacy in both gas and electricity.

The majority of the legislative changes taking place in 2006 relate to previously agreed and publicised MCE policy positions, principally: the AEMA; the MCE Response to the Productivity Commission on the Gas Access Regime; the MCE Decisions on Merits Review; Consumer Advocacy; and the alignment of the objects of the gas and electricity regimes. A significant new policy direction comes from the MCE's response to the Expert Panel.

It is important to note that the breadth of policy issues to be implemented by the 2006 package is greater with regards to gas than electricity, where the new governance framework has already been implemented by the 2005 amendments to the NEL.

3.1.1 Distribution and Retail Transfer

The transfer of the National Retail and Distribution functions to the AER and AEMC will commence in the 2006 legislative package with the transfer of economic regulation to the AER and AEMC. This will mean that all new revenue/pricing determinations in electricity and gas, transmission and distribution that have not begun on 1 January 2007 will be undertaken by the AER according to national rules.

In practice, this means that the current Tasmanian electricity distribution determination review and Victorian gas distribution access arrangement review will continue to be assessed by the relevant jurisdictional regulators, while the NSW and

ACT electricity distribution determinations will be undertaken by the AER. The timing and transition of existing distribution determinations to the AER is being considered by SCO, consistent with the AEMA.

The subject matter for the national distribution and retail framework was agreed in Annexure 2 of the AEMA as follows:

National Functions

1. **Distribution economic regulation -** services to be regulated, the form of regulation and tariff setting.

2. **Service performance incentive scheme –** for network service performance standards (as set by the jurisdiction where elected), and customer service performance standards, linked to economic regulation.

3. **Information disclosure** - information requirements for the AER to undertake its regulatory functions.

4. **Connection and capital contribution requirements** - new connections charges and capital works contributions.

5. **Distribution network expansion** - determining when extensions are part of a regulated service and how charges are levied.

6. **Distributor connection service obligations** - provision of connection and related services to users and the contractual relationship with retailer and customer.

7. **Distributor small customer disconnection/reconnection** - allowable disconnections or reconnections of small customers including those arranged by retailers.

8. **Distributor interface with other market participants -** determining the nature of distributor-retailer and distributor-embedded generator relationships including use of system.

9. **Metering -** obligations to install, maintain and read meters.

10. **Retailer obligation to supply to small customers -** obligation on retailers to supply customers at a default tariff with minimum terms and conditions.

11. **Retailer failure arrangements -** arrangements to ensure customer supply continuity and wholesale market financial integrity.

12. **Retailer - small customer market contracts -** minimum contract terms and conditions.

13. **Retailer - small customer marketing -** marketing conduct obligations.

14. **Balancing regime, settlements, customer transfer** - balancing, settlement and contestable customer churn arrangements to ensure accurate financial reconciliation would be retained by independent market administrators.

15. **Distributor and retailer general business authorisations –** where necessary for matters other than technical capability and safety.

State and Territory Functions (current responsibility retained)

16. **Distributor technical/safety business authorisation -** licensing and authorisation schemes that require demonstration of technical capability.

17. **Small customer dispute resolution** - obligation for distributors and retailers to have internal dispute resolution schemes and participate in independent dispute resolution (Ombudsman) schemes.

18. **Load shedding and curtailment** - customer supply reduction sequence to maintain system security.

19. **Service reliability standards –** standards to ensure network security and reliability.

20. **Metering –** policies on the type of meters required for specific customer classes, accredited service provider arrangements, and load profile arrangements.

21. **Distribution and retail service areas** – specification of geographical areas in which responsibilities/obligations apply.

The initial NGR for the economic regulation of transmission and distribution in gas and amendments to the NER to transfer electricity distribution will be made by the South Australian Energy Minister on the recommendation of the MCE. These Rules will, essentially, cover items 1-3 of Annexure 2 to the AEMA for electricity[4] and items 1-5 of Annexure 2 for gas (consistent with current framework in the Gas Code). Further explanation of these changes is below.

The NGL and NEL will not confer any ability on the AEMC or MCE to make new Rules regarding non-access distribution and retail matters. This issue will be addressed separately by MCE in 2007 (see Part 4 below).

Consistent with clause 14 of the AEMA, the MCE will also be able to direct the AEMC to conduct ongoing reviews into the effectiveness of retail competition for the purposes of providing advice on the retention, removal or reintroduction of retail energy price controls. The details of this process are in the AEMA, and further consultation is currently being undertaken on the criteria for the effectiveness of competition upon which these reviews will be based. The AEMC will commence its reviews in 2007.

4. However, to the extent to which the current NER addresses issues of capital contributions and network expansion, these elements will be transitioned in the NER amendments consistent with the advice of the Expert Panel.

3.1.2 Expert Panel

To provide a sound policy basis on which to develop Law and Rules for the transfer of economic regulation to the AEMC and AER, the MCE commissioned an Expert Panel in December 2005 to advise on a model to achieve a common approach to revenue and network pricing across the energy market. The Expert Panel called for submissions in relation to its terms of reference in December 2005, produced a draft report in March 2006. Following further consultation, it submitted a final report delivering on its terms of reference on 13 April 2006.

In order to meet the timing commitments for the transfer of economic regulation of gas and electricity distribution in the AEMA, the MCE has decided to make its preliminary response to the Expert Panel's advice in the context of producing exposure drafts of the NEL amendments and NGL. It is hoped that this response to the Expert Panel and the exposure drafts themselves will allow meaningful consultation on the implementation of the Expert Panel's recommendations, and allow MCE to make an informed decision on the final legislation proposed for introduction into the South Australian Parliament later in 2006. This document foreshadows elements of that preliminary response relevant to the key changes in the NGL, NEL, NER and NGR.

3.1.3 Common Legislative Framework

As a preliminary point, the NGL and NEL will adopt the Expert Panel's recommendation that a common legislative framework be established with respect to access pricing for both gas transmission and distribution and electricity transmission and distribution.

The common legislative framework comprises the following matters:

a) *Objectives* – the objectives for the regimes;
b) *Scope of regulation* – the scope of regulation, by reference to the transmission and distribution facilities that are subject to the regime (but maintaining the current distinction under which, in the electricity model, the scope is defined on the basis of a statutory description of the relevant facilities and, under the gas model, scope is determined on the basis of a coverage test);
c) *Form of regulation* – the forms of regulation that are available to be provided for in the Rules, and the principles or criteria to be applied in selecting between them and applying them to the various services provided by the regulated facilities;
d) *Regulatory procedures* – the procedural requirements that are to apply to access pricing determinations, with the more detailed procedures to be specified by the AEMC in the Rules;
e) *Pricing principles* – high level pricing principles to guide the AEMC in making Rules with respect to access pricing and the AER in interpreting and applying the Rules, with sufficient flexibility to allow divergent application of the principles between sectors at a detailed level in the Rules;
f) *Information disclosure* – statutory information gathering powers of the AER and a framework for specific accounting and other disclosure requirements; and
g) *Review of decision making* – appeal and review mechanisms, as determined by the MCE.

Further details of existing MCE decisions as to how this framework will be implemented, and some other aspects of the preliminary MCE response to the Expert Panel, are below. A more detailed explanation will be contained in material accompanying the exposure drafts.

3.1.4 Objectives of National Gas Law and National Electricity Law

As announced in the PC Response, the MCE has decided that, for the NGL:

> *The objective of this law is to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of national gas.*

For the NEL, the MCE has decided that:

> *The objective of this law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.*

In making these decisions, the MCE was mindful of the recommendations of the Expert Panel on Energy Access Pricing. The MCE agrees with the Panel that there is no inherent difference between the gas and electricity regimes which requires a difference in basic approach, and that a common objective would have significant benefits in developing a common approach to revenue and network pricing across the energy sector.

In considering a preferred formulation of a common objective for both the NGL and the NEL, the Panel concluded that

> *"One of the perceived benefits of an overriding statement of objectives is that it provides a uniform guiding principle in relation to all aspects of the regime where discretions are required to be exercised or interpretations to be made. This includes the application of the regime by regulators, administrative bodies (including Ministers), the courts and other appeal and review bodies. The narrower scope within which the objective applies in the NEL does not achieve this benefit as effectively as the approach proposed for the NGL. The Panel considers that the NGL approach can and should apply across both regimes"* (Expert Panel on Energy Access Pricing, Report to the Ministerial Council on Energy, April 2006, page 37).

The MCE accepted this view and the Panel's recommendation that the NEL be amended so that the existing national electricity market objective is made a statement of the object of the NEL. In drafting the provisions of the NEL and NGL, the word 'objective' has been used to assist consistent incorporation of the objects clause into the rest of the NEL and NGL.

Just as the AEMC must test Rule changes against the objective of the law when making Rules, the regulator must perform its functions in a manner that will or is

likely to contribute to achieving the objective of the law. The objectives clause therefore is a point of congruence between policy-makers/law-makers (MCE), the Rule-maker (AEMC) and the regulator (AER).

3.1.5 Terminology 'form of regulation' and 'pricing principles'

Two particular Expert Panel recommendations, accepted by the MCE, are worth noting prior to the discussion of the NGL and NEL changes. The first is the market power-based 'form of regulation' criteria. These criteria are intended to guide decisions in both gas and electricity about whether particular services provided by a network service provider should be subject to some type of upfront price control, a negotiate/arbitrate framework or no regulation (see p 57 of the Expert Panel report). These factors are:

a) barriers to entry
b) network externalities
c) countervailing market power
d) substitution possibilities
e) information asymmetry
f) other factors.

The MCE has accepted these criteria. Details of implementation, and how this relates to the net benefit test, are below.

The second is the Expert Panel recommendation, which MCE has accepted, that consistent pricing principles should be applied to both gas and electricity in the NEL and NGL. These principles are to:

(a) provide a reasonable opportunity for a network operator to recover at least the efficient costs of providing services that are the subject of the network pricing determination and complying with a regulatory obligation; and

(b) provide effective incentives to a network operator to promote economic efficiency in the provision by it of services that are the subject of a network pricing determination, including:

  (i) the making of efficient investments in the network owned, controlled or operated by it and used to provide services that are the subject of a network pricing determination;

  (ii) the efficient provision by it of services that are the subject of a network pricing determination; and

  (iii) the making of efficient use of existing assets and proposed new assets that are, or are to be, used to provide services that are the subject of a network pricing determination;

(c) make allowance for the value of assets forming part of a network owned, controlled or operated by a network operator, and the value of proposed new assets to form part of that network, that are, or are to be, used to provide services that are the subject of a network pricing determination;

(d) have regard to any valuation of assets forming part of a transmission or distribution system owned, controlled or operated by a network operator applied in any relevant determination or decision; and

(e) have regard to the economic costs and risks of:

(i) the potential for under-investment and over-investment in assets by the network operator; and

(ii) the potential for under-utilisation and over-utilisation of the capacity of assets forming part of a distribution or transmission system, and the capacity of proposed new assets.

The discussion below notes that gas and electricity-specific terminology, to achieve the policy outlined by the Expert Panel, is being considered in the legislative drafting of these provisions.

3.2 National Gas Law (NGL)

The gas and electricity regimes are co-operative Commonwealth, State and Territory legislative schemes. The Commonwealth and all the States and Territories are part of the gas access regime and all but Western Australian and the Northern Territory participate in the electricity regime.

The schemes work through "lead" legislation in South Australia: currently the *Gas Pipelines Access (South Australia) Act 1997* and *National Electricity (South Australia) Act 1996*. This lead legislation is then applied as the law in the other States and Territories through 'application Acts' which pick up the Schedule/s to the respective South Australian Acts and apply it in their jurisdiction. Western Australia currently enacts its own complementary gas legislation that corresponds to the South Australian legislation and applies the Gas Code .

The Commonwealth currently applies the electricity regime to the offshore area through the *Australian Energy Market Act 2004* and a similar effect is achieved for the gas regime. The current electricity and future gas regime gives functions and powers to the AEMC established by the South Australian *Australian Energy Market Commission Establishment Act 2004,* and to the AER established by Part IIIAA of the *Trade Practices Act 1974.*

Substantial changes to the electricity governance framework were made in 2005 through amendments to the *National Electricity (South Australia) Act 1996*. For the gas regime, the MCE has decided that the most appropriate mechanism to implement the new governance framework would be a new South Australian Act called the *National Gas (South Australia) Act 2006*. This Act will contain a Schedule called the National Gas Law (NGL).

Consistent with the electricity regime, the NGL will be supplemented by National Gas Rules (NGR) and a limited number of regulations dealing with minor matters and the prescription of civil penalties. This new framework would then take the place of the

current *Gas Pipelines Access (South Australia) Act 1997* and the National Third Party Access Code for Natural Gas Pipeline Systems (Gas Code).

With a new NGL, there will need to be new laws which apply the NGL in each jurisdiction. The Commonwealth will amend its *Australian Energy Market Act 2004* in 2006 for this to occur for the offshore area and to ensure the AER, Australian Competition Tribunal, National Competition Council and Commonwealth Minister can take up their relevant functions under the NGL. States and Territories are expected to progress application Acts during the first half of 2007 depending on election cycles and parliamentary timetables. The NGL regime cannot be implemented until all application Acts have been passed and are ready to be proclaimed.

Western Australia will continue to implement complementary legislation consistent with the NGL, and differ only in respect to institutional arrangements, namely retention of its local regulator, the Economic Regulation Authority. Western Australia's complementary legislation will only cover gas pipeline access provisions and will not include future changes in respect to national retail and distribution functions. Western Australia will apply the sections of the National Gas Rules relating to gas access as made by the South Australian Minister.

3.2.1 Introduction (Chapter 1 of NGL)

The NGL will begin with the necessary definitions, outline a process for issuing MCE Statements of Policy Principle and deal with other machinery matters in a manner similar to the NEL.

3.2.2 Functions and Powers of Regulatory Bodies (Chapter 2 of NGL)

The 2006 legislative package will transfer responsibility for economic regulation of gas transmission and distribution networks from the Australian Competition and Consumer Commission (ACCC) and local regulators (excluding Western Australia) to the AER. Western Australia may elect at a later time to be subject to AER regulation for natural gas.

AER

The NGL will confer economic regulatory functions and powers on the AER. These are functions or powers performed or exercised by the AER that relate to the economic regulation of pipeline services provided by means of, or in connection with, a covered pipeline. They include a function or power performed or exercised by the AER that relates to:

- The approval or making of an access arrangement;
- Arbitration decisions;
- Monitoring the price and provision of services by means of a monitored pipeline and the performance of the pipeline service provider;
- Decisions relating to imposing or waiving ring-fencing requirements;
- Voiding associate contracts; or
- Approving or voiding competitive tendering arrangements.

The AER will be statutorily required to perform its economic regulatory functions and powers in a way that will or is likely to contribute to the object of the NGL. Consistent with the recommendation of Expert Panel that the AER be guided by the pricing principles, the AER will be required to take the pricing principles into account when exercising a discretion relating to setting reference tariffs or deciding arbitration on price matters. The pricing principles will be adopted from the Expert Panel report (p 116-117), with necessary drafting amendments relating to gas-specific terminology in the NGL. Similarly, the AER will be required to take the 'form of regulation' factors into account when determining, for a pipeline that requires an access arrangement, whether services require a reference tariff (other than services sought by a significant portion of the market). The 'form of regulation' factors adopted from p 57 of the Expert Panel report will be drafted consistently with existing gas-specific terminology.

The AER will monitor, investigate and enforce compliance with the new NGL and NGR. It will be able to authorise officers to obtain search warrants and require a person to provide information if it has reason to believe that the person has information required for the performance or exercise of its functions and powers. The NGL will also set up the framework for information required for general regulatory reporting, ring-fencing (maintenance of accounts) and at the time of assessing and/or revising access arrangements consistent with the concerns expressed by the Expert Panel.

AEMC

The 2006 legislative package will transfer the functions of the National Gas Pipelines Advisory Committee (NGPAC) and Code Registrar to the AEMC. Rule making functions in relation to gas access will be conferred on the AEMC.

The AEMC itself will not be empowered to initiate any change to the new NGR (other than where the proposed change seeks to correct a minor error or is non-material) and will be required to manage the rule change process and consult and decide on rule changes that are proposed by any person or the MCE.

The AEMC will also conduct reviews as directed by the MCE into: any matter relating to a market for gas; any matter relating to access to pipelines or services provided by means of pipelines; any matter relating to the NGR or the operation and effectiveness of the new NGR, and reviews into the effectiveness of competition in retail energy markets (in Western Australia this latter task will be undertaken by the Economic Regulation Authority). In reporting to the MCE on a review, the AEMC may recommend such changes to the NGR as it considers appropriate (but it will then be for the MCE to decide whether to actually initiate a rule change proposal).

The AEMC must, in performing its functions, have regard to the NGL object and must also have regard to any relevant MCE statements of policy principles in rulemaking or conducting a review.

3.2.3 Access (Chapter 3 and 5 of NGL)

Consistent with the Statement of Approach released by SCO in September 2005, the architecture of the current Gas Pipelines Access Law (GPAL) and Gas Code will be

included in the NGL. This will bring together the core policy changes to the current regime which have been agreed by the MCE in the context of its response to the Productivity Commission Review of the Gas Access Regime and the further advice of the Expert Panel. In understanding this framework it is important to realise that pipelines in Australia will be essentially in one of the five categories below for which the NGL has a range of differing applications:

1) *Uncovered pipelines* – These are pipelines that do not meet the coverage criteria or for which no one has applied to subject them to the regime.
2) *Pipelines with a binding no-coverage ruling* – These pipelines would have applied for an upfront ruling on coverage before commissioning and have been granted a 15 year exemption from the access regime.
3) *Pipelines with a price regulation exemption* – These are international transmission pipelines which have satisfied a public benefit test for being excluded from price regulation for 15 years after commissioning.
4) *Monitored Pipelines* – These pipelines are covered pipelines that do not need to submit an upfront access arrangement (see discussion below).
5) *Access Arrangement pipelines* – These are pipelines for which there is an approved access arrangement which sets reference tariffs that an arbitrator must apply in the event of an arbitration. All the obligations of the NGL and NGR apply to these pipelines other than obligations specifically directed towards monitored or price regulation exemption pipelines.

Classification and Coverage of Pipelines

The full classification and coverage process will be streamlined and included in the NGL consistent with the Statement of Approach and recommendations of the Expert Panel. This will bring together the concepts and process in the GPAL and Chapter 1 of the Gas Code. The Statement of Approach explained that the present provisions of the GPAL and the Gas Code, which provide for coverage, are needlessly complex in that they provide first in the GPAL for the classification of pipelines as transmission or distribution and then separately under the Gas Code for coverage. These decisions are made by Ministers acting - in some instances in the case of classification, and in all instances in the case of coverage - on the recommendation of the National Competition Council (NCC).

Under the NGL, classification and coverage will be dealt with as a one stage process – and not as a two stage process as at present. In this process the NCC will make draft and final recommendations on coverage at the same time as making draft and final decisions on the classification of the pipeline. That final classification decision will therefore determine who is to be the relevant Minister for making the decision on whether the pipeline should be covered or uncovered under the regime.

The existing coverage criteria in 1.9 of the Gas Code will be adopted for the NGL and supplemented with the new requirement for ‘a material increase in competition’ in the first criterion. This is consistent with recommendations by the Productivity Commission in its Review of the Gas Access Regime and current amendments to the Commonwealth *Trade Practices Act 1974*.

The AEMC will also be required to maintain a publicly accessible register of all covered pipelines, coverage determinations, determinations on whether a pipeline will be a monitored pipeline and classification decisions.

The existing Gas Code contains arrangements for competitive tendering arrangements, with prior approval and subsequent verification by the regulator, to determine the reference tariffs to which a newly constructed pipeline will be subject. These are found in 3.28f of the Gas Code. Consistent with the Statement of Approach, these provisions will be simplified and modelled on proposed amendments to the National Access Regime.

Overriding duties for the provision of pipeline services by covered pipelines
The GPAL and Gas Code contain a number of fundamental obligations on the service providers of covered pipelines which are central to the access regime. They are obligations with which all service providers of covered pipelines need to comply.

It is essential that a covered pipeline be a specified legal entity, which, other than for the Crown, needs to be a corporation. This is consistent with 4.1(a) of the Gas Code. The general public accountability and legal framework for corporations is a core safeguard for the protection of user interests for any piece of infrastructure that passes the test for coverage.

The provision currently in s. 13 of the GPAL prohibiting the preventing or hindering of access to a covered pipeline will be included in the NGL in its current form. Similarly, the provision currently in s. 40 of the GPAL concerning certain rights to be offered terms and conditions for the supply or haulage to the exit flange of the pipeline will be included in the NGL.

The obligation for a service provider to comply with an applicable queuing policy in the access arrangement (3.15 of the Gas Code) will be included in the NGL.

The NGL will capture the core transparency principles from Chapter 5 of the Gas Code relating to:
- making available access arrangements and access arrangement information
- requests for access; and
- the obligation to maintain registers of spare capacity.

Structural and Operational Separation requirements (Ring-fencing)
Structural and operational separation requirements, otherwise known as ring-fencing, are an important part of the gas access regime to promote competition in upstream and downstream markets and limit the ability of a service provider to unfairly favour its associates. The obligations help to ensure all service providers provide pipeline services to all users or prospective users:
- as if the pipeline services being provided by the service provider are being provided by an entity different from, and unrelated to, the service provider;
- in a manner that does not discriminate in favour of a user or prospective user as against any other user or prospective user unless that discrimination is warranted on economic grounds, or otherwise allowed by the NGL or NGR; and
- with transparency in the financial, economic, and operational performance of the service provider.

The central ring-fencing requirements from Chapter 4 of the Gas Code will be replicated in the NGL. The core requirements from Chapter 4 of the Gas Code in the NGL are as follows:

- prohibition on carrying on a related business (4.1(b) of the Gas Code);
- disclosure of confidential information (4.1(f) and (g) of the Gas Code); and
- restrictions on the activities of marketing staff (4.1(h) and (i) of the Gas Code).

The existing ability for the regulator to waive or impose additional ring-fencing obligations will be replicated in the NGL but the procedural requirements for the AER will be in the NGR.

The essential elements of the associate contract approvals will be in the NGL and framed consistently with the PC Response.

Monitoring of covered pipelines

The Productivity Commission recommended that a light-handed form of regulation be introduced into the gas access regime which does not involve upfront setting of reference tariffs through the access arrangement approval process. The MCE largely accepted the thrust of the Productivity Commission's proposals and adapted them to be consistent with the new governance framework in its response to the review. It should be noted that both the Productivity Commission and the MCE have recognised that binding arbitration, as a core requirement for certified effective access regimes, needs to be applied to pipelines under this form of regulation. This essentially makes this form of regulation a "negotiate-arbitrate" framework, as understood by the Expert Panel. The NGL will set out the core elements of the monitoring regime that will be supplemented with future detail in the NGR.

Net Benefit Test

Under the NGL, for a covered pipeline to come under the light-handed form of regulation, it must satisfy a net benefit test administered by the AEMC. This test essentially is an assessment of the relative costs and benefits of regulating the pipeline under the requirements of the light-handed regime compared to the access arrangement framework. This requires a future 'with or without' analysis consistent with similar tests in the *Trade Practices Act 1974*. It has been made clear that the costs and benefits include both public and private benefits. The high level assessment will also need to have regard to the 'form of regulation' factors identified by both the Productivity Commission and the Expert Panel.

Who can ask for the test to be applied?

It will be up to the service provider to nominate to be a monitored pipeline under the net benefit test to be administered by the AEMC. Because of the requirement for binding arbitration, some service providers may prefer the certainty of fixed reference tariffs, which the arbitrator is obliged to apply. Consequently, service providers might not wish to apply for this form of regulation. Either during the process of becoming covered, or at any time where a covered pipeline already has an approved access arrangement, the service provider may request a decision as to whether it meets the net benefit test. At any time the service provider may choose to return to the access arrangement framework and so can have this form of regulation revoked at any time. A user will not be able to apply to move a pipeline with an access arrangement to the light-handed form of regulation.

For monitored pipelines subject to the light handed form of regulation, any person, including the AER, can request the AEMC to reapply the net benefit test to determine if an access arrangement would be more appropriate for the pipeline. The AEMC will have discretion to reject incomplete, frivolous or vexatious applications. If a monitored pipeline's light-handed regulation is revoked by the AEMC, the service provider will be obliged to submit an access arrangement for approval by the AER in accordance with the NGL and the terms and conditions for monitored pipelines will continue to apply until that access arrangement is approved. The rules will contain additional principles in relation to the streamlining of this approval process, having regard to any previously approved access arrangement.

The AEMC will be obliged to consult on all applications and on a draft decision in relation to an application. The AEMC may hold public hearings to assist in its consideration of the matter. Additionally, the AEMC will be specifically required to consult with the AER in making its decision.

Access Arrangements
The core elements of the access arrangement approval process and fundamental requirements of an access arrangement previously in Chapters 2 and 3 of the Gas Code will be included in the NGL consistent with the Statement of Approach. However, the detailed requirements for components of an access arrangement and all of the detail on how to determine prices (reference tariffs and reference tariff methodologies) will be in the NGR. Consistent with the Expert Panel, the five pricing principles will provide direction to AEMC with regard to what the NGR should achieve in this area (see p 116-117 of the Expert Panel report).

Guiding considerations
The current 2.24 of the Gas Code sets out a number of general requirements for the regulator to consider in deciding whether to approve an access arrangement. In particular, the access arrangement must satisfy the content and principles in chapter 3 and the regulator's assessment should be guided by seven principles. Both the Productivity Commission and Expert Panel recommended that all but two of the principles be deleted in light of the inclusion of an overarching objects clause for the regime. MCE now considers that the remaining two factors are covered by the objective clause and the prohibition on depriving anyone of protected contractual rights other than exclusivity rights (s. 2.25 of the Gas Code). Accordingly, none of the paragraphs in s. 2.24 will be replicated in the NGL, but the prohibition in s. 2.25 will be enshrined in the NGL.

The high-level requirements of Chapter 3 of the Gas Code will be captured in the NGL by setting out the minimum content of an access arrangement. The NGL will explicitly allow the Rules to provide further detail for the AER to test the access arrangement submitted by the service provider. The existing Rule that reference tariffs should be submitted for at least one service, and all other services likely to be sought by a significant part of the market, will be preserved in the NGL. The NGR or application of the form of regulation factors by the AER may also result in other services requiring reference tariffs.

With regard to pipelines that have been built under an approved competitive tender process, the AER will not be able to make an access arrangement decision inconsistent with the originally approved terms and conditions. This will essentially capture the effect of 3.21f of the Gas Code taking into account the streamlined competitive tender approval process adopted from the amendments to the *Trade Practices Act 1974.*

What pipelines the access arrangement should cover
The existing rights of the regulator and service provider in submitting consolidated or separate access arrangements in s. 2.4 and s. 2.4A of the Gas Code will be preserved in the NGL. The existing right for any pipeline to voluntarily submit an access arrangement with reference tariffs will remain (s. 2.3 of Gas Code).

Monitored pipelines
Pipelines subject to the light-handed monitoring regime will not be required to submit an access arrangement for approval. These pipelines will, however, be required to make public non-price terms and conditions of access in what would otherwise be an access arrangement. If a monitored pipeline wants certainty that non-price terms and conditions would be applied by an arbitrator in an access dispute, the pipeline could apply for its non-price terms and conditions to be approved by the AER under the existing access arrangement approval process.

Approval Process
The approval process for access arrangements will be modelled on the existing process in Chapter 2 of the Gas Code taking into account the views of the Productivity Commission and the Expert Panel and the new governance framework for the energy market. Consistent with the Statement of Approach, the central elements of the process will be included in the NGL to set a clear framework for consultation, natural justice and timely decision making. A number of changes to the existing process will be implemented to put in place the appropriate incentives for the regulator, stakeholders and the service provider to make a timely decision. The key elements of this are as follows:

- the AER will be required to publish the access arrangement proposals for 21 days consultation;
- the AER will be required to make a draft decision consistent with the current 2.13 of the Gas Code and then set a period for revisions;
- an ability for the AER to hold pre-determination conferences similar to s. 107 of the NEL;
- the AER must publish its final decision and there will be no ‘further final decision’ as recommended by both the Productivity Commission and Expert Panel;
- where information has not been provided to the AER, the AER will be able to proceed on the information before it and make assumptions in relation to the information that was not provided or not provided in an appropriate form;
- the AER will be required to make its final decision within 6 months of receiving the access arrangement proposal but that period will not include time when:
    - judicial review proceedings are on foot;
    - a notice period is running, e.g. for consultation, submissions or information.

- there will also be the ability for a single 2 month extension where the decision is 'of sufficient complexity or difficulty or there is a material change in circumstances such that it is in the public interest' that the timeframe be extended.

Consistent with the current Gas Code, where a service provider fails to submit an access arrangement or the AER does not approve the access arrangement, the AER is to make an access arrangement for the service provider consistent with the provisions of the NGL and NGR.

Confidentiality
Confidentiality of information will be appropriately protected due to the operation of s. 44AAF of the *Trade Practices Act 1974.* Nonetheless, the current limited arrangements for disclosure of information based on s. 42 of the GPAL will be retained. This is consistent with 6.2.6 of the National Electricity Rules.

Access Disputes
The central elements of the access dispute process in Part 4 of the GPAL and Chapter 6 of the Gas Code will be placed in the NGL given the central role of arbitration in the gas access regime and the need to capture the differing application of the arbitration framework to the different types of pipelines subject to arbitration.

If a user or prospective user is unable to agree with a service provider about one or more aspects of access to a pipeline service provided by means of a relevant covered pipeline, the user, prospective user or service provider may notify the AER, in writing, that an access dispute exists. This does not stop users and service providers from using other dispute resolution mechanisms outside of the NGL to resolve disputes about access, but is essentially a formal fall back mechanism to give users a legally enforceable right to access.

The AER will be the arbitrator of all access disputes under the NGL and will be constrained by the current procedural limitations in the GPAL and Gas Code.

Guiding principles
Similarly to how the NGL deals with 2.24 of the Gas Code, the Productivity Commission and Expert Panel's recommendations to delete the paragraphs of 6.15 of the Gas Code will be accepted and reflected in the NGL.

Subject to rules about capital contributions and consistent with 6.18 of the Gas Code, the AER cannot make an access dispute decision:
- inconsistent with an applicable access arrangement or queuing policy;
- that deprives a service provider of protected contractual rights; or
- that does not apply an applicable reference tariff.

There will remain the discretion not to make an arbitration decision where the AER considers that there is substantial competition in the market for the provision of the service in question (6.17 of the Gas Code). Where there is no reference tariff set for a service sought by a user (because it did not require a reference tariff or the pipeline was a monitored pipeline), the AER is to take into account the pricing principles in setting a price for access.

3.2.4 Greenfields Pipeline Incentives (Chapter 4 of the NGL)

The MCE has decided that the creation of an appropriate climate for maximising the potential for investment in greenfields pipeline projects is an essential objective of the current energy sector reforms.

Consistent with this object of the NGL, the MCE has agreed to adopt Recommendation 9.1 of the Productivity Commission's "Review of the Gas Access Regime", which allows for a binding no-coverage recommendation from the NCC to the relevant Minister for a period of 15 years if a new pipeline does not meet the pipeline coverage criteria. Further, as an additional option, the MCE has also agreed to a price regulation exemption for 15 years for international transmission pipelines which source gas from outside Australia.

Accordingly, the MCE implemented the two measures in the existing gas access regime in June 2006 and will retain the provisions in the NGL with the necessary drafting amendments to incorporate the terms and structure of the NGL. Additionally, the NGL provisions will consolidate the classification and binding no-coverage procedure to avoid dual processes and will clarify the obligation on pipelines granted a price regulation exemption to publish indicative prices for what would otherwise be reference services consistent with the PC Response (p. 16).

3.2.5 Proceedings under the NGL (Chapter 6 of NGL)

The enforcement model established in Part 6 of the NEL has been adopted in the new NGL. Therefore, the new NGL has, in large part, been developed from the equivalent provisions in the NEL.

In particular, the AER will be empowered to enforce the new NGL, regulations and NGR by application to a Court for an order declaring that a person is in breach of the NGL, regulations or NGR. If the Court makes such a declaration, the Court may also order the person to pay a civil penalty (for civil penalty provisions), to desist from the breach, to remedy the breach or to implement a compliance program. The AER may also apply to the Court for an injunction where a person has engaged in, is engaging in or is proposing to engage in conduct in breach of the new NGL, regulations or NGR. Because the simpler NEL enforcement framework has been adopted, there is no longer any need for the concept of a 'regulatory provision'.

In addition to the enforcement mechanisms in the NEL, Part 5 of the GPAL has the concept of a 'conduct provision'. Any person can take action in a court to enforce compliance with a provision of the access regime that is listed as a conduct provision (see 10.7 of the Gas Code). Under the NGL the concept of a conduct provision will be retained and these will be able to be prescribed by regulation. The significance of a provision being a conduct provision is that in addition to the remedies mentioned above, a person who suffers loss or damage as a result of a breach of a conduct provision can obtain an award of damages. (See s. 36 of the GPAL.)

Also, the AER will be able to issue an infringement notice for breach of any civil penalty provision. A person who receives a notice may either pay the infringement penalty or defend any formal proceedings in respect of the breach. The amount of an

infringement penalty will be $20,000, or a lower amount prescribed for the particular civil penalty provision.

Criminal offences in the GPAL and Gas Code will generally be carried over into the new NGL and NGR. The prosecution of these offences will be within the general prosecution regimes of the Commonwealth, States and Territories. The AER will also be able initiate criminal prosecutions which can be taken over by the relevant Director of Public Prosecutions under the usual State or Territory arrangements.

Review rights, including merits review
The new NGL has been drafted in accordance with the MCE's position on review rights. Provision is therefore made for judicial review of decisions and associated conduct of the AEMC under the new NGL and NGR. Any "person aggrieved" by a particular decision may apply for judicial review of that decision. Decisions of the AER, Commonwealth Minister and NCC are subject to judicial review under the *Administrative Decisions (Judicial Review) Act 1977* (Cth), and decisions of relevant State Ministers are subject to judicial review in accordance with relevant State administrative law regimes.

A limited form of merits review will be available for specified economic regulatory decisions. Merits review proceedings may be brought before the Australian Competition Tribunal (ACT) in respect of the following decisions:

- Ministerial decisions in relation to coverage of gas pipelines (including binding no-coverage determinations but not price regulation exemptions);
- decisions by the AEMC on the form of regulation for individual covered pipelines (price regulation by access arrangement or the light handed monitoring regime);
- AER decisions to draft and approve (or revise) gas access arrangements; and
- AER ring fencing decisions including non-approval or voiding of associate contracts.

These decisions have been identified by the MCE as being suitable for a form of merits review on the basis that (i) they may have a substantial impact on the economic viability of network and service providers and (ii) the decision-making power may involve the exercise of significant amounts of discretion.

The merits review will be on limited grounds, with restrictions placed on the evidence which may be brought to establish any ground of review. The grounds for review will be as follows:

- that the decision-maker made an error of fact and that fact was material to the decision;
- 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.

These grounds will provide a limited merits review that enables correction of errors. An applicant for merits review will need to seek leave from the ACT to bring an action for review and, amongst other things, will need to meet a materiality threshold. The ACT must be satisfied that there is a serious question to be tried. In addition, for revenue-related errors, the amount at issue must exceed $5m or 2% of average annual

regulated revenue, or if quantification is not readily possible, the amount in issue must be material in terms of an entity's regulated revenue. In all other case (ie non-revenue errors) the ACT will have to be satisfied that the error is a material one.

Persons able to commence a merits review action will be network and service providers, users who are materially affected by a decision, and user and consumer groups. However, in the case of coverage decisions, any person adversely affected by the decision will be able to commence a review. There will be a relatively wide scope for persons and groups to intervene in merits review proceedings, once commenced. Persons with a sufficient interest in the original decision are able to intervene, as well as jurisdictions, and user and consumer groups with leave of the ACT.

The ACT will have wide powers. It will be able to affirm or vary the original decision, or set the decision aside and either substitute a new decision or remit the matter to the AER, AEMC or Minister for reconsideration.

3.2.6 The Making of the National Gas Rules (Chapter 7 of the NGL)

This Chapter of the new NGL will be modelled on the NEL. The process for making and changing the NGR will be the same as for making and changing the NER. The AEMC's functions and powers will also be the same. And the NGR, like the NER, will have the force of law.

The power of the AEMC to make rules is expressed generally in Chapter 2 of the new NGL and in Schedule 1, which lists specific matters about which the AEMC may make rules.

In making a decision on a rule change proposal, the AEMC may only amend the NGR if it is satisfied that the amendment will, or is likely to, contribute to the achievement of the objectives of the NGL. The AEMC may give the various aspects of the objectives of the NGL such weight as is appropriate in all the circumstances having regard to any relevant MCE statement of policy principles. If the AEMC is satisfied that a rule will, or is likely to, contribute to the achievement of the objectives of the NGL, the AEMC must make the rule. The AEMC will also be directed by the pricing principles and form of regulation factors when making or amending relevant rules.

The rule change process
In most cases, the AEMC will not be able to initiate a rule change proposal. However, the AEMC will be able to initiate a rule change where the change is to correct a minor error or involves a non-material change to the NGR.

Any person, including the MCE, may apply for a rule change. The AEMC will be able to reject an application:

- where the application does not contain the information prescribed by the regulations; or
- where the application is misconceived or lacking in substance;
- where the AEMC would, if it were to make the proposed new rule, be acting beyond its powers under the NGL.

A further feature of the AEMC's gatekeeper role is that, while a person lodging a rule change proposal may include a suggested rule wording, the AEMC, as the body responsible for the integrity of the NGR as law in the participating jurisdictions, will determine the draft rule wording for consideration in the rule change process.

If the AEMC has accepted a rule change proposal, it will be required to undertake public consultation on the proposal. It will be able to convene working groups and will decide whether or not to hold public hearings. The AEMC will be required to invite submissions on the proposal and subsequently on its draft determination and draft rule change. These steps provide a number of opportunities for interested parties to contribute to the rule making process.

The AEMC will be able to expedite a rule change proposal if it considers the change to the NGR to be:

- non-controversial (that is, the proposed new rule is unlikely to have a significant effect on a market for gas); or
- urgent (that is, the proposed new rule relates to any matter or thing that, if the rule is not made urgently, will result in that matter or thing imminently prejudicing or threatening the supply of gas).

The capacity to expedite a rule change process is a key component in achieving a more streamlined rule making regime. But the AEMC may be required to undertake public consultation in accordance with the usual rule change process if a legitimate objection is made to the rule change proposal being expedited.

The AEMC will publish its final determination on a rule change proposal. It will also publish a notice of a change to the NGR in the South Australian Gazette. Any new Rule will be published on the AEMC's website and copies made available at its office.

3.2.7 Schedules to the NGL

Schedule 1 – Subject matter for the National Gas Rules
This Schedule to the new NGL lists specific matters about which the AEMC may make rules.

Schedule 2 – Miscellaneous provisions relating to interpretation
This Schedule to the new NGL sets out interpretation provisions for the purposes of the new NGL and NGR which will take the place of local (state or territory) interpretation laws. It is modelled on Schedule 2 to the NEL.

Schedule 3 – Savings and transitionals
To ensure a smooth, efficient and equitable transition to the new NGL and NGR, savings and transitional provisions will be included in the new NGL and in regulations to be made under the lead South Australian legislation. Broadly, the savings and transitional provisions are likely to include:

- continuation of current investigations into, or current proceedings in relation to, possible breaches of the GPAL or Gas Code;
- continuation of current processes for determinations by regulators;

- continuation of current merits appeal processes, including those currently being undertaken by state review bodies;
- provision for construction of references in documents to the Gas Code;
- preservation of documents issued or published under the Gas Code; and
- general saving of rights and liabilities accrued under the GPAL and Gas Code, including that the repeal of the GPAL is not to be regarded as a change of law (however defined) under any agreement or deed, and generally ensuring that things done under or for the GPAL and Gas Code are taken to continue for the new NGL and NGR.

3.3 National Gas Rules (NGR)

Similar to the National Electricity Law regime, there will be statutory rules sitting underneath the NGL. These will be called the National Gas Rules (NGR). The new NGR will, to some extent, take the place of the current Gas Code.

The Gas Code was previously a law of Parliament as a schedule to the *Gas Pipelines Access (South Australia) Act 1997* but, unlike most other legislation, could be amended by an executive process of Ministerial agreement. For the new governance arrangements to take effect, a new split between NGL and NGR has been necessary.

To the extent that an obligation is not in the NGL, the rules will largely be based on the current Gas Code but will be made consistent with the new governance and institutional arrangement. Additionally, important policy changes resulting from the MCE Response to the Productivity Commission Review of the Gas Access Regime (MCE PC Response) and the Expert Panel will be incorporated.

The initial NGR are currently being developed and will be released for consultation prior to the introduction of the NGL into the South Australian Parliament. They will be formally made by the South Australian Minister when all the new Commonwealth, State and Territory application Acts for the gas access regime are brought into force. They will then be subject to the AEMC rule change process as explained above at 3.2.6.

3.3.1 Format

The format of the NGR is still being developed. The content of the NGR is discussed below consistent with the current Chapters of the Gas Code.

Coverage and Classification (Gas Code Chapter 1)	There will be no rules on coverage and classification as the NGL will deal with all aspects of these processes.
Access Arrangement (Gas Code Chapter 2 and 3) Access Arrangement Approval Process	The process for approving access arrangements is largely in the NGL. Additional elements of the process and further detail will be dealt with in the NGR.
Content of an Access Arrangement	The highest level of content requirements for an access arrangement is in the NGL, but much of the detail in current Chapter 3 of the Gas Code will remain in the NGR to give further guidance

	on what is required and how the regulator is to assess a submitted proposal.
Ring-fencing (Gas Code Chapter 4)	The NGL sets out the fundamental ring-fencing requirements of the Gas Code. The ability for additional ring-fencing requirements and waiver of ring-fencing obligations is specified in the NGL but the detail of the process will be in the NGR consistent with the current processes in Chapter 4 of the Gas Code.
Information and Timelines for Negotiation (Gas Code Chapter 5)	The general obligations relating to user requests and registers of capacity are in the NGL. The NGR will set out further detail consistent with the current chapter 5.
Dispute Resolution (Gas Code Chapter 6)	Much of the dispute resolution process is in the NGL. The NGR will add some further detail to these matters consistent with Chapter 6 of the Gas Code.
General Regulatory Provisions (Gas Code Chapter 7) *Associate Contract Approvals* *Other aspects of Chapter 7*	The additional detail relating to the associate contract provisions will be in the NGR consistent with the MCE PC Response. Many aspects of Chapter 7 have been included in the NGL. The remainder will be in the NGR.
Reference Tariff Principles (Gas Code Chapter 8)	This chapter will be in the NGR and will take into account the Expert Panel's recommendations.
Code Change (Gas Code Chapter 9)	This will be part of the new NGL.
Interpretation (Gas Code Chapter 10)	The relevant interpretation provisions will be placed in the NGR consistent with the definitions in the NGL. The provision of conduct provisions will be in the regulations.
Access Arrangement Information (Gas Code Attachment A)	This will be appropriately replicated in NGR.
Covered Pipelines at commencement (Gas Code Schedule 1)	This will be dealt with in savings and transitional provisions.

3.4 National Electricity Law (NEL)

Like the gas regime, the electricity regime is a co-operative Commonwealth, State and Territory legislative scheme. The Commonwealth and all States and Territories, except Western Australian and the Northern Territory, participate in the electricity regime. The scheme works through lead legislation in South Australia: the *National Electricity (South Australia) Act 1996*. This lead legislation is then applied as law in the participating States and Territories through application Acts, which pick up the Schedule to the South Australian Act and apply it in their jurisdiction. The Commonwealth applies the electricity regime in offshore areas through the *Australian Energy Market Act 2004*.

There will be amendments to the NEL in the 2006 legislative package to transfer economic regulation of electricity distribution to the AER, to implement particular recommendations of the Expert Panel on Energy Access Pricing, to allow for merits review of certain regulatory decisions, and to make some minor and/or technical

amendments to the NEL. These amendments are less substantial than the new gas framework that implements additional policy changes from the PC Response.

3.4.1 Transfer of economic regulation of distribution

The NEL currently regulates aspects of electricity transmission. Electricity distribution is currently regulated by the NER and administered by jurisdictional regulators. However, most jurisdictions have derogated from the NER and applied various State and Territory jurisdictional regimes administered by the respective jurisdictional regulator. Functions will be conferred on the AER under the NEL and NER relating to the economic regulation of services provided by regulated distribution network service providers by means of, or in connection with, a distribution system, including in relation to the making of distribution determinations.

3.4.2 Expert Panel on Energy Access Pricing

The broad structure and framework of the NEL, as amended in 2005, was endorsed by the Expert Panel report. Accordingly, although significant, the changes arising from the Expert Panel report are not intended to disrupt the essential operation of the NEL and its overarching structure.

Amendments to the NEL will implement those recommendations of the Expert Panel that the MCE has adopted. In particular, s. 16(2) of the NEL will be remodelled so that the AER must take into account the pricing principles recommended by the Expert Panel when exercising discretion relating to a price/revenue determination and when making a binding arbitration decision.

The AEMC will be explicitly directed by the NEL pricing principles and form of regulation factors in making the relevant rules for both transmission and distribution revenue and network pricing. AEMC rules on the procedures for making revenue/price determinations will also need to be consistent with the minimum content recommended by the Expert Panel.

Consistent with the MCE decision on 19 May 2006, the NEL will not mandate a 'propose-respond' decision-making framework in the NEL. Instead, a 'fit-for-purpose' model will be adopted, acknowledging that in any gas access proposal or electricity network service provider offering, there is such a range of dimensions that the capacity to require the regulator to apply either the ‘propose-respond’ or ‘receive-determine’ method, or a more specific test to different elements of a proposal, should be maintained. Accordingly, the NEL will not direct the AEMC as to the decision making standard for AER decisions but will ensure the service provider has an opportunity to make a proposal on pricing and revenue issues at the start of the process.

Similar to the NGL, the framework for information disclosure and regulatory reporting to the AER will be in the NEL, consistent with the concerns expressed by the Expert Panel.

A 'negotiate/arbitrate' framework after the application of the form of regulation factors will be accommodated in the NEL. In particular, the framework for the AER to

arbitrate access disputes with binding decisions (but not wholesale market disputes that remain subject to Chapter 8 of the NER), with procedures similar to the GPAL, will be implemented. It will still be necessary for the Rules to determine whether the access arbitration process would be triggered or the existing Chapter 8 dispute processes utilised.

3.4.3 Review rights, including merits review

The NEL currently provides for judicial review of decisions and associated conduct of the AEMC and the National Electricity Market Management Company (NEMMCO). Any "person aggrieved" by a decision by either of these bodies may apply to a Court for judicial review of that decision. There is no merits review of decisions of these bodies made under the NEL and NER.

Decisions of the AER are subject to judicial review under the *Administrative Decisions (Judicial Review) Act 1977* and merits review is not currently available for AER decisions under the NEL and NER. As publicly indicated, the MCE has reconsidered the issue of merits review for electricity. In accordance with the MCE's position on review rights, there will now be a limited form of merits review available for specified economic regulatory decisions in electricity. Merits review proceedings may be brought before the Australian Competition Tribunal in respect of the following decisions:

- AER pricing and revenue determinations for transmission and distribution (including application of the regulatory test); and
- AER decisions not to exempt entities from ring fencing guidelines or impose additional ring fencing requirements.

These decisions have been identified by the MCE as being suitable for a form of merits review on the basis that (i) they may have a substantial impact on the economic viability of network service providers and (ii) the decision-making power may involve the exercise of significant amounts of discretion.

Other than the particular regulatory decisions that will be reviewable on the 'merits', the limited merits review scheme to be implemented will be the same in both electricity and gas. The NEL will be amended to provide for the merits review scheme announced by the MCE.

3.5 National Electricity Rules (NER)

The MCE is currently developing new Rules to replace Part D and Part E of Chapter 6 of the existing NER to empower the AER to regulate distribution consistent with the MCE position on the recommendation of the Expert Panel. The NEL will enable the MCE, through the South Australian Minister, to amend the current NER to achieve a national framework for the economic regulation of distribution. The MCE intends to conduct extensive consultation on these Rules to ensure it achieves an appropriately consistent framework for decision-making across transmission and distribution, in light of the independent AEMC review of transmission revenue and pricing rules, as required by the NEL and expected to be in place by 1 January 2007.

New distribution revenue/pricing rules

The principal change will be the replacement of the distribution pricing Rules in Part D and Part E of Chapter 6 of the NER and the derogated jurisdictional arrangements, with nationally-consistent distribution revenue and pricing Rules that take into account the advice of the Expert Panel. The policy, to be reflected in the new Rules, is being developed to:

- Implement the advice of the Expert Panel, and in particular the revised pricing principles and framework for decisions on the form of regulation;
- Take into account the work and drafting style of the AEMC in revising transmission revenue and pricing rules;
- Recognise fundamental differences between distribution and transmission networks; and
- Build from the existing distribution arrangements in each State and Territory to ensure unnecessary disruption and uncertainty is not created by the changes to a national regulatory framework required by the AEMA.

Given the diversity of current approaches to the economic regulation of distribution by jurisdictional regulators, the advice of the Expert Panel and the broad range of policy considerations being considered during the Rule development process, the MCE's Rules will be less prescriptive than the AEMC's draft transmission revenue Rule proposal published in February 2006. For example, the parameters for the weighted average cost of capital will not be prescribed, and the MCE will not develop specific lists of network services that fall under control or negotiate/ arbitrate models of regulation in the initial Rules (note that this does not preclude additional prescription being added to the Rules through the Rule-change process). Also, the initial distribution Rules will enable the AER to accommodate certain regulatory needs that are specific to the individual requirements of jurisdictions.

The distribution Rules will also be designed to accommodate the Expert Panel's 'fit-for-purpose' decision-making model. In particular, concerns by the Expert Panel about legally requiring regulators to accept 'reasonable estimates' of various aspects of the building block approach and the need to ensure appropriate procedural fairness protections for service providers will be accommodated in the drafting of the new Rule. A full explanation of the changes will be available when an exposure draft has been prepared for consultation.

Other distribution transfer changes
The Rules will also appropriately reallocate the small number of functions of jurisdictional regulators under other Chapters of the NER to the AER.

3.6 Consumer Advocacy

In November 2005 the MCE decided to strengthen the consumer advocacy arrangements in the gas and electricity regimes and are now implementing that decision principally through amendments to the *Australian Energy Market Commission Establishment Act 2004*.

The MCE agreed to the development of legislative amendments to establish a long-term consumer advocacy model so that:

- The same body can allocate grants to facilitate consumer advocacy and research for both electricity and gas, with a particular focus on small to medium consumers; and
- The funding body is accountable to the MCE and the AEMC.

The legislative basis for the long-term consumer advocacy model will be included in the 2006 legislative package.

The Consumer Advocacy Panel (the Panel) is to be established by a Consumer Advocacy Panel Bill as a 'constituent', but independent, part of the AEMC. This will clearly recognise the Panel's role in energy rather than just gas or electricity. To ensure that the independence of the Panel is not compromised, it will be clearly stated that the Panel's allocation of grants or commissioning of research is not subject to the direction or control of the AEMC or MCE.

The Panel will have the following functions:

a) to allocate grants for consumer advocacy projects and research projects for the benefit of energy consumers; and
b) to identify areas of research that would be of benefit to energy consumers and if required request tenders from other bodies to undertake that research; and
c) to develop guidelines for the allocation of grants for consumer advocacy projects and research projects for the benefit of energy consumers; and
d) to publish the results of research it has commissioned; and
e) to prepare an annual budget; and
f) to exercise any other functions conferred on the Panel by the National Energy Laws or the Jurisdictional Energy Laws.

In performing its functions, the Panel:

- must have regard to any relevant objectives set out in National Energy Laws; and
- must pay primary regard to benefiting small to medium consumers of electricity or natural gas.

The Panel is to comprise a Chair and four ordinary members, to be appointed by the SA Energy Minister on the recommendation of the MCE on terms and conditions specified in the instrument of appointment. Panel members may be appointed for up to four years. The Panel will be assisted by an Executive Director and a small secretariat to provide an administrative and research capability. The Executive Director will be jointly appointed by the AEMC and the Panel.

Although the Panel will be independent from the MCE and the AEMC with respect to individual grant and research decisions, it will be accountable to the MCE and the AEMC in the overall exercise of its functions.

The Panel will prepare, in consultation with interested stakeholders, an annual budget including proposed grants for both gas and electricity. The budget requirements will be submitted by the Panel to the MCE for consideration. Although the MCE could consult with the AEMC on the Panel's budget requirements, an MCE decision on the Panel's budget provides an appropriate level of independence from the AEMC. All NEM -related grants will be funded through NEMMCO participant fees.

A long-term funding mechanism will need to be determined for gas-related grants. It is intended that the MCE will investigate such a mechanism by July 2007.

The Panel will be responsible for directing the AEMC to make grant allocations on criteria to be set out in regulations to be made under the Consumer Advocacy Panel Bill. The Panel will also be required to develop guidelines to apply those criteria in a way which is transparent and will facilitate timely decision-making. These guidelines will be developed in consultation with the AEMC and stakeholders. If no guidelines are approved, the Panel must still apply the criteria as specified in the regulations in assessing grant applications.

It is intended that the proposed initial criteria will be consistent with the criteria currently in the National Electricity Rules, with the additional focus on small to medium end users.

4. 2007 Legislative Package

4.1 National Distribution and Retail Framework Implementation
The MCE is also currently working on developing a legislative package for 2007 to transfer the regulation of distribution (non-economic) and retail (non-price) functions to the AER and AEMC not covered by the 2006 legislative package.

The MCE has agreed to a work program to develop recommendations on the national distribution (non-economic) and retail functions. The work program provides for the recommendations to be developed by an MCE SCO Retail Policy Working Group (RPWG) in consultation with stakeholders and with the assistance of expert legal advice.

The RPWG has been instructed to prepare recommendations, including any proposals for further work, for the MCE in early 2007. A consolidated paper of recommendations will be released for general public consultation, prior to deciding on a final set of recommendations for decision by the MCE, and preparation of national legislation enabling the national framework to commence operations on 1 January 2008.

The RPWG will convene a stakeholder reference group of industry, users and regulators to comment on the recommendations for the national framework as they are developed. The reference group will be drawn initially from nominations from peak industry, user and consumer associations and representatives of existing federal, State, and Territory energy regulators.

The use of a stakeholder reference group and the public consultation on recommendations will ensure the experience and views of industry, users, consumers and regulatory administrators are considered in developing the recommendations to be put to the MCE.

The principal areas of work for the RPWG will be those matters listed under *Consumer Protection* and *Other Distribution and Non-Price Retail Regulation* in the MCE's May 2005 consultation paper prepared by NERA/Gilbert + Tobin ("Public

Consultation on a National Framework for Energy Distribution and Retail Regulation").

The principal areas of work for the RPWG as listed in the NERA/Gilbert + Tobin Consultation Paper are:

Consumer Protection

- Distributor obligation to provide connection services;
- Distributor disconnections and reconnections of small-end customers;
- Distributor small-end customer dispute resolution;
- Retailer obligation to supply to small end customer;
- Retailer small-end customer market contracts;
- Retail small-end customer marketing;
- National obligation for retailer small-end customer dispute resolution.

Other Distribution and Non-Price Retail Regulation

- Business authorisation;
- Distributor interface with retailers
- Distributor interface with embedded generators;
- Balancing regime and settlements effecting customer transfer;
- Metering;
- Load shedding and curtailment;
- Retailer failure arrangements;
- Ring-fencing arrangements;
- Jurisdiction-specific requirements.

The 2007 legislative package will complete the transfer to the AEMC and AER of the national distribution and retail functions listed at Annexure 2 to the amended AEMA. Annexure 2 sets out the activities which will form part of the national distribution and retail regulatory framework for electricity and gas to be developed by the MCE in accordance with the AEMA. As stated above, items 1-3 of Annexure 2 will be implemented in the 2006 package for electricity and items 1-5 for gas.

Annexure 2 also details certain functions that remain the responsibility of each State or Territory. These State and Territory functions may be transferred to the AEMC and/or the AER (with the agreement of the Commonwealth) so long as they are governed by harmonised Rules for all those parties that have transferred each function.

4.2 Other Reforms

Separation of generation and transmission activities in the NEM

The MCE is also developing legislation to implement COAG decision 2.4 from its February 2006 meeting, relating to the separation of generation and transmission activities in the NEM. These will be implemented through amendments to the NEL,

which will be consulted upon in 2007. A regulatory impact statement concerning the changes will be released for consultation later in 2006.

Gas Market Issues

The SCO is currently considering a report from the Gas Market Leaders Group concerning the development of a national gas market. Accordingly, the MCE is yet to respond to their report but may consider implementing some of the changes in future reforms.

Further Reform from COAG

The MCE notes that COAG has established an Energy Reform Implementation Group to provide additional advice relating to transmission, market structure and financial markets. If further legislative change is requested by COAG, consideration would be given as to whether any of the changes could be included in the 2007 package.