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Review of Limited Merits Review Secretariat  
Energy and Environment Division  
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Dear Professor Yarrow

We write to respond to the Review of Limited Merits Review Regime's (the **Review**) Consultation Paper 2, Additional Statement of Issues and Questions (**ASIQ**). Thank you for the opportunity to meet with the Expert Panel earlier this month.

We are not in a position to respond to every question in the ASIQ. However, we would like to make some comments in relation to:

- the policy objectives of the Ministerial Council on Energy (**MCE**) in establishing the limited merits review regime;
- the broad approach taken by the Expert Panel to the review;
- the structural and behavioural influences on the performance of the regime;
- the significance of the AER's s.71O(1) powers; and
- the role of consumers in the appeals processes.

### Policy objectives

In its decision paper of May 2006, the MCE stated that the criteria relevant for selecting the framework for review of decision-making include:

- maximising accountability;
- maximising regulatory certainty;
- maximising the conditions for the decision-maker to make a correct initial decision;
- achieving the best decisions possible;
- ensuring that all stakeholders' interests are taken into account, including those of service and network providers and consumers;
- minimising the risk of gaming;
- minimising time delays and costs.<sup>1</sup>

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<sup>1</sup> Ministerial Council on Energy, Decision: Review of Decision-Making in the Gas and Electricity Regulatory Frameworks, May 2006, p 3.

The also MCE stated that its selection of a limited merits review regime:

will best facilitate the correction of a range of regulatory errors with significant diverse consequences, encourage the making of the best administrative decisions in all the circumstances, and will encourage investment in gas and electricity and across those sectors by promoting confidence in the regulatory process.<sup>2</sup>

While we support the stated criteria, it is our view that the implementation of the limited merits review regime has not achieved the objectives sought by the MCE. In particular, the regime has not encouraged the making of the best administrative decisions in all the circumstances. In this regard, we note the point made by the Expert Panel that the limited merits review regime has resulted in the Victorian distribution network service providers, which each has similar costs of capital, being allowed materially different costs of capital based upon whether they appealed a decision. This result is clearly perverse and at odds with the policy objectives as articulated by the MCE.

In its decision paper, the MCE also stated that such a regime would 'enable correction of a far greater range of regulatory errors that may have significant adverse consequences on participants, including network and service providers, than judicial review'.<sup>3</sup>

With respect, this quote suggests to us that the selection was made in deference to the consequences on networks and service providers, rather than consumers, potentially in contradiction to the overarching policy objective set out in the NEO and NGO.

To be clear, the overarching policy objective in the NEO and NGO is to promote efficient investment in, and efficient operation and use of, energy services for the long term interests of consumers of energy with respect to price, quality, safety, reliability and security of supply of energy. It is our view that the long term interests of consumers was not effectively prioritised when the MCE made the decision to adopt the limited merits review regime.

### **The Panel's broad approach**

We would like to offer our strong support to the Expert Panel's broad approach to the review. We agree that it is appropriate for the Expert Panel to inquire into the nature and character of decision-making by the Australian Competition Tribunal (**ACT**).

While we do not have the technical knowledge to know whether particular ACT decisions on 'gamma' or estimation of debt premiums are 'more correct' or 'preferable' to the initial decision of the Australian Energy Regulator (**AER**), we would re-iterate the point made in our initial submission that there is real scope to debate what is an error and what is a difference of economic opinion. The Expert Panel's use of the terms 'more correct' and 'preferable' only serve to underline this point.

We note further that the fact that an error was made does not automatically lead to a conclusion that a decision ought be reviewed. Indeed we suggest that it would be extremely surprising that

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<sup>2</sup> As above, p 13.

<sup>3</sup> As above.

no errors were made (separate from taking a different positions on the spectrum of economic opinion) in a two year multi party consultative process involving reams of technical and supporting information. The proper question is whether correction of an error leads a to a materially preferable decision.

As noted in our initial submission, our view is that judicial or administrative review is very well suited to address such complexity as such a mechanism essentially undertakes a review of the process by which the decision was made and the legality of the decision. Judicial review is unable to consider the merits of any one of a number of economic theories or analyses, however it will respond to require a new decision where the decision is so unreasonable no reasonable decision-maker could have made it (having regard to the factors required to be taken into account by the decision maker)

Such a mechanism is appropriate protection from an aberrant regulator but also incentivises full and frank engagement with the initial decision-making process by businesses as the option of a 'second bite at the cherry' is much reduced.

In the event the Expert Panel is not minded to prefer a judicial or administrative review option, then we suggest that it is only by consideration of a decision as a whole that a determination can be made as to whether correction of an error result in a materially preferable decision.

### **Structural and behavioural influences of the performance of the regime**

We do not have specific evidence about the relative contribution of the global financial crisis or the fact that the regime is new to the number and type of matters appealed to the ACT. However, if the question raised by the Expert Panel is whether the number of appeals has been artificially increased because of these issues, we doubt this to be the case.

In support of this doubt we note that:

- there were significant numbers of appeals prior to the introduction of the present limited merits review regime. For example, in Victoria, which also had a limited merits review system, a number of business appealed the decision of the Office of the Regulator-General in relation to the 2001-2005 electricity price determination review,<sup>4</sup> and also the decision of the Essential Services Commission in relation to the 2006-2010 electricity price determination review.<sup>5</sup> It is worth noting that in both instances further judicial review was sought from the Supreme Court of Victoria;
- since the commencement of the limited merits review regime, there have been 22 substantive decisions by the ACT which is as far as we are aware an unprecedented rate of appeals under *any* regime old or new;
- a significant number of the appeals under the present regime occurred prior tot eh global financial crisis.

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<sup>4</sup> Each of AGL Electricity, Powercor Australia, TXU Electricity and United Energy appealed the decision pursuant to section 37 of the *Office of the Regulator-General Act 1994 (Vic)*

<sup>5</sup> Each of United Energy Distribution, SPI Electricity Pty Ltd, Powercor Australia Ltd and Citipower Pty Ltd appealed the decision pursuant to section 55 of the *Essential Services Commission Act 2001 (Vic)*.

## **Cherry-picking and the significance of section 71O**

When we refer to 'cherry picking', we mean the tendency for network businesses to only appeal those alleged errors in the first instance decision that are adverse to them. We agree that the limited merits review regime facilitates this by not providing the opportunity for holistic error correction in the appeals process.

In relation to the Panel's seeking of further views on why the AER's s 71O powers have not been actively used as an 'antidote' to cherry-picking, we re-iterate our comments of our previous submission. In short, we believe it is unrealistic to expect the AER to appeal its own decision.

Moreover, given that successful implementation of an appeals regime should result in good outcomes, we think more focus should be given to the fact that the AER has not used these powers, rather than the question of why not. As such, we believe that the focus of the Expert Panel should be to consider whether the merits review regime *can* facilitate 'holistic error correction'. It is our view that a limited merits review regime cannot facilitate such an outcome, but regardless of whether there is broad agreement on that point, it is quite clear it *has not*. Given the limited ability of consumers to participate in the review processes, it is by no means clear that a *de novo* merits review can also achieve such an outcome.

## **Consumers and users**

We strongly agree that, to the extent that consumer participation in the limited merits review regime was considered to be a factor in its successful implementation, this has not been realised. It is our view that consumer participation was intended by the model chosen, as it provided consumer and user groups clear standing to initiate and intervene in appeals.

We note the Panel's view that the AER has not been expected to act as a consumer 'advocate' or 'champion' in regulatory decisions. While this may be true in the context of appeals, we would argue that the AER is also not merely an arbitrator between network businesses and various consumer interests during the initial decision-making process. For such an arrangement to work, most of the AER's resources and expertise would have to be transferred to a consumer agency with the economic regulator taking the role of a tribunal. This is not an arrangement that is proposed or desired.

Further, given there is a not one single consumer voice, the AER does play some role as a consumers' proxy in the initial decision-making process. This is partly why the AER has a mandate to make decisions according to the Rules, which are guided by the NEO and NGO—that is, the long-term interests of consumers. To be clear, this is not to say that the AER are or should be a consumer advocate. As a regulator, the AER rightly takes its independence very seriously. The role of the regulator, then, is to form a view about what is in the long term interests of consumers, informed by its own inquiries and information provided by industry and consumer groups.

Despite this, it is not clear to us that this role continues to apply in the context of the appeals framework. As noted in our initial submission, in the context of the appeal of the Victorian Distribution Price Determination Review, the AER consented to there being a serious error to be


tried and did not play the role of a 'contradictor', as an advocate for consumers or even an advocate for its own decision.

At least in the context of the limited merits review regime, it is as if the role of the AER changes at the point the appeal is made—from that of a decision-maker charged with making a decision in accordance with the rules and in accordance with the long-term interests of consumers, to a role of facilitating the merits review process by explaining its determination. Our view is that the Expert Panel should take this change in role as given, and seek to consider what an appeals process might look like that promotes the overarching policy objectives of the long-term interests of consumers. As noted in our initial submission, our view is that this is best achieved through an appeals process that only allows judicial review and not merits review.

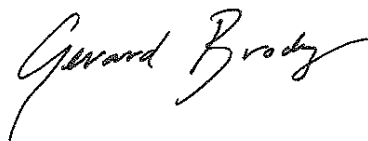
Please contact us on 03 9670 5088 or at [gerard@consumeraction.org.au](mailto:gerard@consumeraction.org.au) should you have further questions.

Yours sincerely

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