13 April 2012

By email: LMR.Secretariat@ret.gov.au

Professor George Yarrow
Chair, Expert Panel
Review of Limited Merits Review Secretariat
Energy and Environment Division
Department of Resources, Energy and Tourism
GPO Box 1564
Canberra ACT 2601

Dear Professor Yarrow

Review of Limited Merits Review

We write to provide some initial views to the Review of Limited Merits Review (the **Review**), commissioned by the Standing Committee on Energy and Resources (**SCER**).

Our initial views are limited to comments in response to the report, *The Merits Review Provisions in the Australian Energy Laws*, authored by Professor Allan Fels for the Energy Networks Association (the **ENA report**). As noted in the terms of reference for the review, Consumer Action together with Consumer Utilities Advocacy Centre published the report, *Barriers to fair network prices: An analysis of consumer participation in the merits review of AER EDPR determinations.* A copy of this report is attached. In accordance with the recommendation of that report, we believe that SCER should repeal the provisions in the national energy laws that enable businesses access to merits review of network pricing determinations. We believe that network service providers that are aggrieved about pricing determinations should only be able to exercise their right of judicial review.

About Consumer Action

Consumer Action is an independent, not-for-profit, campaign-focused casework and policy organisation. Consumer Action provides free legal advice and representation to vulnerable and disadvantaged consumers across Victoria, and is the largest specialist consumer legal practice in Australia. Consumer Action is also a nationally-recognised and influential policy and research body, pursuing a law reform agenda across a range of important consumer issues at a governmental level, in the media, and in the community directly.

We also operate MoneyHelp, a not-for-profit financial counselling service funded by the Victorian Government to provide free, confidential and independent financial advice to Victorians experiencing financial difficulty.

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The ENA report

The ENA report makes primarily three arguments to suggest that the Limited Merits Review regime needs only minor alteration:

1. the right of the Australian Energy Regulator (**AER**) to raise matters not raised by the applicant in any merits review hearing[1] provides a "significant disincentive to applying for merits review, and goes some way to ameliorating the concern that there is no downside to an appeal for a regulated business";
2. it is intellectually inconsistent to say that a *de novo* merits review (as opposed to a limited merits review) would overcome concerns about "cherry picking" given that the AER's decision is in reality a number of constituent decisions and that the AER does not make one overall "reasonable" decision; and
3. that the lack of downside for a regulated business in seeking merits review is not driven by the structure of the limited merits review regime, but by the absence of an effective contradictor.

The ENA report also suggests that although many AER determinations have been appealed, only a small number of matters within each decision have actually be appealed and, as such, the use of merits review has been relatively limited.

We will respond to each of these concerns.

<u>The AER's right to raise a matter not raised by an appealing network business</u>

The ENA report notes that the AER have not, in practice, used its right to raise additional matters but claims that it still acts as a disincentive. We think this it is extremely unrealistic to expect an independent regulator (or anyone) to appeal its own decision. As a matter of common sense, a regulator who has made a decision would be very unlikely to later want to depart that decision, given its significant nature. Further, to do so might have much greater implications. For example, it call into question the AER's capacity in subsequent decisions (that is, it could be claimed that the AER got it wrong last time, how can it get it right the next) and it could be reasonably asked why the AER did not make the correct decision in the first instance.

In our experience attempting to intervene in the recent Victorian Distribution Price Determination merits review at the Australian Competition Tribunal, we were aware that the AER did not object to the businesses' initial application for leave. As part of that application the Tribunal must determine that there is a serious error to be tried pursuant to section 71E of the National Electricity Law (**NEL**); in fact, as we understand it, the AER consented that there was. This supports a related point made in the ENA report that the AER sees its role in the Tribunal process as limited to explain in its decision, rather than litigating against the distributors. If this is the role AER plays, then it is entirely improbable to expect it to raise matters not made by applicants in the merits review process.

<u>Cherry-picking</u>

As noted above, the ENA report characterises an AER pricing determination as, in reality, a number of constituent decisions and that it does not make an overall "reasonable decision". The ENA report argues that the AER and the Tribunal would not be able to balance the overall

[1] Pursuant to, for example, section 71O(1) of the NEL.

decisions to deal with regulatory error on some aspects of the decision, as the rules do not allow for this. These points are made to suggest that *de novo* review could not overcome concerns about network businesses "cherry picking" aspects of a regulatory decision to appeal.

With respect, this analysis seems to ignore the significant practical reality of decision making on this scale. Even leaving aside the diversity of economic opinion on any question relevant to an AER pricing determination, it is farcical to suggest there is a single "correct" decision. The ENA report somewhat agrees with this, where it argues that the term "regulatory error" is undesirable. The ENA report then notes:

> To take that position [the position that the concern of businesses using the process to take a "one-way bet" is of sufficient magnitude as to require the abolition of merits review] is equivalent to arguing that merits review can never exist unless all errors are resolved, as opposed to just some errors. Granted, where a regulatory error has occurred, it needs to be corrected, but the possibility that some errors may go uncorrected following the merits review process is not a coherent reason to abolish it.

This position seems to accept that the current merits review process does allow businesses to "cherry pick" "errors" that benefit them, but other potential errors in the decision are left untouched.

It is clear that, in the context of complex network pricing determinations, there is real scope to debate what is an error and what is a difference of economic opinion. Given this, judicial or administrative review is better suited to review of such economic determinations, as judicial review essentially undertakes a review of the process by which the decision was made and the legality of the decision.[2] Judicial review is unable to consider the merits of any one of a number of economic theories or analyses.

Absence of contradictors

The ENA report argues that a national well-funded consumer body that is able to participate in merits review processes should ensure that the outcomes of such processes are more balanced. The ENA report also makes some recommendations to make participation for consumer groups easier, including extending time frames to seek merits review or intervene; and abolishing the ability for the Tribunal to make costs orders against consumer groups.

While we would, in principle, support these recommendations we think they would be insufficient to ensure consumers can participate as an effective contradictor to network businesses. As noted in *Barriers to Fair Network Prices*, being able to access information held by network businesses poses significant challenges for consumer groups.[3] Even if the problem of commercial-in-confidence information could be overcome (for example, through a protocol for consumer groups to access such information, including information held by sub-contractors), there still exists the practical problem of examining hundreds of thousands of pages of material to determine which grounds an intervener may wish to raise. This, of itself, is an impossible task in the time frames

[2] On bases such as, whether the process of making the decision was reasonable; whether principles of procedural fairness were observed, whether there was bias on the part of the decision-maker, whether the decision was within the power of the decision-maker; and whether the decision is not so unreasonable that no reasonable decision maker could have made it.

[3] Pages 53-54.

currently prescribed, and requires the briefing and involvement of economic experts and external legal teams.

In our attempt to intervene in the Victorian pricing determination, Senior Counsel advised that to successfully intervene, our agencies would need to raise new material and wield it through a 'world leading' expert. We would also have to establish that we could add something that the AER cannot add. Again, these are significant barrier which will be difficult to overcome.

The final aspect of practical reality is that consumer advocacy organisations are not well-equipped to suddenly halt all activity to focus on a network price review appeals process, as participation in such a process requires. This is not how advocacy organisations generally operate, and it would be unrealistic to expect them to do so.

Experiences with appeals

As noted above, the ENA report suggests that the use of merits review has been limited based on the understanding that only a small number of matters within each determination are actually appealed.

However, the ENA report also notes that 37 per cent of matters relate to cost of capital, which is extremely significant in monetary terms. Twenty-three per cent of matters appealed relate to the regulatory asset base, and 16 per cent relate to opex/capex, aspects which have significant commercial importance for regulated businesses.

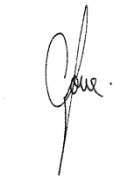
Not only does these statistics demonstrate that appeals are made where it is monetarily significant for the business, it also illustrates that businesses are only appealing aspects that are adverse to them.

Next steps with Review process

We understand that there will be further rounds of consultation as part of this review, including a public forum in May. We look forward to participating in these consultations. In addition, we would welcome meeting with the Expert Panel directly, should it be helpful to do so. We would be pleased to discuss any matters arising out of this submission, or out of our experience with the merits review processes.

Please contact Gerard Brody on 03 9670 5088 or at gerard@consumeraction.org.au if you would like to discuss further.

Yours sincerely
CONSUMER ACTION LAW CENTRE



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