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Should the Law Have a Greater Role in Economic Regulation of Infrastructure Services?

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1. Introduction

The topic could be interpreted in several different ways. It could raise important questions such as whether all States should have legislation providing for possible third-party access to all monopoly infrastructure, along the lines of Part IIIA of the *Trade Practices Act*. Or whether there are entire sectors which cry out for economic regulation. But this paper does not seek to answer those questions because, at heart, they are questions for economists and politicians. Once those large decisions of principle have been made, the law comes into play to implement, to provide checks and balances, to map out processes, to provide dispute-resolution techniques and means of calculating compensation for the infrastructure owner.

Instead of discussing questions of economic principle or political policy, this paper focuses on the role of economic regulators, and considers whether their role would be enhanced by greater support, prescription or intervention from the law.

To answer this question requires an overview of the role which the law currently plays in respect of economic regulators such as the New South Wales Independent Pricing and Regulatory Tribunal (IPART), to create a baseline for comparison.

Throughout the paper, IPART is used as the lead example because it is the economic regulator with which the author is most familiar, but the points hold true for other Australian economic regulators as well, especially State-based regulators as they are not as constrained by constitutional issues as some Commonwealth regulators.

In relation to economic regulators, the role of the law can be broken down into three broad components:

1. The establishment and grant of powers to economic regulators;
2. Governing the core decision-making of economic regulators; and
3. Governing or influencing the processes leading up to and following after the decisions of economic regulators.

2. The establishment and grant of powers to economic regulators

Here the law and, more specifically, statutory law is essential. Economic regulators could not exist without a statutory foundation and statutory powers. Economic and competition regulators of the kind now considered mainstream are creatures of the late twentieth century. They come with the slow but far-reaching acceptance in Western democracies of the pro-competition principles which had their origins in the United States. The United States was first mover in giving pro-competition principles the force of law by passing of the first anti-trust laws in the late nineteenth century. In Australia it took until 1974 for the first version of the *Trade Practices Act* to be passed, with the States lagging some way behind.

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But the real growth of economic regulation and economic regulators came in the 1990s with the acceptance of National Competition Principles, and the subsequent segregation and corporatisation of government businesses, especially infrastructure businesses, and their transition to a competitively neutral or pseudo-competitive environment. The economic regulators were both a product of, and instrumental in, promoting broad understanding and acceptance of concepts such as 'user pays' and the relevance of efficient cost-reflective pricing signals both to investors in and consumers of infrastructure services.

The divestiture and privatisation of a number of formerly government-owned businesses created a need to regulate those businesses – or at least their monopoly infrastructure – once they could no longer be controlled through ownership rights. Telstra is a case in point. In other cases monopoly infrastructure businesses are still owned by government, and the purpose of economic regulation is to simulate a competitive market to drive operational and investment efficiencies.

Everything in this new pro-competition world was built on statute, including the creation of regulators such as the Australian Competition and Consumer Commission (ACCC), the Queensland Competition Authority (QCA) and IPART. The pattern of legislation creating economic regulators has been to give them broad powers to deal with the subject-matters assigned to them under the umbrella of broadly stated pro-competition objectives. IPART is a bit of an exception to this pattern, possibly because it was one of the earliest to be established and pre-dates the adoption by governments of the Competition Principles Agreement in 1995. The IPART Act does not include any over-arching statement of lofty principle. On the other hand, the early creation of IPART has given it time to develop and fine-tune its regulatory approach in several sectors over several price-path periods, and this depth of experience has enabled IPART to take a leading role in some regulatory areas.

Legislation establishing the economic regulators has been largely stable. The legislation establishing IPART, for example, has been amended only a small number of times in almost 20 years and on most occasions this has been to add subject-matters to IPART's jurisdiction, and not to change its fundamental structure or powers.

Accordingly, on the first limb of the topic, the establishment and grant of powers to economic regulators, the law is essential, particularly statutory law, but its contribution is largely already made. Few Australian economic regulators appear to be seriously impeded by gaps in their statutory powers.

3. Governing the core decision-making of economic regulators

The second limb of the topic is the delineation and control of the key substantive decision-making parameters under which economic regulators operate. Here, in the view of the current author, greater intervention of the law is not desirable.

What economic regulators do is to weigh up and balance the conflicting policy objectives in their charters and the competing interests of their stakeholders in an ever-changing economic and political environment. In some instances, such as water regulation, even the ever-changing climatic environment is relevant. The size of the infrastructure service provider, the scope of the exercise, the position of the service provider on the road to pro-competition reform – all these matters vary from review to review. Accordingly, flexibility, adaptability and the proportionality of the regulatory response are all important.

This is not territory in which the law and traditional legal processes are particularly helpful. In a traditional legal contest there are clearly identified parties with more or less defined rights and claims which delineate and confine the scope for decision-making. Decisions are made largely based on the material and arguments which the parties put forward. For each argument there is a proponent and an opponent. The role of the decision-maker is that of umpire rather than originator. The interests of third parties who are not directly involved count for little or nothing.

That is not the world of economic regulation. In the pricing work which IPART does, the agency or utility affected does not always even put forward a proposal. Stakeholders most affected by IPART decisions are not necessarily always represented, and not invariably well represented. The core regulatory approach is, more often than not, originated by IPART, and the interests of all

affected stakeholders are relevant, whether they are represented or not. All important decisions are published in draft for comment, and all submissions are taken into account.

While it is not the function of IPART to arrive at consensus decisions, its processes do have the effect of narrowing down the topics on which stakeholder opinions differ. Sometimes the Tribunal persuades stakeholders to change their minds, and sometimes they persuade the Tribunal. At the end of the day, however, IPART's job is to balance the competing interests and the frequently conflicting parameters set out in the terms of reference, and to find a middle way.

Many of the decisions IPART makes are affected by section 15 of the *IPART Act*. If one looks at the conflicting policy objectives listed in section 15 they include the following:

Matters to be considered by Tribunal under this Act

(1) In making determinations and recommendations under this Act, the Tribunal is to have regard to the following matters (in addition to any other matters the Tribunal considers relevant):

(a) the cost of providing the services concerned,

(b) the protection of consumers from abuses of monopoly power in terms of prices, pricing policies and standard of services,

(c) the appropriate rate of return on public sector assets, including appropriate payment of dividends to the Government for the benefit of the people of New South Wales,

(d) the effect on general price inflation over the medium term,

(e) the need for greater efficiency in the supply of services so as to reduce costs for the benefit of consumers and taxpayers,

(f) the need to maintain ecologically sustainable development (within the meaning of section 6 of the Protection of the Environment Administration Act 1991) by appropriate pricing policies that take account of all the feasible options available to protect the environment,

(g) the impact on pricing policies of borrowing, capital and dividend requirements of the government agency concerned and, in particular, the impact of any need to renew or increase relevant assets,

(h) the impact on pricing policies of any arrangements that the government agency concerned has entered into for the exercise of its functions by some other person or body,

(i) the need to promote competition in the supply of the services concerned,

(j) considerations of demand management (including levels of demand) and least cost planning,

(k) the social impact of the determinations and recommendations,

(l) standards of quality, reliability and safety of the services concerned (whether those standards are specified by legislation, agreement or otherwise).

In addition to the internal tension between many of the section 15 matters, it is important to note the residual discretion given to IPART, to have regard to 'any other matters' the Tribunal considers relevant.

And so IPART balances the need for cost-reflective pricing against the protection of consumers from excessive price shocks. It balances the need of State utilities to be rated BBB+ against the need for consumers to adjust to price increases which are individually manageable but cumulatively difficult. It balances the need for State utilities to invest capital expenditure in big lumps against the needs of consumers to have prices glide upwards rather than step upwards. It balances the interests of those who benefit from capital projects now against those who will benefit from them in the future.

It is hard to see what the law could do to facilitate the ability of an economic regulator such as IPART to weigh up all these matters, when ultimately a significant and unavoidable judgment call is required. The law is uncomfortable with discretion and especially with open-ended discretion. Its approach is usually to seek to define the outer limits of the discretion, to prescribe as closely as possible what must be taken into account and preferably how much weight is to be given to each factor. In the view of this author, neither IPART nor its stakeholders would be assisted by that. It is hard to see how the greater intervention of the law would facilitate or improve the core decision-making task of an economic regulator such as IPART. It seems more likely that the law would constrain and ossify the flexibility, adaptability

and proportionality of IPART's regulatory response to the different circumstances with which it has to deal.

For these reasons it does not seem that the law has a great deal more to contribute to the core decision-making function of an economic regulator like IPART.

4. Governing or influencing the processes leading up to and following after decisions of economic regulators

Having considered the provisions which establish economic regulators and give them their powers, and having dealt with the circumstances in which economic regulators exercise their core decision-making functions, the third limb of the topic is to consider the processes leading up to economic regulatory decisions, and the processes which follow them, to consider whether the law could usefully have a greater input.

Process is the area where the law has perhaps the greatest contribution to make in economic regulation. Many of the things which economic regulators now do more or less intuitively derive from the law or, more specifically, from administrative law – the body of law developed to enable the courts to supervise and control executive power in administrative decision-making, but without exercising that executive power themselves.

The administrative law notion of procedural fairness or natural justice has deeply affected the way in which modern economic regulators go about their decision-making, and is strongly influential in achieving the widespread acceptance which their decisions enjoy.

A key concept in administrative law is that executive power in making administrative decisions must be exercised according to law, no matter how wide the discretion of the decision-maker may appear to be.

'According to law' involves a number of requirements. The power must be exercised *bona fide* for the purpose for which it was given, and not for an ulterior purpose. The decision-maker must be impartial in terms of having no stake in the outcome and in terms of having an open mind and not being biased. The decision-maker must take relevant material into account but must exclude irrelevant material. The decision-maker must actually make the decision and not be merely the ventriloquist's dummy, that is, not be beholden to someone else who has not been given the decision-making power. And so on.

In addition to all of these requirements which derive from the common law of administrative law, there are relatively recent requirements of administrative law statutes such as the Commonwealth *Administrative Decisions Judicial Review Act* which have been adopted and internalised by economic regulators, whether or not the *ADJR Act* (or a State equivalent where these exist) actually applies to them. These additional statutory-based requirements include the need for a regulatory decision to be accompanied by a statement of reasons, and the requirement that a regulator must be able to identify what material it has relied upon and what it has taken into account.

It may come as a surprise that, in 1980 when the *ADJR Act* came into effect, these requirements were by no means mainstream. It is now unimaginable to think of an IPART report, at least, without a lengthy statement of reasons and detailed identification of matters relied upon by the Tribunal in making its decisions.

Failure to observe the requirements of procedural fairness or natural justice as it used to be called, gave the courts a basis to intervene in administrative decision-making. The intervention was never undertaken by the courts to substitute their own decision for that of the original decision-maker, never to express an open view on what would or should have been the correct or preferable decision. The role of the courts was to analyse and correct the process and send the matter back to the original decision-maker to try again. This unwillingness to re-make the actual decision reflected two things – First, the fundamental unwillingness of the legal system to make policy-based decisions for which it does not have the experience, training or subject-matter expertise. Second, it reflected concepts of the separation of powers. The role of the judiciary is two-fold: first to supervise the legislature and decide whether laws made are within power. It is also to supervise executive decision-making and ensure it is done according to law. In the case of administrative decisions which are an example of the exercise of executive power, one cannot maintain the supervisory role of the judiciary and the separation of powers if the judiciary steps in and assumes the role of the person or entity whose decision-making it is supervising.

In the application of these concepts, administrative law has had a very real and tangible role to play in the balance of powers among the legislature, the judiciary and the executive (which includes economic regulators).

Which brings us to merits review. Merits review is unknown in the common law. Merits review is the

review of decisions where the reviewing body can substitute its views on what is the right or preferable decision for that of the original decision-maker. Merits review is the diametric opposite of judicial review described above. Merits review is a relatively new innovation and it is entirely a creature of statute. Merits review is almost always carried out by administrative tribunals such as the Commonwealth Administrative Appeals Tribunal and the Australian Competition Tribunal which have among their members a mixture of lawyers and subject-matter experts.

Turning to the processes which IPART adopts in its investigations and determinations, they are partly regulated, but are largely self-imposed. Among its five core objectives, IPART includes as number one the achievement of fair and transparent processes. This is achieved in a range of ways, all of which can be tied back to administrative law concepts which have been internalised in the decision-making processes of the Tribunal. The Tribunal publishes the timeline for its processes to maximise the notice given to stakeholders of the opportunities they will have for input, and to minimise delays. In areas involving methodologies or modelling of technical complexity, the Tribunal frequently publishes papers outlining the proposed methodologies and conducts public workshops to discuss and test them. All reports are published first in draft and stakeholders have an opportunity to make written submissions and frequently also to attend and speak at public hearings.

According to stakeholder surveys, the Tribunal has succeeded in running processes which are consultative, transparent, inclusive and respectful. Its decisions enjoy widespread acceptance, even from those who don't like the outcome.

It is difficult to see what the difference would be for practical purposes if IPART's processes were legally mandated in fine detail rather than voluntarily adopted and tailored to the needs of individual investigations or reviews and to the particular stakeholder demographic.

IPART is, of course, fortunate in that most of the entities regulated by it come to it seeking price increases to fund capital expenditure or service improvements or both. They have no economic incentive to delay or fail to co-operate with information requests. If they do so it tends to be by reason of a lack of management control rather than with the intention of gaming the regulator. Things may change for IPART in this respect as more decisions arise under the NSW *Water Industry Competition Act*. Other regulators already face a rather different and more difficult task when they are trying to drive change by, for example, pushing down allowed access costs against the commercial interests of an existing incumbent. Under Part XIC of the Trade Practices Act, for example – the telecommunications access regime provisions – examples of gaming the regulator are legion.

The success of an economic regulator's processes can be measured in part by the number of legal challenges to which it has been subject. While the common law of administrative law applies to IPART, it has never been the subject of an application for judicial review. It is not currently subject to merits review and to date there has been no push to create a layer of merits review.

Merits review tends to have three common characteristics –

- Each party pays its own costs irrespective of outcome
- If a new decision is made it is prospective only and not retrospective
- There is no compensation for the time value of money during the review process

In IPART's situation, the introduction of merits review could have the effect of causing regulated infrastructure service providers permanent revenue loss through the delay of price increases caused by the review process. Merits review could play out strategically in areas such as bulk water where a relatively small and identified group of stakeholders has a material commercial interest at stake. If there is no costs risk other than one's own costs, and no interest risk in requesting merits review, it is a relatively simple calculation to work out whether the net present value of price increases delayed by the process is greater than the net present value of legal costs to be spent in launching merits review.

In summary, the processes of economic regulators such as IPART leading up to the making of decisions are well developed and well understood by stakeholders. The processes derive from and mimic many of the requirements of procedural fairness in administrative law. In large part the law has already had a profound effect by the creation of new norms, even where particular legal provisions are not directly applicable to the regulator in question. It is difficult to see what benefit would flow from the law taking an expanded role in this area.

In terms of review, judicial review applies to IPART but has not to date been accessed by anyone. Merits review does not apply and there is no push to introduce it. So, all in all, in this third limb of processes before and after decision-making, IPART is well served by the processes it has developed and tested and refined over an 18-year period, and there is no obvious expanded role for the law.

5. Conclusions

Having broken down the role of economic regulators into three main areas:

- The legal provisions which establish them and give them powers
- The provisions which delineate and control their core decision-making
- Their processes before decision-making, and review of decisions after the event,

the conclusions of this author are that the law is essential to the first, largely unable to add value to the second and highly relevant to the third, but has substantially achieved its objectives without further input being required.

Critical Issues in Regulation – From the Journals

'Does Electricity (and Heat) Network Regulation Have Anything to Learn from Fixed Line Telecoms Regulation?', Michael Pollitt, *Energy Policy*, 38, 2010, pp. 1360-1371**.**

This paper considers the lessons for electricity regulation arising from the recent history of telecommunications deregulation in the UK and, to a lesser extent, the EU. Would a regulatory regime that envisages the possibility of deregulation in the future be more appropriate? According to Pollitt, telecommunications deregulation provides two clear models of how future deregulation of electricity might be justified – by providing a regulatory regime that encourages facilities-based competition and unbundled local access.

Pollitt notes that the imperatives of climate change enhance the potential for structural change in electricity. In this regard, the Ofgem has developed five plausible scenarios for electricity networks in 2050. These are briefly summarised in Pollitt's paper. Three of these scenarios, termed 'radical' by Pollitt, envisage reduced reliance on the main grid and significantly more competition at the local level from own-generation, local generation and large central power plants than at present – a form of facilities-based competition. This distributed generation (DG) would be connected at lower voltages and lie within the network architecture of traditional distribution network operators (DNOs). The 'radical' scenarios also envisage that networks will be part of a flexible electricity system that allows consumers to choose their level of reliance on the main grid. It is in this context that, according to Pollitt, the lessons from fixed-line telecommunications deregulation becomes of interest.

Despite similarities between the configuration of telecommunications and electricity networks, Pollitt acknowledges that there are differences that need to be taken into account when considering the extent to which lessons learned in telecommunications regulation might be applied in electricity. In particular, there is little facilities-based competition in electricity. That is, electricity networks are not 'switched' in the sense that traffic can be directed down a particular route between an entry and exit point. Charging mechanisms for electricity are generally not as sophisticated or granular as for telecommunications; and there is less scope for innovation in products and service in electricity compared with telecommunications. Nevertheless, Pollitt argues that these differences may lessen over time as the electricity industry evolves, including through the use of control technology and smart metering. Furthermore, Pollitt considers that technological change in response to the climate-change agenda may erode the natural monopoly characteristics of distribution networks if micro-grids and own-generation play a similar role in electricity as facilities-based competitors in telecommunications. However, the lessons from telecommunications are tempered by the fact that electricity networks develop more slowly and the assets are longer lived than in the telecommunications sector. Climate change targets and incentives are also crucial in underpinning the development of the energy sector.

Pollitt makes a number of suggestions for the future regulation of electricity in the UK. These include:

- the implementation of measures to reduce the costs of entry into markets for local energy provision;
- the introduction of nodal pricing to encourage efficient location of DG;
- allowing for the possibility of deregulation in areas where facilities-based competition emerges; and
- trialling local wire unbundling as a way for energy service companies based on DG to gain non-discriminatory access to network services and reconfiguring ownership of existing assets to facilitate DG.

Pollitt contemplates the complete deregulation of electricity networks in the longer term, facilitated by a simpler, more permissive regulatory regime in the interim.

'The Role of International Benchmarking in Developing Rail Infrastructure Efficiency Estimates', Andrew Smith, Phill Wheat and Gregory Smith, *Utilities Policy*, 30, 2009, pp. 1–8.

This paper summarises the international benchmarking work used by the UK's Office of Rail Regulation (ORR) in informing its efficiency view during the 2008 periodic review for Network Rail.

The national rail network, owned and operated by Network Rail, is subject to the RPI–X incentive regulation administered by the ORR. The determination of X – the productivity offset factor – may require an assessment of the potential scope for Network Rail to improve its efficiency.

The lack of domestic comparators in the industry necessitates the use of international benchmarking. During previous periodic reviews, the ORR has conducted some international benchmarking studies to examine the efficiency of Network Rail relative to

other international comparators. The ORR has primarily used the International Union of Railways' (UIC) dataset to conduct the international benchmarking studies. The dataset covers 13 national rail operators in Western Europe over a period of eleven years (1996–2006).

The ORR also collects regionally disaggregated data for a number of rail operators in Western Europe and North America for a shorter time period. The international regional benchmarking results were used to verify the results derived from the UIC dataset.

The 2008 ORR work considered a number of efficiency estimation techniques, including Date Envelopment Analysis (DEA) and Corrected Ordinary Least Squares (COLS), before choosing the preferred model – a stochastic frontier model that relates total maintenance and renewal costs to the relevant cost drivers and allows for time-varying cost efficiency.

The authors argue that this process ensured that the most appropriate model was selected and also resulted in a range of estimates that could be used for cross-checking.

The results from the preferred model show that:

1. Efficiency improvement occurred to the British rail network in the early years after privatisation and during the third control period starting in 2004;
2. Compared to the upper quartile of international comparators, Network Rail operated relatively inefficiently with a cost gap of 37 per cent.

According to the authors, the econometric results are considered to be robust to a variety of estimation methods and sensitivity tests, which consistently suggested a 30 to 50 per cent efficiency gap between Network Rail and the upper quartile of the peer group. Supplementary work commissioned by the ORR suggested that the main area for cost saving is efficiency improvement as international practices using alternative technologies or working methods are readily applicable to the British rail network.

The authors discuss the likely circumstances for using international benchmarking in informing regulatory decisions. They note that the role of international benchmarking has become increasingly important in the UK rail regulation as a result of improvements in data availability, quality and analysis. They also point out that it may take many years to develop the international benchmarking framework and collect the required data. Given the many empirical and policy challenges associated with the international benchmarking, the work can be better developed between periodical reviews.

'Pricing, Competition and Policy in Australasian Air Travel Markets', T Hazeldine, *Journal of Transport Economics and Policy*, 44(1), January 2010, pp. 37–58.

Hazeldine's paper investigates competition between two incumbent legacy carriers on the New Zealand and Tasman routes (Qantas and Air New Zealand (Air NZ)), and the extent to which their pricing is constrained by new entry from a low-cost carrier (Pacific Blue) and a Fifth Freedom carrier (Emirates).

Hazeldine's paper begins with a review of the history of entry to the Trans-Tasman and New Zealand domestic markets by Emirates and Pacific Blue. This potential and actual competition was a major impetus for Air NZ and Qantas to jointly apply in December 2002 to the Australian Competition and Consumer Commission (ACCC) and the New Zealand Commerce Commission (NZCC) for authorisation to form a 'strategic alliance' which would have, according to Hazeldine, cartelised all Trans-Tasman and New Zealand domestic routes operated by either airline. The application was turned down by both regulators and failed on appeal to the NZ High Court in 2004. However, a rehearing before the Australian Competition Tribunal (ACT) in 2004 found in favour of the applicants. Encouraged by this ruling, Qantas and Air NZ proposed a more restricted 'Tasman Networks Agreement' in April 2006, which again involved cartelisation of their operations, but only in relation to Trans-Tasman flights. Following rejection by the ACCC in November, the airlines withdrew their application.

Qantas's and Air NZ's argument that the Tasman Networks Agreement would not be anti-competitive hinged on the view that the low-cost position of Emirates and Pacific Blue would prevent any attempt by the cartel to raise prices. This proposition was accepted by the ACT in its finding in favour of the alliance. It is that proposition which Hazeldine seeks to test in this paper by hypothesising that current market shares overstate the price-setting market power of incumbents in air travel markets when these are subject to actual or potential competition from other lower-cost airlines who are able to undercut the incumbents on price. The hypothesis is tested using cross-sectional data on 1001 flights collected for two time periods. The first dataset consists of eight domestic New Zealand routes plus the Auckland-Sydney route over the period 17 November 2004 to 5 January 2005. The second dataset includes all direct Trans-Tasman flights and flights from smaller New Zealand cities observed on 29 June 2005, 6 July 2005 and 13 July 2005. The data are used to infer the consequences of structural change in markets.

Hazeldine examines some of the issues associated with econometric analysis of his hypothesis – in particular, the potential for market structure (which is

treated as an independent or exogenous variable) to be endogenously determined by market price (which is the dependent variable in Hazeldine's model). This may be an issue if strategic pricing is used to deter entry, and thus maintain a particular market structure. The emergence of the low-cost carrier model may also have had an influence on market structure. After considering the case-specific issues, Hazeldine concludes that endogeneity is unlikely to be a significant concern for his study.

Hazeldine's models price as a semi-logarithmic function of market structure, costs, load factors and dummy variables which account for peak period and business travellers (when prices are likely to be higher). The model was estimated using generalised least squares. Hazeldine finds that prices vary substantially across different routes. Much of the difference was explained by distance-related costs. However, Hazeldine also found a substantial and significant role for demand and market structure factors. His main findings are: (i) that routes on which Qantas and Air NZ were in competition tended to have air fares around 20 per cent lower than Air NZ's monopoly routes; (ii) the entrants, Emirates and Pacific Blue, offered much lower fares across the Tasman (around 25 per cent), but did not achieve substantial market share. Hazeldine infers that this finding implies that (iii) Emirates and Pacific Blue do not offer much competitive constraint on the pricing of Air NZ and Qantas. In particular, air fares on routes in which Qantas and Air NZ were in competition tended to be significantly lower than fares for which Air NZ was the monopoly supplier.

Hazeldine suggests that his results demonstrate a lack of empirical support for the argument that competition from Emirates and LCCs would effectively constrain a legacy cartel from significantly raising airfares. Thus he concludes that his findings provide no evidence in support of the ACT's findings.

'Network Effects in Infrastructure Regulation: Principles and Paradoxes', T. Brennan, *Review of Network Economics*, 8(4), December 2009, pp. 279–301.

This paper explores the influence of network effects in infrastructure regulation. While these network effects are beneficial, they can also cause monopoly and complicate the management of partial transitions to competition in telecommunications and electricity.

Network effects arise when the value to a consumer of using a product or service increases with the number of its other users. An oft-cited example is Microsoft's Windows operating system and applications. The value to any one user of Windows arises partly because of its near-ubiquity in use by other users. This enables communication through sharing files, and enables anyone with Windows experience to work on almost any computer in the world.

Network effects may also arise along a supply chain. For example, manufacturers may want to make their goods compatible with the products of other firms, as happens when a standard is established or mandated.

In US telephony, two factors made local telephone services a monopoly: scale economies and network effects driven by demand-side externalities. More recently, technological changes such as VoIP telephony and digital mobile telephony have become alternatives to the landline network. However, network effects remain: everyone still wants to be connected to everyone else. The Federal Communications Commission (FCC) implemented an interconnection regime so that, at a minimum, all carriers can deliver traffic to all other carriers. Of course, carriers can coordinate and set an interconnection fee equal to monopoly profits. In addition to protecting the ability of entrants to compete, regulators also need to ensure that a nominally competitive group is not effectively a cartel.

A broader context or definition for network externalities is non-pecuniary horizontal network externalities. The non-pecuniary network externalities are gains arising to consumers/producers from being connected to a network that are not priced in the market. The non-pecuniary network externalities may require private coordination or public policy so that these externalities are internalised and an efficient outcome is achieved.

In electricity transmission, for example, an interconnected transmission network enables 'loop flow' in which electricity takes multiple paths to arrive from generators to customers. If one entity increases transmission capacity, the cost to others of offering transmission services fall (note, however, that this phenomenon is less relevant to 'linear' transmission networks, such as Australia compared to grid-like transmission networks such as those seen in the US). However, a transmission provider will only consider the private returns from undertaking investment to expand its transmission capacity in the network, and therefore public policy or private coordination may be necessary to encourage an efficient expansion that includes the external benefits of lowering costs to generators and/or customers.

Brennan argues that this network effect in electricity creates two problems for regulators. The first is whether transmission networks and generators can operate without the need to coordinate. In the short run, access prices to the transmission grid need to be set on a node-by-node time-varying basis to provide the correct signals so generators do not inject into congested lines. These prices require constant

adjustment to prevent excess profits accruing to transmission businesses. In the long run, expansion of the network requires coordination between generators and transmission businesses.

The second problem is ensuring the grid remains reliable while individual generators compete. Because of network effects from interconnected transmission networks, a blackout from one supplier can spread across the grid as a whole. Reliability is therefore a public good in the economist's sense. One solution is the development of capacity markets. This gives rise, however, to other questions such as defining capacity, and how prices for capacity services translate to end-user prices.

Brennan notes that network effects involve a fundamental logical flaw in conventional legal treatments of monopolisation or abuse of dominance around the globe. The standard treatment assumes that for a firm to abuse its market power, it must have the power in the first place. A paradox then arises: a firm can illegally acquire market power only if it has the power in the first place. Legal cases may be stronger if they focused on the abuse *creating* dominance rather than abuse *of* dominance. Brennan cites the example of Microsoft. While network effects, scale economies and lock-in were behind Microsoft's vast market power, these factors *creating* dominance were overlooked. Instead, the focus was on the abuse *of* dominance via the packaging of a mere browser.

'Endogenous Regulatory Constraints and the Emergence of Hybrid Regulation', L. Blank and J.W. Mayo, *Review of Industrial Organization*, 35, 2009, pp. 233-55

Models of public utility regulation are often framed as either rate-of-return (ROR) or price-cap regulation. This paper develops a model that endogenously yields hybrid regulatory constraints as the regulator's optimum choice.

The authors note that ROR regulation arises in practice despite the Averch-Johnson effect in which the regulated utility over-invests in capital even though, for a given level of output, it can lower costs by substituting for more labour. Besanko (1984) developed a model in which the regulator adopts ROR regulation to attenuate information asymmetry regarding the firm's production function.

Academic literature has demonstrated that price-cap regulation eliminates the over-capitalisation distortion associated with ROR regulation, and by the 1990s became increasingly adopted by regulators. Despite this, transition to price-cap regulation has been slow. Indeed, the authors note that regulators have been transitioning to a hybrid of ROR and price-cap regulation. Even in regulatory regimes that are nominally 'rate of return' or 'price-cap', the components of the regime often incorporate elements of the other. The AER's revenue-cap regime for electricity transmission providers is cited as an example of a hybrid regime.

The authors therefore developed a model which tries to establish how and why regulators may establish particular regulatory instruments.

In the model, the regulator maximises total political support from the regulated utility and from customers. The utility's political support function increases with profits, while customers' (or consumer advocates) political support increases with consumer surplus – or decreases with price – and is inversely related to the ROR.

The utility's political support is at its maximum when economic profits are at their unconstrained maximum, while customers' political support is maximised when economic profits are zero. Using their political support function, the regulated firms' marginal political support is maximised when economic profits are at the unconstrained maximum (and converse for the consumers' marginal political support). Political support is therefore maximised somewhere between zero and the unconstrained maximum economic profits.

Under ROR regulation, the regulator can enhance total political support at the margin by sacrificing profit (political support from the utility) for a lower price (and higher political support from customers). Similarly, under a price cap, the regulator can enhance total political support by sacrificing profit for a lower ROR, which results in higher customer political support.

The paper therefore proposes that neither ROR regulation nor a price cap maximises total political support. In other words, total political support is maximised under a hybrid ROR-price cap regime. This still results in over-capitalisation but to a lesser degree than pure ROR regulation.

Other papers mentioned

D. Besanko, 'On the Use of Revenue Requirements Regulation Under Imperfect Information', in *Analyzing the Impact of Regulatory Change*, 1984, M.A. Crew, Lexington, Lexington Books.

'Snakes and Ladders: Unbundling in a Next Generation World', Martin Cave, *Telecommunications Policy*, 34(1-2), February 2010, pp. 80–85.

Martin Cave is a Professor at the Warwick Business School, a popular and frequent speaker at the ACCC's annual regulatory conference, and the originator of the notion of the 'ladder of investment' which has gained some popularity in telecommunications circles. The idea of the ladder of

investment has both a positive and a normative dimension. The descriptive or positive part is the hypothesis that, as their market share rises, competing telecommunications providers rely less and less on the dominant incumbent's facilities and more and more on their own. The normative dimension to the notion of the ladder of investment is more controversial. It basically asserts that regulators should work out where the leading firms are on the ladder (that is, determine the extent to which they are relying on their own facilities), determine the investment they would require to move to the next rung of the ladder, and then adjust the regulatory parameters (access rules, access prices, etc.), so as to push the firm to invest to the next level. While the ladder of investment has its adherents, to some this version of the ladder of investment seems like interventionism and micromanagement of the industry. This approach seems to be some distance from the notion that competitive market processes are the best long-run determinant of who succeeds and who fails, what investments will be made, and by whom.

In this short paper, Cave explores the implications of the transition to Next Generation Access (NGA) networks for the ladder of investment notion. The paper is built around the observation that, with large-scale investment in fibre to the home (or close to the home), access to the unbundled copper local loop will no longer be possible. Instead, competing providers will be forced to either deploy their own fibre networks, which seems unlikely, or to slide back down the ladder to just provide bitstream service – essentially just reselling the service of the incumbent network. The irony is that, as Cave points out, competing providers have been, over the last few years, moving away from resale/bitstream services towards local loop unbundling (which requires a degree of investment by the competing provider) – at the encouragement of regulatory authorities. Now, just as they are becoming increasingly successful, they are being forced to slide back down the 'snake' to a lower level on the ladder and become resellers.

The central question of this paper is whether or not the notion of the ladder of investment still applies for NGA networks. Cave argues that an equivalent notion of the ladder of investment exists for NGA and 'regulators can use their powers to nudge operators upwards'. However, in the Australian context, our understanding is that when the new national fibre network is constructed there will be no scope for partial or full local loop unbundling. And the potential for creation of a duplicate fibre network seems negligible, at least in the next few decades. The notion that regulators should push firms up the ladder of investment always seemed questionable. Now, at least in Australia, the idea becomes irrelevant. There will simply be, for competing providers, no further rungs on the ladder.

Regulatory Decisions in Australia and New Zealand

New Zealand

The New Zealand Commerce Commission's Draft Report Recommends Telecommunications Resale Deregulation

See Notes on Interesting Decisions.

New Zealand Commerce Commission (NZCC) Issues Guidelines for Bundled Telecommunications Products

On 20 August 2010, the NZCC issued guidelines to help telecommunications retailers understand their obligations under the Fair Trading Act in relation to the disclosure of bundled telecommunications products. The guidelines include a checklist of points for companies to consider when planning the advertising of bundled telecommunications products. The NZCC has indicated that it will adopt an active enforcement approach to the guidelines. The New Zealand Commerce Commission (NZCC) has observed that product bundling is an important development in retail telecommunications market. Such bundling can lead to cheaper prices and increased competition if prices, terms and conditions are clearly explained to consumers. Thus disclosure of bundled retail telecommunications products is a key element of effective competition in retail telecommunications markets. **Guidelines**

NZCC Publishes Draft Decision to Amend the Default Price-Quality Path

See Notes on Interesting Decisions.

NZCC Announces Indicative Process for Regulation of Mobile Termination Rates

The NZCC on 4 August 2010 announced its indicative process for determining mobile termination rates, following the announcement by the Minister for Communications and Information Technology, that he has accepted the NZCC's recommendation to regulate the mobile termination access service (MTAS). The Minister's decision is expected to take effect in September 2010. Once the necessary legislative changes come into force, the NZCC expects to commence a standard terms development process for MTAS. **Media release**

NZCC Releases Draft Review of Unbundled Local Loop Backhaul Services

The NZCC on 6 August 2010 released a draft report on its review of where Telecom faces competition in the provision of backhaul services for the unbundled copper local loop, and thus where regulation may no longer be required. The draft report concludes that Telecom faces competition on two of the links that were reviewed. Thus on those links, regulation will be removed. The draft review decision also assesses another 25 links for the first time, and on all of these links the NZCC found no evidence that Telecom is subject to competition and thus these links will be available as regulated backhaul services. Submissions were due 13 August 2010. **Media release**

NZCC Releases Starting Price Adjustment Consultation Paper

The NZCC on 5 August 2010 released a consultation paper on its proposed framework for making 'starting price adjustments' under a default price-quality path applied to regulated electricity distribution businesses and to gas pipeline businesses. The NZCC is required to set starting prices for each supplier at the beginning of a regulatory period to establish the cap on its prices or revenues. The consultation paper sets out a proposed framework for making starting price adjustments and the components of that framework, including the determination of those components. The paper also discusses the proposed treatment of certain efficiencies in the context of the starting price, including those arising from merger or acquisition. The deadline for submissions was 10 September 2010. **Consultation paper**

New Zealand Telecom Settles over Wholesale Loyalty Offer

The NZCC, on 9 July 2010, reached a $1.6 million settlement with Telecom Corporation of New Zealand Limited. The settlement follows an investigation into whether Telecom Wholesale's "loyalty offers☐ breached Telecom's Separation Undertakings which require Telecom not to discriminate between or against its wholesale customers. The NZCC's investigation concluded that the loyalty offers were likely to breach the Undertakings. Telecom's Independent Oversight Group (IOG) also investigated and determined that the Wholesale's loyalty offers were "non-trivial☐ breaches of the Undertakings.

NZCC Releases Draft Decisions on Individual Price-Quality Path for Transpower

On 28 June 2010 the NZCC released its draft decisions and reasons on the application of individual price-quality regulation to Transpower. The NZCC published its draft decisions on the basis of the NZCC's recommendation to the Minister that individual price-quality regulation apply to Transpower. The deadline for submissions on the draft decisions was 6 August 2010. **Draft decisions and reasons**

NZCC Releases Draft Decisions on Input Methodologies for Transpower

On 25 June 2010, the NZCC announced publication of the fourth in a series of papers on the development of input methodologies for regulated industries under Part 4 of the Commerce Act. The purpose of input methodologies is to promote certainty for suppliers and consumers in relation to the rules, requirements and processes applying to the regulation, or proposed regulation, of goods or services under Part 4. The latest paper set out the NZCC's draft decisions and reasons on the input methodologies to be applied to Transpower. The deadline for submissions was 6 August 2010. **Input methodologies**

Australian Competition and Consumer Commission (ACCC)

ACCC Grants Interim Approval to Wiggins Island Coal Producers

See Notes on Interesting Decisions.

ACCC Objects to Sydney Airport's Proposed Increase in Charges for Regional Airlines

The ACCC on 17 September 2010 issued its decision objecting to Sydney Airport Corporation Limited's proposal to increase charges for regional airlines that serve passengers travelling within New South Wales. On 9 July 2010, the ACCC released an issues paper seeking comment from interested parties on Sydney Airport's proposal to increase the prices it charges to regional airlines that serve intrastate passengers. Sydney Airport intended increasing these prices by a maximum of 2.9 per cent, which represented an increase of about $4.70 for each aircraft movement. Submissions were due 30 July 2010.

- **Issues paper**
- **Objection**

ACCC Proposes New Simpler Approach for Wholesale Fixed Line Telecommunications Services Pricing

On 17 September 2010 the ACCC released a draft report and draft indicative prices to apply to the regulated fixed line telecommunications services. These services are currently used by communications companies to provide voice, facsimile and broadband products to consumers and businesses over Telstra's copper network. The ACCC is yet to consider pricing on fibre access networks. Submissions on the draft report and indicative prices are due by 22 October 2010. **Link**

ACCC Consults on Revised Hunter Valley Rail Access Arrangements

On 16 September 2010 the ACCC announced commencement of public consultation on a revised Hunter Valley rail network access undertaking submitted by the Australian Rail Track Corporation. The deadline for submissions on the current consultation is 11 October 2010. **Link**

ACCC Proposes to Deny Authorisation for Virgin Blue – Air New Zealand alliance

The ACCC issued on 10 September 2010 a draft determination proposing to deny authorisation for an alliance between Virgin Blue and Air New Zealand on their flights between Australia and New Zealand. Under the alliance, the airlines would take a coordinated approach to a range of issues including pricing, revenue management, schedules, capacity and routes flown. Feedback was due 24 September 2010. **Link**

ACCC Imposes Penalties and Secures Compensation Under Water Termination Fees Rules

The ACCC announced on 9 September 2010 that it has agreed to accept a court enforceable undertaking from Murrumbidgee Irrigation Limited (MI) and issued it with three infringement notice penalties, totalling $66,000, following multiple breaches of the Water Charge (Termination Fees) Rules 2009.

Following an investigation by the ACCC, MI admitted that it had breached the Rules by charging termination fees in 27 instances that exceeded the maximum amount permitted by the Rules. MI also admitted that on 12 occasions it had charged termination fees prior to, or in the absence of, written notice of termination having been given by the customers. **Link**

ACCC Allows Joint Marketing of Natural Gas from the North West Shelf Project

On 8 September 2010, the ACCC issued a decision allowing the partners in the North West Shelf Gas Project to jointly market and sell natural gas produced from the project to customers in Western Australia.

The ACCC had announced on 8 July 2010 its proposal to grant conditional authorisation to the partners. To address concerns about the potential for commercially sensitive customer information to be shared between competing gas projects in WA, the ACCC proposed imposing conditions to ensure adherence to robust ring fencing arrangements. The ACCC proposed granting authorisation until 31 December 2015, as some potential existed for the WA gas market to develop by this time, in particular

with the introduction of new sources of supply. The deadline for submissions was 30 July 2010. **Link**

Agreement between NBN Co and Telstra on Deployment of NBN

The Australian Government announced on 20 June 2010 that Telstra and NBN Co have entered into a Financial Heads of Agreement. This agreement facilitates the deployment of the National Broadband Network (NBN) by enabling NBN Co to reuse suitable Telstra infrastructure (including pits, ducts and backhaul fibre), thus avoiding unnecessary infrastructure duplication. It also provides for the progressive migration of customers from Telstra's copper and pay-TV cable networks to the new fibre network, providing for structural separation of Telstra. The ACCC will examine the competition aspects of this Agreement. The Government will progress a number of policy reforms to support the transition to NBN, including the establishment of a new universal service provider from 1 July 2012. Telstra, NBN Co and the Commonwealth agencies will now negotiate detailed Definitive Agreements to be put to Telstra shareholders and the government for final approval. **Announcement**

Government to Retain Retail Fixed-line Price Caps

The ACCC announced on 2 July 2010 that the Australian Government has released its proposed extension of price control arrangements, which applies price-caps on Telstra fixed-line phone calls and line rentals for a further two years. This follows a review of price controls completed by the ACCC, which recommended that the controls be extended by two years, and that their overall scope and composition remain unchanged. The proposed amendment will delay the expiry date of the price control arrangements to 30 June 2012. A more comprehensive review of pricing policy will be conducted in 2011 to assess the impact of the deployment of the NBN on the industry.

- **Determination**
- **Review of price controls**

Australian Energy Regulator (AER)

The Australian Energy Regulator's Proposed Amendments to the Roll Forward Model and Post-Tax Revenue Model

The AER has recently published proposed amendments to the roll-forward model and the post-tax revenue model (the PTRM) that will apply to future electricity transmission determinations. The AER expects to make its final decision on the proposed amendments for both the roll forward model and the PTRM in December 2010.
Proposed Amendments

AER Publishes Consultation Paper on CitiPower's and Powercor's Proposed Security Fee Scheme

On 28 June 2010, the AER released a consultation paper on CitiPower's and Powercor's proposed security-fee scheme for charging certain groups of new customers a security-fee, and the terms and conditions for such charges. A Distribution Network Service Provider may require a security fee where it fairly and reasonably considers there to be a risk that it will not recover the incremental revenue in relation to a connection offer. The deadline for submissions was 26 July 2010. **Consultation paper**

AER Publishes Retail Exemptions Issues Paper

The AER published in June 2010 an issues paper on its proposed approach to retail exemptions under the National Energy Retail Law and Rules, including proposed determinations of class exemptions. Under the proposed Retail Law, a person wishing to sell energy must hold a retailer authorisation or have an exemption from that requirement. The AER will be required to develop a guideline about retail exemptions, and develop classes of exemptions. The deadline for submissions on the issues paper was 2 August 2010. **Exemptions paper**

AER Publishes Final Regulatory Investment Test for Transmission and Application Guidelines

The AER published by 1 July 2010 its final regulatory investment test for transmission (RIT-T), application guidelines and a final decision setting out its reasons for decision and responses to submissions received on the AER's draft RIT-T and application guidelines. The RIT-T has replaced the existing regulatory test for transmission investments commenced on 1 August 2010. The purpose of the RIT-T is to identify the transmission investment option which maximises net economic benefits and, where applicable, meets the relevant jurisdictional or Electricity Rule based

reliability standards. The RIT-T provides a single framework for all transmission investments and removes the distinction in the regulatory test between reliability-driven projects and projects motivated by the delivery of market benefits.

- **Final decision**
- **Application guidelines**
- **Final regulatory investment test**

AER Issues Preliminary Positions Paper on the Framework and Approach for Aurora Energy

The AER released at the end of June 2010 a preliminary positions paper on the framework and approach for Aurora Energy, the electricity distribution network service provider in Tasmania. Aurora Energy's current economic regulator is the Office of the Tasmanian Economic Regulator (OTTER). The AER will be the economic regulator for the next distribution determination for Aurora Energy, commencing 1 July 2012 and is required to release a framework and approach paper by November 2010. The framework and approach paper will outline the likely classification of Aurora Energy's services, the form of control to apply to those services and the likely application of the AER's incentive schemes and guidelines to Aurora Energy. The deadline for submissions was 9 August 2010. **Preliminary positions paper**

Tribunal Reviews AER Electricity Distribution Determinations

On 2 July 2010, the AER announced that its May 2010 determinations regarding the respective electricity distribution networks owned by Energex, Ergon Energy and ETSA Utilities (the DNSPs) were the subject of an application for review in the Australian Competition Tribunal (Tribunal). The DNSPs sought review of the AER's decision regarding the value of imputation credits (gamma). Ergon Energy also sought review of aspects of its capital expenditure allowance, forecast customer service costs, demand forecasts, alternative control services (quoted services), the classification of street lighting services, the service target performance incentive scheme, and labour cost escalators. ETSA Utilities also sought review of the value of its opening regulatory asset base. **Review**

National Competition Council (NCC)

Draft Recommendations Allow For Queensland Railways to Operate Under the Queensland Rail Access Regime

The NCC, on 14 September 2010, released its draft recommendations on several applications that relate to third party access to rail infrastructure in Queensland.

The NCC is considering an application by the Queensland Government that certifies the Queensland Rail Access Regime as an effective access regime. Certification of the Queensland regime will mean that regulation of access to certain rail infrastructure, including the Central Queensland Coal Network (CQCN), will be subject to the Queensland Competition Authority (QCA) Act.

The NCC is concurrently examining a set of applications by Pacific National for the CQCN to be declared under the national third party access regime in Part IIIA of the Trade Practices Act (TPA). If the CQCN falls under the national access regime, any access issues that arise will be under the TPA, which is administered by the ACCC.

Upon reviewing applications and considering the first round of submissions from interested parties, the NCC proposes to recommend to the Commonwealth Treasurer that the Queensland Rail Access Regime be certified as an effective regime for a period of ten years. This means that the NCC will recommend to the Queensland Premier that the CQCN should not be declared and therefore should not fall under the national access regime.

The NCC is seeking submissions on its draft recommendations before finalising its recommendations. The closing date for further submissions is 14 October 2010.

- **Draft Recommendation**
- **Media Release (14 September 2010)**

Australian Capital Territory

Independent Competition and Regulatory Commission (ICRC)

ACT Greenhouse Gas Emissions Reduction Target Inquiry – Commission Submission on Cost Effectiveness Analysis

The ICRC, on 5 August 2010, announced it has been asked by the Legislative Assembly's Standing Committee on Climate Change, Environment and Water to expand upon the ICRC's June 2009

submission to the Standing Committee's draft report on its inquiry into ACT Greenhouse Gas Reduction Targets, and to provide further detail on the appropriate methodology to use in undertaking this analysis. This informed the ICRC's submission in July 2010 'Cost Effectiveness Analysis'.

The Standing Committee's draft report, released in October 2009, recommended that "the Government undertake social, environment and economic impact analysis of all policies and programs introduced to implement legislated targets and that this analysis be publicly available". The Government responded in agreement with this and recommended the establishment of a new role for the ICRC in providing independent advice on the robustness of the analyses. **Interim Report and the Government's Response**

ACT Electricity Feed-in Scheme Summary Report – June 2010 Quarter

The ICRC, on 30 July 2010, released a summary report on activity for the Electricity Feed-in Scheme for feed-in from renewable energy generators to the electricity network. The Scheme was established under the *Electricity Feed-in (Renewable Energy Premium) Act 2008 (ACT)* and commenced on 1 March 2009. The summary report covers this period to 30 June 2010.

The Electricity Feed-in Code is an industry code determined by the Commission under Part 4 of the *Utilities Act 2000* (ACT). The Code sets out practices and standards for the operation of the Scheme. Under the Code, licensed electricity suppliers and ActewAGL Distribution, the ACT's only licensed electricity distributor, are required to report quarterly to the Commission on a number of key indicators. **Summary Report**

Cotter Dam Water Security Project Investigation

The ICRC, on 30 June 2010, released its final report on its investigation of the Enlarged Cotter Dam water security project. On 19 November 2009, Attorney General Simon Corbell MLA referred an investigation to the ICRC of the projected costs and other matters of the enlarged Cotter Dam project to provide enhanced water security for the ACT.

- **Final Report**
- **Media Release (30 June 2010)**

Variation of Consumer Protection Code

The ICRC determined that from 1 July 2010 variations to the Consumer Protection Code under section 59 of the *Utilities Act 2000* would take effect. The substantive variations relate to clause 32 which sets out a requirement for the "informed consent" of a customer prior to the transfer of a customer's gas or electricity supply. A new clause 32A clarifies that the "informed consent" requirements do not apply when the transfer occurs as part of the sale of a company or its assets. Clause 32A requires that affected customers must be provided with certain information and assurances within a specified timeframe.

- **Consumer Protection Code (July 2010)**
- **Commission's letter to stakeholders**

New South Wales

Independent Pricing and Regulatory Tribunal (IPART)

Voluntary Transitional Pricing Arrangements for Supply of Natural Gas to Small Gas Customers

The IPART, on 23 July 2010, announced 1 July 2010 agreements with four suppliers continuing until 30 June 2013 the light-handed approach to Default Prices for Small Gas Customers that was established under the Voluntary Pricing Principles July 2001 to June 2004, and continued under Voluntary Transitional Pricing Arrangements July 2004 to June 2010.

- **Country Energy**
- **Actew AGL**
- **AGL Retail Energy Ltd**
- **Origin Energy Retail Ltd**

Final Report – Review of Regulated Retail Tariffs and Charges for Gas 2010-2013

The IPART, on 25 June 2010, released a final report reviewing the wholesale gas costs proposed by the Standard Retailers. Arrangements for regulating retail gas tariffs for small customers in NSW were due to expire on 30 June 2010. The NSW government decided to retain the option of regulated tariffs until at least 2013 and asked the IPART to put in place new arrangements for the 2010 regulatory period with the Standard Retailers for different parts of NSW; AGL, ActewAGL, Country Energy and Origin Energy. **Final Report**

Northern Territory

Utilities Commission

Review of Options for the Implementation of a Customer Service Incentive Scheme for Nothern Territory Electricity Customers

The Utilities Commission, on 23 August 2010, released the Final Report for the Review of Options for Implementation of a Customer Service Incentive Scheme for Northern Territory Electricity Customers. **Final Report**

Queensland

Queensland Competition Authority (QCA)

Final Decision on Application for Waiver of Ring-Fencing Guidelines by Ergon Energy

The QCA, on 13 April 2010, received an application from Ergon Energy applying for a waiver of section 1(b) of the Authority's Ring Fencing Guidelines, in respect of a 1000kW network support generator in the Barcaldine region. The application was made on the basis that the administrative cost of complying with the obligations would outweigh the benefit, or likely benefit, to the public. The QCA released its Draft Decision, which was to approve the application, on 20 May 2010. Submissions on the Draft Decision closed on 24 June 2010 and no submissions were received. Following consideration of Ergon Energy's application and in the absence of any submissions to the contrary, the QCA's Final Decision was to issue a notice under section 21 of the Guidelines to waive the requirement for Ergon Energy to comply with section 1(b) in respect of its Barcaldine network support generation site. All other provisions of the Guidelines continue to apply to the operation of the Barcaldine generation site. On 1 July 2010 responsibility for Ring-Fencing compliance transferred to the Australian Energy Regulator with the Guidelines and any existing waivers, including this one, remaining in force until the Australian Energy Regulator makes alternative arrangements. **Final Decision**

2010-11 Interim Price Monitoring of SEQ Water and Wastewater Distribution and Retail Activities

The Premier and the Treasurer have referred to the QCA for price monitoring from 1 July 2010 to 30 June 2013, the monopoly distribution and retail water and wastewater business activities of Queensland Urban Utilities, Allconnex Water and Unitywater. Under the referral, the QCA must:

a. provide timely and transparent information to customers about the costs and other factors underlying the annual increase in water and wastewater prices, including distinguishing the bulk and distribution/retail components; and

b. monitor the revenues of each activity over the interim regulatory period, based on the total costs of carrying on the activity.

The QCA must provide a Final Report for 2010-11 by 31 March 2011. For 2011-12 and 2012-13, the Authority must report by 31 December 2011 and 2012 respectively. The QCA invited submissions from interested parties by 31 August 2010.

2010 Draft Access Undertaking

The QCA approved in June 2010 QR Network's proposal to extend the term of the 2008 access undertaking and apply new reference tariffs to coal-carrying train services in the central Queensland coal region and the Western system. The proposal had been submitted on 11 June 2010. This June 2010 extension DAAU included tariffs and price-setting rules largely consistent with the June 2010 draft decision. It also extended the termination date, and introduced transitional arrangements relating to the division of ownership and responsibility for the network between QR Network Pty Ltd and Queensland Rail Ltd (formerly known as QR Passenger Pty Ltd).

On 28 June 2010, the QCA approved the June 2010 extension DAAU, so tariffs consistent with the Authority's June 2010 draft decision on the 2010 DAU apply in central Queensland and on the western system, back-dated to 1 July 2009. The remainder of the matters included in the 2010 DAU were to be dealt with in a subsequent decision to be released by the Authority.

On 9 September 2010, QR Network submitted a 2009-10 adjustment charge proposal to the QCA for approval. As part of its consideration of the proposal, written submissions from interested parties are invited by 1 October 2010.

- **Draft DAAU**
- **Adjustment Charge Proposal**

Dalrymple Bay Coal Terminal (DBCT) Access Undertaking Amendments and Activities

On 15 June 2006, the Queensland Competition Authority published its decision to approve DBCT Management's 2006 Draft Access Undertaking. The access undertaking sets out the terms and conditions under which DBCT Management will provide access to the terminal and also addresses the process required for an access seeker to negotiate access to the infrastructure and how any disputes in relation to access are to be resolved. In addition, once approved, aspects of the undertaking may be subject to amendment through a draft amending process under the **QCA Act**. Prior to any such amendments being approved or rejected, the Authority consults with stakeholders on these matters.

On 25 August 2010, BBI (DBCT) Management Pty Limited (DBCT Management) submitted a voluntary draft amending access undertaking (DAAU) seeking to revise the Annual Revenue Requirement (ARR), Revenue Cap and Reference Tariff for the Dalrymple Bay Coal Terminal, based on the actual costs of expanding the terminal from 68 million tonnes per

annum (mtpa) to 85 mtpa (phase 2/3 expansion). Submissions to the Authority in respect of the DAAU were due by 16 September 2010. In the absence of stakeholder submissions, the Authority will consider proceeding directly to a final decision on the DAAU. **Link**

DBCT Non-Expansion Capital Expenditure 2008-09

On 24 June 2010, the QCA made a final decision to approve the draft amending access undertaking (DAAU) for expenditure incurred on NECAP projects completed in 2008-09.

On 20 May 2010, DBCT Management submitted a draft DAAU seeking to adjust the Annual Revenue Requirement (ARR), Revenue Cap and Reference Tariff for the Dalrymple Bay Coal Terminal (DBCT), based on the expenditure incurred on non-expansion capital (NECAP) projects completed in the 2008-09 financial year. NECAP works are not designed to increase terminal capacity, but are undertaken to satisfy workplace, health & safety and environmental requirements or are beyond the scope of the operator's annual maintenance plan.

DBCT Management sought approval for expenditure of $11.1 million incurred on NECAP projects completed during 2008-09 financial year. As a result, DBCT Management proposed to increase the revenue cap by around $1.4 million per annum and to increase the terminal infrastructure charge by around $0.016 per tonne. DBCT Management proposed that the charge for 2009-10 be paid as a one-off payment, with the exact amount to be settled in consultation with the Authority. On 21 May 2010, the Authority published the DAAU on the Authority's website and invited submissions from stakeholders by 10 June 2010. No submissions were received. **Final Decision**

South Australia

Essential Services Commission of South Australia (ESCOSA)

Customer Information Requirements for the Energy Retail Market in South Australia – Draft Decision

On 7 September 2010, the ESCOSA released a Draft Decision following a review of the relevant information available to the state's energy consumers.

The energy retail sector in South Australia is contestable, meaning that all electricity and gas consumers are able to enter into retail market contracts with a licensed retailer of their choice. The ESCOSA believes that through their choices, consumers encourage businesses to compete and innovate. To promote competitive and fair market conduct in the energy retail market, the ESCOSA must ensure that its regulatory framework establishes and maintains a market environment in which consumers are not only aware of their ability to choose their electricity and/or gas retailers but also be confident to actively engage in the market process. An important factor for facilitating the ongoing competitiveness of the energy retail market is ensuring that consumers have access to relevant information necessary to allow them to actively participate in the market.

As a companion to the ESCOSA's 2010 Review of Retail Electricity Standing Contract Price Path Draft Inquiry Report and Draft Price Determination for the electricity standing contract price path to apply to AGL SA for the period 1 January 2011 to 30 June 2014, the ESCOSA is conducting a review of the current energy price disclosure requirements in its regulatory framework. The review is aimed at ensuring that energy consumers have access to relevant information to allow them to actively participate in the market. Feedback on the ESCOSA's Draft Decision is due 5 October 2010. A Final Decision will be prepared in November 2010. **Draft Decision**

Methodology for Setting Electricity Standing Contract Prices – Final Report

The ESCOSA released on 12 August 2010, the final report on the review of the methodology to be utilised in setting electricity standing contract prices for residential and small business customers from 1 January 2011. The report outlines the reasons for diverging away from the existing 'building block' approach and implementing a new hybrid cost-based and index-based approach to setting electricity standing contract prices. In addition, the report provides an overview of the RPM indexation methodology, including the necessary market assumptions and ongoing data requirements that will ensure the methodology best serves the long-term interests of South Australian consumers of electricity.

The report followed consideration of submissions received to the ESCOSA's March 2010 consultation paper that outlined the proposed Relative Price Movement (RPM) indexation methodology for setting electricity standing contract prices. In addition, the ESCOSA has received advice from the South Australian Centre from Economic Studies in relation to the proposed RPM methodology. **Final Report**

Competition in South Australia's retail energy market – Report on interviews with participants

On 15 July 2010, the ESCOSA released a report on in-depth interviews with 14 energy market participants, conducted in May 2010. In April 2010, the ESCOSA engaged ACIL Tasman to conduct interviews of South Australian industry participants to ascertain their views on the competitiveness of the South Australian retail energy market. The objective of the interviews was to identify common factors being experienced by licensed retailers and which were having an impact on the level of competition in the South Australian energy retail market. The ESCOSA will review the findings contained in the report, and provide a regulatory response where it is considered beneficial in the long-term interest of South Australian consumers with respect to the price, quality and reliability of essential services. **Report**

2010 Electricity Standing Contract Price Path Inquiry – Submissions Received

On 6 September 2010, the ESCOSA released a Draft Report and Draft Price Determination for its Inquiry into electricity standing contract prices for small customers in South Australia, to apply from 1 January 2011 to 30 June 2014. The Inquiry commenced in May 2010. Comment on this Draft Inquiry Report and Draft Price Determination is required by 4 October 2010. **Link**

Essential Services Commission of South Australia: 2010 Electricity Standing Contract Price Path Inquiry – Draft Decision

See Notes on Interesting Decisions.

Tasmania

Office of the Tasmanian Energy Regulator (OTTER)

Electricity Price Investigation – Draft Report

On 30 August 2010 the OTTER, pursuant to regulation 29 of the *Electricity Supply Industry (Price Control) Regulations 2003*, released the 'Draft Report of its 2010 Investigation of Maximum Prices for Declared Prices For Retail Electrical Services on Mainland Tasmania', which includes the Regulator's analysis and draft proposals for maximum retail electricity tariffs and retail special services prices. Submissions are invited by 30 September 2010. A Final Report will then be prepared, along with the 2010 Determination. **Draft Report**

Aurora Pay As You Go Price Comparison Reports

The OTTER has published the fourth ***APAYG Price Comparison Report*** that compares APAYG rates effective from 1 August 2010 with the standard regulated tariffs available for residential customers as at 1 July 2010. Aurora Pay As You Go (APAYG) is a prepayment option offered to residential customers as an alternative to electricity supply via the standard tariffs. The price comparison is based on the typical customer methodology established by the Regulator in his ***Information Paper Typical Electricity Customers, March 2006***. The methodology describes a set of typical customers based on consumption patterns and the combination of tariffs from which they are supplied. In simulating costs for typical APAYG customers a number of assumptions have been amended to take account of the differences between pricing structures for APAYG as compared to standard tariffs. APAYG rates differ between summer and winter, weekdays and weekends, and time of day.

Guideline – Regulatory Reporting

On 28 July 2010, OTTER issued the **Regulatory Reporting Guideline** along with a **Statement of Reasons** explaining the outcomes of public consultation (concluded on 23 June 2010) on the draft Guideline. This stemmed from the proposal that the Guideline be expanded beyond being specific to the electricity supply industry in Tasmania and to the regulatory responsibilities of the Energy Regulator, under the Electricity Supply Industry Act 1995 and the Tasmania Electricity Code, to include the gas supply industry and the water and sewerage industry.

Victoria

Essential Services Commission (ESC)

Implementation of the New Ports Price Monitoring Regime

On 18 August 2010, the ESC announced it had made the Price Monitoring Determination for Victorian Ports 2010, giving effect to the new price monitoring framework that will apply to Victorian ports over the five year period from 1 July 2010 to 30 June 2015. In December 2009, the Victorian Government responded to the ESC's 2009 Review of Victorian Ports Regulation supporting all but one of the ESC's recommendations. The Government's decision meant that the ESC had to amend the existing Price Monitoring Determination. **Final Decision**

Developing a Hardship-related Guaranteed Service Level Measure

The ESC, on 17 August 2010, announced that a working group comprising a range of stakeholders including the water businesses, consumer representatives, and Victorian Government Departments, was formed and met twice in March 2010, providing useful detail to inform the Commission's development of a hardship-related Guaranteed Service Level (GSL) measure.

During the 2009 metropolitan price review process the ESC suggested the following Guaranteed Service Level (GSL): *Restricting the water supply of, or taking legal action against, a customer in hardship who is complying with an agreed payment plan.* The ESC noted that the suggested measure was limited in that it did not provide an incentive for businesses to extend their hardship policies to eligible customers. Nevertheless, in light of approved price increases, and recognising that affordability would be an issue for some customers, the ESC determined that it would work with stakeholders on defining and implementing an effective hardship GSL measure.

Formal submissions were due to the ESC by 30 July 2010. The ESC will consider these and prepare an updated paper outlining its final position, by 30 September 2010.

- **Developing a Hardship Related Guaranteed Service Level Measure**

Melbourne Water's Special Drainage Areas – Price Review 2010-11

On 18 August 2010, the ESC announced that it had accepted an application submitted by Melbourne Water for 2010-11 prices for its special drainage areas under the annual review process as set out in clause 4.4 of the 2008 Melbourne Water Determination – Metropolitan drainage services and diversion services.

The ESC has assessed the price proposals in accordance with procedural requirements and pricing principles as set out in schedule 4.4 of the ESC's *2008 Melbourne Water Determination.* As part of the review, the ESC had engaged an independent consultant to assess the efficiency of proposed capital works expenditure at Tidal Waterways. The ESC is satisfied that the conditions in schedule 4.4 have been met.

- **Melbourne Water - Special Drainage Areas Charges for 2010-11**
- **2009 Review of Melbourne Water Patterson Lakes Tidal Waterways - Tidal Gates Project**

Western Australia

Economic Regulation Authority (ERA)

Notice – Draft Decision – Mid-West and South-West Gas Distribution Systems Revised Access Arrangement

On the 17 August 2010 the Economic Regulation Authority (ERA) issued its draft decision not to approve WA Gas Network's proposed revisions to the Mid-West and South-West Gas Distribution Systems access arrangement. The reasons for the ERA's decision are set out in the draft decision. The ERA requires WA Gas Networks to respond to the draft decision and provide revisions to its access arrangement proposal by 1 October 2010. Public submissions are invited by 29 October 2010. **Draft Decision**

Goldfields Gas Pipeline – Revised Access Arrangement

On 25 August 2010 the ERA published on its website two applications for review of the Goldfields Gas Pipeline (GGP) further final decision, released by the Authority on 5 August 2010. Based on the revisions proposed by Goldfields Gas Transmission Pty Ltd (GGT) to the access arrangement for the GGP, the Further Final Decision is not to approve the proposed revised access arrangement submitted by GGT on 4 June 2010. The GGP provides gas predominantly to the mining industries in the East Pilbara and the North East Goldfields region. The GGP also transports gas used to service households and small businesses in Kalgoorlie and Esperance.

Under the *Energy Arbitration and Review Act 1998,* the Western Australian Electricity Review Board will consider the 25 August 2010 applications for review in accordance with the *Gas Pipeline Access (Western Australia) Act 1998.*

The ERA considered that GGT's proposed revised access arrangement did not incorporate or substantially incorporate all the amendments required in the Authority's Final Decision or otherwise address to the ERA's satisfaction the matters identified in the Final Decision as being the reasons for requiring these amendments. Consequently, the ERA has drafted and approved its own revised access arrangement consistent with the requirements of the *National Third Party Access Code for Natural Gas Pipeline Systems* (Code). This access arrangement became effective on 20 August 2010.

- **Notice - Further Final Decision**
- **25 August 2010 Applications for Review**

Gas Compliance Reporting Manual – Energy Coordination Act 1994

The ERA, on 15 July 2010, approved the publication of the Gas Compliance Reporting Manual (Manual). The Manual has been revised to include the amendments to the *Compendium of Gas Customer Licensing Obligations*, also known as the *Gas Customer Code 2008*, that were approved by the Authority in June 2010. **Notice**

Western Power Invites Further Submissions on its Proposed Mid-West Energy Project

Western Power has now advised the Authority of its intention to invite further submissions on a revised options paper for the proposed Mid-West Energy Project (Southern Section), which includes details on the transmission assets to be constructed by Karara Mining Ltd. This second round of consultation closes on 29 September 2010. On 14 July 2010, the ERA announced that Western Power had invited submissions on its proposal to construct a new double circuit transmission line from Neerabup to Eneabba and a new terminal at Three Springs. Under the *Electricity Networks Access Code 2004* (Access Code) Western Power was required to consult with the public and interested parties about major augmentations to its covered network (the Western Power Network) and advise the ERA of its intention to do so. Pursuant to Chapter 7 of the Access Code, the ERA must publish Western Power's invitation for submissions on the ERA's website. This public consultation period has now closed. **Revised Options Paper**

Notes on Interesting Decisions

ACCC Grants Interim Approval to Wiggins Island Coal Producers

The ACCC has granted interim authorisation to permit coal producers to commence collective negotiations with the Queensland Rail (QR) Network (or any other QR Group entity or any entity that may acquire the relevant rail assets following the privatisation of QR Network) for access to its Moura and Blackwater rail systems. The transportation of coal to the new Wiggins Island Coal Export Terminal at the Port of Gladstone in Queensland requires access to the below rail systems operated by Queensland Rail.

In particular, the applicants sought authorisation to engage in collective bargaining with QR for the purposes of negotiating price and non-price terms and conditions for access to the below-rail system. The negotiations for access to the rail system are to include: all expansions to these systems; access to any other rail infrastructure necessary to support the Terminal; below rail infrastructure to support the relocation of capacity from Barney Point to the Terminal and RG Tanna Coal Terminal; and all services relating to access for the purpose of transporting coal to the Terminal (the 'Identified Rail Infrastructure and Services').

The coincident investment in the coal mines and port facilities requires complementary access to the below rail system. That is, development of the mines in the region will coincide with a multi-stage construction of the new export terminal over several years. And to support stage 1 of the terminal's development, Wiggins Island producers need to secure rail access. The interim authorisation is only granted in relation to the stage 1 negotiations, and any access agreement that is concluded between the parties require final authorisation of the ACCC.

In general, authorisation provides immunity from court action for conduct that might otherwise raise concerns under the competition provisions of the *Trade Practices Act 1974*. That is, more broadly, the ACCC may grant an authorisation when it is satisfied that the public benefit from the conduct outweighs any public detriment. Interim authorisation allows the parties to engage in the conduct prior to the ACCC considering the substantive merits of the application. **Link**

ACCC Imposes Penalties and Secures Compensation Under Water Termination Fees Rules

The ACCC has agreed to accept a court enforceable undertaking from Murrumbidgee Irrigation Limited (MI) and issued it with three infringement notice penalties, totalling $66,000, following multiple breaches of the *Water Charge (Termination Fees) Rules 2009* (the Rules).

MI is one of the largest irrigation infrastructure operators in the Murray Darling Basin – it owns and operates infrastructure that services more than 3,200 properties in New South Wales.

Following an investigation by the ACCC, MI has admitted that it breached the Rules. MI admitted that in 27 instances it charged termination fees that exceed the maximum amount permitted by the Rules. MI also admitted that in the absence of, or prior to, written notice of termination, it has on 12 occasions charged its customers termination fees.

In response to ACCC concerns, MI has ceased imposing termination fees that do not comply with the Rules and has voluntarily refunded $640,000 in total to affected customers. The refund includes the amount of the overcharge and interest on the overcharge.

During the course of its investigation, the ACCC expressed concern about the number of separate breaches of the Rules, the size of the amounts MI overcharged its customers and MI's failure to address the ACCC's concerns when contacted by the ACCC.

The decision by the ACCC to give MI three infringement notices reflects the seriousness of MI's conduct. In addition to agreeing to accept a court enforceable undertaking from MI, the ACCC issued its first infringement notices under the *Water Act*.

While the ACCC has indicated that all irrigation infrastructure operators are under warning that it will take strong enforcement action if there are continuing breaches of the Rules, the ACCC acknowledged that the Rules are new and that MI paid refunds to all affected customers.

Under the Rules, irrigation infrastructure operators may charge termination fees to customers or irrigation operators where they have given written notice of termination. The Rules cap termination fees at ten times the amount of the total network access charge payable by a customer for the year in which notice of termination is given. The Rules on the termination fees are designed to balance the interests of those irrigators that wish to exit an irrigation district and those that wish to remain.

MI provided an undertaking, committing the irrigator to implementing a compliance program which ensures that the termination fees charged to exiting customers do not exceed the maximum amount authorised by the Rules. **Link**

New Zealand Commerce Commission Draft Decision: Reset Default Price-Quality Path to Include a Revenue Differential Term

On the 13 August 2010, the New Zealand Commerce Commission released its consultation paper with a draft decision to amend the default price-quality path (DPP) for electricity distribution businesses (EDBs) by including a revenue differential term. The amendment is for the period 2010 to 2015.

EDBs provide electricity lines services between Transpower (which owns and operates New Zealand's high-voltage electricity grid) and end-users. All EDBs, except for those exempt on the basis of consumer ownership as defined in section 54D of New Zealand's *Commerce Act 1986*, must comply with the DPP set by the Commission.

A DPP sets the maximum prices or revenues that suppliers can charge within a framework that defines the standards for quality of services. Electricity distribution businesses may apply to the Commission for a customised price-quality path if their circumstances do not reflect the default price-quality profile.

The objective of the DPP is to promote the long-term benefit of consumers through lower prices and higher quality. That is, the DPP is designed so that suppliers have incentives to innovate and invest, improve efficiency, and share efficiency improvements with consumers and limit the ability of EDBs to extract excessive profits.

Under the DPP suppliers are allowed to increase annual prices by an allowed rate of change. The allowed rate of change is equal to the annual change in the Consumer Price Index (CPI) that is published by Statistics New Zealand. The 2010–2015 DPP, which took effect in April 2010, set the maximum allowable revenue for each supplier in the form of a compliance assessment formula. The formula is currently specified so that a supplier's maximum allowable revenue in a given year is derived using the prices it charged in a previous period.

For the period 1 April 2010 to 31 March 2015, the determination sets out that all EDBs (with the exception of those that are consumer owned) will:

- have starting prices that are equal to actual prices on 31 March 2010;
- be subject to an X-factor of zero per cent per annum; and
- have quality standards based on reliability and expressed as annual System Average Interruption Duration Index (SAIDI) and System Average Interruption Frequency Index (SAIFI) limits.

The effect of these decisions is that EDBs will be allowed to increase prices by the rate of inflation whilst the quality of supply to consumers is maintained.

Included in the DPP compliance formula is a revenue differential term. The proposed revenue differential term modifies the formula to separate the relationship between a supplier's maximum allowable revenue and the prices it charges during the regulatory period. The revenue differential term will return any EDBs breaching their price path back to the level of allowed revenues and allow any EDBs pricing below their price path to restore prices to their price path.

The Commission published its draft decisions on input methodologies for electricity distribution services on 18 June 2010 and the corresponding draft determinations on 2 July 2010. The paper also includes the Commission's initial views on the effects of the forthcoming GST increase on the Consumer Price Index as used to index the 2010-2015 DPP, and potential changes to the 2010-2015 DPP to reflect the draft input methodologies. The Commission is currently consulting on the potential effects of the forthcoming GST increase on the DPP.

- **Link**
- **Draft Decision**

The New Zealand Commerce Commission's Draft Report Recommends Telecommunications Resale Deregulation

On 26 August 2010, the New Zealand Commerce Commission released its draft report into whether the services that New Zealand Telecom provides to other telecommunications companies to be resold should remain subject to the *Telecommunications Act 2001*.

Resale services are retail services that Telecom provides on a wholesale basis to other telecommunications service providers. The resale services are provided commercially by Telecom's wholesale division and, as part of Telecom's fixed line communications network, they include:

- retail services
- residential local access and calling services
- any bundle of retail services, and
- retail services offered as part of a bundle.

Since resale services are subject to the *Telecommunications Act*, if wholesale customers are unable to agree commercial terms with Telecom, they can request that the Commission determine the price and non-price terms and conditions for the supply of these services by Telecom.

In the Commission's preliminary view it stated that, given low take up and availability of alternative

services, wholesale broadband services, business data services and bundled resale services should not be subject to the *Telecommunications Act*.

The Commission also considered that in areas where there is a significant take up of specific resale services and limited availability of substitutes to Telecom services (for example, residential and business lines and smart phone services, like Call Minder), these services should remain subject to the *Telecommunications Act* so that, if commercial negotiations were to fail, these services would continue to be provided by Telecom.

The Commission's view is that where there is considerable effective competition or when there are alternative services available to access seekers, regulatory intervention in telecommunications should be reduced. The Commission considers that its objective is to scale back regulation of telecommunications markets as effective competition develops and that regulation should not impose or maintain burdens that are unnecessary.

Under Schedule 1, Part 2, subpart 1 of the *Telecommunications Act*, retail services are designated access services. On 1 October 2009, the Commission announced that it had decided to investigate whether or not resale services should be omitted from Schedule 1 of the *Telecommunications Act*. If the Commission considers that they should not be omitted, the Commission would consider whether or not should they be amended in some form.

Under Schedule 3 of the *Telecommunications Act*, the Commission can commence an investigation into whether or not the list of regulated telecommunications services contained in Schedule 1 of the Act should be amended or omitted. In other words, the Commission can determine whether regulated telecommunications services can be amended by adding a new service, a regulated service or services can be omitted, or a regulated service or services can be amended in terms of an existing service. Under Schedule 3, the Commission can also investigate whether a specified telecommunications service should become a designated telecommunications service (that is, should become a service where the price and non-price terms and conditions can be set by the Commission). On the basis of its investigation, the Commission then makes a recommendation to the Minister for Communications and Information Technology. **Link**

Essential Services Commission of South Australia: 2010 Electricity Standing Contract Price Path Inquiry – Draft Decision

On 6 September 2010, the Essential Services Commission of South Australia released a Draft Report and Draft Price Determination for its Inquiry into electricity standing contract prices for South Australian small customers. The Draft Price Determination is to apply from 1 January 2011 to 30 June 2014.

Small customers (residential and small business customers) who have not entered into a market contract with their retailer of choice fall under the standard contract. The standard contract applies to approximately 27 per cent of small electricity customers. AGL South Australia is the declared electricity standing-contract retailer for this State.

During its Inquiry, the Commission reviewed various key cost components of electricity retail services, including wholesale energy costs, retail operating costs and the retail margin. The review had regard to the price path proposed by AGL South Australia (that was subsequently released for public consultation) and advice from independent experts on the cost projections.

The Commission's Draft Price Determination proposed that the standing contract price be equivalent to $233.75/MWh from 1 January 2011. This proposed standing contract price comprises of a retail component of $132.99/MWh, and the remaining 43 per cent of the price reflects the electricity network charges – as determined by the Australian Energy Regulator. The retail component of Draft Price Determination is approximately 3 per cent less than the amount proposed by AGL South Australia – if allowance is made for AGL South Australia's incurrence of costs via the Residential Energy Efficiency Scheme.

The Commission estimates that from 1 January 2011, its Draft Price Determination will increase the annual electricity bill by approximately 7 per cent for a typical residential standing-contract customer who consumes 5 MWh per annum (inclusive of network charges).

At the start of each financial year in the period 1 January 2011 to 30 June 2014, the Commission will adjust the standing contract price in response to any movement in market contract prices. However, only market contract price movements within a Commission-specified price floor and price ceiling will inform the subsequent adjustment of the standard contract price.

On releasing its Draft Price Determination and Draft Inquiry Report, the Commission invited comment from interested parties. Submissions are due by 4 October 2010. **Draft Decision**

Regulatory News

2010 ACCC Regulatory Conference

The Regulatory Conference for 2010, 'Market Structure Revisited' took place on 29 and 30 July 2010 at the Gold Coast, attended by 460 delegates. All the sessions provided high-quality presentations and discussions. Planning for the 2011 conference has now commenced. **Conference papers and slides**

Evaluating Infrastructure Reforms and Regulation: A Review of Methods

It is now 15 years since the introduction of National Competition Policy reforms. The question of 'what has been the impact of economic regulation on Australia's infrastructure industries' and the related question 'what can be learned from this'? are obviously very significant issues for government and the community. However, before any assessment can be made a major hurdle has to be jumped. That hurdle revolves around selecting the 'right' evaluation method. This working paper aims to provide a comprehensive coverage of the issues that can arise, and the methods that can be used, in conducting *ex post* evaluations of competition, institutional and regulatory reforms affecting economic infrastructure in seven key areas: energy, communications, water and wastewater, post, rail, airports and ports. The paper draws upon research in the academic literature as well as that of public bodies and other organisations that have conducted such evaluations in the past. The paper explains the economic basis for reforms in infrastructure areas, discusses the evaluation process and the difficult issue of how to approach the counterfactual problem. It then reviews a number of techniques that can be used to evaluate competition reforms – social cost benefit analysis, computable general-equilibrium modelling, econometric analysis, productivity studies and qualitative methods. A number of conclusions are then drawn, including that the approach to evaluation will depend critically on the starting question and that trade-offs will inevitably be required between the theoretically ideal approach and that which can be taken in practice. The working paper has been developed to help encourage future evaluations of competition, institutional and regulatory reforms. **Methods working paper**

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