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Challenges for the Economic Regulation of Infrastructure

Cristina Cifuentes[1]

Infrastructure regulation has arguably being a feature of economic and social life since human beings first began to devise communal rules for sharing the resources that were available to them, be they caves in which they sheltered, fires for warmth and cooking, or tools and weapons. Shared infrastructure was essential for the survival of the community, and the rules around its use provided the foundation for efficient and equitable outcomes aimed at maximising the economic and social welfare of the group.

Fast forward quite a few thousand years and the basic issues of infrastructure regulation remain largely the same. Infrastructure continues to play a very important role in delivering economic and social benefits and the regulatory regimes that apply are often the main interface between infrastructure owners and operators and the community they serve. It follows that a robust regulatory framework is an essential feature of maximising the potential for regulated infrastructure to deliver on these economic and social outcomes.

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Given the complex nature of infrastructure decisions, the institutional settings within which these investments take place will be a crucial determinant of their success. Arrangements for infrastructure regulation face challenges such as the impact of rapidly evolving technology and the seemingly, at times, disparate requirements of government policy makers, investors, infrastructure managers and consumers. These challenges are common to many countries and across different regulated industries. In Australia, recent work examining regulatory best practices for the economic regulation of infrastructure has included the Australian Energy Regulator's (AER) Better Regulation program. The OECD is also addressing a range of matters relating to infrastructure regulators. The OECD's Regulatory Policy Committee (RPC) and its subsidiary body, the Network of Economic Regulators (NER) provide a platform to help countries in building and strengthening their regulatory reform tools and institutions through design, application and enforcement of better rules.

These challenges give rise enduring and new questions such as:

- Why do we regulate?
- Are current regulatory regimes capable of dealing with rapidly changing technology and new areas of potentially contestable economic activity or are they potentially stifling innovation and competition?
- What is the interplay between a body as economic regulator, a consumer-protection agency and an industry/market enforcement agency, and are these roles compatible?
- How can regulatory frameworks deliver on competing objectives via processes which are timely and efficient but thorough, responsive to, and inclusive of consumer needs, predictable and open to review?
- What is the role of the regulator in the investment decision governance framework and what is it that investors need from the regulatory regime?

[1] Cristina Cifuentes is a Commissioner of the Australian Competition and Consumer Commission and a Board Member of the Australian Energy Regulator. Prior to these roles Cristina served as a member of the NSW Independent Pricing and Regulatory Tribunal.

- How do we measure the effectiveness of our decisions and impact on infrastructure provision?

This is an evolving area of thought and practice and involves consideration and active participation in the debate, not just by regulators but by governments, regulated industries, consumers as well as independent research and advisory bodies. Although this article draws mainly from recent experience in the energy sector in Australia, many of the issues apply across other regulated infrastructure sectors.

Objectives of the Economic Regulation of Infrastructure

Internationally the role or objectives of economic regulators of infrastructure tends to include one or more of the standard economic objectives of achieving economic efficiency, encouraging investment, promoting competition, mitigating monopoly power, allowing cost recovery and protecting the interests of consumers. In some cases regulators are also required to consider broader social, environmental and industry development objectives in making their regulatory decisions. (Albon and Decker 2015, p. 22).

Many of the standard economic objectives should be consistent with the overall objective of achieving economic efficiency as in many cases it may be possible for an economic regulator to align these objectives in practice. However, as noted by Decker (2010, p. 2) there might, for example be a conflict between a regulatory decision designed to encourage long-term investment and one to promote the interest of consumers which may have a much shorter time horizon. For the regulators of Australian energy and communications infrastructure these two objectives are arguably made more compatible by the legislative objectives, which make reference to promoting efficient investment in infrastructure and the long-term interests of consumers.[1]

Whilst it's desirable for economic infrastructure regulatory frameworks to have the achievement of economic efficiency as a central aim, this is not to suggest that other issues should not be considered. For example, low-income consumers may not be able to afford significant price rises which may be required to underpin new investments and may need additional protection or assistance. A question is whether or not this should be a decision for the economic infrastructure regulator?

Standard economic theory supports the view that policy objectives relating to issues such as social equity, environmental protections and industry development are more properly delivered through appropriate, transparent and accountable mechanisms, than embedded in economic regulatory decisions. This is because their inclusion introduces objectives that may be in conflict with the main regulatory task of promoting economic efficiency. This can: reduce regulatory effectiveness; increase regulatory uncertainty and risk; and potentially compromise regulatory independence (Decker 2010).

Moreover, economic regulators are arguably not well placed to give effect to these policy objectives to the extent that they involve subjective judgements on policy – or trade-offs between these other objectives and economic efficiency. The existence of separate legislation, regulations and government agencies or departments with a focus on these matters will allow governments to make the appropriate trade-offs (for example, via the level of funding for social programs and the strength of other regulatory controls on business) and likely see both the efficient economic regulation of infrastructure and these other objectives delivered in a more efficient and expert fashion.

Changing Market Structures and Appropriate Regulatory Frameworks

Having a clear objective is a fundamental aspect of the efficacy of a regulatory regime and a regulatory regime has to be 'fit for purpose' given the stated objectives.

In this context, there has been a great deal of commentary recently on 'disruptive' technologies and innovative forms of competitive activities (such as the shared economy, substitutable digital communication, and alternative energy supply and storage models) and how these may shape the future direction of regulation. Traditional service and product markets are rapidly evolving in response to changing consumer preferences.

This is driving a redefinition of where the lines are drawn between functions that are subject to economic regulation and those that can be provided through competition. This raises the question of whether current regulatory regimes, based on traditional market models, are capable of dealing with these forces, or are they potentially stifling innovation and competition?

The starting point for examining this is the proposition that consumers themselves are increasingly driving change and they are in the best position to decide what they need and want, the way in which those demands should be met, and who should meet them and on what terms and prices. Ideally, the new

[1] *National Electricity (South Australia) Act 1996* s. 7, *National Gas (South Australia) Act 2008,* s.23 and *Competition and Consumer Act 2010* s.152AB.

products and services that are developing to meet consumer demands should be provided through contestable markets. Contestable markets are more likely to be innovative, to allocate risk to those best able to manage it and to meet consumer expectations.

The key proviso to this is that consumers must have confidence and trust in the ability of the market to do this. Where there remains a potential for likely market failure and public detriment, there remains a need for consumers to be protected through appropriate regulation.

In the context of infrastructure assets, the need to separate natural monopoly and potentially competitive activities remains an enduring concern. Without this separation, there is a risk that a regulated service provider may confer an unfair advantage on an affiliate operating in a contestable market by engaging in the following types of anti-competitive behaviours:

- cross-subsidising an affiliate's services in the contestable market with revenue derived from its regulated services;
- providing an affiliate with access to commercially sensitive information acquired through the provision of regulated services; and/or
- restricting the access of other participants in the contestable market to the infrastructure services provided by the regulated entity, or providing access on less favourable terms than its affiliate. Importantly, even if access is not misused, the potential for it to happen may deter efficient new entry.

A regulated business may also have certain efficiency advantages in the provision of a contestable service due to comparative advantage stemming from, for example, the scale and scope of its monopoly activities.

In this context, a fit-for-purpose regulatory framework is one which: is responsive to innovative forms of competitive activities; optimises the ability of regulated monopolies and emerging players to offer services in contestable markets in a way that benefits consumers; and protects consumers from potential or likely market failures. From this perspective, a 'level playing field' between monopoly infrastructure owners and other potential providers is essential if competition in contestable services is to be promoted. Long-established regulatory tools, such as structural separation and ring-fencing guidelines, remain an enduring part of the regulatory landscape.

The emergence of these new activities and the centrality of consumers in driving these changes bring along with them a blurring of the traditional boundaries of regulatory roles – economic regulation, consumer protection and enforcement – and whether the needs of the community are better served through industry and role specific regulators or multi-function and cross sectoral bodies.

Prima facie, this will reflect the specific objectives of the regulatory framework in question, but at the heart of regulation is an essential public interest objective – making markets work efficiently for the benefit of consumers. Thus, in a broad sense, these three functions should be compatible and the issue of whether this is best provided through a multi-function/multi sectoral body or function/industry specific framework is far from clear.

Models of independent economic infrastructure regulation across OECD countries include industry-specific, sector-specific (multi-industry), multi-sectoral and integration of all areas of infrastructure regulation within a national competition authority. Advantages in regulators covering a range of industries or sectors may include: less prospect of industry capture; regulatory consistency; appreciation of economic linkages between industries in a sector; and organisational economies of scale and scope. Disadvantages might include less prospect of agency-specific experimentation or testing of ideas within separate regulators that might be subsequently adopted more broadly if successful, or that regulatory errors will be spread more widely (Albon and Decker 2015 pp. 23, 25-26).

Most OECD countries have a number of sectoral regulators and there has been a trend towards the conglomeration of industry regulators to sectoral regulators as infrastructure regulatory regimes have evolved over the past 10 or 15 years (Albon and Decker p. 23). The existence of single multi-sectoral regulators, outside or integrated with the national competition authority is relatively unusual.

Several of the advantages of multi-industry or sector regulators apply for the regulator as a combined economic regulator, consumer protection and an enforcement agency. However such integration will likely require the acceptance of an overarching common objective, such as the promotion of economic efficiency. As technological change serves to break down natural monopolies as is happening in telecommunications and electricity markets, the argument for a multi-functional regulatory agency is perhaps made stronger to the extent it enables a wider perspective on the virtues of such changes for consumers and increases receptiveness to the adoption of alternative regulatory treatments.

Australia and New Zealand are early examples of combined economic regulatory, competition and consumer regulators and it is telling that this model was recently adopted by Spain and the Netherlands, both of which previously had separate agencies, including separate sectoral regulators (Albon and Decker 2015, p. 27).

Regulatory Processes and Engagement – Australian Energy Regulation in Focus

The regulatory regime for energy in Australia has undergone significant change prompted by a desire to improve the capability of the framework to deliver better outcomes in the long-term interests of energy consumers.

The Australian Energy Regulator's (AER) 'Better Regulation' program followed from changes made to the National Electricity and Gas Rules by the Australian Energy Market Commission (AEMC). These changes were accompanied by reforms to the Limited Merits Review framework (Office of Best Practice Review, 2013).

As part of the Better Regulation program, the AER, in extensive consultation with industry participants developed a series of guidelines outlining its intended approach to assessing proposed capital and operating expenditure, the rate of return and consumer engagement.

Despite these initiatives, the assessment process remains lengthy, complex and detailed and as a consequence is more time and resource intensive than ever. The adversarial element of the regulatory process remains and in some respects is being seen as a 'business as usual' step rather than a last resort feature of the process.

The AER's revenue determinations for network businesses (NSPs), from first instance of developing the 'framework and approach' (F and A) consultation paper to final determination, generally takes around two years. This does not include any time period for subsequent appeals to final decisions or any re-working of decisions that might come about as part of judicial or merits review. The regulatory control period is generally five years. The F and A is followed by data requests, detailed, lengthy and often highly technical proposals from the NSPs, AER issues papers for comment, consultation with stakeholders, further information requests if necessary to clarify the proposals, a draft determination, a revised revenue proposal from the NSP, further information requests and consultation and a final determination. The AER's decision document itself can run into multiple hundreds of pages.

Given the centrality of consumers in driving change, an essential element of the regulatory process is the need for effective stakeholder and consumer engagement. Done properly, this should promote informed decision making and transparency and enhance stakeholder confidence in regulatory development and implementation. Consultation should be inclusive, deliberative and begin at the earliest possible time when proposals are being formulated and where there is scope to influence the policy outcome.

Amongst other things, the AEMC rule changes required that the AER look to ways to improve consumer participation in the determination process. As part of this, the AER:

- developed a consumer engagement guideline setting out its expectations for energy network service providers to better engage with their consumers with the aim of service providers better aligning their services with consumers' long term interests;
- established a Consumer Reference Group to make it easier for consumer representative groups to have input into the Better Regulation consultative process without necessarily writing formal submissions; and
- established a Consumer Challenge Panel (CCP) within the AER, the role of which is to provide an independent consumer perspective to challenge the AER and network service providers during determination processes.

The NSPs also spent considerable time and financial resources in their customer engagement strategies, including: setting up consumer consultative groups; running consumer forums; undertaking willingness to pay and other consumer preference surveys; and meeting with consumer groups and the CCP.

However as part of its revenue reset assessment process, the AER found that, in some instances, consumer engagement had not been effective. This was supported by the advice presented to the AER by the Consumer Challenge Panel. The OECD's 2015 Regulatory Policy Outlook noted that, whilst OECD countries are looking at various ways to engage stakeholders in making, implementing and reviewing regulations, there are nonetheless doubts as to whether these engagement strategies are actually meeting their goals.

It would appear that part of the problem is not that there is any lack of information. Rather, there appears to be too much information and with such complexity that consumers are finding it difficult to engage in any meaningful way. This might reflect the

fact that consumers may not understand the decision making process and the information provided to them is not clear enough. Despite endeavours to use plain English and summarised consultation documents with explanations and targeted questions, because of the nature of the issues, many documents still use complicated language that makes it difficult for the wider public to express their opinions.

A prime example of this is the discussion on the appropriate rate of return (ROR) in the energy reset decisions. The ROR accounts for up to 60 per cent of network revenue making it a substantial factor in the prices consumers ultimately pay for the energy. To help consumers and consumer groups to participate in its consideration of the issue, the AER provided on its website issues papers, fact sheets and guidelines as well as running public forums and information sessions for consumer groups on the relevant issues and its approach to assessing the ROR.

The contribution of the CCP and other consumer representative groups in putting forward a consumer perspective on the ROR was invaluable. However, the highly technical nature of the positions raised by the NSPs in their revenue proposals and as a consequence, the AER's response to those submissions, does raise the question about the ability of ordinary consumers to engage in any meaningful way in such processes.

Submissions to the AER's determinations on the ROR for the businesses in New South Wales and the Australian Capital Territory ran to around 18,000 pages with over 200 consultant reports, academic papers, and other material. The submissions were undisputedly of a very complex, technical and legal nature. The AER's assessment on the ROR (and gamma) ran to round 650 pages. The AER's decisions on the ROR were subject to appeals under the Limited Merits Review framework to the Australian Competition Tribunal (ACT) by the NSPs, and by the Public Interest Advocacy Centre on behalf of consumers. The ACT decision ran to over 300 pages.

A key aspect then facing policy makers and regulators is whether the increased complexity and length of the process has resulted in materially better outcomes. The difficulty in assessing this is that the decisions are by their nature often incremental and long term in their impact. Isolating the effect of the decisions can border on the impossible given that outcomes are often influenced by factors outside of the decision itself, for example, changing technology, general economic conditions, consumer responses and the interaction with other government policies.

Market Structure and Investment Issues

Given the long-term impact of regulatory decisions, it is a natural response of industry participants to ask whether regulators have a role beyond implementing the policies that other arms of government decide upon and design. Put another way, should regulators be actively involved in developing a strategic vision for infrastructure and use their decisions to more actively influence market structure/design?

There is no doubt that there is room for regulators to participate in the industry debate and policy makers' processes for developing and implementing regulatory programs. Advocacy and market studies are a central aspect of this. The ACCC, for example, has argued that advocacy is complementary to its functions as a competition agency and that market studies can be integral in enabling it to perform its enforcement and other activities (ACCC, 2014, pp. 89-91). In many countries, competition advocacy and market studies are a legislated aspect of their competition regulators' functions, which applies only to a limited extent for the ACCC.

However, it is questionable whether the economic regulator should be able to go a further step and determine market structure, such as by specifying how many competitors there should be in a market and/or their market shares. This determination of market structure does occur, at least in part, in the case of a competition agency where it is required to make decisions on mergers and acquisitions. However, this power tends to be reactive rather than pre-emptive to market activity. By contrast, in overseeing an access regime, an infrastructure regulator need not have in mind a target number of access seekers to enter the market, but rather to determine suitable terms and conditions under which entry of an unspecified number of access seekers can occur. Nevertheless, there may be decisions within the regulatory remit of particular regulators where a neat distinction of its role is not as straightforward to make, such as in deciding whether certain infrastructure should be treated as a natural monopoly for regulatory purposes.

However, it should not be the role of the regulator to 'pick winners' either in terms of approving specific infrastructure projects or structuring regulation to favour particular technologies. This reflects the 'moral hazard' potential of regulators giving an implicit tick to investments put forward by regulated entities, and replacing the capital markets (shareholder and debt providers) in investment decisions.

In the context of economic regulation and revenue proposals in the energy sector, the role of the AER is

not to 'approve' specific projects proposed by the NSPs, but to address the issue of prudency and efficiency of forecast expenditure (operating and capital) and to set the revenue that NSPs may recover from consumers to reflect the assessed forecast. Decisions on prioritising individual projects given the overall revenue allowed to be recovered remain the responsibility of the NSP.

This has implications for investor expectations and needs from the regulatory framework.

At the outset it is notable that, in Australia at least, there would appear to be no lack of appetite for investing in a range of infrastructure, regulated or otherwise, across a number of industries.

The recent sale of the 99-year lease of one the electricity transmission business, Transgrid, attracted strong investor interest. The $10.3 billion (US$7.5 billion) auction was won by a consortium led by Hastings Funds Management (Hastings) and backed by Middle Eastern and Canadian investors (NSW Government Media Release), beating rival bids backed by State Grid of China and Australian and Canadian pension funds.

Other recent infrastructure investment transactions of note include:

- the sale in 2015 of the Iona Gas Storage Facility to the Queensland Investment Corporation (QIC) for $1.78 billion;
- the sale in 2014 of a 98-year lease on the Port of Newcastle, the world's biggest coal port, to a consortium of Hastings and China Merchants for $1.75 billion (NSW Government Media Release); and
- the sale in 2012 of a 50-year lease of the Sydney desalination water plant to Hastings and the Ontario Teachers' Pension Plan for $2.3 billion(see here).

Governments around Australia are exploring further opportunities for private sector investment in, and management of economic infrastructure. The NSW Government is currently considering proposals to lease just over 50 per cent of electricity distribution businesses Ausgrid and Endeavour. Similarly, the Australian Government (Finance Minister 26 February 2016) is considering options for the management of the Australian Securities and Investments Commission (ASIC) Registry including the development of value-added products and services and the future management, operation and ownership of the Australian Rail Track Corporation. The Australian Government is also currently considering public and private sector options to develop the inland railway between Melbourne and Brisbane.[2]

In telecommunications, we are seeing significant expansion by network operators of their various networks. Over the past couple of years Optus, Telstra and Vodafone Hutchinson (VHA) all made significant investments in their 4G mobile networks (which deliver higher quality data services than 3G networks), and on radiofrequency spectrum. For example, in the 2014 Digital Dividend auctions, Telstra and Optus both acquired 700 megahertz (MHz) and 2.5 gigahertz (GHz) spectrum, investing around $650 million and $1.3 billion respectively. Further, in the recent 1800 MHz spectrum auction Optus, Telstra, VHA and TPG all acquired spectrum, spending between $68 million and $196 million. Optus states that it invested over $1.5 billion in its mobile network, including on: acquiring spectrum; expanding 4G coverage; boosting capacity; and switching on new mobile towers.[3] Telstra (Annual Report 2015, pp. 6, 23) states that it invested $1 billion in its mobile network over 2014–15 and that it will invest $5 billion in its network over the three years to June 2017. VHA (Annual Report 2014, p. 4) also continued to invest in its mobile network, making improvements to its core network and expanding its 4G coverage.

In ports we are seeing ongoing investment by wheat port operators and stevedores in new technology and facilities and in airports.

Arguably given the importance of ongoing investment in infrastructure, the two most important considerations for investors would be an appropriate rate of return on investments and certainty of regulatory arrangements by which is meant predictability of regulatory arrangements and processes rather than certainty of regulatory outcomes.

Whilst this might seem like a fine distinction, actual regulatory outcomes will depend on a range of external factors such as prevailing market conditions in the case of cost of capital decisions, the relative efficiencies of businesses in terms of capex and opex in revenue decisions or the state of competition in the case of access or declaration of services.

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[2] The ARTC provides a 'one-stop' shop for operators seeking access to the national interstate rail network, and is responsible for the management, capital investment, infrastructure maintenance, and sale of train operator access across the ARTC network.

[3] See: Optus Media Release, 'Optus boosts Ballarat mobile reliability and data speeds', 20 October 2015.

The regulatory regime and process however should be well established, well understood and transparent. It should be applied consistently but with enough flexibility to take into account new or emerging circumstances. There should be a robust consultation period during which the approach to regulation will be discussed by the regulator and industry participants and the resulting framework and expectations will be clear so that informed investment decisions can be taken.

The AEMC Rule changes gave the AER greater discretion to question the NSPs expenditure forecasts and wider scope for determining the appropriate rate of return. The AER consulted widely with industry participants in developing guidelines setting out its approach to regulation under the new rules with the aim of improving predictability and transparency.

The first round of regulatory determinations under the new rules and guidelines was made by the AER during 2015. The importance of predictability and transparency to investors was acknowledged by investor advisory groups such as Standard and Poor's and Moody:

> The pricing decisions for the New South Wales state-owned regulated utilities and SA Power Networks confirm the tightening bias that the sector had widely anticipated. Nevertheless, we consider the regulatory landscape remains strong and transparent for Australia's regulated utilities, enabling predictable and stable cash flows.[4]

Other investment analysts said of the decisions for the SA and Victorian NSP determinations that, whilst typically regulatory resets would be a risk event; in the current round this was not so much a concern with the AER having completed a thorough review of its guidelines in 2013 and having applied them consistently and formulaically for the NSW, SA and Queensland networks.

Notwithstanding, many aspects of the decision were contested in appeals to the ACT by the NSPs, and by the Public Interest Advocacy Centre on behalf of consumers under the Limited Merits Review framework. The ACT decision found some aspects of the appeals in favour of the NSPs and some in favour of the AER. The NSPs' appeal on the AER's approach to opex was upheld as were their appeals on the AER's allowances for their returns on debt, the value the AER set for gamma and one NSP's Service Target Performance Incentive Scheme allowance. The NSP's challenges to the AER's decision on their returns on equity, Efficiency Benefit Sharing Scheme and metering issues were not upheld. The ACT essentially remitted the decision back to the AER and acknowledged that the decisions, being made under new, untested legislation, meant that the AER's task (and its own review) of resolving those issues was more demanding than it might have otherwise been. It noted that the impact on the NSPs' revenues, and hence the prices they may charge, would not be known until the AER remakes its decisions.

The original determination process took well over a year. Given the complexity of the ACT's decision and the fundamental nature and inter-relationship of the issues raised, the remaking of the remitted determination will undoubtedly take some time as it will involve not only examining and testing alternative approaches as directed by the ACT, but further consultation on these (AER Statement on Australian Competition Tribunal Decisions). At first glance, it would appear that the process has not provided the certainty that was hoped for.

A further point in regard to regulatory certainty is in respect to the privatisation of monopoly or near-monopoly assets without an appropriate *ex ante* regulatory regime. A consistent theme in ACCC submissions to numerous inquiries has been that, if implemented appropriately, privatisation can facilitate innovative management and improve the efficiency of infrastructure in the interests of users and the general community.[5]

However, the economic efficiency benefits will only be realised where there is strong potential for competition or where, in the absence of competition due to monopoly or near monopoly characteristics, there are appropriate structural reforms and/or sufficient regulatory oversight to ensure that competition in upstream or downstream markets is not hindered.

The ACCC considers that governments should appropriately deal with these issues early and upfront in the privatisation process. This provides greater certainty for bidders than *ex post* arrangements, and is essential for promoting efficient investment incentives. By understanding how assets will be structured and regulated upfront, potential acquirers of assets can factor these arrangements into their purchase price and bid accordingly.

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[4] See: Angela Macdonald-Smith, 'S&P says harsher regulatory decisions put pressure on networks' credit', *SMH business Day*, 7 May 2015.

[5] See the ACCC Submission to the Competition Policy Review and the ACCC Submission into the Proposed Lease of the Port of Melbourne.

These are not new issues. The 1995 Competition Principles Agreement recognised that in relation to structural reform of, and prior to the privatisation of public monopolies, governments should undertake a review into, relevantly:

- the merits of separating any natural monopoly elements from potentially competitive elements of the public monopoly;
- the merits of separating potentially competitive elements of the public monopoly; and
- the price and service regulations to be applied to the industry.

This is important not just as a mechanism to limit the potential for excessive charges or restricted access for users, but also to clearly signal to potential investors the regulatory regime that will apply so that they can make informed investment decisions. This should reduce the uncertainty for investors when governments sell assets on the basis of limited regulation and that may subsequently change with significant impacts on the value of the investment.

Concluding Comments

Over the years, substantial effort has been put into designing and implementing infrastructure regulatory regimes that address community needs and concerns, meet policy-makers' objectives and provide the right incentives for investment and efficient use of resources and concerns. However, the evolving nature of consumer preferences, policy objectives and markets highlights the enduring dilemma for regulators – the need to balance the competing demands of processes and decisions which:

- are less intrusive but more effective;
- provide predictability and flexibility;
- are timely, efficient but thorough;
- are inclusive, transparent and address the important issues; and
- are open to review.

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Critical Issues in Regulation – From the Journals

Behavioural Economics and Policy Analysis, Tim Brennan, *Journal of Benefit-Cost Analysis*, 5, 1, 2014, pp. 89-109.

This article deals with issues surrounding the compatibility of behavioural economics (BE) and benefit-cost analysis (BCA). BE posits a number of cognitive biases and limitations, which raises questions as to whether revealed willingness-to-pay equals true willingness-to-pay. If so, BCA, with a number of methodological advantages, would need to be replaced. According to the author, the three prior analyses of the issue (by Cass Sunstein; Robert Sugden; and Douglas Bernheim and Antonio Rangel) fail to offer guidance that would avoid substituting centralised judgments for decentralised information on benefits and costs. Alternatives include using: post-implementation valuations; libertarian paternalism; and direct democracy on policy issues. However, these also have conceptual or practical limitations. A tentative suggestion is democratic delegation, which is somewhat appealing because it is already applied to cope with bounded rationality and non-efficiency values. The practical lesson may be to require very strong evidence of substantial choice failure before abandoning BCA. Tim Brennan offers these three guiding principles from Robert Sugden: first, consider the merits of viewing policy evaluation in terms of market simulation rather than welfare terms; second, restrict BE to settings where customers have not learned or have not been informed of the putative error of their decisions; and third, demand clear evidence of differences between revealed and actual willingness to pay before rejecting the findings of conventional BCA.

This article is available by subscription to the *Journal of Benefit-Cost Analysis*.

Incentives to Quality and Investment: Evidence from Electricity Distribution in Italy, Carlo Cambini, Elena Fumagalli and Laura Rondi, *Journal of Regulatory Economics*, 49, 1, February 2016, pp. 1-32.

This paper investigates the relationship between output-based incentives for service quality and the use of capital and non-capital resources to meet regulatory targets in the electricity industry. To conduct the empirical analysis the authors use a dataset collected with the support of the Italian energy regulatory authority, comprising micro data on monetary incentives and physical assets for the largest electricity distribution operator in Italy (86 per cent of the market). There are thirty-seven references in the list at the end of the article.

The authors' results show that physical assets and operational expenditures do affect service quality. Moreover, when the authors investigate causality in the relationship between incentives to quality and the use of capital and non-capital resources, they find that incentives Granger-cause capital expenditures (and not *vice versa*). Finally, the authors' results reveal an asymmetric effect of rewards and penalties on capital expenditure decisions across areas with different quality levels. From these findings, several policy implications are derived.

The article can be accessed by subscription to the *Journal of Regulatory Economics*.

Regional Distribution of Photovoltaic Deployment in the UK and its Determinants: A Spatial Econometric Approach, Nazmiye Balta-Ozkan, Julide Yuldirim and Peter Connor, Energy Economics, 51, September 2015, pp. 417–429.

This article is about UK climate change and energy policy goals. These legislate an 80 per cent emissions reduction target from 1990 levels by 2050 via the Climate Change Act, while ensuring security of supply and affordability. Additionally, the European directive 2009/28/EC imposes a target for the UK to meet 15 per cent of all energy consumption from renewable energy sources by 2020. Photovoltaic (PV) panels offer significant potential for contributing to the UK's energy policy goals relating to decarbonisation of the energy system, security of supply and affordability. Recognising that there has been no comprehensive analysis of the determinants of PV deployment in the UK, this paper addresses this gap by employing spatial econometrics methods to a recently available dataset at a fine geographical detail. There are approximately ninety items in the reference list.

The substantial drop in the cost of PV panels since 2007, coupled with the introduction of the Feed-in Tariff (FiT) Scheme in 2010, has resulted in a rapid increase in installation of PV panels in the UK, from 26.5MWp in 2009 to over 5GW by the end of 2014. Following a traditional regression analysis, an approach has been adopted where spatial variations in the relationships have been examined utilising the spatial Durbin model using the cross-sectional data relating to the UK NUTS level 3 data.

Empirical results indicate that these factors are among those that affect PV uptake in a region: demand for electricity; population density; pollution levels; education level of households; and housing

types. Moreover Lagrange Multiplier test results indicate that the spatial Durbin model may be properly applied to describe the PV uptake relationship in the UK as there are significant regional spillover effects.

Over-the-Top (OTTs) Players: Market Dynamics and Policy Challenges, Study for the IMCO Committee of the European Parliament, December 2015.

This report comprises a study on over-the top (OTT) services prepared by consultants TNO and WIK-Consult at the request of the European Parliament's Committee on the Internal Market and Consumer Protection. The study: examines current and emerging business models for OTT services (including Voice over IP, instant messaging services, and streaming video and music services); identifies costs and barriers to European online service development including OTT; reviews the regulatory environment for online services in Europe including in contrast to the environment in other jurisdictions; and provides policy recommendations related to the achievement of a European Digital Single Market.

OTT services are defined in the report as online services that are substitutes, to some extent, for traditional media and telecommunications services. Examples are online video services (such as Netflix) that are increasingly becoming a substitute for traditional television services; and IP-based calls (for example, Skype) and messaging (for example, iMessage) that are increasingly being used instead of telephone and messaging services supplied by traditional telecommunications operators.

The report identifies impediments to the development of OTT services overall, and to European OTT services as opposed to foreign (largely US) based services. This includes consideration of whether traditional services may face particular regulatory advantages or disadvantages in competing with OTT services, with a key objective of the study being to ensure that regulatory conditions create a 'level playing field' (neutrality) for both types of services and that rules are applied uniformly across countries of the EU.

In relation to the level-playing-field objective, particular regulatory concerns are expressed about sectoral legislation that tends to impose more stringent rules on traditional telecommunications carriers than on OTT providers for supply of very similar services. It is considered that anti-competitive discrimination by telecommunications operators towards OTTs can be addressed adequately via the Telecommunications Single Market provisions on net neutrality. Interconnection payment arrangements between telecommunications operators and OTTs are not considered to be of major concern and, if they were to emerge as an issue, are considered capable of being addressed via existing rules.

Regulatory barriers that are identified relating specifically to the development of European online services and OTTs include restrictions on the free flow of data and content between European countries.

The study makes a number of policy recommendations to address the above and other concerns in the context of the continuing development of the European Digital Single Market. These include a combination of specific proposals (such as sectoral and horizontal harmonisation of rules) and suggestions for further research (particularly in relation to the competition policy implications of possible dominant online platforms).

Reassessing Competition Concerns in Electronic Communications Markets, Martin Peitz and Tommaso Valletti, *Telecommunications Policy*, 39, 10, November 2015, pp. 896-912.

This paper is about the implications of packet switching and over-the-top (OTT) applications for the assessment of competition and the role of economic regulation. Keywords are: telecommunications; ISP (internet service provider); OTT; relevant market; two-sided markets; market power; and network effects.

The authors reach three key conclusions. First, while these developments have made the combination of internet access, communication services and media services more valuable to users, it may be difficult for telecommunications carriers to monetise the benefits from these enhanced services. There is a basic property of complementarity between network infrastructure and content services. To the extent that the benefits go to OTT providers and consumers, there is a risk that mutually beneficial estimates will be delayed or even not undertaken. Business models are observed to be diverse and evolving. Second, 'efficiency of pricing solutions should be analysed in light of recent economic theory, taking into account that ISPs and OTTs are multi-sided platforms'. Third, when defining markets, demand substitutability should be the key criterion used. In particular, a SSNIP test for mobile voice services must take all relevant substitution possibilities into account. These include OTT voice substitutes (such as Skype) and substitution of parts of their calls by messages (SMS or OTT services such as WhatsApp).

The exposition is substantially non-technical, relying instead on verbal descriptions and explanations; stylised schematics and empirical observations (mainly from Europe). The authors list 45 items in

the reference list, and these are mainly articles published in professional journals such as the *Economic Journal*, the *Journal of Regulatory Economics*, the *Rand Journal of Economics* and *Telecommunications Policy*. More than half of these articles have been published since 2010.

This article can be accessed by subscription to *Telecommunications Policy*.

Report on the State of the Postal Market in 2014, Office of Electronic Communications (UKE), Republic of Poland, May 2015.

This report on the state of the Polish postal market in 2014 was drafted in accordance with Article 43 (6) of the Postal Law Act of 23 November 2012 (Journal of Laws of 2012, item 1529), based on information obtained from postal operators under Article 43(1) and (2) of this Act. These provisions require the postal operators to submit to the President of the Office of Electronic Communications reports of postal activities carried out in 2014. The reports were submitted by the designated operator providing universal postal services (Poczta Polska S.A.) and 165 alternative postal operators. Postal activity, as stipulated in Article 1 of the Postal Law Act means the performance of business activity that consists in providing postal services in domestic or cross-border markets.

The 2014 report finds that the Polish postal market has been steadily evolving in recent years as a result of gradual market liberalisation and growing demand for postal services from business and residential customers. The evolution of competition has a significant impact on the emergence of new postal services and the upgrading of existing services by offering added value. In the process of delivering postal services, new differentiated ways of service provision can be observed. Universal postal services are provided by Poczta Polska S.A. While fulfilling its role of the designated operator, it has a statutory obligation to ensure the continued provision of universal services, available throughout the whole nation (including rural areas) in a uniform manner, at a specific quality level and at affordable prices. The report is about sixty pages in length and contains numerous tables and charts to present the data.

Regulation, Renegotiation and Capital Structure: Theory And Evidence from Latin American Transport Concessions, Alexander Moore, Stephane Straub and Jean-Jacques Dethier, *Journal of Regulatory Economics*, 45, 2, April 2014, pp. 209-232.

This article examines the capital structure of regulated infrastructure firms using a panel dataset, consisting of data on the regulatory regime, annual financial performance and contract negotiations, of 124 transport concessions in Brazil, Chile, Colombia and Peru over 1992-2011.

The authors develop a model which shows that leverage (the ratio of liabilities to assets) is lower under high-powered regulation, and that businesses operating under high-powered regulation make proportionally larger reductions in leverage when the cost of debt increases. The model specified is a multiple regression, with the leverage ratio being the dependent variable regressed against a set of explanatory variables including a dummy variable for whether the project was subject to price-cap regulation. Other regressors include sets of vectors for contract characteristics, project financial variables and macro-financial variables.

Potential weaknesses of the model are discussed, including an omitted-variable problem, as not all relevant project characteristics were taken into account, and endogeneity issues, as it is reasonable to assume that businesses bidding for price-cap contracts are less risk-averse than those bidding for rate-of-return contracts, thus, they will more likely rely on debt financing.

The authors found that the price-cap dummy variable was statistically insignificant in all specifications, possibly owing to previously discussed endogeneity issues. This is not unexpected, as it would be reasonable to assume that the choice of regulation and other contract clauses (for example, government guarantees) are non-randomly assigned to projects. Thus, to deal with this endogeneity, leverage changes within projects, due to an increasing cost of debt, are analysed. The data supported the claim that, when there is a shock to borrowing costs, price-cap businesses reduce leverage more than others.

The authors concluded that the firm's ability to increase prices by using leverage is determined by the regulatory regime, and that when regulation is high-powered, such as a price-cap, prices are unresponsive to costs. In such a case, the incentive to use leverage is limited and thus, *ceteris paribus*, leverage is lower under high-powered regulation.

The reference list contains thirty-one items.

This article can be accessed by subscription to the *Journal of Regulatory Economics*.

New Approach to Estimating the Cost of Common Equity Capital for Public Utilities, Pauline M. Ahern, Frank J. Hanley, and Richard A. Michelfelder, *Journal of Regulatory Economics*, 40, August 2011, pp. 261-278.

This paper provides a general, yet simple consumption-based asset pricing specification to model the risk-return relationship for stocks and

estimate the cost of common equity for public utilities in response to the widely known problems with traditional models such as the CAPM. The authors also investigate whether assets such as utility stocks are a consumption (business cycle) hedge.

The model proposed by the authors estimates the risk-return relationship directly from asset pricing data, and utilises modern time series methods to produce a prediction of the equity risk premium, which is driven by predicted volatility. The estimation method used the GARCH model, as it accommodates for ARCH (volatility persistence) effects and improves the efficiency of parameter estimates. It also allows for forecasting of the conditional volatility of the asset's risk premium.

The proposed model was tested to – (1) determine whether the equity-to-debt risk premium indices for utilities of different risk specified by different bond ratings are validated by the asset pricing model, (2) determine whether equity-risk premia can be predicted and fit the model and therefore be used to estimate the cost of common equity, (3) empirically test the consumption asset pricing model, and (4) determine whether utility stocks are assets that hedge shocks to the marginal utility of consumption.

The estimated model shows a positive and significant slope (Sharpe Ratio) at the 99 per cent level for all assets, except the utility stock returns with Baa bonds, which was significant at the 95 per cent level. Since the slope is positive, it was found that public utility stocks are not hedge shocks to the marginal utility of consumption. The variance equation shows that all GARCH coefficients are significant at the one per cent level and that the residuals of the risk premium equation follow a GARCH process, with temporary persistence of volatility shocks on returns and prices of utility stocks.

The proposed model was shown to be able to predict the *ex ante* risk premium with a conditionally predicted volatility. The estimates compare well with rates of return on the book value of common equity and with the traditional CAPM. The results of the model are stable and consistent over time. The authors contend that the model should be considered as part of regulatory processes as it provides additional evidence on the cost of common equity in general and specifically in utility regulatory proceedings.

The reference list contains twenty-one elements.

This article can be accessed by subscription to the *Journal of Regulatory Economics*.

A New Industry Concentration Index, Nejat Anbarci and Brett Katzman, *Economic Papers*, 34, 4, December 2015, pp. 222-228.

This paper is about indices for the measurement of concentration for industries and the assessment of mergers. Nejat Anbarci and Brett Katzman propose an index that is alternative to the familiar Herfindahl-Hirschman Index (HHI). The proposed index emphasises what the authors call the 'concept of competitive balance' and attaches importance to the size of the merging parties ('dominant' or 'fringe'). Using this new index, a merger of two non-dominant firms can increase economic welfare even though the HHI increases. This is because the newly-created entity will provide greater competition to the dominant firm(s) in the industry. The authors explain this in terms of first, the merging parties seeking cost economies and becoming a 'dominant' firm, and second, the operation of a version of the familiar 'dominant firm' model with more than one dominant firm. There are eleven items in the reference list with year of publication ranging from 1967 to 2011.

This paper can be accessed by subscription to *Economic Papers*.

Regulatory Decisions in Australia and New Zealand

Australia

Australian Competition and Consumer Commission (ACCC)

Airport Monitoring Report for 2014-15 Released

See 'Notes On Interesting Decisions'.

NBN Co's Revenue Controls – Draft Determination

On 15 March 2016 the ACCC **issued a draft determination** on NBN Co's revenue controls for 2014-15. It has also set out its view that NBN Co's prices did not exceed maximum regulated prices during the 2014-15 financial year.

Australian East Coast Gas Market – Chairman Sees Difficult Times for the Changing Gas Market

On 9 March 2016, at the Australian Domestic Gas Outlook Conference in Sydney, ACCC Chairman **Mr Sims provided key observations** on the east coast gas market; ahead of the ACCC's formal report to Government.

Patrick Bulk Wheat Facility at Port Adelaide – Proposal to Grant an Exemption

On 25 February 2016 the ACCC released **its draft determination** proposing to exempt Patrick Stevedoring Pty Ltd from having to comply with Parts 3 to 6 of the Port Terminal Access (Bulk Wheat) Code of Conduct in relation to its facilities at Berth 29, Port Adelaide.

New ACCC Commissioner

On 24 February 2016 the ACCC announced the Government's **appointment of Mr Mick Keogh as Commissioner**.

ACCC Proposal to Conditionally Authorise Queensland LNG Producers to Coordinate their Maintenance Schedules

On 18 February 2016 the ACCC issued a draft determination proposing to authorise for five years Australia Pacific LNG Pty Ltd, Gladstone LNG, and the Queensland Curtis LNG Project to discuss their maintenance schedules, maintenance providers and maintenance techniques. LNG facility maintenance can result in large changes to the wholesale price of gas. **The ACCC is seeking submissions on its draft determination**, including the proposed condition of authorisation, before making a final decision.

ACCC September Quarter 2015 Petrol Report

On 15 December 2015 the ACCC released its fourth quarterly report into the Australian petroleum industry for 2015. The report examines petrol prices up to September 2015 report and shows **the highest retail margins since monitoring began in 2002.**

ACCC appoints its first Chief Economist

On 8 December 2015 the ACCC announced **the appointment of Dr Graeme Woodbridge** as its new Chief Economist.

Australian Competition Tribunal (ACT)

Seven Applications to Review AER Decisions

On 26 February 2016, the ACT announced applications made to it to review decisions of the AER made on 30 April 2015. **The applications were by**: Public Interest Advocacy Centre Ltd and Essential Energy; Public Interest Advocacy Centre Ltd and Endeavour Energy; ActewAGL Distribution [2016] ACompT 4; Jemena Gas Networks (NSW) Ltd [2016] ACompT 5; Public Interest Advocacy Centre Ltd and Ausgrid [2016].

Australian Energy Market Commission (AEMC)

Gas Pipeline Access across the East Coast – Discussion Paper

On 3 March 2016 the AEMC released a discussion paper which provides the next layer of detail on the **its proposed reforms to the contract carriage model for gas transport** which operates in eastern Australia outside Victoria's Declared Transmission System.

Proposed Reforms to Victoria's Declared Wholesale Gas Markets – Discussion Paper

On 3 March 2016 the AEMC released a discussion paper which explores key design issues related to development of a virtual southern hub covering Victoria's gas transmission system. **Submissions are due by 29 March 2016**.

New AEMC Chief Executive

On 15 February 2016 the AEMC appointed Ms Anne Pearson, the organisation's Senior Director Market Development, to the role of Chief Executive.

Australian Energy Regulator (AER)

AER Statement on Australian Competition Tribunal Decisions

On 26 February 2016, following an appeal of the AER's April and June 2015 electricity and gas revenue decisions in New South Wales and the Australian Capital Territory, **the Australian Competition Tribunal handed down its decisions**, following its limited merits review. The appeals were brought by the NSW and ACT electricity and gas distribution network businesses seeking greater revenue to be recovered from customers through electricity and gas bills. The Public Interest Advocacy Centre also appealed the AER's decisions seeking lower revenues to be recovered from customers.

National Gas Law Compliance 2014-15 Overview

On 17 February 2016 the AER **published** an Overview of the 2014-15 Gas Law Compliance reports.

Electricity Distribution Networks Pay Penalties for Alleged Breaches of Life Support Obligations

On 11 February 2016 the AER announced that three electricity distribution businesses, SA Power Networks, Energex, and ActewAGL Distribution, paid penalties totalling $160 000 for **alleged breaches of the life support obligations** under the National Energy Retail Rules.

SA Power Networks' Application to Review the AER's Pricing Decision – Dismissed by Federal Court

On 23 December 2015 **the AER announced the Federal Court's decision** dismissing SA Power Networks' application for judicial review of the AER's 2015 South Australian pricing proposal decision.

State of the Energy Market Report 2015 Released

On 18 December 2015 the AER **released** the ninth annual report on the State of the Energy Market in Australia.

National Competition Council (NCC)

Application for Declaration of Shipping Channel Services at the Port of Newcastle

On 29 January 2016 **Glencore Coal Pty Limited applied to the Australian Competition Tribunal for a review** of the Acting Treasurer's decision not to declare the shipping channel service at the Port of Newcastle. On 10 November 2015, the NCC had sent to the Federal Treasurer its final recommendation in respect of the application by Glencore Coal Pty Ltd for declaration of the shipping channel service at the Port of Newcastle.

Australian Capital Territory

Independent Competition and Regulatory Commission (ICRC)

Technical Paper on Water Demand Elasticity

On 29 February 2016 the ICRC released a technical paper on the demand for water in the ACT, as part of its review of Icon Water's water and sewerage services tariffs. **Feedback on the paper is required by 1 July 2016**.

New South Wales

Independent Pricing and Regulatory Tribunal (IPART)

Prices for Water Management Services Provided by DPI Water (formerly the NSW Office of Water)

On 8 March 2016, IPART released a Draft Report and Determination on the prices that the Water Administration Ministerial Corporation (WAMC) can charge for its monopoly water management services. These services are currently delivered on its behalf by DPI Water (formerly the NSW Office of Water). Feedback is required by 4 April 2016. **IPART will then release its Final Report and Determination** in June, for new prices to apply from 1 July 2016.

Review of Maximum Price for Wholesale Ethanol in NSW

On 24 February 2016 the IPART published the draft terms of reference for commencing an investigation into the maximum price for wholesale ethanol used in petrol blend. **Feedback was required by 24 March 2016, with a view to producing a final report by February 2017.**

Retail Gas Prices from 1 July 2016 – Proposed Changes

On 11 February 2016 the IPART, as part of its review of regulated retail tariffs and charges for small retail gas customers in NSW from 1 July 2016, announced that **AGL, ActewAGL and Origin Energy have submitted pricing proposals**.

Sydney Water Pricing Review

On 13 January 2016 the IPART **commenced** its periodic review of the prices that Sydney Water Corporation can charge to provide water, wastewater and stormwater. The prices set will apply from 1 July 2016.

Northern Territory

Utilities Commission

Utilities Commission Commences Port Access and Price Regulation Role

See Notes on Interesting Decisions.

Queensland

Queensland Competition Authority (QCA)

DBCT's Ring-fencing Arrangements – Draft Decision Released

On 29 February 2016 the QCA released a draft decision on Dalrymple Bay Coal Terminal Management's (DBCTM's) November 2015 ring-fencing draft amending access undertaking (DAAU): **to not approve DBCTM's DAAU**, and to indicate where it considers the DAAU should be amended in order for it to be approved.

Development of a Replacement Undertaking for Central Queensland Coal Network

On 16 December 2015 the QCA released a consolidated draft decision on Aurizon Network's 2014 Draft Access Undertaking. **The QCA anticipates a new undertaking being in place in 2017**.

Retail Electricity Prices for 2016-17

On 11 December 2015 **the QCA released an interim consultation paper** on regulated retail electricity prices in regional Queensland for 2016-17. Submissions on this first round of consultation were due by 18 January 2016.

South Australia

Essential Services Commission of South Australia (ESCOSA)

Electricity Retailer Feed-in Tariff – Review of Regulatory Arrangements

On 18 March 2016 the ESCOSA **commenced a review** of the regulatory arrangements for the electricity retailer feed-in tariff by releasing an issues paper.

Dr Patrick Walsh's appointment as Commissioner and Chairperson Concludes

On 1 March 2016 the ESCOSA announced that **Dr Patrick Walsh's second five-year term** as its Commissioner and Chairperson concluded on 16 February 2016.

SA Water Regulatory Determination 2016

On 10 February 2016 the ESCOSA announced a review **to determine the prices it will charge for water and sewerage services over the four year period 1 July 2016 to 30 June 2020**.

Tasmania

Office of the Tasmanian Economic Regulator (OTTER)

2016 Regulated Feed-in Tariff Rate Investigation and Determination

On 5 February 2016 the OTTER **published its Draft Report** for the 2016 Regulated Feed-in Tariff Rate Investigation, together with its Draft Determination.

2014-15 Energy in Tasmania Performance Report – Published

In January 2016 **the OTTER published the performance report** on Tasmanian energy.

Victoria

Essential Services Commission (ESC)

Melbourne Water Price Review – Draft Decision

On 11 March 2016 **the ESC released its Draft Decision** on the Melbourne Water Price Review.

Goulburn-Murray Water Price Review – Draft Decision

On 26 February 2016 **the ESC released its Draft Decision** in relation to Goulburn-Murray Water Price Review.

Victorian Electricity Distributors' Guaranteed Service Level Payment Scheme – Final Decision

On 23 December 2015 the ESC **released the Final Decision of its review** of the Victorian Guaranteed Service Level (GSL) payment scheme for the 2016-2020 regulatory-control period.

Western Australia

Economic Regulation Authority (ERA)

Urban Water Utilities – National Performance Report 2014-15

On 17 March 2016 the ERA announced that the Bureau of Meteorology has published the 2014-15 National Performance Report: Urban Water Utilities. **View the report.**

Rate of Return Guidelines for Gas Transmission and Distribution Networks – 2016 Review

On 18 December 2015 the ERA announced that it **has decided not to commence a review** of the rate of return guidelines to apply to regulated gas networks and transmission pipelines, unless it becomes apparent that the ERA's access functions will not transfer to the Australian Energy Regulator.

New Zealand

New Zealand Commerce Commission (CCNZ)

Airport Land Valuation Rules – Release of Final Amendments

On 24 February 2016 the CCNZ released **its final decision on the application of the airport land valuation rules** as part of the input methodologies review. The next airport price-setting events are anticipated in mid-2017.

Unfair Contract Terms in Telecommunications – Report Released

On 10 February 2016 the CCNZ released a report detailing **the findings of its review of standard form consumer contracts in the telecommunications sector**.

Z Energy's Application to Acquire Chevron NZ – Decision Date Extension

On 18 December 2015 the CCNZ announced an extension to 29 April 2016, for **its decision on Z Energy's application to acquire Chevron NZ**, due to the complexity of the matter.

Wholesale Broadband Prices – Final Decision

On 15 December 2015 the CCNZ **released its final decision** setting the prices that Chorus can charge for use of its local copper lines and broadband service over the next five years. These are wholesale prices that Chorus charges retail telecommunications providers.

Notes on Interesting Decisions

Annual Airport Monitoring Report Released

On 23 March 2016 the Australian Competition and Consumer Commission (ACCC) **released** its annual Airport Monitoring Report for 2014-15, finding that the monitored airports at Brisbane, Melbourne, Perth, and Sydney, continue to enjoy high profit margins in both aeronautical and car parking activities. The Australian Government has directed the ACCC to monitor the performance of the four largest airports until 2020. It is required to monitor both aeronautical and car parking activities. It is required to consider prices, profits and quality of service. The ACCC derives its quality of service information from responses to surveys of passengers, airlines and landside operators (such as off airport car parking operators, buses and taxis), and from objective data from the monitored airports. The 'overall average quality of service' measure is calculated as an average of these ratings (excluding responses from landside operators).

The 23 March 2016 report showed that:

- Profit per dollar of aeronautical revenue ranged from a low of 40.2 cents at Perth Airport to a high of 50.1 cents at Sydney Airport. Sydney Airport's result is the highest by any monitored airport over the period from 2004-05 to 2014-15. Return on assets for aeronautical services ranged from a low of 6.2 per cent for Brisbane Airport to a high of 12.4 per cent for Sydney Airport, with two airports (Melbourne and Perth) reporting declines in this measure for 2014-15. (However, the ACCC notes that return on asset figures can be affected by airport revaluations of assets.)
- As the only suppliers of car parking on airport grounds, the four monitored airports continue to make significant profits from car parking. The profits per dollar of car parking revenue ranged from a low of 63.7 cents for Perth Airport to 73.2 cents for Melbourne Airport. However, increasingly, motorists are taking advantage of the discount rates available by booking car parking online.
- Despite the high profit margins, the quality of service has not been increasing over the years. Brisbane Airport was once again found to have the highest quality of service of the four monitored airports. Both Brisbane and Perth were found to provide 'good' quality of service, while Melbourne and Sydney airports were again rated as 'satisfactory'. These overall ratings are drawn from survey results (both airlines and passengers) and objective indicators. However, quality of service may improve in the future following new investment. Melbourne ($484 million), Brisbane ($334 million), and Perth ($250 million) each invested in aeronautical assets at record levels in 2014-15.
- Notable projects include: the new runway at Brisbane Airport; the new domestic terminal at Melbourne Airport; and Perth Airport's Terminal 1 International and Domestic Pier.
- Passengers benefited from an increased proportion of domestic flights that were on-time. The average proportion of arrivals and departures that were on-time in 2014-15 was the highest since 2006-07. The timeliness of flights can depend on factors such as the airline performance, weather, and passengers themselves. However, investment by airports can help to ensure that there is sufficient capacity for the number of flights per day.
- Passenger growth across the airports was relatively flat during 2014-15. International passengers (3.7 per cent) grew more strongly than domestic passengers (0.7 per cent). The slowdown in the resources sector (and therefore flights by fly-in-fly-out workers) contributed to a 1.0 per cent decrease in passengers at Perth Airport.
- The ACCC took a closer look at airport rail links in this year's report and the extent to which they act as a constraint on the significant market power that airports possess with the supply of car-parking services. There are existing rail links at Brisbane and Sydney Airports, while one is under construction in Perth. The report found that rail links do not appear to provide a strong constraint on airports' car parking pricing, but rather they compete more closely with other modes of transport (such as taxis and other public transport services).
- Over the past two years, monitored airports have raised concerns with the ACCC around the operations of the Australian Border Force (ABF) and delays for international passengers through customs. The ABF acknowledged to the ACCC that its past performance had suffered. However, both the ABF and airports said that recent performance had been significantly improved by the deployment of more technologically advanced SmartGates and increased staffing.
- In April 2014, the Australian government confirmed its intention to develop a new major airport in Western Sydney at Badgerys Creek. A

second significant airport has the potential to provide competition with the current Sydney Airport which could drive reduced prices and/or improved facilities. However, the ACCC found this potential benefit was lost during the privatisation process when the Australian Government provided the acquirer of Sydney (Kingsford Smith) Airport with the right of first refusal to develop and operate any second airport within 100 kilometres of the CBD.

Comparisons between airports should be treated with caution because results can be affected by factors such as different terminal configurations, passenger mix, and different approaches to valuing assets.

The ACCC's monitoring role does not involve direct regulation of monitored airports; nor does it have any power to intervene in the airports' setting of terms and conditions of access to their infrastructure.

The ACCC's monitoring role for aeronautical services relates only to those terminals that are owned and operated by the airports. Some domestic terminals at the monitored airports are leased to and operated by domestic airlines, and these terminals are not subject to the ACCC's monitoring. Such terminals include the Qantas domestic terminals at Melbourne, Perth and Sydney airports, and the Qantas and Virgin Australia domestic terminals at Brisbane Airport.

Northern Territory Utilities Commission Commences Port Access and Price Regulation Role

On 18 January 2016 the Utilities Commission **announced** that Darwin Port Operations Pty Ltd has commenced as the private port operator for the Port of Darwin. The Utilities Commission's regulatory role relates to prescribed services provided by the private port operator and involves approving an access policy and reporting in relation to material non-compliance with an access policy; it is also responsible for monitoring the prices of prescribed services. The Utilities Commission is required to review the port access and pricing regime in accordance with section 123 of the Act in three years from the appointment of a private operator, and in each successive five-year period thereafter. In undertaking a review of whether there is an ongoing need for regulatory oversight and whether there is a need to change the form of regulatory oversight, the Utilities Commission will take into account the access and pricing principles specified in section 133 of the Act, which include that the price of prescribed services is expected to generate revenue sufficient to meet efficient costs of providing the service, and the functions of the Commission in accordance with section 6(2) of the *Utilities Commission Act* which requires that the Utilities Commission have regard to the need to promote economic efficiency, ensure an appropriate rate of return on regulated industries and the interests of consumers. The Utilities Commission's role in port regulation is broadly divided into two categories: access policy and price regulation.

Part 11, Division 2 of the *Ports Management Act* provides a framework for the private port operator to prepare and submit an access policy to the Utilities Commission for approval. The private port operator is required by legislation to comply with its access policy.

The private port operator is required to report to the Utilities Commission each year on material instances of non-compliance with the private port operator's access policy. The Utilities Commission provides a report to the Minister each year on material instances of non-compliance with a private port operator's access policy and if there has been any material instance of non-compliance with the Utilities Commission's determination.

The *Ports Management Act* and Regulations provide a framework for the Utilities Commission to make a determination to the charges fixed by a port operator in relation to the provision of prescribed services. The Regulations provide that the determination must use price monitoring of the price levels of a prescribed service as the form of price regulation.

Regulatory News

The Seventeenth ACCC/AER Regulatory Conference, Brisbane, Thursday 4 and Friday 5 August 2016

The seventeenth annual ACCC/AER Regulatory Conference will be held in Brisbane on Thursday 4 and Friday 5 August 2016. The theme of the conference this year is 'The Future of Economic Regulation; Does the Conventional Wisdom Still Apply?'. Confirmed speakers for the conference include: Janice Beecher, Jeffrey Church, Scott Hempling, Justice John Mansfield, Richard Schmalensee and Rod Sims. A draft program for the conference and details about how to register will be available on the ACCC website in mid-April.

Network is a quarterly publication of the Australian Competition and Consumer Commission for the Utility Regulators Forum. For editorial enquiries please contact Rob Albon (Robert.Albon@accc.gov.au) and for mailing list enquiries please contact Genevieve Pound (Genevieve.Pound@accc.gov.au).