



ABN 70 250 995 390
180 Thomas Street, Sydney
PO Box A1000 Sydney South
NSW 1235 Australia

19/09/2017

Committee Secretary
Senate Environment and Communications Legislation Committee
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Committee

Competition and Consumer Amendment (Abolition of Limited Merits Review) Bill 2017

TransGrid welcomes the opportunity to make a submission on the Abolition of Limited Merits Review Bill.

TransGrid is the operator and manager of the high voltage transmission network connecting electricity generators, distributors and major end users in New South Wales and the Australian Capital Territory. TransGrid's network is also interconnected to Queensland and Victoria, and is central to interstate energy trading.

TransGrid supports all efforts to develop energy policies that increase reliability, put downward pressure on household prices, and assist in the transition to sustainable sources of energy, because this is in the interests of consumers.

However, the removal of limited merits review, without the commensurate improvements in the overall checks and balances in the energy market may create serious unintended consequences for stakeholders. This includes:

- > higher prices for consumers
- > less certainty for Australian and international investors and
- > a greater use of cumbersome and expensive judicial reviews by stakeholders impacted by the Australian Energy Regulator's decisions.

Limited merits review holds the Australian Energy Regulator accountable, serving as an incentive for it to make considered and reasonable decisions. Its removal under the Competition and Consumer Amendment (Abolition of Limited Merits Review) Bill 2017 may therefore exacerbate the current reliability and pricing issues in the supply of energy, and spread these issues to the transmission and distribution of energy.

TransGrid recommends that amendments to the current limited merits review regime for the energy sector should be considered as part of broader energy sector reform set out in the Finkel review. Should limited merits review be abolished, TransGrid strongly suggests that alternative checks and balances be put in place to ensure a stable, long-term investable electricity network to support a strong national economy.

If you would like to discuss any matter raised in this submission, please do not hesitate to contact me on [redacted]. TransGrid looks forward to engaging further with the Committee on this issue.

Yours faithfully,

Tony Meehan
Executive General Manager Regulation

TransGrid submission – Abolition of Limited Merits Review Bill

19/09/17

1. Introduction

TransGrid welcomes the opportunity to make a submission on the Abolition of Limited Merits Review Bill.

TransGrid strongly supports the Government's energy policies focusing on increasing reliability, putting downward pressure on household prices and transitioning to sustainable sources. Regarding limited merits review, TransGrid fully supports the recommendations from the Finkel Review adopted by the Government and for amendments to the current limited merits review regime to be considered as part of broader energy sector reforms.

However, TransGrid advises caution in considering the proposed removal of limited merits review as it could result in current reliability and price issues in the supply side of the sector spreading to the network side. Ensuring reliable and affordable transmission and distribution network services is central to the public interest – approximately half of a customer's bill relates to the network component.

The remainder of this submission sets out the potential risks of completely removing access to limited merits review in the energy sector. In particular, it sets out: the key functions of limited merits review, the impacts of its removal, and a proposed alternative which fits with the Government's objectives of increasing network reliability and putting downward pressure on energy prices for consumers. Further, our proposed way forward aligns with the recommendations set out in the Finkel Review.

2. The importance of limited merits review

The limited merits review regime is a fundamental pillar of the regulatory framework in the energy sector:

- > It holds the Australian Energy Regulator (AER) accountable, serving as an incentive for it to make considered and reasonable decisions.
- > It provides a process of checks and balances to ensure a better outcome for the sector and consumers. Indeed, the limited merits review process has enabled the correction of material errors in previous determinations that the AER itself has agreed to.

As a forum to debate decisions, limited merits review also operates to clarify how fundamental elements of the National Electricity Rules and National Gas Rules are to be interpreted and applied which improves regulatory decisions over time. This is particularly important in the face of revisions to fundamental elements of the regulatory framework such as the 2012 changes to the rules.

In performing these functions, the limited merits review regime provides greater certainty and predictability for investors and consumers who are impacted by the AER's decisions. This

lowers the cost of capital for investment in network services and therefore lowers the price customers pay for these services.

Underlining the importance of limited merits review parties identified matters of difference that involved sums as significant as \$7 billion in the first set of applications since the rules were significantly revised.

Given these benefits, limited merits review or similar review arrangements are not unique to the energy sector - they are a key feature of arrangements throughout other sectors and jurisdictions in Australia as well as overseas.

3. Potential impacts of proposed removal of limited merits review in the energy sector

Amendments to the current regime have the potential to lead to greater reliability in the network and put downward pressure on prices. However, TransGrid recommends these amendments are carefully considered and consulted on as some changes, such as the complete removal of limited merits review, are likely to exacerbate current reliability and pricing issues in the supply of energy and spread these issues to the distribution and transmission of energy as well.

Further, the removal of limited merits review may result in a regulatory framework that will lack the flexibility and agility to keep up with more dynamic aspects of the industry. It is also likely to lead to an increase in the use of the judicial review process by stakeholders which is a far less efficient process.

3.1 Increased network prices and poorer reliability for consumers

The proposed removal of limited merits review in the energy sector would remove the checks and balances that ensure the AER is accountable for its decisions. It also removes the forum in which decisions are debated and understood, which fundamentally underpins the stability and certainty in the current regulatory framework.

The resulting reduction in certainty for investors and consumers in the sector will lead to adverse investment outcomes, most likely through an increase in the cost of capital. This in turn would put upward pressure on prices for consumers. Where the AER does not allow increases in the cost of capital to compensate network investors for the increased risks they face, this may result in insufficient levels of network investment leading to lower levels of reliability for customers.

These outcomes are not in the long term interest of consumers. They are also in direct opposition with the Government's stated intent of increasing stability and putting downward pressure on prices for consumers.

3.2 Increase in sovereign risk

Investors in electricity networks across Australia have committed substantial capital to the sector. A significant factor in the commitment of capital by investors in TransGrid has been the existence of a stable, well-functioning regulatory regime, including the option to seek merits review of revenue determinations by the AER.

The removal of limited merits review in the energy sector could send an unintended signal to overseas investors and have adverse implications for business' credit ratings and the current

high standing and perceived stability of the Australian regulatory environment. The removal of limited merits review therefore creates a perceived sovereign risk for investors.

This would likely result in an increase in the cost of capital for networks which in turn would put upward pressure on prices for consumers. Where the AER does not allow increases in the cost of capital to compensate investors for the increased risks they face, this may result in insufficient levels of network investment leading to lower levels of reliability for customers.

This risk, which may not be quarantined to the energy sector alone, is likely to be increased by a reform process which circumvents the COAG Energy Council and contradicts the Government's announced intentions and the recommendations from the Finkel Review.

3.3 Less flexible regulatory framework

The level of discretion afforded to the AER in the National Electricity Rules and National Gas Rules has been provided in the context of the regulatory regime as a whole. The proposed removal of limited merits review is likely to create pressure for a substantial rewrite of the rules to limit the discretionary components of the AER's decision making.

These changes would be required to provide more certainty to investors in order to minimise the detrimental impact on the cost of capital and sovereign risk. The resulting regulatory framework and process will lack the flexibility and agility to keep up with the more dynamic aspects of the industry.

3.4 Increase in use of judicial review by stakeholders

An increase in appeals for judicial review is likely to occur if limited merits review is removed. There are many drawbacks to this appeals mechanism. In particular, it is narrow in scope, very expensive, cumbersome in terms of providing for decisions, and prohibitive in terms of meaningful participation by consumer groups and other stakeholders.

4. TransGrid's recommendations

TransGrid is a strong supporter of increasing stability and putting downward pressure on prices. Further, it supports the implementation of an overarching energy strategy from Government to deal with the issues facing the sector in order to achieve these policy objectives.

In this regard, TransGrid supports the implementation of the Finkel review recommendations. This includes a recommendation for the COAG Energy Council to finalise and implement the reforms proposed in its 2016 review of the limited merits review regime.

Finally, should limited merits review be abolished, TransGrid strongly recommends the consideration of additional checks and balances to ensure a robust regulatory framework for energy networks. This would likely take the form of a re-write of the National Electricity Rules and National Gas Rules to limit the discretionary components of the AER's decision making.