

22 December 2006

# Consistency of the Transmission Rules with the Competition Principles Agreement

A report for the Australian Energy Market Commission

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## 1. Introduction

This report considers the consistency of the Australian Energy Market Commission's ('the Commission's') approach to developing the regulatory framework for electricity transmission services with the principles contained in clauses 6(2) to 6(4) of the Competition Principles Agreement ('CPA').<sup>1</sup> We understand that in developing the transmission rules, the Commission has sought to ensure that the framework developed for transmission revenue regulation and pricing satisfies the CPA principles, thereby allowing, at least for this part of the regulatory framework for electricity, for the energy market regime to be certified in accordance with the provisions of the *Trade Practices Act 1974* ('TPA').<sup>2</sup>

For this to occur, the arrangements for the regulation of energy access must satisfy the criteria for certification as an 'effective access regime'. In summary, the certification process is as follows:

- § each state and territory jurisdiction must apply to the National Competition Council ('the NCC') seeking certification of the electricity access regime. Section 44M(4) of Part IIIA of the TPA requires the NCC to decide whether clauses 6(2) to 6(4) of the CPA are satisfied; and
- § the NCC makes its recommendation for certification to the relevant Commonwealth Minister who must decide whether to certify the regime as effective. The Minister must specify the period for which the regime is to be considered certified, in accordance with s.44N of the TPA.

Once the regime is certified, access seekers must use the certified regime to obtain access, and are therefore unable to seek declaration of electricity facilities in accordance with those provisions of the TPA. The benefit that arises from certification is the certainty created for both access seekers (transmission and distribution service users) and infrastructure providers alike surrounding the rules for determining the terms and conditions, including price, for the services offered. This creates appropriate incentives for ongoing efficient investment in, and use of, electricity transmission and distribution infrastructure.

This report outlines some of the key issues associated with the certification of the new electricity regime in accordance with the requirements of the TPA. Whilst the Commission has directed NERA to focus on its approach to developing the regulatory framework as it applies to electricity transmission services, we are also mindful that the regulatory framework as it applies to distribution services will also be relevant to the regime's certification.<sup>3</sup> Accordingly, this assessment is incomplete since it only relates to the rules for transmission

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<sup>1</sup> Clauses 6(2) to (4) of the CPA are presented in their entirety in Appendix A.

<sup>2</sup> The Ministerial Council on Energy ('the MCE') has indicated that it intends to seek certification for the energy regulatory regime, as the national model for energy access. The Council of Australian Governments ('COAG') confirmed this approach at its meeting in Canberra on 10 February 2006, see: COAG Meeting, 10 February 2006, Communiqué.

<sup>3</sup> Accordingly, this assessment is incomplete since it only relates to the rules for transmission services. At the time of an application for certification, a more complete and comprehensive review of the entire regime against the CPA requirements will need to be undertaken.

services. At the time of an application for certification, a comprehensive review of the entire regime against the CPA requirements will be required. In undertaking this review, we have highlighted two key areas:

- § the need for the creation of a **framework for obtaining access that bestows an enforceable right of access**; and
- § the **effectiveness of the dispute resolution frameworks** contained in the national electricity regime.

A number of other relatively minor issues are also discussed including implications of the NEL Rule making framework on certification. Above all, we have sought to examine the Commission's approach to the rules relating to the economic regulation of transmission services, as they impact on a future application for certification of the national electricity regulatory regime. This report is structured as follows:

- § section 2 provides a brief overview of the certification process, including the matters the NCC is required to consider, and its approach to those issues based on previous certification issues;
- § section 3 considers the coverage of the electricity access regime, including whether it is appropriate for the Commission to consider the CPA criteria when assessing a Rule change proposal;
- § section 4 considers whether the electricity access regime incorporates appropriate forms of regulation for each covered transmission service;
- § section 5 outlines the means by which the electricity access regime facilitates access to those services covered by the regime, and in particular, whether the framework bestows an enforceable right to access those covered services;
- § section 6 assesses whether the electricity access regime incorporates an effective dispute resolution framework to resolve issues of contention between service providers and access seekers;
- § section 7 addresses a number of additional certification requirements that arise under the CPA criteria; and
- § section 8 summarises our key findings and sets out a series of recommended changes to address the key issues identified, thereby improving the prospects of certification.

## 2. Certification Process

Part IIIA of the *Trade Practices Act 1974* provides three pathways to access significant natural monopoly infrastructure:

- § through an application for **declaration** of the infrastructure services by an access seeker;
- § approval of an access **undertaking** by the Australian Competition and Consumer Commission ('ACCC'), submitted by the infrastructure provider; or
- § **certification** of a state-based access regime, following a recommendation by the NCC to the relevant Minister.

The MCE has indicated that it intends for each state and territory within the National Electricity Market ('NEM') to submit the national electricity regime to the NCC for certification, in accordance with the recent national energy reforms. These reforms have developed the new institutional and governance framework for the regulation of the NEM, with the establishment of the Commission as the Rule making body, and the Australian Energy Regulator ('AER') as the Rule enforcing body.

This section provides a brief overview of the third 'pathway' to access – the certification process – as provided for by the TPA.

### 2.1. Broad Objective of Certification

The process for certification is detailed in sections 44M to 44O of Part IIIA of the TPA, and requires a state or territory to apply to the NCC for a recommendation to the relevant Minister that the regime is an 'effective access regime'. In determining the effectiveness of the access regime, the NCC is required, in accordance with s.44M(4), to determine whether the regime satisfies the requirements of clauses 6(2) to 6(4) of the CPA.

The NCC has indicated its approach to interpreting the CPA requirements will be consistent with the objective of the TPA as provided in section 2:<sup>4</sup>

“The object of this Act is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.”

The CPA principles, combined with the TPA objective, have been characterised by the NCC as reflecting the efficiency goals of access regulation, including efficient use of and investment in natural monopoly infrastructure, in addition to promoting competition in markets that rely on the infrastructure.<sup>5</sup> In assessing these broad efficiency goals the NCC has indicated it favours a holistic approach, namely:

“In the certification process, the Council’s broad focus is on whether an access regime establishes an appropriate framework for these goals to be achieved.”

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<sup>4</sup> National Competition Council, “The National Access Regime: A Guide to Part IIIA of the Trade Practices Act; Part C, Certification of Access Regimes” February 2003, p11, [2.2] (Hereafter: ‘NCC Guide to Certification’).

<sup>5</sup> NCC Guide to Certification, p11, [2.4].

It is therefore relevant in assessing the Commission's approach to the development of rules for the economic regulation of transmission services against the CPA requirements, to consider the statutory Rule making test, and how it relates to the requirements of the CPA. The Commission is required to assess Rule change proposals against the NEM Objective, being:<sup>6</sup>

“[T]o promote efficient investment in, and efficient use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.”

The requirement for the Commission to consider the NEM Objective in assessing Rule change proposals or undertaking reviews directed by the MCE appears to be broadly consistent with the approach applied by the NCC in assessing access regimes against the requirements of the CPA.

In seeking to achieve these objectives, the access regime must satisfy the requirements of clause 6(i), which requires access outcomes to balance the legitimate commercial interests of facility owners and other parties, the efficient operation of the facility, and benefits to the public from having competitive markets. In this regard, the national electricity regime must result in terms and conditions of access that balance these interests.

Finally, in relation to the objective of clauses 6(4)(a) to (c), the NCC has indicated that:<sup>7</sup>

“[T]he underlying objective of the clauses 6(4)(a)-(c) model of commercial negotiation, supported by appropriate regulatory guidance, is to deliver outcomes that mirror, as closely as possible, those that would be derived if the infrastructure service market was effectively competitive – that is, outcomes that can generally be expected to lie within an efficient range.”

Taken as a whole, these comments suggest the regulatory regime should result in outcomes that can generally be considered efficient. We note that given the rules are required to satisfy the highly analogous NEM Objective, one would expect the national electricity regime to satisfy this requirement. Nonetheless, as indicated above, the NCC is required to assess the access regime against specific criteria specified in clauses 6(2) to 6(4) of the CPA.

## 2.2. Specific Certification Requirements

An application for certification requires evidence that each of the specific criteria contained in clauses 6(2) to 6(4) of the CPA have been satisfied. However, we note that s.44DA of the TPA requires the NCC to treat the clause 6 criteria as *guidelines* rather than binding rules. This has the effect of allowing an access regime to contain matters additional to those outlined in the requirements in the CPA, subject to the caveat that any additional requirements are not inconsistent with the CPA requirements.

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<sup>6</sup> *National Electricity Law*, Section 7 (Hereafter: 'NEL').

<sup>7</sup> NCC Guide to Certification, p30, [3.35].

Upon certification, the access regime remains certified for the period specified by the relevant certifying Minister, provided the regime is not altered to such an extent that it no longer satisfies the CPA requirements and *lapses* from certification.<sup>8</sup>

To assist applications for certification of access regimes, the NCC has provided a useful guide to its approach to assessing regimes against the requirements in the CPA. In so doing, it groups the requirements into a number of broad categories. It is worth noting that whilst this taxonomy assists the subsequent analysis, the categories do not exist in watertight compartments. Indeed, there is considerable overlap between them, for example, one cannot have an effective dispute resolution framework absent an enforceable right of access, and vice versa. The categories are:<sup>9</sup>

§ **coverage of services:** requires that the access regime specify the services subject to it – clauses 6(3) and 6(4)(d);

§ **negotiation framework:** requirement that the access regime provide an access framework that is effective for those covered services including:

- appropriately defined services – clauses 6(4)(a)-(c); and
- an enforceable right to access those services – clauses 6(4)(a)-(c), (e), (f), (g)-(i), (m), (n) and (o);

§ **dispute resolution:** requirement that the access regime provide an effective dispute resolution framework to resolve issues of contention between service providers and access seekers – clauses 6(4)(a)-(c), (g), (h), (i), (j), (k), (l) and (o);

§ **treatment of interstate issues:** the access regime must ensure there are no impediments to interstate access arising from state based regime differences, preferably through the provision of a single process for access – clauses 6(2) and 6(4)(p); and

§ **appropriate terms and conditions of access:** the regime must result in appropriate terms and conditions of access – clauses 6(4)(a)-(c), (e), (f), (i), (k) and (n).

In the balance of this report we supplant the term ‘negotiation framework’ with ‘access framework’. We believe this is a more appropriate terminology for considering the electricity regime, given that the access arrangements relate to prescribed as well as negotiated services as defined in the Rules. In the following sections we examine each of these requirements in turn as they apply to the national electricity regime.<sup>10</sup>

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<sup>8</sup> NCC Guide to Certification, p8, [1.16].

<sup>9</sup> NCC Guide to Certification, p13, [2.12].

<sup>10</sup> Note that we do not explicitly consider whether the regime is likely to result in appropriate terms and conditions of access. Provided the preceding criteria are met, this requirement will be met by implication.

### 3. Coverage of Services

For an access regime to be considered effective it must facilitate access to significant infrastructure facilities that cannot be economically duplicated. In assessing the national electricity regulatory regime against the requirements in these two clauses, two principal issues arise:

- § First, what elements of the national electricity regime would form the access regime to be certified?; and
- § Second, does the regime define transmission services in a manner consistent with the requirements of clause 6(3) of the CPA?

Before considering these issues we first outline the certification requirements as they relate to coverage in greater detail.

#### 3.1. Certification Requirements – Coverage

The relevant CPA requirements relating to the coverage of the access regime are in clauses 6(3) and 6(4)(d). These are reproduced for reference below.

- 6(3) For a State or Territory access regime to conform to the principles set out in this clause, it should:
  - (a) apply to services provided by means of significant infrastructure facilities where:
    - (i) it would not be economically feasible to duplicate the facility;
    - (ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market; and
    - (iii) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirements, appropriate arrangements exist; and
  - (b) incorporate the principles referred to in subclause (4).
- 6(4) (d) Any right to negotiate access should include a date after which the right would lapse unless reviewed and subsequently extended; however, existing contractual rights and obligations should not be automatically revoked.

Clause 6(3) limits the application of the access regime to significant infrastructure that is not economically feasible to duplicate. It further requires that access be necessary to allow effective competition in upstream and downstream markets. Clause 6(3)(a)(iii) however, allows for access to be limited to maintain the safe use of the facility at an economic cost. In addition, clause 6(4)(d) requires that the right to access is reviewed on a periodic basis.

The NCC has indicated that these clauses require an effective access regime to clearly define the services to be covered. It suggests that this requirement necessitates the defining of a generic service, such as electricity transmission services, followed by particular services that are covered for access, for example connection services.<sup>11</sup>

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<sup>11</sup> NCC Guide to Certification, p14, [2.16].

## **3.2. Applying the Coverage Criteria to Electricity Transmission**

As outlined above, two principal issues arise from a consideration of the coverage of the national electricity regime. First, what elements of the national electricity regime would form the access regime that would be certified? Second, does the regime define transmission services in a manner consistent with the requirements of clause 6(3) of the CPA? These issues are addressed in turn below.

### **3.2.1. What comprises the access regime?**

The national electricity regime comprises the NEL and the Rules. The NEL provides the legislative framework for the operation of the regime, including the establishment of the AEMC, with responsibility for *amending* the Rules, and the AER, with responsibility for *implementing* the Rules.

Section 34 of the NEL provides the subject matter for the Rules, thereby defining their coverage. It allows the Commission to make rules, for or with respect to the operation of the national electricity market, the national electricity system and the activities of persons participating in the national electricity market or system. It also provides for rules to be made in relation to the items provided in Schedule 1 of the NEL. The items relevant to transmission system revenue and pricing are outlined in items 15 to 24 of Schedule 1. Further, the *national electricity system* is defined in the NEL as including:

- (b) the interconnected transmission and distribution system in the participating jurisdictions used to convey and control the conveyance of electricity to which are connected –
  - (i) generating systems and other facilities; and
  - (ii) loads settled through the wholesale exchange operated and administered by NEMMCO under this Law and the Rules;

The NEL and the Rules therefore apply to electricity transmission and distribution facilities, both of which can readily be considered significant national infrastructure facilities by virtue of their essential role in delivering electricity from generators to users. Transmission and distribution assets also exhibit declining average costs, rendering them uneconomic to replicate. Finally, due to the vertically separated nature of the electricity industry, access to transmission and distribution services is necessary to promote competition in up- and down-stream markets – electricity generation and retailing.

Accordingly, the NEL and the Rules in combination would satisfy the requirements of 6(3)(a) as a necessary precursor to the assessment of the national electricity regime being an effective access regime.

A related issue is whether the inclusion of the Rule change process provided within the NEL in the access regime would threaten ongoing certification. This might arise, for example, where a Rule change process satisfied the requirements of the NEM objective, but meant that the CPA principles were no longer satisfied. The NCC has taken a general view that even if such a scenario were feasible, potential changes to an access regime would not preclude the

access regime from obtaining *initial* certification. However, it may result in certification *subsequently lapsing* were a future Rule change to have such an effect.<sup>12</sup>

The NEM Objective test, outlined in section 7 of the NEL, differs from the extensive criteria contained in clauses 6(2) to 6(4) of the CPA used to determine the effectiveness of the access regime. The NEM Objective is:

“[T]o promote efficient investment in, and efficient use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.”

There are a number of examples where it may be possible for a Rule change proposal to satisfy the NEM Objective, but be inconsistent with the CPA requirements. These may include, for example where:

- § economic efficiency (or, at least one dimension of it) required the interests of persons holding contracts for the use of the facility (clause 6(4)(i)(iv)) to be set aside, for example as could arise in converting a market network service provider (‘MNSP’) to an open access transmission line;
- § the owner’s legitimate business interests (say, arising from protection of regulatory asset values in a context where those assets had become stranded) were found to be inconsistent with economic efficiency; and
- § efficient dispute resolution called for the use of a ‘pendulum arbitration’ regime, which may not be consistent with the apparent requirement of clause 6(4)(i) of the CPA, for an arbitrator to exercise discretion, having regard to a range of considerations.

Whilst we are unaware of any proposed Rule changes that are similar to these examples, the important implication is that there may be instances where a Rule change proposal does satisfy the NEM Objective, resulting in the national electricity regime no longer being considered certified. However unlikely it is that these circumstances may arise, there may be some merit in placing a requirement on the Commission to take into consideration the CPA principles (in addition to satisfying the NEM Objective), prior to the approval of a Rule change process. This would remove any uncertainty that might arise from a Rule change being inconsistent with the CPA principles.

A relatively simple means of incorporating the CPA principles as a relevant consideration for the Commission when assessing Rule change proposals might be for the MCE to issue a suitably framed *Statement of Policy Principles*. The *Statement* would require the Commission in accordance with s.33 of the NEL to consider the CPA principles – and thus the ongoing certification of the access regime – when assessing Rule changes. Such a *Statement* might also require the Commission to consider consulting with the NCC on those Rule changes where it felt there was a risk of inconsistency between the NEM Objective and the CPA criteria. We believe this measure would likely be sufficient to preclude certification from lapsing subsequent to a Rule change.

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<sup>12</sup> NCC Guide to Certification, p8, [1.16].

### 3.2.2. Services defined by the Commission in the rules

Turning now to coverage of specific services, the Commission has sought to clarify the definition of services subject to the application of the transmission rules. The Commission has indicated that its intention was to provide a clearer delineation of transmission services between a control form of regulation and less intrusive forms, such as negotiate/arbitrate, in line with the relative market power and degree of contestability for the services provided.<sup>13</sup> This approach is consistent with the view of the NCC, which has indicated that:<sup>14</sup>

“The required extent of regulatory intervention and the structure of the access regime as a whole depend on the nature of the services covered by the access regime. Where the services covered are characterised by an incumbent service provider and many relatively small potential access seekers, a greater degree of regulatory intervention and a more prescriptive access regime may be required to satisfy the clause 6 principles. The greater degree of prescription may be necessary to address, in particular, information and negotiating power asymmetries between access seekers and the infrastructure service provider. Addressing such asymmetries through the access regime may be necessary to facilitate effective access negotiations.”

The Commission has defined three separate categories of transmission services for application of the Rules. These are:

§ *prescribed* transmission services, which constitute those provided by shared network infrastructure that exhibit strong economies of scale and externalities such that competition is unlikely to be feasible, and are limited to those that have relatively uniform preference characteristics across the network, specifically (see Chapter 6A, Rules 6A.2-6A.8):<sup>15</sup>

- use of system services supplied by the shared transmission network which meet (but do not exceed) the network performance requirements specified under legislation of a participating jurisdiction (including instruments made or issued under such legislation, eg, regulations, codes, licences) and the network performance requirements set out in Schedule 5.1 of the Rules;

§ *negotiated* transmission services, which are those dedicated or requested by specific parties and characterised by either a lack of homogeneity, limited market power, or material countervailing power, specifically (see Rules, Part C – “Negotiated Transmission Services – Regulation of Pricing”, 6A.9):<sup>16</sup>

- connection services (entry, exit and TNSP to TNSP connection services);
- use of system services supplied by the shared transmission network that exceed the network performance requirements under any legislation of a participating jurisdiction

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<sup>13</sup> Australian Energy Market Commission, “Rule Determination: National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 No.18” 16 November 2006, pxvi, (Hereafter: ‘AEMC Final Report’).

<sup>14</sup> NCC Guide to Certification, p12, [2.8].

<sup>15</sup> Part C of Chapter 6A of the Rules defines prescribed transmission services and regulates the revenues that may be earned from such services.

<sup>16</sup> Part D of Chapter 6A of the Rules defines negotiated transmission services and regulates the prices that may be charged by TNSPs for the provision of such services.

(including instruments made or issued under such legislation, eg, regulations, codes, licences) or which are above or below the network performance requirements set out in Schedule 5.1 of the Rules; and

- use of system services in respect of agreed transmission network augmentations or extensions for loads, generators and MNSPs; and

§ *market network services*, which are any transmission services that are not, and never have been, the subject of a revenue determination or any prescribed distribution service.<sup>17</sup>

Having classified services in this way, the Rules assign forms of regulation to each, commensurate with their market power characteristics:

§ for *prescribed* transmission services, the Rules require the AER to use a *CPI-X revenue cap* form of price control and the associated revenue allowance using the building block methodology. The Commission has indicated that it considers this approach allows the AER to apply appropriate constraints on the exercise of market power, the recovery of efficient costs while providing incentives for cost efficiency improvements in the future, consistent with the requirements of the NEL;<sup>18</sup>

§ for *negotiated* transmission services, where there are fewer market failure concerns, the Rules specify the less intrusive and less administratively costly *commercial negotiation* form of regulation. The Commission has indicated it expects the end-users of these services to be larger and better resourced, possess countervailing market power, making commercial negotiations a feasible proposition, consistent with the NEM Objective;

§ for *market network services*, *no regulation* applies.

Services that fall outside these definitions, for example consultancy services, are not subject to any form of regulation, and have been treated by the Commission as being outside of the Rules. These services would not satisfy the requirements of clause 6(3)(a) of the CPA, and therefore could not form part of the access regime. Importantly, unlike the previous electricity code, the Rules make no reference to these ‘unregulated services’, since the electricity regulatory regime does not apply to them.

The Rules also provide a definition of a *contestable* service, which for a transmission service is defined as:

“[A] service which is permitted by the laws of the relevant *participating jurisdiction* to be provided by more than one *Transmission Network Service Provider* as a contestable service or on a competitive basis.”

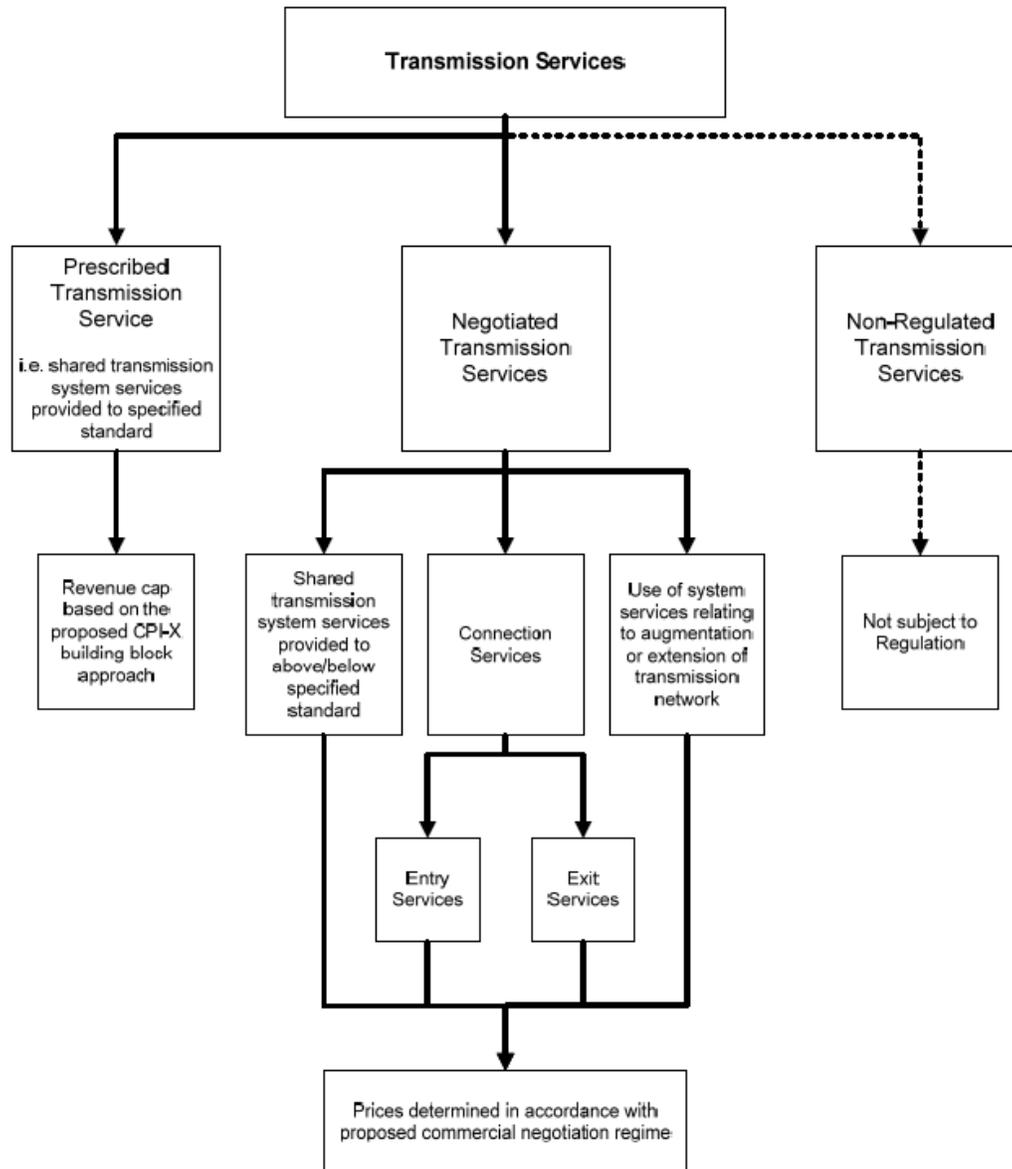
The Rules are silent on the form of regulation to apply to these contestable transmission services, since they fall outside of the definitions of prescribed and negotiable transmission services. Clause 5.3.3(b)(3) provides that a TNSP must inform a connection applicant where a network service is contestable. Importantly, because the definitions for prescribed and negotiated transmission services do not relate to the definition of contestable services, there

<sup>17</sup> Rule 2.5.2 defines the conditions that must be satisfied for a network service to be classified as a market network service.

<sup>18</sup> Section 35(3)(a) and (b), NEL.

is no scope for a state or territory jurisdiction to alter the application of the controlled or negotiated forms of regulation to these services, absent an appropriate Rule change.<sup>19</sup> Figure 1 below summarises the three broad transmission service classifications.

Figure 1: Categories of Transmission Services



<sup>19</sup> This is not the case for negotiable distribution services that excludes contestable distribution services. For distribution therefore, a state or territory jurisdiction could alter the application of the Rules to otherwise negotiable distribution services through the passing of a law making the service contestable. While the presence of this link in the definition of negotiable distribution service to contestable services is unlikely to impact on an application for certification of the electricity regime, it may affect certification if a jurisdiction chose to modify the application of the Rules to distribution services in a specific jurisdiction.

Finally, the Rules incorporate various requirements relating to the standard at which transmission services must be provided. The ‘standard’ requirements are outlined in Schedule 5.1 and 5.1a of the Rules. However, in developing the service definitions, the Commission indicated that it was keen to provide incentives for TNSPs to negotiate prices and terms and conditions for dedicated service and non-standard use of system services directly with generators and large users. Accordingly, there is flexibility in the Rules for services to be provided in excess of these standards by agreement.

Moreover, in its final service taxonomy, the Commission acknowledged that there may be instances where it would be efficient for TNSPs to undertake investments that exceed the Schedule 5.1a and 5.1 requirements in anticipation of future performance requirements. To achieve this, the Commission has defined an *above-standard system shared transmission service* where an above standard investment leads to system-wide benefits. These are each intended to provide further incentives for cost and performance efficiency improvements.

### 3.2.3. Scope for review

Clause 6(4)(d) requires an access regime to provide scope for review of the application of access rights. The national electricity regime provides this requirement through:

- § the Rule change process in Part 7 of the NEL, whereby any person can request the Commission to make a Rule;<sup>20</sup> and
- § the right to judicial review of Commission decisions, contained in Division 3 of the NEL.

These elements of the regime allow any person potentially to alter the coverage of the access regime through proposing a Rule change to that effect. Such a Rule change proposal might be accepted if the market power characteristics of the services, as currently defined, had changed sufficiently to warrant a change to the applicable form of regulation.

### 3.3. Summary

By way of summary, our key conclusions in relation to coverage are:

- § the NEL, the Rules and the *Australian Energy Market Commission Act 2005* would likely form the basis of the electricity access regime for the purposes of certification;
- § the inclusion of the Rule change process, as provided for in Part 7 of the NEL, is unlikely to affect the prospects for *initial* certification of the regime - however to the extent a *subsequent* Rule change might satisfy the Rule making test, but not the CPA requirements, this may result in certification lapsing;
  - to rectify this concern, it may be prudent to require the Commission to take into consideration the CPA requirements, in addition to the NEM Objective, when assessing Rule change proposals;

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<sup>20</sup> Section 91(1) NEL.

- this could potentially be effected through the issuance by the MCE of a suitably framed *Statement of Policy Principles* which, in accordance with s.33 of the NEL, must be considered by the Commission when assessing Rule change proposals;
- § the Commission has split those transmission services subject to regulation under the rules into two broad categories – *prescribed* and *negotiated* transmission services based on their market power characteristics;
- prescribed services are subject to control form of price regulation; while
  - negotiated services are subject to a negotiate form of regulation with access to binding arbitration; and
  - any services falling outside of these two definitions are not subject to any form of regulation; and
- § there is scope for these service definitions – and thus the coverage of the regime – to change through the Rule change and judicial review processes contained in the NEL.

**Conclusion:** The electricity access regime as defined by the NEL and the Rules appears to satisfy the CPA requirements relating to the coverage of services.

## 4. Appropriate Forms of Regulation

The access regime must specify appropriate forms of regulation for the transmission services covered by the regime. In assessing the Commission's approach to classifying transmission services and assigning forms of regulation against the CPA criteria, two key issues emerge.<sup>21</sup>

- § First, has the Commission defined *prescribed* and *negotiated* services consistently with the requirements of the CPA?; and
- § Second, for *prescribed* services, can the regime be said to conform to the balancing criteria specified in clause 6(4)(i) of the CPA?

Before considering these issues we first outline the certification requirements as they relate to the composition of the access framework in greater detail.

### 4.1. Certification Requirements – Forms of Regulation

The relevant requirements regarding the definition of transmission services are contained in clauses 6(4)(a)-(c) of the CPA. In summary, these clauses of the CPA as they relate to the application to the transmission regulatory regime require:

- § the access regime to provide an appropriate form of regulation to the transmission services covered by the regime; and
- § for *prescribed* services, evidence that the regime accounts for the requirements of clause 6(4)(i), meaning that the Commission has undertaken an appropriate balancing of the clause 6(4)(i) factors.

These clauses of the CPA are discussed in greater detail below.

#### 4.1.1. Appropriate forms of regulation

Clause 6(4)(a) of the CPA establishes commercial negotiation as a cornerstone in determining access outcomes, with formal arbitration as the principal mechanism to resolve disputes.<sup>22</sup> The principle includes negotiation on price and other non-price matters such as safety and service standards. It states:

- 6(4) (a) Wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the persons seeking access.

However, markets characterised by certain structural features or dynamics may be poorly suited to the negotiate/arbitrate model of facilitating access. In particular, where countervailing bargaining strength is lacking or significant information asymmetries exist, more intrusive forms of regulation than the negotiate/arbitrate model of access may more

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<sup>21</sup> The access framework must also meet a number of additional requirements under the CPA, eg, that separate accounting arrangements be maintained for those services covered by the regime. These requirements are comparatively straightforward and pose only minor issues, hence they are discussed only briefly in section 7 below.

<sup>22</sup> CPA, clauses 6(4)(g) and (h).

closely replicate the outcome of a competitive market. Employing a negotiate/arbitrate framework in inappropriate circumstances risks creating protracted and costly disputes and inefficient access prices, as the NCC has acknowledged:<sup>23</sup>

“For industries where access seekers have relatively poor information on which to base negotiations and/or where many access disputes are likely, a negotiate/arbitrate model may not ensure efficient outcomes.”

Accordingly, clauses 6(4)(b) and (c) complement clause 6(4)(a) by recognising the need for underpinning regulatory measures where an access provider possesses substantial market power. In conjunction, clauses 6(a)-(c) require an **appropriate balance** between commercial negotiations and more intrusive regulatory intervention to facilitate access. The criteria contemplate that a regime may require independent regulatory guidance on indicative tariffs or reasonable price boundaries to best replicate the outcome of a competitive market. Specifically, the NCC has expressed that a proper consideration of clauses 6(4)(a)-(c) must include:<sup>24</sup>

“[A]n assessment of whether regulatory arrangements establish an environment in which third parties can enter effective access negotiations. In particular, the regulatory framework should appropriately guide market participants to address information and market power asymmetries.”

In this regard, the NCC has indicated that access regimes may legitimately seek to restrict the role of the arbitrator and/or regulator in determining disputes or providing guidance on the terms and conditions of access. Such restrictions may be highly prescriptive, such as embedding into the access regime regulated tariffs that cannot be overturned, or less so, such as specifying asset valuation methodologies that a regulator is to apply.<sup>25</sup> However, the NCC has stated that in those instances where the terms and conditions of access are highly prescribed, the *process* by which those terms and conditions are brought about becomes particularly important.

Provided that regulatory processes are independent, and are also developed through open and transparent processes that allow appropriate stakeholder consultation, the precise regulatory terms and conditions will not be subjected to detailed scrutiny by the NCC.<sup>26</sup> However, the NCC has flagged that further inquiry will be warranted when:

- § the terms and conditions of access are highly prescribed; and
- § it has concerns with the regulatory process that brought about those terms and conditions.

In these circumstances, the NCC has indicated that before granting certification it will turn to consider whether actual and expressed outcomes are appropriate on the basis of the balancing

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<sup>23</sup> NCC Guide to Certification, p15 [2.19].

<sup>24</sup> NCC Guide to Certification, p25, [3.17].

<sup>25</sup> NCC Guide to Certification, p47, [3.109].

<sup>26</sup> NCC Guide to Certification, p48, [3.108].

criteria outlined in clause 6(4)(i). The balancing process implicit in clause 6(4)(i) is outlined in section 4.1.2 below.

#### 4.1.2. Striking an appropriate balance

Clause 6(4)(i) of the CPA sets out a series of considerations that a dispute resolution body must apply when determining terms and conditions of access. Where the *regulator* has at least part responsibility for clause 6(4)(i) – as is the case when the regulator determines prices by applying a regulatory process established in the regime – clause 6(4)(i) requires an appropriate balance to be struck between the range of factors. Specifically:

- 6(4) (i) In deciding on the terms and conditions for access, the dispute resolution body should take into account:
- (i) the owner’s legitimate business interests and investment in the facility;
  - (ii) the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets;
  - (iii) the economic value to the owner of additional investments that the person seeking access or the owner has agreed to undertake;
  - (iv) the interests of all persons holding contracts for use of the facility;
  - (v) firm and binding contractual obligations of the owner or other persons (or both) already using the facility;
  - (vi) the operational and technical requirements necessary for the safe and reliable operation of the facility;
  - (vii) the economically efficient operation of the facility; and
  - (viii) the benefit to the public from having competitive markets.

To further assist in delineating this balancing exercise, the NCC has usefully indicated that the criteria can be grouped into three broad categories, as follows:<sup>27</sup>

§ criteria (i), (iv) and (v), which account for **the interests of the facility owner** and existing facility users;

§ criteria (ii), (iii) and (vi), which account for the **costs of providing access**. Such costs must be necessary and not reflect ‘gold-plating’ or other unnecessary measures; and

§ criteria (vii) and (viii), which expressly account for **efficiency objectives** and the benefits arising from competitive markets.

These categories are not mutually exclusive, which means that difficulties can arise when the criteria conflict. To this end, the NCC has indicated that the requirements will be satisfied

<sup>27</sup> NCC Guide to Certification, p57, [3.147].

provided the outcomes of the regulatory process are likely to lie within an ‘appropriate range’, taking into account the clause 6(4)(i) criteria and the underlying intent of Part IIIA of the TPA.<sup>28</sup> In specifying the bounds of an ‘appropriate range’ the Council has noted that:<sup>29</sup>

“[T]he underlying objective of Part IIIA ... is to promote efficiency. The Council considers that a universal goal for economic regulation is to replicate (as far as possible) the efficiency outcomes that could otherwise be expected from the existence of effective or workable competition ... On this basis, the Council considers that outcomes in an effective access regime can be expected to lie within a range of outcomes consistent with those likely to be achieved in an effectively competitive market.”

In other words, those components of the access regime which depart from commercial negotiations as the means of facilitating access and for which the NCC has reservations regarding the regulatory processes will be assessed by reference to a widely accepted yardstick of regulatory effectiveness.

## 4.2. Application to Electricity Transmission Services

To recap, there are two principal issues that must be considered when examining the framework contained in the electricity regulatory regime. First, does the national electricity regime appropriately define *prescribed* versus *negotiated* services? Second, for *prescribed* services, can the regime be said to conform to the balancing criteria specified in clause 6(i) of the CPA. These issues are addressed in turn below.

### 4.2.1. Does the regime appropriately define transmission services?

The Commission’s approach to defining transmission services and the relevant form of regulation to apply to each was informed by an assessment of the relative market power characteristics for each defined service:

- § for **prescribed services**, where the Commission believed there was significant potential for the exercise of market power by TNSPs, the Rules provide for access via a revenue cap form of price control, based on the building block methodology;
- § for **negotiated services**, where there are likely to be fewer market failure concerns, the Commission specified in the Rules for a commercial negotiation form of regulation; and
- § for **services that fall outside these definitions**, eg, consultancy services, no regulation applies.

The Commission appears to have been highly cognisant of the need to aim to replicate as closely as possible the outcome of a competitive market in determining the forms of regulation to apply to access. Throughout its review of the economic regulation of transmission services the Commission has repeatedly emphasised that the key role of

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<sup>28</sup> NCC Guide to Certification, p49, [3.111].

<sup>29</sup> NCC Guide to Certification, p57, [3.149].

economic regulation is to support measures to contain the exercise of market power with targeted incentives for efficient investment and operation of transmission services:<sup>30</sup>

“Providing incentives to regulated businesses is intended to reproduce, to the extent possible, the behaviours and outcomes that would occur in an effectively competitive market. Such incentives are an important means of addressing the information asymmetry problem and of aligning the performance of TNSPs with the interests of network users.”

The classification exercise implicit in clauses 6(a)-(c) as articulated by the NCC thus appears to be wholly consistent with the approach employed by the Commission in classifying transmission services in its recent review of the Rules relating to the economic regulation of transmission services. In deciding upon this broad taxonomy, the Commission was of the view that:<sup>31</sup>

- § its approach to **prescribed services** allows the AER to apply appropriate constraints on the exercise of market power, whilst facilitating the recovery of efficient costs and providing incentives for cost efficiency improvements in the future, consistent with the requirements of the NEL; and<sup>32</sup>
- § for the expanded ambit of services to which **commercial negotiations** apply, the end-users of those services are likely to be larger and better resourced, and possess countervailing market power, making such negotiations a feasible and efficient proposition.

In assigning the forms of regulation to apply to each transmission service – and thus the means by which access is obtained – the Commission has therefore very likely struck an appropriate balance between commercial negotiations and more intrusive regulatory intervention, consistent with the CPA requirements.

Furthermore, the Rules seem to provide sufficient direction and guidance about the **regulatory principles and procedures** governing the obtainment of access to *prescribed* transmission services. This would therefore likely preclude the NCC from undertaking an assessment of the regulatory arrangements pertaining to prescribed services by reference to clause 6(4)(i) of the CPA.<sup>33</sup> Indeed, the framework would appear to feature robust regulatory design and should, over time, increase the predictability and consistency of regulatory decision making. In particular:

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<sup>30</sup> AEMC Draft Report, pxvii.

<sup>31</sup> Australian Energy Market Commission, “Review of the Electricity Transmission Revenue and Pricing Rules: Transmission Revenue: Rule Proposal Report, Draft National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006, February 2006, p35 (Hereafter: “AEMC Draft Report”).

<sup>32</sup> Section 35(3)(a)&(b), NEL.

<sup>33</sup> The NCC has indicated that in those circumstances where the regulator becomes the de facto dispute resolution body – as is effectively the case when the AER determines the regulated revenue cap under chapter 6 – it will undertake a clause 6(4)(i) assessment if it feels the regulatory processes were deficient. See the discussion in section 4.1.2 for more detail.

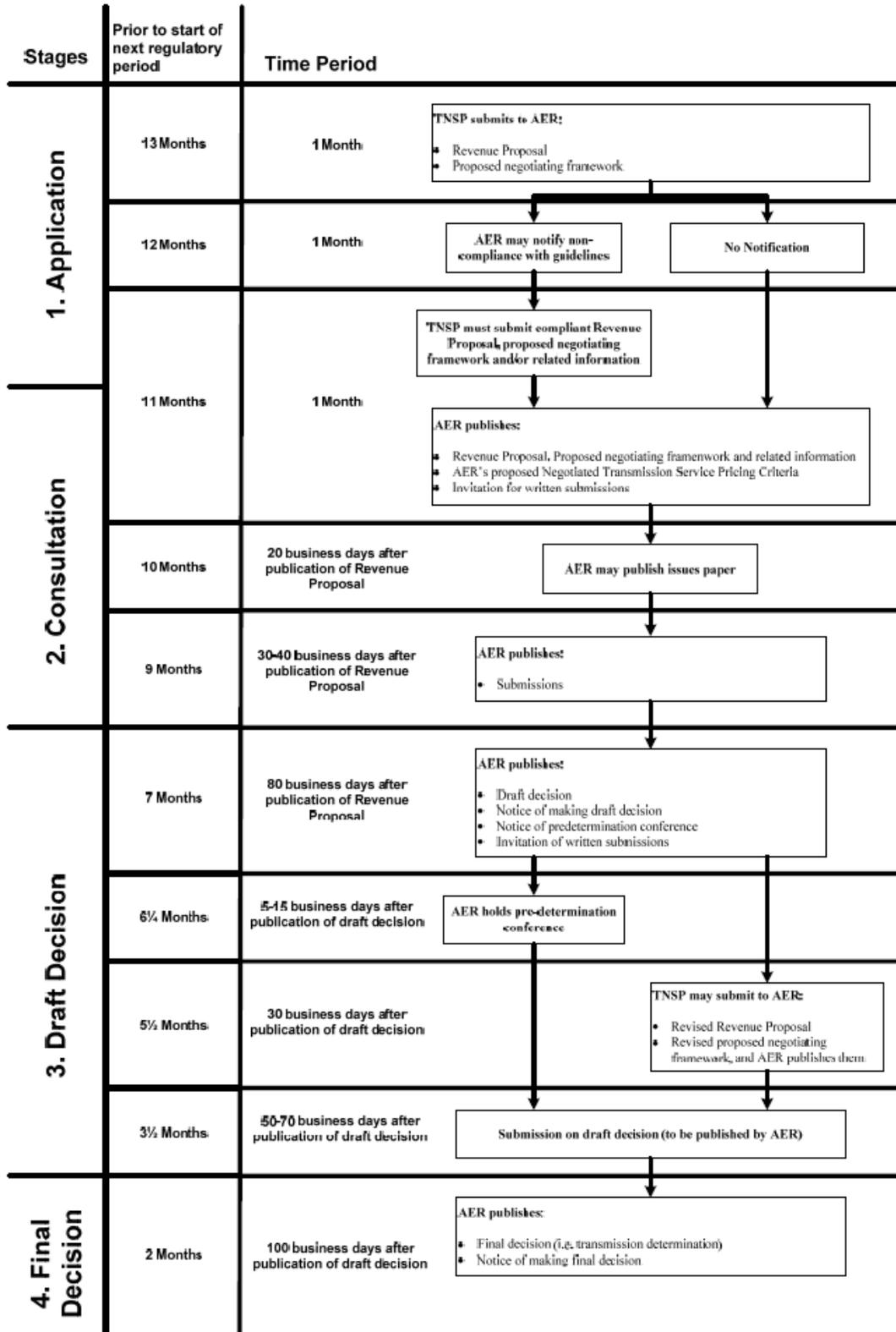
- § the Rule making process that brought about the regulatory regime relating to both prescribed *and* negotiated services (ie, the review of the economic regulation of transmission services) has involved an open, transparent regulatory decision making process; and
- § the regulatory processes ultimately enshrined within the Rules – particularly as they relate to *prescribed* services – are likely to result in terms and conditions for access that will maximise market efficiency.

The Rule making process *itself* has involved, and will likely continue to involve, substantial formal consultation and numerous opportunities for involvement by all interested stakeholders. Moreover, the transparent and timely processes incorporated in Part E of the rules *following* the Rule making process appear well suited to:

- § reduce regulatory risk, which is a key requirement for effective regulation;
- § provide certainty about the dates for regulatory decisions knowing there is no scope for delays;
- § provide TNSPs with an incentive to provide their best available information; and
- § require the AER to assess proposals in a timely manner.

The Part E process codifies the comparative regulatory practice under the ACCC's *Statement of Regulatory Principles* ('SRP'). A high-level summary of the regulatory process is reproduced in figure 2 below.

Figure 2: Timeline for Regulatory Processes



The codified regulatory processes will very likely improve the efficiency and quality of regulated decisions pertaining to the terms and conditions of access for prescribed services. In turn, this will improve the likelihood that market outcomes will better reflect those obtainable in an effectively competitive market. In other words, the actions of the Commission in classifying prescribed and negotiated transmission services were procedurally robust.

Nevertheless, were the NCC to have some concerns with these regulatory processes, it would need to consider the access arrangements for prescribed services by reference to the clause 6(4)(i) criteria. Our assessment of the regulatory framework relating to prescribed services against the clause 6(4)(i) requirements is outlined below.

**Summary:** In assigning the forms of regulation to apply to each transmission service the Commission has very likely struck an appropriate balance between commercial negotiations and more intrusive regulatory intervention, consistent with the CPA requirements. The Rules seem also to provide sufficient direction and guidance about the regulatory principles and procedures governing the obtainment of access to *prescribed* transmission services.

#### 4.2.2. Was an appropriate balance struck for *prescribed* services?<sup>34</sup>

If the NCC were to examine the regulatory framework relating to prescribed transmission services against the clause 6(4)(i) criteria, the balancing exercise undertaken by the Commission in specifying prescribed versus negotiated services would very likely conform to the requirements articulated by the NCC. In determining the regulatory arrangements governing terms and conditions for prescribed services, the Commission has indicated that it sought to reflect and balance the need for economic regulation to provide:<sup>35</sup>

- § “an appropriate degree of certainty about the regulatory framework and investment environment in order to encourage timely and efficient development of network capacity;
- § effective incentives to encourage TNSPs to build and operate their systems efficiently;
- § incentives for TNSPs to effectively manage the risks that are reasonably within their control; and
- § incentives for TNSPs to improve service quality where this is sufficiently valued (collectively) by customers and disincentives for TNSPs to increase profitability by inefficiently reducing service quality, particularly at times where it is most valued by the market.”

This approach appears to be wholly consistent with the balancing exercise contemplated by clause 6(4)(i) in that it expressly accounts for:

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<sup>34</sup> Note that this assessment relates solely to *prescribed* services, for which the AER is essentially the dispute resolution body (subject to judicial review). The clause 6(4)(i) criteria as it relates to negotiated services is discussed in section 6.2 below when the chapter 8 and 6A dispute resolution frameworks are examined.

<sup>35</sup> AEMC Draft Report, pxviii.

- § the **interests of the facility owner** and the **costs of providing access**, that is, by endeavouring to provide certainty surrounding the regulatory framework and incentives to effectively manage risks; and
- § **efficiency objectives**, that is, by encouraging TNSPs to build and operate their systems efficiently and improve service quality where this is sufficiently valued by customers.

Indeed, the Rules provide a number of incentives to achieve this balance. For example, efficient investment and operational incentives that balance the interests of the facility owners and the costs of providing access within the building blocks regime are provided through, among other measures, the following:

- § the CPI-X revenue cap rewards out-performance and penalises under performance relative to the capped revenue forecast;
- § capital expenditure will not be optimised except in specific situations where the TNSP has failed to reasonably manage the risks of commercial stranding;
- § the efficiency incentive for capital expenditure will include both depreciation and the cost of capital in the calculation of the associated rewards and penalties;
- § the allowed rate of return on assets will be based on benchmark assumptions, which will encourage TNSPs to pursue strategies to lower their cost of capital relative to the regulatory WACC as they will be entitled to retain the difference within the regulatory period; and
- § the operating expenditure efficiency incentive scheme provides for symmetrical rewards and penalties which can be carried over to the next period to provide even incentives in each year of the regulatory control period.

Similarly, incentives for efficient investment in, and operation of, the transmission system in circumstances of cost or timing uncertainties and/or major unforeseen conditions and events are provided for in the rules through the following measures:

- § a separate contingent projects regime applies for capital expenditure required for specific large projects triggered by particular events, with an associated incentive mechanism similar to that applicable to other capital expenditure;
- § scope to reopening revenue cap determinations in genuine *force majeure*- situations; and
- § the provision of an allowance for appropriate pass-through of costs to avoid exposing TNSPs to risks that are beyond their reasonable control.

Accordingly, whilst the NCC is unlikely, in practice, to turn its mind to such matters, the balancing exercise the Commission has undertaken appears to be consistent, and in satisfaction of, the requirements in clause 6(4)(i). The Rules as they relate to the economic regulation of transmission services, are clearly intended to provide a balanced package of incentives for TNSPs to facilitate access to prescribed transmission services efficiently, whilst accounting for the costs of providing access and TNSPs legitimate interests, thereby maintaining the quality and reliability of such services.

**Summary:** The balancing exercise the Commission has undertaken in determining prescribed services, and the form of regulation applicable to those services, appears to satisfy the requirements in clause 6(4)(i).

### 4.3. Summary

By way of broad summary, our key conclusions in relation to the taxonomy of transmission services and the applicable forms of regulation are:

- § the regulatory regime developed by the Commission for the economic regulation of prescribed and negotiated transmission services in chapter 6A of the Rules is consistent with the CPA requirements for access:
- the Commission’s approach to defining prescribed versus negotiated services, which balances the market power elements against the benefits arising from less intrusive forms of regulation, is very likely consistent with the requirements of clauses 6(4)(a) to (c); and
  - although the NCC would be unlikely to find it necessary to consider whether the Commission’s approach to defining prescribed services was consistent with the requirements of clause 6(4)(i) of the CPA, were it to do so the requirement would very likely be met.

**Conclusion:** The electricity access regime as defined by the NEL and the Rules is currently likely to satisfy the CPA requirements relating to the appropriate form of regulation for covered services.

## 5. Enforceable Right to Access

To obtain certification an access framework must not only appropriately define the respective services within its ambit, but also it must provide an *enforceable right to access* those services. In assessing whether the national electricity regime bestows such a right, two key issues emerge:

- § First, does the interaction between chapters 5 and 6A of the rules, combined with an AER determination and/or judicial review create an enforceable right to access *prescribed* transmission services?; and
- § Second, does the interaction between chapters 5, 6A and 8 create an enforceable right to access *negotiated* transmission services?

Before considering these issues we first outline the certification requirements as they relate to the composition of the access framework in greater detail.

### 5.1. Certification Requirements – Enforceable Right of Access

The relevant requirements regarding the enforceable right of access are contained in clauses 6(4)(b) and (c) of the CPA. Clause 6(4)(b) of the CPA requires an access regime to establish a *legal right* for parties to negotiate access and clause 6(4)(c) requires a credible enforcement process to support this right. Specifically, they state:

- 6(4) (b) Where such agreement cannot be reached, Governments should establish a right for persons to negotiate access to a service by means of a facility.
- (c) Any right to negotiate access should provide for an enforcement process.

The importance of a regime bestowing such a right was emphasised by the NCC during the recent review of the Gas Access Regime. It cautioned that the absence of binding arbitration under the proposed price monitoring option would preclude certification:<sup>36</sup>

“[T]he Commission’s current proposal does not meet the requirements of the CPA. In order for an access regime to be certified as effective, clause 6(4)(c) of the CPA requires the access regime to include a means to enforce the access rights granted by coverage ... the Council considers that it is essential for any price monitoring regime operating under the Gas Code to include a mechanism for resolving access disputes.”

In other words, an effective access framework must appropriately define the respective services within its ambit, in addition to providing an enforceable right to access those services on certain terms and conditions.

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<sup>36</sup> National Competition Council, *Submission in response to Productivity Commission’s draft report on the review of the National Gas Access Regime*, March 2004, p13.

## 5.2. Application to Electricity Transmission Services

To determine whether the national electricity regime creates an enforceable right to access regulated transmission services it is necessary to consider the process for obtaining access. These processes are determined largely by the *type* of transmission service for which access is sought. Specifically:

- § to receive negotiated or prescribed transmission services, a registered participant must first *physically connect* to a transmission network - the framework for establishing or modifying a connection is contained in **chapter 5** of the Rules;
- § for *prescribed* services, the terms and conditions of access are determined in accordance with the requirements in **chapter 6A** and an associated **AER revenue determination**; and
- § for *negotiated* services, ‘price’ terms for access are determined in accordance with the requirements in **chapter 6A** and ‘non-price’ terms and conditions are determined in accordance with the requirements of **chapter 8**.

The key issue to satisfy the CPA requirements is whether this approach creates an enforceable right to access *prescribed* and *negotiated* transmission services, respectively. In the following sections we first examine the content and operation of chapters 5, 6A and 8 of the Rules, and then assess whether the interaction between these Rules creates an enforceable right to access the covered transmission services.

### 5.2.1. Chapter 5 – connecting to a transmission network

To receive network services, a person must physically connect to a transmission network. Chapter 5 of the Rules provides the framework for establishing or modifying such connections. It establishes:

- § the **principles and guidelines** governing connection and access to a network (clause 5.1.2(a)(2)(i)); and
- § the **process** by which an access seeker may obtain or modify a network connection (clause 5.1.2(a)(2)(ii)).

It specifies (amongst other things) that:

- § all registered participants should have the *opportunity to form a connection* (clause 5.1.3(a));
- § the terms and conditions upon which that connection is granted, and the service offered, should be set out in *commercial agreements on reasonable terms* (clause 5.1.3(b)); and
- § subject to certain exceptions, the technical terms and conditions of connection agreements should comply with *minimum standards of performance*, with the object that the *power system operate securely and reliably* (clause 5.1.3(b1)).

Schedules 5.1 and 5.1a of chapter 5 also denote various power system performance and quality of supply standards with which registered participants must comply. Overall, the purpose of chapter 5 is to bring long-term benefits to registered participants in terms of the

cost and reliability of the power system, and to encourage open communication and information flows (clause 5.1.3(d)).

Rule 5.3 details the process by which connections are to be established or modified. A registered participant, or a person eligible to become a registered participant wishing to connect must first lodge a *connection enquiry* with the local TNSP (clause 5.3.2(a)), which must, to the extent possible, detail the technical requirements of the connection (clause 5.3.2(d)). In its response, the pertinent TNSP must provide a range of material to the access seeker, including:

- § the identity of other participants that will need to be involved in planning to make the connection (clause 5.3.3(1)(i));
- § a *preliminary program* showing proposed milestones for connection and access activities (clause 5.3.3(b)(4)); and
- § written details for each technical requirement related to relevant access standards (clause 5.3.3(b1)).

An access seeker may then make an *application to connect* in accordance with Rules 5.3.4 and 5.3.4A, containing the specified information and the relevant application fee. An *application to connect* may be at:

- § the automatic access standard specified in Rule 5.3.4;
- § at any applicable plant standard; or
- § at a negotiated access standard, provided that standard is:
  - no less onerous than the corresponding *minimum access standard* (clause 5.3.4A(a)(1));
  - set at a level that *will not adversely affect power system security* (clause 5.3.4A(a)(2)); and
  - set at a level that *will not affect the quality of supply for other network users* (clause 5.3.4A(a)(3)).

The service provider must then prepare an *offer to connect* in response. In so doing it must (among other things):

- § use its *reasonable endeavours* to advise the access seeker of all risks and obligations in respect of the proposed connection associated with planning and environmental laws outside the rules (clause 5.3.5(b)); and
- § provide *such other additional information* in relation to the application to connect as the access seeker reasonably requires to assess the technical performance and costs of the required connection (clause 5.3.5(c)).

Subject to certain exceptions, the *offer to connect* must be made within the time period specified in the *preliminary program* (clause 5.3.6(a)) and must contain (among other things):

- § for each technical requirement, the applicable service standard, whether automatic or negotiated (clause 5.3.6(b)(1));
- § details of the connection point (schedule 5.6(a));
- § authorised demand which may be taken or supplied at the connection point (schedule 5.6(c));
- § connection service charges (schedule 5.6(d));
- § agreed protocols for maintenance coordination (schedule 5.6(j)); and
- § arrangements relating to load shedding (schedule 5.6(k)).

The *offer to connect* must be *fair and reasonable* and *consistent with the safe and reliable operation of the power system* (clause 5.3.6(c)). The TNSP must also use its *reasonable endeavours* to provide the applicant with an offer to connect in accordance with its *reasonable requirements*, including without limitation (clause 5.3.6(d)):

- § the location of the connection point; and
- § the level and standard of power transfer capability that the network will provide.

Chapter 5 specifies that connection applicants and TNSPs are entitled to negotiate with each other in respect of the provision of the connection and, if such negotiations occur, each is required to conduct such negotiations *in good faith* (clause 5.3.6(g)).

If the connection applicant wishes to accept an *offer to connect*, it then enters into a *connection agreement* with the service provider. That offer must conform to the requirements specified in Rule 5.4A. Specifically, parties must negotiate *in good faith* to reach agreement in respect of the *access arrangements* sought by the connection applicant (clause 5.4A(b)). As a basis for negotiations:

- § the connection applicant must provide (clause 5.4A(c)):
  - its generating units (in the case of a generator);
  - its network elements (in the case of a network service provider);
  - its plant (in the case of any other connection applicant); and
- § the service provider must provide any information as is reasonably requested to allow it to fully assess the commercial significance of the access arrangements.

The service provider must also use *reasonable endeavours* to provide the access arrangements being sought, subject to those arrangements being consistent with good electricity practice. This obligation is subject to the potential augmentations or extensions required to be undertaken on all affected transmission and/or distribution networks considering the requirements of other affected registered participants (clause 5.4A(e)).

If the parties fail to reach an agreement, either party may initiate the dispute resolution procedure contained in either chapter 6A or 8, as the case may be. In other words, chapter 5 seems only to bestow a *right to negotiate* with a TNSP, and recourse to the dispute resolution

mechanisms contained in chapter 6A and chapter 8. These mechanisms are examined in turn below.

**Summary:** Nothing residing in chapter 5 of the Rules appears to grant an access seeker an enforceable right to access any transmission network service. Chapter 5 seems only to bestow a *right to negotiate* with a TNSP, and recourse to the dispute resolution mechanisms contained in chapter 6A and chapter 8 of the Rules.

## 5.2.2. Chapter 6A – ‘price’ issues

The application of chapter 6A differs in its treatment of *prescribed* transmission services as distinct from *negotiated* transmission services. These are addressed in turn below.

### 5.2.2.1. Prescribed services

For *prescribed services*, chapter 6A provides for access via a **revenue cap** form of price control, based on the building block methodology (see chapter 6A, Rules 6A.2-6A.8). The Rules give effect to that form of control as follows:

§ a service provider must prepare and submit to the AER a *revenue proposal* (see Chapter 6A, Part E – “Revenue Determinations and Negotiating Frameworks”, Rules 6A.10-6A.16) that complies with the requirements in chapter 6A, and in particular must:

- be prepared using the post-tax revenue model (Rule 6A.5); and
- comply with the requirements of the submission guidelines (Rule 6A.10.2).

§ the AER must respond to the revenue proposal by preparing a *revenue determination* for the relevant revenue regulatory control period that must:

- contain all of the elements specified in the Rules, for example, appropriate methodologies for the indexation of the regulatory asset base (Rule 6A.4.2); and
- adhere to the regulatory procedures outlined in the rules, including specified decision-making timeframes (Rule 6A.10).

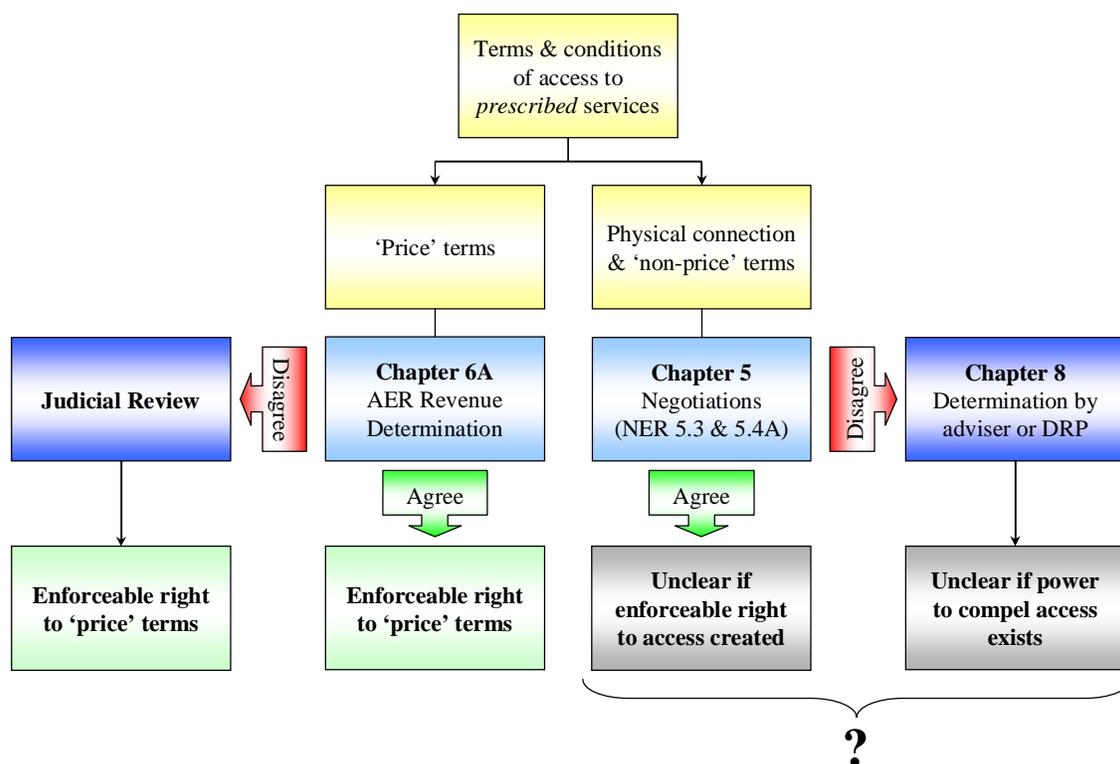
In other words, if access is sought to a *prescribed* service, it is intended that the terms and conditions of access are wholly governed by Parts B, C and E of chapter 6 of the Rules, which respectively set out the framework for the economic regulation of prescribed transmission revenue. These chapters specify the means by which the AER must determine revenue and prices for access. There is no direct interaction between an access seeker and a provider, other than in the initial obtainment of a network connection, which is governed by Rules 5.3 and 5.4A.<sup>37</sup> Disputes regarding an AER price determination are subject to judicial review, rather than a regulatory dispute resolution process.<sup>38</sup>

<sup>37</sup> See section 5.2.1 above for a detailed discussion of the chapter 5 process.

<sup>38</sup> The MCE has indicated that it intends to provide a limited merits review process for decisions by the AER in relation to price determinations. This will also form part of the dispute resolution mechanism for prescribed services.

The clear policy intent of the chapter 6A framework is to compel service providers to grant registered participants access to prescribed services in accordance with the pricing terms and conditions determined by the AER, or a judicial review process, at the non-price terms and conditions governed by Rules 5.3 and 5.4A, outlined above. However, despite that ostensible intention, it is not clear that the framework achieves that outcome. As figure 3 below illustrates, it appears that at no place in the Rules is there an explicit requirement placed on service providers compelling access on certain terms and conditions.

Figure 3: Access to *Prescribed* Transmission Services



Absent a Rule either explicitly bestowing a right to access prescribed services, or expressly empowering a dispute resolution body to compel access, there must therefore be some doubt about whether the national electricity regime does in fact bestow an enforceable right of access to prescribed transmission services. Accordingly, despite the clear policy intent to the contrary, it is currently unclear whether the framework contained in chapter 6A (and partly in chapter 5) for facilitating access to *prescribed* services is consistent with the clause 6(b) and (c) requirements in the CPA.

**Summary:** Neither chapter 6A nor chapter 5 appear to contain an explicit Rule bestowing an enforceable right to access *prescribed* transmission services. Thus, despite the clear policy intent to the contrary, it is unclear whether an enforceable right of access to *prescribed* services can be said to exist under the national electricity regime.

### 5.2.2.2. Negotiated services

For *negotiated services*, where there are likely to be fewer market failure concerns, chapter 6A provides for access via a **negotiate/arbitrate** form of regulation (see chapter 6A, Part C – “Negotiated Transmission Services – Regulation of Pricing”, 6A.9). The chapter 6A process is limited to negotiations and disputes concerning (Rules 6A.9.1, 6A.9.2(c), 6A.9.4(a), 6A.9.8):

- § the **price** of negotiated transmission services; and
- § the amount of any **access charge**.

The chapter 6A mechanism operates in conjunction with the aforementioned chapter 5 framework. In particular, Rule 6A.9.2 states that when negotiating prices and access charges for negotiated transmission services, parties must also comply with:

- § Rules 5.3 and 5.4A, when negotiating for the provision of connection services and the associated connection service charges; and
- § Rule 5.4A when negotiating the use of system service charges and access charges to be paid to or by a network user.

The chapter 6A framework for accessing negotiated services comprises two discrete stages – commercial negotiation followed by commercial arbitration if necessary.

#### 5.2.2.2.1. Stage 1: commercial negotiations

The Rules give effect to the negotiation regime by requiring a TNSP to prepare a *negotiation framework*, setting out the procedure to be followed during negotiations (Rule 6A.9.5). This document must comply with applicable *transmission determinations* (clause 6A.9.5(b)(1)) and must, at a minimum, specify (among other things):

- § a requirement for the provider and access seeker to *negotiate in good faith* (clause 6A.9.5(c)(1));
- § a requirement for a provider and access seeker alike to provide *all reasonable commercial information* as may reasonably be require by the other party to enable it to engage in effective negotiation (clauses 6A.9.5(c)(2) and (4));
- § a requirement for the provider to (clause 6A.9.5(c)(3)):
  - identify and inform the access seeker of all *reasonable costs* and/or the increases and decreases in costs of providing the negotiated service; and
  - demonstrate to the access seeker that the charges for providing the negotiated service reflect those costs and/or the cost increment or decrement;
- § a *reasonable period of time* for commencing, progressing and finalising negotiations, and a requirement that each party use reasonable endeavours to adhere to such time-frames (clause 6A.9.5(c)(5));
- § a process for dispute resolution in accordance with S6A.3 (clause 6A.9.5(c)(6));

- § the arrangement for payment by an access seeker of a provider's *reasonable direct expenses* incurred in processing the application (clause 6A.9.5(c)(7)); and
- § as outlined above, a requirement that the negotiating framework be in no way inconsistent with the requirements of Rules 5.3, 5.4A and Part C of chapter 6A (clause 6A.9.5(c)(8)).

A TNSP must also comply with the *negotiated transmission service pricing criteria*, which specifies the applicable pricing principles for such services (Rule 6A.9.1). This is to be approved by the AER as part of a *transmission determination*. It is to set out the criteria that are to be applied by the provider in negotiating prices and access charges (clause 6A.9.4(a)(1)). This criteria must give effect to and be consistent with the *negotiated transmission service pricing principles* set out in Rule 6A.9.1, which state (among other things):

- § the price for a negotiated service should be based on the *costs incurred* in providing that service (clause 6A.9.1(1));
- § the price for a negotiated service should in most cases be at least equal to the *avoided* cost of providing it but no more than the cost of providing it on a *stand-alone* basis (a floor/ceiling test) (clause 6A.9.1(2));
- § prices must be the same for all users unless a *material cost difference* exists (clause 6A.9.1(5));
- § prices should be *adjusted over time* to the extent the assets used to provide the service are provided to other persons, in which case adjustments should reflect the extent to which the costs of that asset are being recovered through charges to those other persons (clause 6A.9.1(6));
- § prices should be based on terms and conditions that are *consistent with the safe and reliable operation of the power system* in accordance with the Rules (clause 6A.9.1(7));
- § the price should enable the provider to recover the *efficient costs of complying with all regulatory obligations* associated with the provision of negotiated services (clause 6A.9.1(8));
- § the price should take into account the need for the service to be provided in a manner that *does not adversely affect the safe and reliable operation of the power system* in accordance with the Rules (clause 6A.9.1(9)).

If commercial negotiations are successful, the parties may execute a written agreement recording the details of that agreement (schedule 6A.3.7(a)). However, Rule 6A.9.7 explicitly limits the scope of that agreement. It states that nothing in chapter 6A imposes an obligation on a service provider to *provide service* to an access seeker. This is deliberately intended to confine the chapter 6A negotiations to matters of price, thereby preserving the integrity of the chapter 8 mechanisms outlined below.

Thus, whilst a written agreement can create a binding obligation on a provider to adhere to the negotiated *pricing* terms and conditions, it *cannot compel access to the services themselves*. Failure to comply with the agreed pricing terms constitutes a breach of the Rules,

in relation to which the AER may take action under the NEL (clause S6A.3.7(c)).<sup>39</sup> Alternatively, if negotiations are unsuccessful and no agreement is reached, an arbitration process ensues.

**Summary:** Nothing in chapter 6A imposes an obligation on a service provider to provide access to negotiated transmission *services*. The scope of the chapter 6A negotiation process is intentionally limited to *pricing* terms and conditions as distinct from the obtainment of access itself.

#### 5.2.2.2.2. Stage 2: commercial arbitration

The arbitration process is initiated by a provider or an access seeker notifying the AER in writing that a dispute exists (schedule 6A.3.2). The AER must then appoint a commercial arbitrator following the nomination of two persons by each party (sub-schedules 6A.3.3(a) and (b)). The arbitrator is required to be experienced in dispute resolution techniques (sub-schedule 6A.3.3(c)) and have no conflict of interest (sub-schedule 6A.3.3(d)). The arbitrator may then give to the parties such directions as it considers necessary, including in relation to:

- § the provision of documents and information to the other party and the making of oral and written submissions (sub-schedule 6A.3.4(a)(1));
- § the use and disclosure of information (sub-schedule 6A.3.4(a)(2)); and
- § the participation (if any) of legal representatives in proceedings (sub-schedule 6A.3.4(a)(3)).

In determining the dispute, the commercial arbitrator must apply the aforementioned *negotiated transmission service pricing criteria* (sub-schedule 6A.3.5(a)) and must determine the dispute as quickly as possible and at most, within 30 business days (sub-schedule 6A.3.5(b)).<sup>40</sup> However, schedule 6A.4.1 limits the scope of an arbitrator's determination. Specifically, determinations must be limited to disputes concerning the price of negotiated transmission services and the amount of any access charge. This limitation results in the commercial arbitrator:

- § being required to 'assume' the terms and conditions for the provision of the relevant negotiated transmission service (clause 6A.3.5(b)(1)(ii)); and
- § being precluded from ordering the relevant transmission network service provider to provide that service (sub-schedule SA.3.5(c)).

Like Rule 6A.9.7 in the negotiation framework, the intent of schedule 6A.4.1 is to confine chapter 6A arbitrations to matters of price, thereby preserving the integrity of the chapter 8 mechanisms outlined below. Thus, whilst an arbitrator's determination creates a binding obligation on parties to adhere to the negotiated *pricing* terms and conditions, it *cannot*

<sup>39</sup> It is worth reiterating, however, that the agreement is only enforceable insofar as it relates solely to the price for negotiated services and/or access charges.

<sup>40</sup> The costs of the commercial arbitrator are generally borne equally by the parties (sub-schedule 6A.3.6(a)) and the costs of determining the dispute itself may be allocated by the arbitrator in its determination (sub-schedule 6A.3.5(b)).

*compel the provider to provide access to the services themselves.* Any failure to comply with the pricing terms and conditions for negotiated services so determined constitutes a breach of the Rules in respect of which the AER may take action under the NEL (sub-schedule 6A.3.7(c)).<sup>41</sup>

**Summary:** Chapter 6A explicitly precludes a commercial arbitrator from granting access to *negotiated* transmission services. An arbitrator's power is limited to determinations related to *pricing* terms and conditions of access – it cannot mandate access itself.

### 5.2.3. Chapter 8 – ‘non-price’ issues

The chapter 8 dispute resolution process governs disputes over the **non-price terms and conditions of access**, specifically:

- § the non-price terms of access contained in connection agreements (clause 8.2.1(4));
- § the failure of any registered market participants to reach an agreement on a non-price matter where the rules require negotiations in good faith, for example, negotiations in respect of the provision of a connection (clause 8.2.1(2));
- § any non-price matter relating to or arising out of the Rules to which a contract between two or more registered market participants provides that the chapter 8 dispute resolution procedures are to apply (clause 8.2.1(6)); and
- § any non-price matter relating to or arising out of the Rules in respect of which two or more registered market participants have agreed in writing that chapter 8 should apply (clause 8.2.1(7)).

Clause 8.2.1(e) specifies that it is intended that the chapter 8 framework should, to the extent possible:

- § be guided by the NEM objective;
- § be simple, quick and inexpensive;
- § preserve and enhance the relationships between the parties to the dispute;
- § take account of the skills and knowledge that are required for the relevant procedure;
- § observe the rules of natural justice;
- § place emphasis on conflict avoidance;
- § encourage resolution of disputes without formal legal representation or reliance on legal procedures.

Like its chapter 6A counterpart, the chapter 8 framework comprises two discrete stages – commercial negotiation followed by binding adjudication by a dispute resolution adviser (‘adviser’) or a dispute resolution panel (‘DRP’) if necessary.

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<sup>41</sup> Again, the determination is only binding insofar as it relates solely to the price for negotiated services and/or access charges.

#### 5.2.3.1.1. Stage 1: commercial negotiations

The first stage is initiated by a party serving a notice on another market participant outlining the particulars of the dispute (clause 8.2.4(a)), at which point commercial negotiations commence between market participants. Rule 8.2.2 requires the AER to appoint a *dispute resolution adviser* to ensure the effective operation of the dispute resolution process (clause 8.2.2(a)). Commensurately, Rule 8.2.3 requires each registered market participant and NEMMCO to adopt and implement a *dispute management system* that must, among other things:

- § be consistent with guidance notes from the adviser (clause 8.2.3(b)(1));
- § provide that the party must respond to a request for information from another registered participant in relation to any of the disputes set out above within 5 business days (clause 8.2.3(b)(3));
- § set out the procedures that the party must follow in responding to requests for information from other registered participants (clause 8.2.3(b)(4)); and
- § set out any requirements and procedures necessary to ensure the party is able to comply with the time-limits and requirements outlined in figure 4 below (clause 8.2.3(b)(5)).

If commercial negotiations are successful, the parties may execute a written agreement recording the details of that agreement (clause 8.2.9(a)). Failure to comply with the terms and conditions of such an agreement constitutes a breach of the Rules of which the AER may take action in accordance with the NEL. Alternatively, if commercial negotiations fail, the second stage ensues.

#### 5.2.3.1.2. Stage 2: dispute resolution adviser or dispute resolution panel

In the second stage of the chapter 8 dispute resolution framework, the parties may agree to resolve a dispute in one of two ways:

- § by any means the adviser deems appropriate (clause 8.2.5(c)(1)); or
- § if the parties do not agree with the methodology suggested by the adviser, the dispute is referred to a dispute resolution panel ('DRP') (clause 8.2.5(c)(2)).

A DRP ordinarily comprises three members that are experts in the relevant field, or experienced in dispute resolution techniques (clause 8.2.6A(f)). The DRP has discretion to give parties such directions as it considers necessary for the proper conduct of the proceedings (Rule 8.2.6C). It may give to the parties such directions relating to the use and disclosure of information obtained from other parties as it considers necessary in the circumstances (clause 8.2.6C(c)). Chapter 8 contains no explicit dispute resolution criteria guiding the decisions made by a DRP.<sup>42</sup> Indeed, clause 8.2.6D(d) appears to create a very wide discretion for a DRP to make a determination. Specifically, a DRP may:

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<sup>42</sup> This is in contrast with clause 6.15 of the Gas Code, which identifies eight mandatory considerations, many of which mirror the criterion contained in clause 6(4)(i) of the CPA.

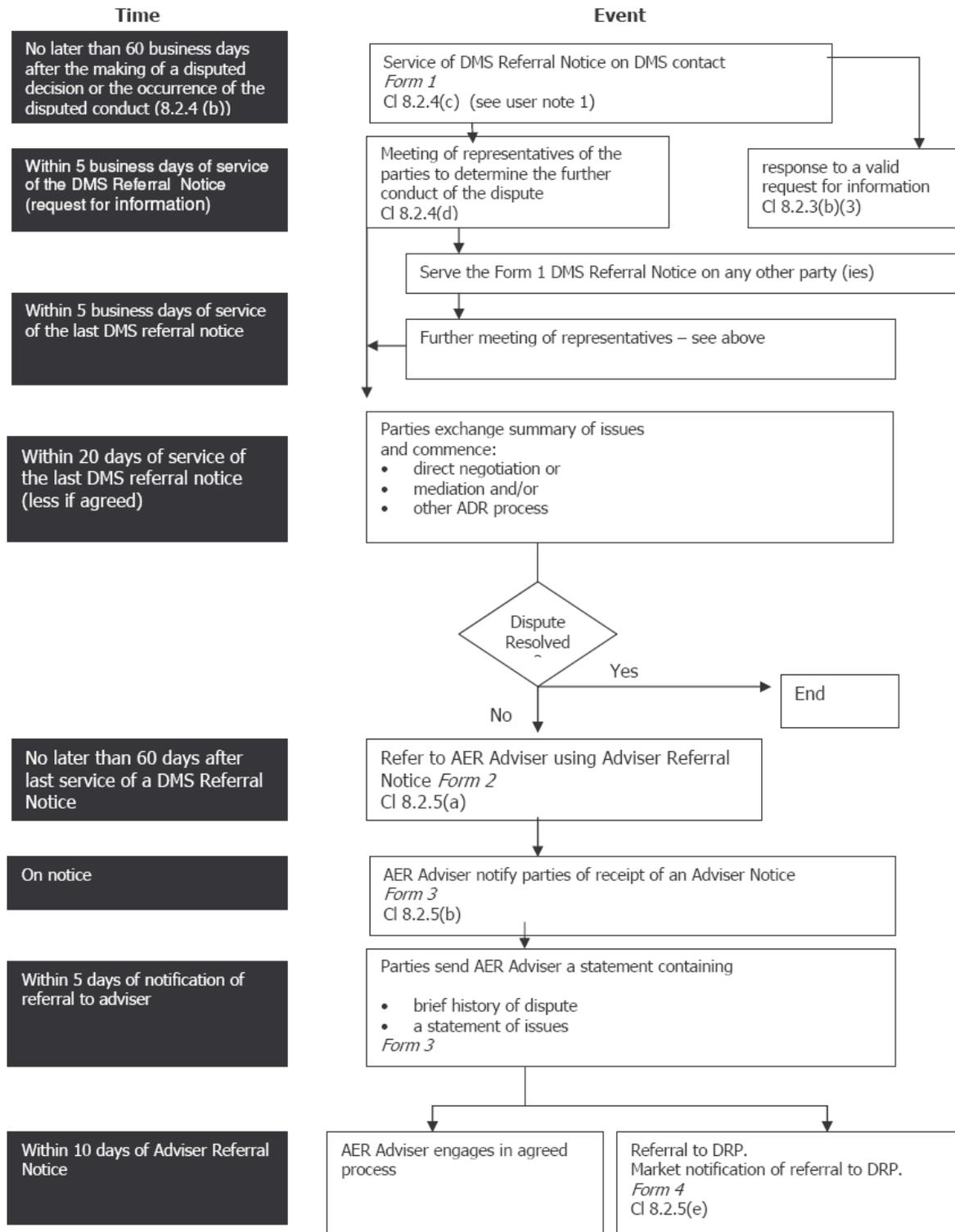
- § require a party to **take specified action**;
- § require a party to **refrain from taking specified action**; and/or
- § require a party to **pay a monetary sum** to another party.

A determination of the DRP or the adviser is binding on the parties to the dispute (clause 8.2.9(b)). Failure to comply with the terms and conditions of such a determination constitutes a breach of the rules of which the AER may impose sanctions in accordance with the NEL (clause 8.2.9(d)). Rule 8.2.11 preserves the right for a party to appeal on a question of law against a decision or determination of an adviser or a DRP in accordance with section 71 of the NEL<sup>43</sup>. Figure 4 below provides a high-level summary of the two-stage dispute resolution framework contained in chapter 8.

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<sup>43</sup> Rule 8.2.8 requires that the costs incurred by the adviser and the DRP are generally to be borne equally by the parties to the dispute.

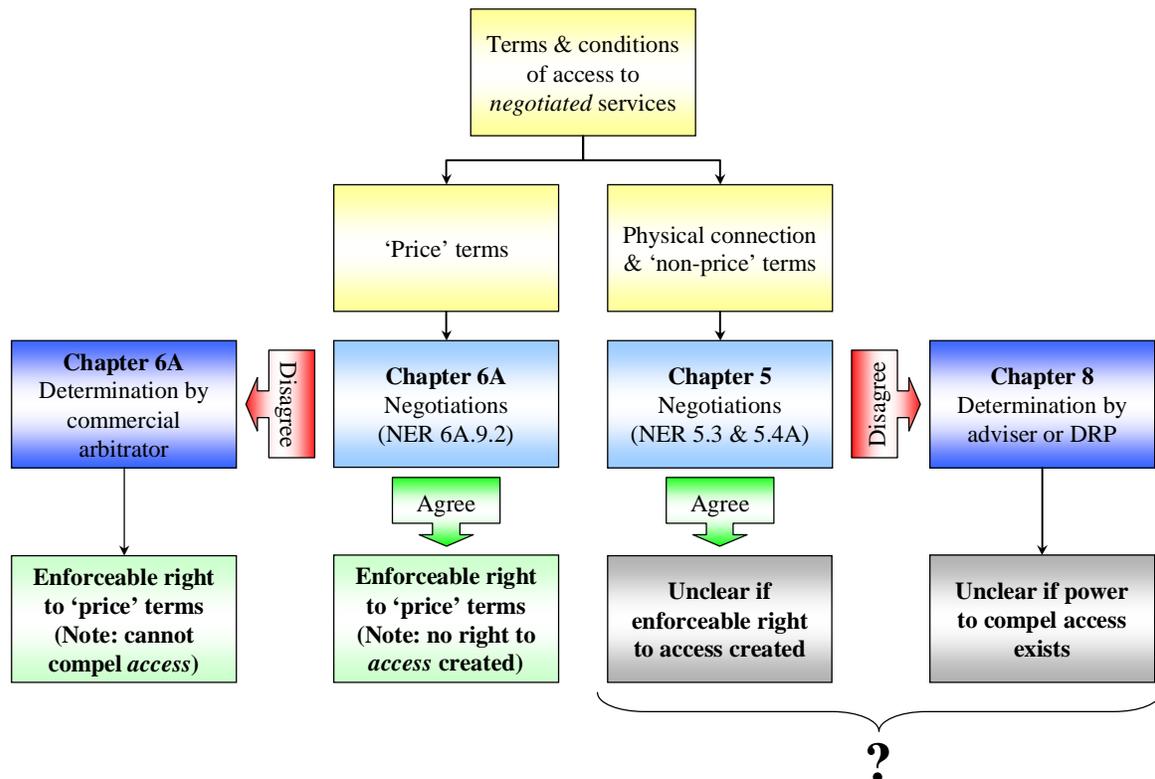
Figure 4: Chapter 8 Dispute Resolution Framework



The key issue is whether the ostensibly wide discretion created by chapter 8 – and clause 8.2.6D(d) specifically – creates an enforceable right to access *negotiated* transmission services. Put slightly differently, can an adviser or a DRP compel a service provider to grant access? In our view, this is at best unclear. Whilst clause 8.2.6D(d) allows an adviser or a DRP to require ‘a party to take specified action’, the power is not without bounds. For example, clause 8.2.6D(d) would not allow a DRP to require a service provider to offer access at a level of performance below the *minimum access standards* set out in schedules 5.1, 5.2, 5.3 and 5.3a such that the safety and reliability of the power system were threatened. To do so would violate clause 5.1.3(b)(1) of the Rules. In other words, the discretion is necessarily contained within the scope of the Rules and the NEL. Chapter 8 therefore cannot empower an adviser or a DRP to do anything other than what the Rules would otherwise allow.

To this end, we note that currently no Rule within the ambit of chapters 5 or 8 either: a) expressly establishes an unambiguous right for access seekers to access *negotiated* transmission services upon certain non-price terms and conditions, or: b) explicitly empowers a dispute resolution body to compel access upon certain non-price terms and conditions. Accordingly, despite the clear policy intent to the contrary, chapter 8 may currently be insufficient to create an enforceable right to access *negotiated* transmission services in a manner consistent with the clause 6(b) and (c) requirements in the CPA. At best, the existence of such a right is unclear. Figure 5 below summarises the interaction of chapters 5, 6A and 8 as they relate to *negotiated* transmission services. It illustrates that despite the patent policy intention to provide an enforceable right to access such services, it is at best unclear whether, in culmination, the Rules bestow such a right.

Figure 5: Access to *Negotiated* Transmission Services



**Summary:** Whilst chapter 8 ostensibly creates a wide discretion for an adviser or a DRP to resolve disputes, the scope of that power must be construed by reference to the balance of the Rules. No Rule in the balance of chapter 8 (or chapter 5) expressly establishes an unambiguous right of access to *negotiated* services. Accordingly, it is unclear whether an adviser or a DRP would have the power to compel a service provider to provide access to *negotiated* transmission services. Thus, despite clear policy intent to the contrary, doubt surrounds whether an enforceable right to access such services is created by chapter 8.

### 5.3. Summary

By way of broad summary, our key conclusions in relation to the existence or otherwise of an enforceable right to access covered transmission services are:

- § nothing in **chapter 5** would appear to grant an access seeker an enforceable right to connect to a transmission network on certain terms and conditions - it merely bestows a power to negotiate with a TNSP, and recourse to the dispute resolution mechanisms contained in chapter 6A and chapter 8 in the event negotiations are unsuccessful;
- § it is doubtful whether the operation of **chapter 6A** creates an enforceable right to access either *prescribed* or *negotiated* transmission services, since:
  - chapter 6A does not contain an explicit Rule bestowing an enforceable right of access to *prescribed* transmission services – thus, despite the clear policy intent to the contrary, it is unclear whether an enforceable right to access *prescribed* services can be said to exist under the national electricity regime;
  - nothing in chapter 6A imposes an obligation on a *service provider* to provide access to *negotiated* transmission services – the scope of the chapter 6A negotiation process is deliberately limited to pricing terms and conditions as distinct from the obtainment of access itself; and
  - chapter 6A explicitly precludes a *commercial arbitrator* from granting access to *negotiated* transmission services – an arbitrator’s power is limited to determinations related to pricing terms and conditions of access – it cannot mandate access itself.
- § it is doubtful whether the operation of **chapter 8** creates an enforceable right to access *negotiated* transmission services, since:
  - whilst it ostensibly creates a wide discretion for an adviser or a DRP to resolve disputes, the scope of that power must be construed by reference to the balance of the Rules, and no Rule in the balance of chapter 8 (or chapter 5) expressly establishes an unambiguous right of access to *negotiated* services; and
  - as a consequence, it is unclear whether an adviser, or a DRP would have the power to compel a service provider to provide access to *negotiated* transmission services.

**Conclusion:** The electricity access regime as defined by the NEL and the Rules is unlikely to satisfy the CPA requirements relating to the access framework since it is doubtful whether the regime either: a) creates an enforceable right to access either *prescribed* or *negotiated* transmission services, or: b) empowers a dispute resolution body to compel access to such services.

## 6. Dispute Resolution Framework

The third area that requires consideration is the means by which the access regime *resolves disputes* that arise over price and non-price access issues. To be effective, an access regime must incorporate appropriate dispute resolution mechanisms to resolve issues of contention between service providers and access seekers. In assessing whether the national electricity regime entails an effective dispute resolution mechanism, three key issues emerge:<sup>44</sup>

- § First, what is the impact of the potential absence of an enforceable right to access covered transmission services on the effectiveness of the dispute resolution framework?;
- § Second, does the existence of separate mechanisms to deal with price and non-price disputes, respectively, compromise the effectiveness of the overall dispute resolution framework?; and
- § Third, do the dispute resolution regimes embedded in the Rules satisfy the clause 6(4)(i) criteria as they relate to *negotiated* services?

Before considering these issues we first outline the certification requirements as they relate to the effectiveness of dispute resolution processes in greater detail.

### 6.1. Certification Requirements – Dispute Resolution

The relevant requirements regarding the dispute resolution framework are contained in clauses 6(4)(b), (c) and (i) of the CPA. In summary, these clauses of the CPA require the dispute resolution process to:<sup>45</sup>

- § provide for an enforceable right to access covered services (clauses 6(4)(b) and (c)); and
- § promote confidence among the parties by producing credible and reasonably consistent outcomes – to this end a dispute resolution body must consider and balance all of the requirements in clause 6(4)(i).

These clauses of the CPA are discussed in greater detail below.

#### 6.1.1. Enforceable right to access

The relevant requirements regarding the enforceable right of access are contained in clauses 6(4)(b) and (c) of the CPA, and are presented in their entirety in section 5 above. To recap, they require an access framework to provide an enforceable right of access to those services covered by the regime.

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<sup>44</sup> The dispute resolution framework must also meet a number of additional requirements under the CPA, eg. that pre-existing appeal rights be preserved. These requirements are comparatively straightforward and pose only minor issues, hence they are discussed only briefly in section 7 below.

<sup>45</sup> A number of these clauses (eg. 6(4)(a)-(c)) have been discussed in detail in section 4 above as they relate to the access framework itself. Hence they are only broached again here insofar as they relate to unique dispute resolution requirements.

### 6.1.2. Striking an appropriate balance

Clause 6(4)(i), which is set out in its entirety in Appendix A, introduces a series of considerations that a dispute resolution body must apply when determining terms and conditions of access. The NCC's interpretation of the respective criterion in clause 6(4)(i) can be summarised as follows:<sup>46</sup>

§ criterion (i) requires the actual price paid and invested in a facility by a facility owner to be taken into account in determining the terms and conditions of access, provided such acquisition or investment took place in a legitimate manner;

§ criterion (iv) requires regimes to consider the interests of all persons holding contracts for the use of a facility, and for those varying interests to be balanced against the remaining clause 6(4)(i) criteria and the overall objectives of access regulation; and

§ criterion (v) requires that the actual value of firm and binding contractual obligations of the owner or other persons (or both) already using a facility be taken into account, even if they include monopoly returns.

⇒ Together, criteria (i), (iv) and (v), account for **the interests of the facility owner** and existing facility users.

§ criterion (ii) requires that the costs to the provider of providing access be taken into account, with the exception of losses associated with increased competition in upstream or downstream markets, costs incurred by over-capitalisation, those unnecessarily incurred to provide access or an inappropriate attribution of common costs;

§ criterion (iii) requires that the economic value<sup>47</sup> to the owner of 'any additional investments that the person seeking access or the owner has agreed to undertake' be considered, with the exception of costs incurred by over-capitalisation, those unnecessarily incurred to provide access or an inappropriate attribution of common costs; and

§ criterion (vi) requires that the operational and technical requirements necessary for the safe and reliable operation of the facility be taken into account, provided the expenditure was necessary and not reflective of 'gold-plating'.

⇒ Together, criteria (ii), (iii) and (vi) account for the **costs of providing access**. Such costs must be necessary and not reflect 'gold-plating' or other unnecessary measures.

§ criterion (vii) requires consideration of the operation of a facility in an economically efficient manner as the term is generally considered by economists – however, criterion (vii) may be inconsistent with, and may need to be balanced against, the legitimate business interests of the owner (criterion (i));

§ criterion (viii) requires a consideration of the public benefit, ie, the efficiency gain, from having a workably competitive market (that is, one in which no firm has a substantial degree of market power in the longer-term).

<sup>46</sup> NCC Guide to Certification, p50, [3.118].

<sup>47</sup> Namely, the present value of future revenues less the present value of future costs.

⇒ Together, criteria (vii) and (viii) expressly account for **efficiency objectives** and the benefits arising from competitive markets.

An obvious difficulty that the NCC has recognised is that these grouped criteria are not mutually exclusive and may conflict. To this end, as noted above, in balancing the three groups of criteria to determine an appropriate range of outcomes the NCC has, in the past, been cognisant that the underlying objective of Part IIIA is to promote efficiency. On that basis, the NCC has indicated that provided a dispute resolution process acknowledges the respective criterion, and is likely to produce results that lie within a range of outcomes consistent with those likely to be achieved in an effectively competitive market, the clause 6(4)(i) requirement will be met.

## 6.2. Application to Electricity Transmission Services

To recap, in assessing whether the national electricity regime entails an effective dispute resolution mechanism, three key issues emerge. First, what is the impact of the possible absence of an enforceable right to access transmission services on the effectiveness of the dispute resolution framework? Second, does the existence of separate mechanisms to manage price and non-price disputes compromise the effectiveness of the overall framework? Finally, does the framework satisfy the clause 6(4)(i) criteria? These issues are addressed in turn below.

### 6.2.1. What is the impact of the uncertainty surrounding the enforceable right to access?

To be effective, a dispute resolution framework must create an enforceable right to access covered services. Absent such a right, or a measure empowering a dispute resolution body to compel access, a dispute resolution mechanism – and thus the overall access framework, as discussed in section 5 – cannot be considered effective. As section 5 explained, it is doubtful whether the national electricity access regime currently creates an enforceable right to access either *prescribed* or *negotiated* transmission services, or empowers a dispute resolution body to compel access to such services. A direct consequence of this doubt is that the effectiveness of the dispute resolution framework is similarly uncertain.

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| <p><b>Summary:</b> A direct consequence of the potential absence of an enforceable right to access is that the effectiveness of the dispute resolution framework is also uncertain.</p> |
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### 6.2.2. Do the separate price and non-price regimes hinder the effectiveness of the overall framework?

The Rules currently comprise two discrete dispute resolution processes. The commercial arbitration regime contained in chapter 6A encompasses ‘price’ disputes, and the negotiate/arbitrate model that spans chapters 5 and 8 manages ‘non-price’ disputes.<sup>48</sup> In our view, the separation of price versus non-price disputes likely constitutes an ineffective means of resolving access disputes overall. The reason is that price and non-price terms and

<sup>48</sup> See section 5.2 for a comprehensive overview of each regime.

conditions are intrinsically linked – one cannot be determined in isolation from the other. Simply put, one cannot sensibly determine a price without knowing the characteristics of the service in question.

The present situation, whereby a commercial arbitrator in determining price terms is: a) precluded from compelling access (clause S6A.3.5(c)); and b) required to ‘assume’ the ‘non-price’ terms and conditions (clause 6A.3.5(b)(1)(ii)); is highly artificial. It also precludes an arbitrator from balancing interests in relation to both price and non-price terms and conditions. Moreover, splitting the resolution of price and non-price terms and conditions may present opportunities to access seekers and service providers alike to game the arbitration processes. In our view, it would be far preferable for the Rules to provide a *single dispute resolution body* to be responsible for determining both ‘price’ and ‘non-price’ terms and conditions.

It is important to recognise that the current disjoint between regimes is not a carefully crafted aspect of the Rules. Rather, it is a consequence of the staggered nature of the recent reform process. The Commission has indicated that, but for the statutory constraints on its Rule making powers, it would very likely have also incorporated ‘non-price’ disputes into the newly introduced chapter 6A commercial arbitration framework.<sup>49</sup> Being unable to do so, it had little choice but to create the artificial separation. The Commission acknowledges that this is an unsatisfactory outcome,<sup>50</sup> and most likely means the overall dispute resolution framework contained in the NEL and the Rules is ineffective when considered against the CPA criteria.

**Summary:** The present separation of ‘price’ and ‘non-price’ access disputes under the Rules is artificial, presents risks for opportunistic gaming, and most likely constitutes an inefficient means of resolving disputes overall. The dispute resolution framework in the Rules is therefore unlikely to be effective.

### 6.2.3. Does each framework strike an appropriate balance?

Clause 6(4)(i), set out in section 4.1.2 above, introduces a series of considerations that a dispute resolution body must apply when determining terms and conditions of access. As explained in section 6.1.2, the NCC has indicated that the criteria can be broadly grouped as follows:

- § criteria (i), (iv) and (v), account for **the interests of the facility owner** and existing facility users;
- § criteria (ii), (iii) and (vi), account for the **costs of providing access**. Such costs must be necessary and not reflect ‘gold-plating’ or other unnecessary measures; and
- § criteria (vii) and (viii), expressly account for **efficiency objectives** and the benefits arising from competitive markets.

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<sup>49</sup> AEMC Draft Report, p97.

<sup>50</sup> Ibid.

As discussed in section 4.1.2, since these grouped criteria are not mutually exclusive and may conflict the NCC has indicated that the 6(4)(i) requirement will likely be met provided a dispute resolution process:

- § recognises and acknowledges the criteria, either explicitly or implicitly; and
- § is likely to produce a range of outcomes consistent with those that would be observed in an *effectively competitive market*.

In the following sections, we separately examine the chapter 8 and chapter 6A dispute resolution frameworks by reference to these criteria.

#### 6.2.3.1. Assessment of the chapter 6A dispute resolution framework

In our view, the chapter 6A dispute resolution regime as it relates to price and access charge disputes very likely meets the clause 6(4)(i) requirements. Indeed, the *negotiated transmission service pricing principles* set out in Rule 6A.9.1, whilst differently constructed, are in many respects analogous to the clause 6(4)(i) criteria. Of paramount importance for the purposes of the clause 6(4)(i) criteria are:

- § clause 6A.9.1(1), which specifies that the price for a negotiated service should be based on the costs incurred in providing that service;
- § clause 6A.9.1(2), which specifies that the price for a negotiated service should in most cases be at least equal to the avoided cost of providing it but no more than the cost of providing it on a stand-alone basis;
- § clause 6A.9.1(5), which specifies that prices must be the same for all users unless a material cost difference exists;
- § clause 6A.9.1(6)), which specifies that prices should be adjusted over time to the extent the assets used to provide the service are provided to other persons, in which case adjustments should reflect the extent to which the costs of that asset are being recovered through charges to those other persons (clause 6A.9.1(6));
- § clause 6A.9.1(8), which specifies that the price should enable the provider to recover the efficient costs of complying with all regulatory obligations associated with the provision of negotiated services; and
- § clause 6A.9.1(9), which specifies that the price should take into account the need for the service to be provided in a manner that does not adversely affect the safe and reliable operation of the power system.

In our view, in combination the rules outlined above adequately consider the interests of the facility owner and existing facility users, the costs of providing access and efficiency objectives. We base this conclusion on the following factors:

- § First, clauses 6A.9.1(1) and (8) expressly states that prices for negotiated services should reflect the cost of providing those services, including the costs of complying with regulatory obligations – a requirement that in our view is consistent with all three of the broad criteria identified by the NCC.

- § Second, clause 6A.9.1(9) prohibits prices that would in any way threaten the ongoing safety of the power system, which is clearly consistent with all three of the broad criteria identified by the NCC.
- § Third, clause 6A.9.1(5) effectively prohibits inefficient price discrimination, which will enhance market efficiency and better ensure that access prices align with the costs of providing access to particular access seekers, or classes of access seekers. In a similar fashion, clause 6A.9.1(6) seeks to ensure that access prices reflect costs to access seekers over time, further advancing the two broad objectives.
- § Fourth, clause 6A.9.1(2) refines the pricing requirement by creating a specific cost band within which prices must be negotiated. The stand-alone cost ‘ceiling’ prevents the access provider from extracting monopoly profits. Conversely, by basing the ‘floor’ price on avoidable costs, access seekers are forced to pay at least the costs that they impose specifically upon the network. The existence of the ‘floor’ thereby ensures the interests of facility owners are preserved, whereas the ‘ceiling’ ensures negotiated prices are cost reflective. Most fundamentally, the floor/ceiling band reflects the boundaries of pricing that would exist if the market was open to competition and so provides an economically defensible method of regulation, as the NCC has acknowledged:<sup>51</sup>

“In general, efficient outcomes can be expected to lie in a band between short run (avoidable) costs and the long term efficient (full) cost of supplying the services demanded.”

Accordingly, on balance, the chapter 6A dispute resolution framework for resolving ‘price’ disputes, and in particular, the criteria outlined in Rule 6A.9.1 very likely meets the clause 6(4)(i) requirements. The framework considers each of the three broad criteria identified by the NCC and is therefore well placed to produce negotiated access prices that fall within a range one would observe in an effectively competitive market.

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| <p><b>Summary:</b> The chapter 6A dispute resolution framework for resolving ‘price’ disputes likely meets the requirements specified in clause 6(4)(i) of the CPA.</p> |
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#### 6.2.3.2. Assessment of chapter 8 dispute resolution framework

In the past, the Commission has noted that the chapter 8 framework that applies to ‘non-price’ disputes is cumbersome and not well suited to the timely resolution of disputes arising from commercial negotiations. Indeed, it recently acknowledged that the introduction of the chapter 6A dispute resolution framework was due in large part to perceived shortcomings in the chapter 8 framework.<sup>52</sup> It is therefore not altogether surprising that several reasons exist to believe that the chapter 8 framework would not meet the requirements required in clause 6(4)(i). These include:<sup>53</sup>

<sup>51</sup> NCC Guide to Certification, p59, [3.154].

<sup>52</sup> AEMC Final Report, p95.

<sup>53</sup> Whilst the chapter 8 criteria was approved by the ACCC when it accepted the NEM Access Code, this was under a broader statutory test – section 44ZZAA(3) of the TPA, which contains no explicit guidance regarding dispute resolution requirements, unlike clause 6(4).

- § the wide discretion it provides an adviser or a DRP;
- § the absence of time-limited processes, for example, clause 8.2.6D(c)(2) allows a DRP to extend the period for rendering a determination if the AER agrees in writing; and
- § the absence of certain explicit dispute resolution criteria guiding the decisions made by an adviser or a DRP.

Under the chapter 8 framework, an adviser is empowered, provided parties agree, to resolve a dispute by ‘any means’ it deems appropriate, provided it conforms to the requirements of clause 8.2.1(e) (clause 8.2.5(c)). Clause 8.2.6D(d) grants a DRP a similarly wide discretion. However, as section 5.2.3.1.2 explained, this is not a boundless power. Specifically, it must be read subject to the balance of the Rules, and in particular, the requirements of **chapter 5**. An adviser or a DRP would therefore be obliged to consider, and comply with, a range of factors when determining a ‘non-price’ access dispute, including:

- § subject to certain exceptions, the technical terms and conditions of connection agreements should comply with *minimum standards of performance*, with the object that the *power system operate securely and reliably* (clause 5.1.3(b1));
- § a negotiated access standard must be:
  - no less onerous than the corresponding *minimum access standard* (clause 5.3.4A(a)(1));
  - set at a level that *will not adversely affect power system security* (clause 5.3.4A(a)(2)); and
  - set at a level that *will not affect the quality of supply for other network users* (clause 5.3.4A(a)(3));
- § an *offer to connect* must be *fair and reasonable* and *consistent with the safe and reliable operation of the power system* (clause 5.3.6(c));
- § all registered participants must ensure that a *connection agreement* requires the provision and maintenance of all required facilities consistent with *good electricity industry practice* (clause 5.2.1(b)); and
- § compliance with a *connection agreement* should not adversely affect the quality or security of network service to other network users (clause 5.2.3(b)(3)).

Notwithstanding these myriad non-price criteria, it is unclear whether chapter 5 and chapter 8 provide for an appropriate balancing of the clause 6(4)(i) criteria. For example, neither appears to explicitly require an adviser or a DRP to take into account the interests of the facility owner and existing facility users, or the interests of others with contracts for use of the pertinent facility, as expressly contemplated by clause 6(4)(i). Moreover, as section 7.2.3 below explains, the absence of certain non-price criteria relating to extensions and augmentations may also pose certain issues under the clause 6(4)(j) criteria.

Chapter 8 contains few explicit dispute resolution criteria guiding the decisions made by an adviser or a DRP. A DRP is required only to take account of the series of high level

principles set out in clause 8.2.1(e).<sup>54</sup> This is in contrast to chapter 6A, and also clause 6.15 of the National Gas Code, which identifies eight mandatory considerations, many of which mirror the criterion contained in clause 6(4)(i) of the CPA.

Accordingly, whilst the provisions in chapters 5 and 8 do not necessarily preclude an adviser or a DRP from reaching an appropriate determination, they are sufficiently unclear as to not promote confidence among the parties that credible and reasonably consistent outcomes will occur, consistent with clause 6(4)(i). Indeed, we are unaware of any instance that the chapter 8 dispute resolution framework has been invoked in relation to resolving an access dispute.<sup>55</sup> Accordingly, there is a significant likelihood that the chapter 8 framework would not comply with the clause 6(4)(i) criteria.

**Summary:** There is a significant risk that the chapter 8 framework would not comply with the clause 6(4)(i) criteria.

### 6.3. Summary

By way of broad summary, our key conclusions regarding the effectiveness of the dispute resolution framework in the national electricity access regime are:

- § the potential absence of an enforceable right to access creates similar uncertainty surrounding the effectiveness of the dispute resolution framework;
- § the present separation of ‘price’ and ‘non-price’ access disputes under the Rules is artificial, presents risks of opportunistic gaming, and likely constitutes an inefficient means of resolving disputes overall;
- § the chapter 6A dispute resolution framework for resolving ‘price’ disputes likely *meets* the requirements specified in clause 6(4)(i) of the CPA; and
- § there is a significant risk that the chapter 8 framework *would not* comply with the clause 6(4)(i) criteria.

**Conclusion:** The electricity access regime as defined by the NEL and the Rules is currently unlikely to incorporate an effective dispute resolution framework consistent with the CPA requirements.

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<sup>54</sup> These principles are set out in their entirety in section 5.2.3.

<sup>55</sup> AEMC Draft Report, p95.

## 7. Other Certification Requirements

In addition to the requirements outlined in detail above, for an access regime to be considered effective, it must satisfy a number of additional requirements. Specifically, in addition to the requirements outlined in section 4 above, the CPA requires an access framework to also:

- § require that service providers use all reasonable endeavours to accommodate access seekers' requirements (clause 6(4)(e));
- § incorporate the principle that access to a service need not be on exactly the same terms and conditions for all persons seeking access (clause 6(4)(f));
- § prohibit conduct for the purpose of hindering access (clause 6(4)(m)); and
- § include appropriate ring fencing arrangements (clause 6(4)(n)).

In addition to the requirements outlined in section 6 above, to be considered effective, a dispute resolution framework must also:

- § incorporate the principle that where the owner and a person seeking access cannot agree on terms and conditions for access, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so (clause 6(4)(g));
- § incorporate the principle that the decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved (clause 6(4)(h));
- § allow, in certain situations, for an arbitrator to require an extension to a facility when parties cannot reach agreement (clause 6(4)(j));
- § allow parties to apply for a revocation or modification of the access arrangement if there has been a material change in circumstances (clause 6(4)(k));
- § require that a dispute resolution body only impede the existing right of a person to use a facility where it has considered whether there is a case for compensation of that person, and, if appropriate, determined such compensation (clause 6(4)(l)); and
- § include arrangements allowing regulatory bodies and arbitrators with the information required to undertake their responsibilities (clause 6(4)(o)).

The access regime must also ensure that there are no impediments to interstate access arising from state based regime differences, preferably through the provision of a single process for access (clause 6(2) and 6(4)(p)). Finally, the regime must result in appropriate terms and conditions of access.<sup>56</sup>

The extent to which the various components of the national electricity regime satisfy these requirements is assessed below.

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<sup>56</sup> We do not explicitly address this requirement, since by definition, provided the other requirements are met, appropriate terms and conditions of access should eventuate.

## 7.1. Additional Access Framework Requirements

In this section we assess the national electricity regime access framework against the requirements contained in clauses 6(4)(e), (f), (m) and (n) of the CPA.

### 7.1.1. Requirement to use reasonable endeavours to accommodate access

Clause 6(4)(e) of the CPA requires service providers to use all reasonable endeavours to accommodate access seekers' requirements. The NCC has indicated that an access regime may incorporate clause 6(4)(e) either explicitly or through general provisions that have the same effect.

Parts E and F of **chapter 6A** of the Rules create a comprehensive regime for the regulation of *prescribed* services, including the information gathering processes outlined in section 7.2.6 below. These measures should sufficiently ensure that service providers use all reasonable endeavours in their provision of *prescribed* services.

The **chapter 5** framework for negotiating 'non-price' terms and conditions of access for *negotiated* services also incorporates a number of explicit requirements in this regard, including:

- § a service provider must use its reasonable endeavours to provide the applicant with an offer to connect in accordance with its reasonable requirements (clause 5.3.6(d));
- § connection applicants and service providers are entitled to negotiate with each other in respect of the provision of the connection and, if such negotiations occur, each is required to conduct such negotiations in good faith (clause 5.3.6(g));
- § when finalising a connection agreement a service provider must use its reasonable endeavours to negotiate in good faith with all parties (clause 5.3.7(a)(2)); and
- § that connection applicants and service providers alike adhere to specified timeframes throughout the negotiation process.

In combination, these provisions very likely satisfy the clause 6(4)(e) requirement. Access regimes certified by the NCC in the past – including the Gas Code – have incorporated broadly similar measures.<sup>57</sup>

The **chapter 6A** framework incorporates a number of similar provisions as it relates to the provision of *negotiated* services. Specifically, a service provider must, in its negotiation framework:

- § undertake to negotiate in good faith the price at which negotiated services are to be provided (clause 6A.9.5(c)(1));
- § provide all such commercial information as an access seeker may reasonably require to enable that person to engage in effective negotiation with the provider as to the price at which the negotiated service is to be provided (clause 6A.9.5(c)(2));

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<sup>57</sup> NCC Guide to Certification, p36, [3.63].

- § specify a requirement for the provider to advise an access seeker of the reasonable costs of providing the negotiated service (clause 6A.9.5(c)(3)(i)); and
- § specify a requirement for the provider to demonstrate to an access seeker how the charges reflect those costs (clause 6A.9.5(c)(3)(ii)).

Accordingly, it would appear that the dispute resolution framework would satisfy the clause 6(4)(e) requirement.

**Conclusion:** The dispute resolution framework would likely meet the requirement contained in clause 6(4)(e) of the CPA.

### 7.1.2. Access need not be on the same terms and conditions

Clause 6(4)(f) requires that access to a service need not be on exactly the same terms and conditions for all persons seeking access. The NCC has, in the past, considered that this clause is intended to ensure the scope for commercial negotiation is not limited. Rather, prescribed terms and conditions should be limited to those services for which a reasonable outcome cannot be negotiated. As indicated earlier, this was precisely the Commission’s approach to attributing forms of regulation to transmission services.

In developing chapter 6A of the rules, the Commission indicated that it sought to ‘roll-back’ wherever possible the application of the more intrusive forms of regulation applying to prescribed services, in recognition that:<sup>58</sup>

“[O]ver-inclusion of services in a revenue cap will distort market outcomes by crowding out the opportunities for competitive supply of services and commercial negotiations between TNSPs and users.”

Homogeneous, prescriptive forms of regulation are thus limited to those transmission services for which there is thought to currently be no genuine prospect of successful commercial negotiations. Moreover, both the chapter 5 and 6A commercial negotiation processes ostensibly provide scope for access seekers and service providers to reach unique terms and conditions of access. Accordingly, the national electricity access regime appears to comply with the requirement in clause 6(4)(f) of the CPA.

**Conclusion:** The national electricity regime appropriately limits the scope of homogeneous forms of regulation and thus very likely complies with the requirement specified in clause 6(4)(f) of the CPA.

### 7.1.3. Prohibition against hindering access

Clause 6(4)(m) of the CPA prohibits the owner or user of a service from engaging in conduct for the purpose of hindering access to that service by another person. The NCC has stated that an access regime may incorporate this clause explicitly or contain general provisions to the same effect.<sup>59</sup> Currently the Rules do not contain an explicit prohibition against hindering

<sup>58</sup> AER Draft Report, p12.

<sup>59</sup> NCC Guide to Certification, p69, [3.193].

access and it is unclear whether one could be legitimately implied. Accordingly, the national electricity regime likely does not comply with the requirement outlined in clause 6(4)(o) of the CPA.

**Conclusion:** The Rules do not contain an explicit prohibition against hindering access and it is unclear whether one may be implied. Accordingly, the national electricity regime likely does not comply with clause 6(4)(o) of the CPA.

#### 7.1.4. Separate accounting arrangements

Clause 6(4)(n) requires that separate accounting arrangements be maintained for the elements of a business which are covered by the access regime. The NCC has indicated that requirement will be satisfied if a facility owner:<sup>60</sup>

- § maintains a separate set of accounts for each service that is subject to an access regime;
- § maintains a separate consolidated set of accounts for all activities undertaken; and
- § allocates any costs that are shared across multiple services.

The underlying motivation for this requirement is to address concerns arising from vertically integrated businesses favouring internal affiliates above competitive businesses in related markets. The market structure is therefore a relevant consideration in assessing an access regime's compliance with clause 6(4)(n).

Part I of chapter 6A of the Rules developed by the Commission require service providers to comply with transmission ring-fencing guidelines, developed by the AER.<sup>61</sup> The AER must develop the ring-fencing guidelines in accordance with the requirements in Rule 6A.21.2. In developing the ring-fencing requirements, the AER must:

- § provide for the accounting and functional separation of prescribed transmission services (clause 6A.21.2(a));
- § consider the need for consistency between federal and state ring-fencing regulation, and the need for consistency with the distribution ring-fencing guidelines (clause 6A.21.2(c)); and
- § consult with stakeholders (clause 6A.21.2(d)).

While the NCC's consideration of clause 6(4)(n) suggests that separate accounts should be maintained for all services, the Rules do not provide for ring-fencing of negotiated service costs from prescribed and any other services provided by a service provider. This is unlikely to affect the regime's satisfaction of clause 6(4)(n). There are two reasons for this:

- § a requirement for separate accounting for negotiated transmission services would impose additional costs on a service provider, for little, if any benefit; and

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<sup>60</sup> NCC Guide to Certification, p70, [3.197].

<sup>61</sup> Clause 6A.21.1.

§ it has the potential to significantly stifle the scope for efficient negotiations, since prices will likely be invariably based on the costs identified through separate accounting.

In other words, imposing ring-fencing requirements on negotiated services would likely serve to undermine the reasons for introducing that form of regulation in the first place.

**Conclusion:** The ring-fencing regime developed for service providers is likely consistent with the requirement in clause 6(4)(n) of the CPA.

## 7.2. Additional Dispute Resolution Framework Requirements

In this section we assess the national electricity regime’s dispute resolution framework against the requirements contained in clauses 6(4)(g), (h), (j), (k), (l) and (o) of the CPA.

### 7.2.1. Independent dispute resolution body

Under clause 6(4)(g), an effective access regime must contain a mechanism to ensure the parties to a dispute have recourse to an independent dispute resolution process. It states:

“Where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.”

An effective access regime must also address the circumstances where the parties cannot agree on *how* to resolve a dispute, including the identity of the dispute resolution body. It therefore must contain a mechanism for *appointing* an independent body to resolve such disputes. Clause 6(4)(g) also requires parties to a dispute to fund some or all of the costs of arbitration, although the NCC has indicated that it is mindful that the costs of arbitration should not deter parties from seeking access.<sup>62</sup>

Further, the NCC has indicated that to be considered independent, a dispute resolution body must be independent of service providers, users, access seekers and governments. However, the NCC has stated that it is not opposed to the principle of the same body having the regulator and arbitrator roles, provided jurisdictions consider the inclusion of appropriate safeguards to address these issues, including the development of practice and procedure notes that the body can follow to conduct its dispute resolution functions independently of regulatory functions.<sup>63</sup>

The chapter 8 and chapter 6A dispute resolution regimes both appear to meet the clause 6(4)(g) requirements. Each regime clearly specifies the process by which specified disputes are to be managed, and clearly defines the identity of the appropriate dispute resolution body and the process for establishing that body, namely:<sup>64</sup>

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<sup>62</sup> NCC Guide to Certification, p40, [3.77].

<sup>63</sup> NCC Guide to Certification, p40, [3.81].

<sup>64</sup> Note that for *prescribed* services the AER is in effect the dispute resolution body. As outlined in section 4.2 above, the NCC has indicated that clause 6(4)(g) will be satisfied for prescribed services, provided the AER sets access terms in

- § the chapter 8 regime specifies that for stage two disputes, the relevant dispute resolution body is to be either:
- the independent dispute resolution adviser, provided the parties agree to the dispute resolution process proposed by that adviser (clause 8.2.5(c)(1)); or
  - if the parties do not agree, the adviser must appoint a dispute resolution panel (clause 8.2.5(c)(2)), which will ordinarily comprise three independent members that are experts in the relevant field and/or experienced in dispute resolution techniques (clause 8.2.6A(f)); and
- § the chapter 6A regime specifies the AER must appoint an independent commercial arbitrator (sub-schedule 6A.3.3(a)) experienced in dispute resolution techniques (sub-schedule 6A.3.3(c)).

Parties to both chapter 8 and chapter 6A disputes must bear the costs of those disputes. In each instance it is customary for the cost of the adviser or the dispute resolution panel (Rule 8.2.8) or the arbitrator (sub-schedule 6A.3.6(a)) to be shared equally between the parties. In other words, each regime incorporates adequate funding mechanisms. Given that the majority of access seekers will be well resourced corporate entities, it seems unlikely that the costs of resolving disputes will deter parties from seeking access.

**Conclusion:** The chapter 8 and chapter 6A dispute resolution frameworks should each meet the requirements specified in clause 6(4)(g) of the CPA.

### 7.2.2. Binding decisions coupled with appeal rights

Clause 6(4)(h) provides that an effective access arrangement should have credible enforcement arrangements to ensure a dispute resolution body’s decision is binding. It states:

“The decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved.”

The NCC has indicated its view that the regime should give effect to the enforcement process through legislative provisions, with appropriate sanctions and remedies for non-compliance.<sup>65</sup> Existing rights of appeal should be preserved. The NCC has, in the past, considered it unnecessary for an effective access regime to include a mechanism for conducting a merits review of a dispute resolution body’s decision. However, any *diminution* of existing appeal rights, eg, rights to seek a judicial review on the grounds of an alleged breach of natural justice, may offend clause 6(4)(h).

The chapter 8 and chapter 6A dispute resolution regimes both appear to meet the clause 6(4)(h) requirements. Each regime provides for binding arbitral decisions that may be enforced by the AER through the NEL. Specifically:

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accordance with effective regulatory processes and, if not, consistent with the clause 6(4)(i) criteria. For the reasons outlined in 4.2.2 the regulatory arrangements for prescribed services likely meet these requirements.

<sup>65</sup> NCC Guide to Certification, p45, [3.98].

- § chapter 8 states that parties must comply with a requirement or determination of a DRP and any agreement that is recorded in accordance with clause 8.2.9(a) - failure to do so is a breach of the Rules in respect of which the AER may take action in accordance with the NEL (clause 8.2.1(d)); and
- § chapter 6A states that determinations by a commercial arbitrator are binding, and any failure to comply with such an agreement or determination constitutes a breach of the Rules in respect of which the AER may take action in accordance with the NEL (sub-schedule 6A.3.7(c)).

Moreover, chapter 6A preserves the pre-existing right to seek judicial review<sup>66</sup> and chapter 8 explicitly incorporates a right for a party to appeal on a question of law against a decision or determination of a DRP in accordance with section 71 of the NEL (Rule 8.2.11).

However, whilst decisions are binding and enforceable, there are presently limitations on *what may be decided*. In particular, for the reasons outlined in section 5, neither chapter 8 nor chapter 6A explicitly provides for the pertinent dispute resolution body to *compel access* on certain terms and conditions. Neither an adviser, nor a dispute resolution panel, nor a commercial arbitrator is expressly empowered to make a determination to this effect.

In other words, whilst chapters 6A and 8 ostensibly comply with clause 6(4)(g) in that each allows for binding arbitral decisions coupled with appeal rights, neither framework is likely to create an *enforceable right* to access, as required by clauses 6(4)(b) and (c) of the CPA.<sup>67</sup>

**Conclusion:** The Rules' dispute resolution framework likely meets the requirements specified in clause 6(4)(h) of the CPA. However, neither chapter 8 nor chapter 6A would appear to allow a dispute resolution body to make a binding decision *compelling access* to covered transmission services.

### 7.2.3. Extension to facilities

In some situations the needs of an access seeker can only be met by an extension of a facility's geographic range or an expansion of its capacity. The NCC has indicated that such matters should be subject, in the first instance, to negotiation between the parties. However, clause 6(4)(j) of the CPA requires that an arbitrator be empowered to require an extension when parties cannot reach agreement. This power must be subject to:

- § such an extension being technically and economically feasible and consistent with the safe and reliable operation of the facility;
- § the owner's legitimate business interests in the facility being protected; and
- § the terms of access for the third party taking into account the costs borne by the parties for the extension and the economic benefits to the parties resulting from the extension.

<sup>66</sup> The MCE has also indicated that it intends to provide a limited merits review process for decisions by the AER in relation to price determinations. This will also form part of the dispute resolution mechanism for prescribed services.

<sup>67</sup> For a detailed analysis of the requirements of clauses 6(4)(b) and (c) of the CPA see section 5 above.

The chapter 5 negotiation framework contemplates a service provider undertaking an augmentation or an extension to its network, if that extension is required to effect or facilitate the connection of a *connection applicant* and the connection is the subject of a *connection agreement*. Specifically, the Rules state that:

- § any *offer to connect* (and thus any connection agreement) must be *fair and reasonable* and consistent with the safe and reliable operation of the power system (clause 5.3.6(c)); and
- § a service provider use *reasonable endeavours* to provide the access arrangements sought by an access seeker, including extensions, provided (clause 5.4A(e)):
  - they are consistent with good electricity industry practice; and
  - account for the affect on transmission and/or distribution networks and thus the requirements of other affected registered participants.

However, for the reasons outlined in section 4, it is not whether the Rules would presently compel an arbitrator to make a binding determination compelling an extension to be undertaken and a service offered. This can be contrasted with the Gas Code, which explicitly states that in making a determination an arbitrator may require a service provider to expand the *capacity* of a covered pipeline to meet the requirements of a prospective user, provided that (clause 6.22):<sup>68</sup>

- § the service provider is not required to extend the geographical range of a covered pipeline;
- § the expansion is technically and economically feasible and consistent with the safe and reliable provision of the service;
- § the service provider's legitimate business interests are protected;
- § the prospective user does not become the owner of a covered pipeline or part of a covered pipeline without the agreement of the service provider; and
- § the service provider is not required to fund part or all of the expansion (except where the extensions/expansions policy in the access arrangement for the covered pipeline states that the service provider will fund the new facility and the conditions specified in the extensions/expansions policy have been met).

Supposing an adviser or a DRP were expressly empowered to compel an extension,<sup>69</sup> it is debatable whether the aforementioned chapter 5 criteria would be sufficient to satisfy the 6(4)(j) requirements. The existing framework would appear to adequately manage the first criterion, namely that extensions be technically and economically feasible and consistent with the safe and reliable operation of the facility. However, its compliance with the remaining criteria is less certain.

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<sup>68</sup> We note that Part 4.5 of the *National Gas Law Exposure Draft* provides for the AER to make a similar determination, provided certain pricing principles and various other criteria are met.

<sup>69</sup> For the reasons outlined in section 4 it is not altogether clear whether that is the case.

One might legitimately argue that the framework implicitly accounts for the legitimate business interests of service provider's and the costs incurred by third parties. For example, an offer to connect must be 'fair and reasonable' and access arrangements must account for the impact of an extension on third parties. Nonetheless, in our view, there is a risk that in the absence of explicit criteria analogous to those in the Gas Code the NCC may construe the chapter 5 framework as being insufficient to comply with the requirements of clause 6(4)(j).

**Conclusion:** There is currently a risk that the dispute resolution framework would not meet the requirements specified in clause 6(4)(j) of the CPA.

#### 7.2.4. Material change in circumstances

Clause 6(4)(k) of the CPA states that if there has been a material change in circumstance, parties should be able to apply for a revocation or modification of the access arrangement which was made at the conclusion of the dispute resolution process.

For *prescribed* services, the Rules include provisions allowing the revenue cap to be reopened during a regulatory period where an event occurs that sufficiently impacts on the financial viability of the business, or its scope to respond to unforeseen circumstances, specifically, when (Rule 6A.7):

- § an event occurs that could not have been foreseen by a service provider;
- § in response to that event, the service provider must invest in a project without which network reliability or system security would be compromised;
- § the project requires capital expenditure exceeding 5 per cent of the service provider's regulatory asset base in the year of the event;
- § the project requires capital expenditure that the service provider cannot otherwise reasonably fund within the period; and
- § there is no existing allowance (including in the contingent projects allowance) for that project.

The Rules also provide an allowance for the pass-through of significant increases (or decreases) in a service providers costs resulting from certain categories of unexpected events that may occur during the regulatory period, including changes in applicable taxes and terrorism events (Rule 6A.7.3). The AER may also revoke and remake a revenue determination *in its entirety* in the event a determination was set on the basis of false or misleading information, or where a material error has been made (Rule 6A.15).

For *negotiated* services, neither the chapter 8, nor the chapter 6A dispute resolution processes would appear to explicitly preclude any party from re-negotiating an access agreement following a material change of circumstances. Moreover, one would expect it would be commonplace for such agreements to explicitly incorporate provisions triggering re-negotiation in certain identified circumstances, for example if there were, say, a 20 per cent shortfall in the demand forecast that underpinned the price for a negotiated service.

**Conclusion:** The dispute resolution framework likely meets the requirement specified in clause 6(4)(k) of the CPA.

### 7.2.5. Impediment of existing rights

Clause 6(4)(l) requires that a dispute resolution body should only impede the existing right of a person to use a facility where it has considered whether there is a case for compensation of that person and, if appropriate, determined such compensation. For example, the Gas Code precludes an arbitrator from making any decision that would impede the existing right of a user to obtain services (clause 6.18).

Whilst various aspects of chapter 5 require a service provider, and thus an adviser or DRP, to consider the impact of connection agreements on third parties, there does not appear to be any explicit provision restricting the impediment of existing rights to circumstances where compensation has been considered.<sup>70</sup> Similarly, neither chapter 8 nor chapter 6A incorporate explicit provisions to this effect. Accordingly, it is at best unclear whether the dispute resolution framework complies with the requirements of clause 6(4)(l) of the CPA.

**Conclusion:** There is currently a risk that the dispute resolution framework would not meet the requirements specified in clause 6(4)(l) of the CPA.

### 7.2.6. Access to information

Clause 6(4)(o) requires an effective access regime to provide the dispute resolution body and other relevant bodies, eg, regulators and appeals bodies, with the right to inspect all financial documents pertaining to the service. It states:

“The dispute resolution body, or relevant authority where provided for under specific legislation, should have access to financial statements and other accounting information pertaining to a service.”

Part F of chapter 6A of the Rules details information that must be provided by a service provider to the AER in the context of a *transmission determination*. The key elements of the information provision requirements include:

- § the development and publishing of information guidelines by the AER which specify the information that must be provided by a TNSP to the AER, which are developed in accordance with the consultation procedures;
- § the provision by a TNSP of annual statements, in accordance with information guidelines, to the AER that provide – clause 6A.17.1(b):
  - a true and fair statement of the financial and operating performance of the provider;
  - and
  - are certified in accordance with the information guidelines;
- § the AER has a power to request additional information that is reasonably required – clause 6A.17.1(d):
  - to monitor and enforce compliance with the total revenue cap, the maximum allowed revenue and any other requirements imposed in a transmission determination;

<sup>70</sup> See for example the discussion of clauses 5.3.6(c) and 5.4A(e) in section 7.2.3 above.

- to monitor, report on and enforce compliance with the provider’s cost allocation methodology;
- as an input regarding the financial, economic and operational performance of the business for the purposes of the AER’s decision making; and
- to monitor performance in relation to a service target performance incentive scheme.

The information gathering requirements are expected to provide sufficient information to the AER for the purposes of allowing it to implement the regulatory regime as defined in the rules.

Likewise, the dispute resolution frameworks contained in chapters 8 and 6A appear to provide adequate scope for dispute resolution bodies to obtain the information necessary to render determinations. Specifically:

§ Clause 8.2.6C(c) allows a DRP in the context of a chapter 8 non-price access dispute to give to the parties such directions relating to the use and disclosure of information obtained from other parties as it considers necessary in the circumstances; and

§ schedule 6A.3.4(a) allows a commercial arbitrator in the context of a chapter 6A access price dispute to give the parties such directions as it considers necessary, including in relation to the provision of documents and information to the other party (clause S6A.3.4(a)(1)) and the use and disclosure of information (sub-schedule 6A.3.4(a)(2)).

**Conclusion:** The dispute resolution framework contained in the Rules likely meets the requirement specified in clause 6(4)(o) of the CPA.

### 7.3. Interstate Issues

Clauses 6(2) and 6(4)(p) of the CPA require that an access regime ensure that there are no impediments to interstate access arising from state based regime differences.

In our view, the new national electricity regime will satisfy these requirements. A clear motivation for the current energy reforms has been to provide a nationally consistent approach to energy regulation to address perceived differences in the regulatory approach adopted by state based regulators interpreting the previous National Electricity Code. The new national framework will allow the AER to provide consistent approaches across state jurisdictions, thereby ensuring that there are relatively few, if any, impediments to interstate access arising from the regime.

**Conclusion:** The transmission access framework is unlikely to create any impediments to interstate access arising from state-based regime differences.

## 8. Summary and Recommendations

Our key conclusion from this analysis is that the Rules developed by the Commission for the economic regulation of transmission services, are consistent with the principles required for certification and specified in clauses 6(2) to 6(4) of the Competition Principles Agreement. Concerns arise however in relation to whether the Rules provide an ‘enforceable right of access’ to transmission services, and the effectiveness of the dispute resolution mechanism, particularly because of the split in arbitration processes for price and non-price terms and conditions between chapter 6A mechanism and that provided in chapter 8.

In the following sections we summarise our key findings and provide a series of recommendations, which seek to improve the prospects of the national electricity regime, as it relates to transmission services, satisfying the certification requirements of the CPA.

### 8.1. Summary of Key Findings

In summary, our view is that the national electricity regime as it relates to transmission services would likely meet the requirements of the CPA for an effective access regime in all but the following respects:

- § the access framework is currently unlikely to satisfy the requirements in clauses 6(4)(b) or (c) of the CPA since it is doubtful whether the regime creates an enforceable right of access to either prescribed or negotiated transmission services;
- § the dispute resolution framework is currently unlikely to satisfy the requirements in clause 6(4)(i) of the CPA since:
  - the separation of ‘price’ and ‘non-price’ access disputes under the Rules is artificial, presents risks of opportunistic gaming between dispute processes, and likely constitutes an inefficient means of resolving disputes overall; and
  - there is a significant risk that the chapter 8 framework in particular would not strike an appropriate balance in accordance with the clause 6(4)(i) criteria; and
- § the Rules do not contain a prohibition against hindering access, hence the regime likely does not comply with clause 6(4)(o) of the CPA, which prohibits such hindering.

In the following sections we provide a series of recommendations to resolve these issues, thereby better improving the prospects of an application for certification being successful.

### 8.2. Recommendation 1: Creation of an Enforceable Right to Access

We believe the prospect of certification would be significantly improved if the regime incorporated an enforceable right to access those transmission services covered by the access framework on terms and conditions consistent with the Rules.

Such a right could be created in a number of ways, including by the inclusion in the Rules of an explicit right for any person to access prescribed or negotiated transmission services. Including an enforceable right of access is an integral part of an effective access regime, since it prevents a TNSP from refusing to provide access, irrespective of the terms and conditions required either by the Rules, or through an arbitration process.

### 8.3. Recommendation 2: Single Dispute Resolution Framework

In our view, there would be considerable merit in consolidating price *and* non-price access disputes within a single dispute resolution framework. The chapter 6A commercial arbitration framework should likely form the foundation of the consolidated dispute resolution regime since it has distinct advantages over its chapter 8 counterpart, including its incorporation of explicit pricing principles consistent with the requirements of clause 6(4)(i).

In order to include ‘non-price’ disputes within the ambit of chapter 6A two things are required:

§ the chapter 6A arbitration framework would need to be applied to disputes regarding *non-price* terms and conditions. In particular, the following aspects of the Rules would need to be recast:<sup>71</sup>

- the *Negotiated Transmission Service Pricing Principles* (Rule 6A.9.1);
- the *Negotiated Transmission Service Pricing Criteria* (Rule 6A.9.4); and
- the *Negotiating Framework* (clause 6A.9.2(c)); and

§ the chapter 8 framework must be excluded for any disputes covered by the amended chapter 6A arbitration framework, whilst preserving the integrity of the *chapter 5* requirements, for example, technical requirements relating to minimum access standards.

For the reasons outlined in section 6.2.3.1, in our view, the criteria that a commercial arbitrator must consider when determining the *price* for a negotiated service or an *access charge* are wholly consistent with the clause 6(4)(i) criteria. However, the ‘non-price’ criteria contained in chapter 5 may be insufficient, in combination, to satisfy the requirements of clause 6(4)(i), (j) or (l).<sup>72</sup> A key issue is therefore what additional ‘non-price’ criteria should appropriately be included in chapter 6A for consideration by a commercial arbitrator?

Whilst the regulatory framework for gas is currently undergoing wide-ranging reform,<sup>73</sup> the National Gas Code nonetheless provides a useful example. It incorporates a single dispute resolution framework for simultaneously resolving price and non-price disputes that

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<sup>71</sup> To this end, the *Negotiated Transmission Service Pricing Principles* and the *Negotiated Transmission Service Pricing Criteria* would henceforth be better termed the *Negotiated Transmission Service Access Principles* and the *Negotiated Transmission Service Access Criteria*, or similar, respectively.

<sup>72</sup> See section 6.2.3.2 for a detailed analysis.

<sup>73</sup> The new legislative framework for gas, proposed by the MCE is in many respects similar to the newly cast National Electricity Regime. In the recently release exposure draft, the proposed *National Gas Law* establishes the AER as the primary arbitrator of access disputes (price and non-price). In making a determination, Part 4.5, as presently drafted, would require the AER to comply with a number of overarching regulatory principles, many of which closely mirror those contained in chapter 6A of the National Electricity Rules. For example, s.21(2) requires that a service provider be provided with a reasonable opportunity to recover at least the efficient costs of providing reference services and complying with regulatory obligations and instruments. In other words, the gas and electricity regimes appear to be converging in many important respects.

successfully obtained certification from the NCC. It requires a commercial arbitrator to take into account:<sup>74</sup>

- § the service provider's legitimate business interests and investment;
- § the costs to the service provider of providing access, with the exception of costs associated with losses arising from increased competition in related markets;
- § the economic value to the service provider of any additional investment that the access seeker or the service provider has agreed to undertake;
- § the interests of all users;
- § firm and binding contractual obligations of the service provider or other persons (or both) already using the covered pipeline;
- § the operational and technical requirements necessary for the safe and reliable operation of the covered pipeline;
- § the economically efficient operation of the covered pipeline; and
- § the benefit to the public from having competitive markets.

However, an arbitrator's decision is subject to certain restrictions, including, it cannot make a decision that:

- § would impede the rights of existing users (clause 6.18(b));
- § is inconsistent with any applicable queuing policy (clause 6.18(d)); or
- § requires the service provider to provide, or the user or prospective user to accept, a reference service at a tariff other than the reference tariff (clause 6.18(e)).

A comparison of the various price and non-price criteria contained within the certified Gas Code with the price and non-price criteria contained within chapters 5 and 6A of the national electricity regime reveals clear differences between the *forms* that many of the criteria take in the national electricity code *vis-à-vis* the Gas Code. In substance however, the approaches are predominately the same.

For example, while the Gas Code includes an explicit requirement to consider the *legitimate business interests and investment* of service providers, we do not consider that the absence of an explicit requirement is a concern for the Rules. For the reasons outlined in section 6.2.3.1 above, in our view, the existing chapter 6A criteria, in combination, adequately consider the interests of the facility owners. To recap:

- § clauses 6A.9.1(1) and (8) expressly states that prices for negotiated services should reflect the cost of providing those services, including the costs of complying with regulatory obligations – a requirement that is consistent with the interests of facility owners;

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<sup>74</sup> In addition, as section 7.2.3 explained, the Gas Code also incorporates explicit criteria for an arbitrator to apply when considering whether an extension to capacity should take place.

- § clause 6A.9.1(9) prohibits prices that would in any way threaten the ongoing safety of the power system, which is also consistent with facility owners' interests;
- § the floor/ceiling test contained within clause 6A.9.1(2) ensures access seekers are forced to pay at least the costs that they impose specifically upon the network, thereby ensuring the interests of facility owners are preserved.

We do believe however that there is merit in including in the Rules a requirement that an arbitrator consider firm and binding contractual obligations of the service provider and/or other persons, and whether a decision (including with regards to an extension) would impede the rights of other existing users. In our view, were these additional principles inserted into the *Negotiated Transmission Service Pricing (or 'Access') Principles* (Rule 6A.9.1),<sup>75</sup> the requirements of clause 6(4)(i), (j) and (l) of the CPA would likely be met by the framework overall.

We therefore recommend that if chapter 6A were to be expanded to include non-price access disputes, the Rules be amended to include such criteria. In addition, we note that it would likely be necessary to include in the Rules a requirement that would preclude a commercial arbitrator from imposing a price for a *prescribed service* that departs from an AER revenue determination or a judicial review ruling, as the case may be.

Finally, it will be necessary to ensure that any overlap that may be created between the application of the expanded chapter 6A and the chapter 8 framework. Indeed, it is conceivable that disputes about the price (or non-price) terms and conditions on which a negotiated transmission service is to be supplied could continue to be amenable to the dispute resolution process under chapter 8 despite an expansion to chapter 6A.<sup>76</sup> In our view, these amendments would likely ensure that the dispute resolution regime would resolve disputes in an efficient and effective manner, thereby meeting the CPA requirements. However, it is beyond the scope of this report to examine the legal implications posed by such amendments.

#### **8.4. Recommendation 3: Include Prohibition against Hindering Access**

We believe there is merit in including in the Rules a prohibition against a service provider engaging in conduct that hinders access to a regulated service by another person. Currently the Rules do not contain an explicit prohibition against hindering access and it is unclear whether one could be legitimately implied. Explicitly including a prohibition would remove any doubt surrounding the regime's compliance with clause 6(4)(o) of the CPA. It is again beyond the scope of this report to examine the legal implications posed by such an amendment.

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<sup>75</sup> And thus also the *Negotiated Transmission Service Pricing Criteria* (Rule 6A.9.4) and the *Negotiation Framework* (clause 6A.9.2(c)).

<sup>76</sup> One way to achieve this might be to incorporate an additional Rule in chapter 8 that effectively stated that chapter 8 would no longer apply to those clauses also covered by the expanded chapter 6A.

## 8.5. Summary of Recommendations

To recap, our key recommendations for potentially improving the certification prospects of the national electricity regime are:

- § to create an enforceable right to access transmission services covered by the access framework on terms and conditions consistent with the Rules;
- § to create a single dispute resolution framework by consolidating the application of chapter 8 and chapter 6A such that the latter covers disputes upon both price *and* non-price terms and conditions; and, in addition to the existing criteria, also required an arbitrator to consider:
  - firm and binding contractual obligations of the service provider and/or other persons; and
  - whether a decision (including with regards to an extension) would impede the rights of existing users; and
- § to include an explicit prohibition against a service provider engaging in conduct that hinders access to a regulated service by another person.

In our view, were these recommendations implemented, the national electricity regime, as it relates to electricity transmission services would likely comply with the certification requirements as an effective access regime.<sup>77</sup>

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<sup>77</sup> It should be re-emphasised that the regulatory framework as it applies to *distribution services* will also be relevant to the regime's certification. Accordingly, this assessment is incomplete since it only relates to the rules for transmission services. At the time of an application for certification, a more complete and comprehensive review of the entire regime against the CPA requirements will need to be undertaken.

## Appendix A. Competition Principles Agreement

- 6(2)** The regime to be established by the Commonwealth legislation is not intended to cover a service provided by means of a facility whether the State or Territory Party in whose jurisdiction the facility is situated has in place an access regime which covers the facility and conforms to the principles set out in this clause unless:
- (a) the council determines that the regime is ineffective having regard to the influence of the facility beyond the jurisdictional boundary of the State or Territory; or
  - (b) substantial difficulties arise from the facility being situated in more than one jurisdiction.
- 6(3)** For a State or Territory access regime to conform to the principles set out in this clause, it should:
- (a) apply to services provided by means of significant infrastructure facilities where:
    - (i) it would not be economically feasible to duplicate the facility;
    - (ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market; and
    - (iii) the safe use of a facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist; and
  - (b) incorporate the principles referred to in subclause (4).
- 6(4)** A State or Territory access regime should incorporate the following principles:
- (a) Wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the person seeking access.
  - (b) Where such agreement cannot be reached, Governments should establish a right for persons to negotiate access to a service provided by means of a facility.
  - (c) Any right to negotiate access should provide for an enforcement process.
  - (d) Any right to negotiate access should include a date after which the right would lapse unless reviews and subsequently extended; however, existing contractual rights and obligations should not be automatically revoked.
  - (e) The owner of a facility that is used to provide a service should use all reasonable endeavours to accommodate the requirement of person seeking access.
  - (f) Access to a service for persons seeking access need not be on exactly the same terms and conditions.
  - (g) Where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.
  - (h) The decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved.
  - (i) In deciding on the terms and conditions for access, the dispute resolution body should take into account:
    - (i) the owner's legitimate business interests and investment in the facility;

- (ii) the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets;
  - (iii) the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake;
  - (iv) the interests of all persons holding contracts for use of the facility;
  - (v) firm and binding contractual obligations of the owner or other persons (or both) already using the facility;
  - (vi) the operational and technical requirements necessary for the safe and reliable operation of the facility;
  - (vii) the economically efficient operation of the facility; and
  - (viii) the benefit to the public from having competitive markets.
- (j) The owner may be required to extend, or to permit extension of, the facility that is used to provide a service if necessary but this would be subject to:
- (i) such extension being technically and economically feasible and consistent with the safe and reliable operation of the facility;
  - (ii) the owner's legitimate business interests in the facility being protected; and
  - (iii) the terms of access for the third party taking into account the costs borne by the parties for the extension and the economic benefits to the parties resulting from the extension.
- (k) If there has been a material change in circumstance, the parties should be able to apply for a revocation or modification of the access arrangement which was made at the conclusion of the dispute resolution process.
- (l) The dispute resolution body should only impede the existing right of a person to use a facility where the dispute resolution body has considered whether there is a case for compensation of that person and, if appropriate, determined such compensation.
- (m) The owner or user of a service shall not engage in conduct for the purpose of hindering access to that service by another person.
- (n) Separate accounting arrangements should be required for the elements of a business which are covered by the access regime.
- (o) The dispute resolution body, or relevant authority where provided for under specific legislation, should have access to financial statements and other accounting information pertaining to a service.
- (p) Where more than one State or Territory regimes applies to a service, those regimes should be consistent and, by means of vested jurisdiction or other cooperative legislative scheme, provide for a single process for persons to seek access to the service, a single body to resolve disputes about any aspect of access and a single forum for enforcement of access arrangements.