Long on Flaws, Short on Fixes

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According to the ACCC's consultants, price and access regulation of gas and electricity networks has increased national wealth by somewhere between $2 billion and $11 billion. On several occasions the ACCC's Energy Commissioner, Ed Willett, has cited these estimates. The first time he did so they were faithfully reported by a naÃ¯ve cadre of journalists, keen to ingratiate themselves with an ACCC ever willing to offer inside information in private briefings.

However, under scrutiny the ACCC's estimates have been demolished. They stem from economic modelling based on price reductions mandated by the ACCC. Illogically, the modelling would show even greater gains if the ACCC had required prices to be set at zero! This carries particular weight in the light of a series of successful challenges to the price determinations the ACCC has set for gas pipelines.

The Productivity Commission's (PC) recently released Review of the Gas Access Regime included a scholarly dismantling of the ACCC's trumpeted estimated benefits from its price decisions. The PC review is the latest in a series of reports the Commonwealth has commissioned into the regulatory arrangements for gas. The PC rejects the ACCC's stoutly maintained view that its regulatory approach encourages rather than deters investment. Like earlier reviews of gas, the latest PC Review recommended some deregulation of the present controls on the gas pipeline industry, especially with regard to new facilities. Such recommendations have been endorsed by deregulatory rulings of Australian Competition Tribunal regarding the Eastern Gas Pipeline (Bass Strait to Sydney) and by the Minister Macfarlane on the Moomba to Sydney pipeline.

However, the PC's fine analysis is let down by the anodyne nature of its recommendations. Following the series of earlier reviews and decisions, forceful and specific recommendations were needed from the Productivity Commission in order to operationalise a less intrusive regulatory regime.

Unfortunately the PC has largely relied upon setting overarching objectives which can be readily interpreted to support a wide range of positions. Central to its recommendations is an objects clause, 'To promote economically efficient operation and use of, and economically efficient investment in, the services of transmission pipelines...'. Any regulator would readily claim such wording as describing precisely how it currently operates. Yet the PC is clearly dissatisfied with the decisions taken by regulatory agencies (the ACCC and National Competition Council)

The PC offers no guidance on when market disciplines provide better outcomes than regulation for existing networks and how (or whether) to provide a transition to a deregulated state. It should, for example, have offered firm guidelines that regulation is unnecessary once a market is supplied by competing pipelines.

In addition, although it reiterates findings of other advisory bodies in recommending regulatory holidays for new pipelines, it advocates Ministerial discretion over such a decision rather than making it automatic. This guarantees an additional regulatory hurdle.

Similarly, recognising the costly and lobby-intensive nature of the current intrusive price setting model, the PC also recommends a light handed monitoring option. However its recommendations on this were somewhat weaker in its final report compared to the draft report. The latter envisaged that the present approach of 'access arrangements with reference tariffs would only occur in the more extreme circumstances'.

Again, although it assesses that the price determinations by the ACCC have been inappropriately harsh to the supplier, the PC's solutions to counter these offer little promise of improvement. Thus, the PC recommends that tariffs should be set to meet the efficient costs of providing access to the reference services and give a return commensurate with the risks. This might amount to little more than an exhortation to the regulator to undertake the process it already considers

it follows.

And the PC makes a suggestion that prominent people be assembled to develop a consensus position of how to set an agreed 'capital asset pricing model' by Australian regulators. It is doubtful that the desired consensus could emerge.

Unfortunately therefore, although the PC offers robust criticism of current heavy handed and intrusive regulatory practices, its report is remarkably short in offering future directions on how to correct this. This is regrettable in view of the pivotal role most authorities consider that gas must take in Australia's energy policy.

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