

# Review of the role of the Tasmanian Economic Regulator

December 2014

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## **Summary of key proposals**

The Department of Treasury and Finance is reviewing the role of the Tasmanian Economic Regulator and examining related issues. There is a range of activities that the Regulator currently performs that no longer appear to be required, due to a range of circumstances, and removing unnecessary functions will reduce regulatory costs for the Tasmanian community. There are also some activities or powers that need to be amended to ensure the Regulator can operate in an effective manner. A summary of the key proposals on which Treasury is seeking feedback is set out below.

### **Metro pricing investigations (page 9)**

The Regulator ceases undertaking Metro pricing investigations. Instead, the Department of State Growth is responsible for prices oversight and providing advice on Metro's pricing, in conjunction with the Department of Treasury and Finance, to the Minister for Infrastructure and Treasurer, with the Regulator to provide an advisory role to the Departments as required.

### **MAIB pricing investigations (page 10)**

The Regulator continues to undertake MAIB pricing investigations.

### **Performance reporting on the electricity supply and the water and sewerage industries (page 12)**

The Regulator is only required to produce an industry performance report for the electricity supply industry if directed to by the Minister responsible for the *Economic Regulator Act 2009* and the *Electricity Supply Industry Act 1995*.

The Regulator is only required to produce industry performance reports for the water and sewerage industry shortly before each water and sewerage prices investigation, likely to occur every five years.

### **Interstate energy price comparisons (page 13)**

The Regulator is required to produce interstate energy price comparisons only if directed to by the Minister responsible for the Economic Regulator Act and the Minister responsible for the relevant legislation that applies to the electricity supply industry or the gas industry.

### **Reporting on electricity network reliability (page 14)**

The Regulator is required to prepare a report on electricity network reliability every three years or if directed to by the Minister responsible for the Economic Regulator Act and the Electricity Supply Industry Act.

### **Competitive neutrality arrangements (page 14)**

The Minister responsible for the Economic Regulator Act, with the agreement of the relevant Portfolio Minister, has the power to direct councils to take actions recommended by the Regulator when the Regulator has upheld a competitive neutrality complaint.

No significance test is applied with respect to competitive neutrality complaints.

### **Newspaper notifications (page 15)**

The Regulator is not required to publish notices relating to its activities.

### **Compliance powers of the Regulator (page 16)**

The Regulator has the power to impose financial penalties in cases of material or sustained non-compliance by regulated entities in the electricity and gas industries.

### **Extending the functions and powers of the Regulator (page 16)**

There is no extension of the role of the Regulator into other areas.

## Background

The Tasmanian Economic Regulator is an independent statutory body, currently made up of a three person panel. It has responsibilities in relation to the Tasmanian electricity, gas and water and sewerage sectors as well as in the pricing of some State Government businesses. The Regulator also investigates competitive neutrality complaints and may conduct taxi fare methodology inquiries.

As part of the State Government's review of boards and committees, the Government intends to change the composition of the Regulator in light of some recent changes to the scope of the Regulator's functions, most notably the transfer of regulatory oversight of electricity distribution to the Australian Energy Regulator (AER).

Changes are also being considered to the role and powers of the Regulator. These changes will require amendments to the *Economic Regulator Act 2009*.

## Structure of the Regulator

A number of different models for reducing the membership of the Regulator are being considered by the Government.

One option is to base the model on the previous prices regulator, the Government Prices Oversight Commission (GPOC). Under this model, the Commissioner was appointed by the Governor, the same arrangement that applies to the Director of the Environment Protection Authority. The GPOC model required one or more Assistant Commissioners to be appointed for each pricing investigation. The legislation allowed, but did not require, members of the Commission to be State Service officers.

A second option is to have a one person Regulator, without any ability to appoint additional members. As with the other options, there would be the capacity to appoint an Acting Regulator and to delegate some of the Regulator's functions. This option would generate the most savings, but there would be less flexibility in the event that the Regulator's workload increased.

A third option is to amend the Economic Regulator Act so that the Regulator comprises a minimum of one person, allowing the option for another person to be added if the workload requires it. This is the model that applies in the ACT. Under this option, the Economic Regulator Act would continue to provide the option for State Service officers to be appointed to the Regulator. This option would appear to provide for the greatest flexibility.

The intended changes to the composition of the Regulator, scheduled to commence from 1 July 2015, are expected to deliver expenditure savings, with the majority of the benefits flowing through to customers of regulated entities. The new arrangements will not affect the independence of the Regulator as the Economic Regulator Act and other legislation set out the objectives, principles and criteria that the Regulator must take into account in making recommendations or decisions. Furthermore, the Act already provides that the Regulator is not subject to ministerial control and maintains other protections, such as allowing access to the Ombudsman in cases of complaints.

Treasury is seeking comments from stakeholders on the options discussed above.

The Treasurer has also directed Treasury to review the Regulator's functions. There is a range of activities that the Regulator currently performs that no longer appear to be required, due to a range of circumstances. Removing unnecessary functions will reduce regulatory costs for the Tasmanian community. There are also some activities or powers that need to be amended to ensure the Regulator can operate in an effective manner.

This Paper therefore contains a number of proposals to change the Regulator's responsibilities and other statutory obligations. The paper also identifies some other potential legislative changes relating to the roles of the Regulator.

There are advantages, disadvantages and risks associated with each of these proposals and Treasury seeks feedback from all stakeholders, including regulated entities, customer representatives and potentially other regulators.

There will be discussions with stakeholders in December 2014 and January 2015.

Written submissions are sought from stakeholders and members of the public. Submissions should be emailed to [economic.reform@treasury.tas.gov.au](mailto:economic.reform@treasury.tas.gov.au) by **30 January 2015**. All submissions will be treated as public documents unless the authors request otherwise.

## **Current functions of the Regulator**

The Regulator's current functions are established under the *Economic Regulator Act 2009*, the *Electricity Supply Industry Act 1995*, the *Water and Sewerage Industry Act 2008*, the *Gas Act 2000* and the *Gas Pipelines Act 2000*.

### **Economic Regulator Act**

The Regulator's key functions under the Economic Regulator Act are to:

- conduct independent investigations and inquiries into the pricing policies of certain Government-owned bodies, that are monopoly, or near monopoly, providers of services in Tasmania, currently Metro Tasmania and the Motor Accidents Insurance Board (MAIB);
- recommend maximum prices chargeable by these bodies in respect of the supply of those services;
- conduct investigations into complaints of breaches of the national competition policy competitive neutrality principles by State and local government bodies;
- undertake inquiries relating to or affecting the pricing policies of Local Government and State Government bodies; and
- conduct taxi fare methodology inquiries when requested by the Government on behalf of the Transport Commission.

### **Electricity Supply Industry Act**

The Regulator administers the Electricity Supply Industry Act, the Tasmanian Electricity Code and is responsible for other related regulatory instruments. The Regulator has a number of key responsibilities:

- administering the licensing system for electricity supply industry entities, other than retail businesses, and monitoring and enforcing their compliance with licence conditions;
- issuing and maintaining the Tasmanian Electricity Code;
- monitoring and regulating technical standards in the electricity supply industry;
- conducting investigations into the pricing policies of entities that provide monopoly or near monopoly services that are determined to be declared electrical services;
- regulating standing offer retail prices while there is no effective competition for household electricity customers;

- regulating electricity feed-in tariff prices for eligible small scale renewable generation systems; and
- administering the arrangements for the regulation of certain wholesale financial contracts offered by Hydro Tasmania to electricity retailers operating in Tasmania.

In undertaking these functions, the Regulator's objectives include:

- the promotion of efficiency and competition in the electricity supply industry;
- the establishment and maintenance of an efficient system of electricity generation, transmission, distribution and supply;
- the establishment and enforcement of proper standards of security, reliability and quality in the electricity supply industry; and
- the protection of the interests of electricity consumers.

### **Water and Sewerage Industry Act**

The Regulator also has responsibilities under the Water and Sewerage Industry Act, which provides the framework for the licensing and economic regulation of the water and sewerage sector, including:

- determining maximum prices for regulated water and sewerage services;
- promoting efficiency in terms of costs and pricing arrangements;
- issuing and administering licences for water and sewerage service providers;
- establishing and administering minimum customer service standards through the Tasmanian Water and Sewerage Customer Service Code; and
- monitoring the performance of the industry.

### **Gas Act and Gas Pipelines Act**

The Gas Act, the Gas Pipelines Act and associated codes establish the procedural and institutional arrangements for what has been a fully contestable gas market since its commencement. Excluding price regulation, the Regulator's functions are similar to its functions in relation to the electricity supply industry with key objectives of:

- facilitating the development of a gas supply industry in Tasmania;
- promoting efficiency and competition in the gas supply industry; and
- protecting the interests of consumers of gas.

## **The role of the Office of the Tasmanian Economic Regulator**

The Economic Regulator Act allows for the Regulator to make arrangements to utilise State Service employees to support its functions. The Office of the Tasmanian Economic Regulator (OTTER) is a branch of the Department of Treasury and Finance that supports the Regulator by:

- undertaking research and analysis and presenting recommendations for consideration by the Regulator;
- preparing reports and other written documentation;
- administering licensing regimes;
- monitoring compliance by regulated entities;
- liaising with key stakeholders within government as well as customers and stakeholder representatives; and
- providing general administration support.

The Regulator's Budget, which includes the cost of OTTER and the Regulator panel, was \$1.8 million, with approximately \$1.3 million in salary costs and \$500 000 in non-salary costs.

The Regulator is funded largely through fees it levies on regulated entities. In 2013-14, the Regulator received approximately 90 per cent of its funding from these entities.

## **Recent actions to reduce regulatory costs**

The Regulator's activities result in costs not only in respect of the work of the Office, but also for regulated entities in providing information to the Regulator, preparing reports and responding to regulatory issues as they emerge.

The Regulator has undertaken a number of recent actions, within the scope of its discretion under the relevant regulatory provisions, to reduce regulatory costs and is continuing to identify and progress further opportunities such as aligning electricity transmission and distribution performance reporting obligations with national arrangements and streamlining incident reporting arrangements.

In terms of actions taken to date, the Regulator has:

- adopted a risk-based approach for auditing regulated entities' compliance with their licence and statutory obligations;
- changed its consultation processes to allow minor and technical changes to be made to codes and guidelines without the need for stakeholder consultation;
- aligned water and sewerage reporting requirements with national reporting requirements to avoid duplication in reporting;
- held discussions with the owners of Basslink with the objective of streamlining their reporting obligations; and
- reduced and reorganised the content of the annual industry performance reports (ie the Energy in Tasmania and the Water and Sewerage State of the Industry reports) to make these reports more concise.

## Proposals to change the Regulator's functions

While the Regulator has undertaken a number of actions to reduce regulatory costs, its scope of responsibilities is largely governed by legislation. Therefore, the Regulator has only a limited scope to implement major changes in its operations that may lead to reduced regulatory costs. Any major changes would require legislative amendments, which is a matter of Government policy.

At the same time, there are some other measures which could lead to improved regulatory outcomes which may, in the long run, reduce the workload of the Regulator.

Some proposals have been identified that would result in further changes in the Regulator's responsibilities.

These proposals cover:

- Metro Tasmania pricing investigations;
- MAIB pricing investigations;
- performance reporting on the electricity supply and water and sewerage industries;
- interstate energy price comparisons;
- reporting on electricity network reliability;
- competitive neutrality arrangements;
- newspaper notifications;
- compliance powers of the Regulator; and
- extending the functions and powers of the Regulator.

These proposals are discussed below.

### Monopoly service pricing investigations

Under the Economic Regulator Act, the Regulator is required to undertake periodic pricing investigations relating to monopoly services of prescribed public entities, currently MAIB and Metro Tasmania. The Regulator is required to determine the current cost of efficiently providing these services, including a return on the assets employed, and to recommend maximum fares that may be charged over a specified period.

The relevant Minister sets the maximum fares in respect of those services over that period under a Pricing Order, after considering the recommendations of the Regulator and any comments from the entity and other Ministers.

The purpose of these pricing investigations is not specified in the Act. Equally, the Act does not set out any criteria that must be satisfied before the services of a public entity are declared as subject to this regulation, except that they must be monopoly services.

These provisions were initially in the *Government Prices Oversight Act 1995*. At this time, State Government businesses were required to be more commercially focussed. It was not known how their behaviour would change, including the information and advice they would provide to the Government and the prices they would propose, which generally required parliamentary

approval. In the Second Reading Speech for this Act, the rationale for an independent review of their activities was that as these government businesses become more commercially focussed, their pricing should not reflect the exercise of monopoly power and should be related to their costs.

At the time, most attention was on the Hydro-Electric Commission, which had been a quasi-regulatory body as well as the only electricity supplier in the State. The HEC was initially listed as a prescribed body, together with the bulk water authorities, the former Metropolitan Transport Trust and the MAIB. Metro Tasmania and the MAIB, the only remaining businesses requiring these investigations, are now well established as government businesses under the modern framework.

Another advantage of the pricing investigations is that they provide independent information on the efficiency of the business, as compared with industry benchmarks, which can be used to improve productivity and business performance. It is unclear, however, whether this external scrutiny is needed or whether these businesses should have, as good business practice, their own arrangements to assess their performance and identify opportunities for improvements.

It is standard practice that the investigated body bear the full costs of an investigation by the Regulator. The body can also incur significant costs of its own under the process. These costs are passed on to the monopoly provider's customers in the case of the MAIB while, for Metro Tasmania, they are shared between customers and taxpayers through the Consolidated Fund. The issue, therefore, is whether the current regulatory framework, with its attendant costs, is still required or whether there are lower cost options that would provide satisfactory outcomes. For example, if the Regulator ceased undertaking pricing investigations, a Government Department could become responsible for prices oversight. However, even this lower cost option is still likely to incur some level of additional cost for a Department which may need to be recovered from the investigated bodies. In these circumstances, appropriate checks would need to be put in place to satisfy the investigated bodies that a Department is only spending the minimum amount required to advise the Government.

### **Metro pricing investigations**

Under the Economic Regulator Act, the Regulator is required to undertake Metro pricing investigations every five years. The Regulator is required to determine the current cost of efficiently providing bus services, including a return on the assets employed, and to recommend maximum fares that may be charged over the following five years. In practice, these pricing investigations have focussed on the maximum revenue that Metro should receive to provide all its services at efficient cost. The Regulator also includes in the final report a review of the 'Metro Index', which contains the weights of labour costs, fuel costs and other costs that it recommends should be used in any escalation of Metro's maximum revenues, the relevant weighting of those costs and the mechanism for change in each of the components.

The Order issued by the Minister only covers the maximum full adult fare for a single trip and the discount to be applied to travel by those passengers pre-purchasing travel using the Greencard and does not other cover other fares, such as the adult concession fares and student fares or other discounts. The most recent Order was issued in November 2014. Other fares charged by Metro Tasmania, such as adult concession fares and student fares are determined in accordance with Government policy, and the indexation arrangements for those fare types, are provided for in a ten year contract for Metro's services involving Metro and the Secretary of the Department of State Growth. Indexation is by application of the Metro Index to these concession fares. Accordingly, the Regulator has an indirect role only in determining concession fares.

Concession passengers make up almost 80 per cent of Metro's passengers. Metro's total revenue from its fares is well below the level that would enable Metro to recover all its efficient costs, accounting for around 22 per cent of its revenue. The remainder of Metro's revenue comes from a payment under the contract.

Therefore, the pricing investigation does not directly influence the level of most Metro fares. For full adult fares, the pricing investigation report shows whether these fares are around the cost recovery level or greater or less than this level.

An advantage of the Metro pricing investigation is that it provides information on efficient costs. This is useful in understanding the efficiency of the company's operations. The Metro Index also provides important information on how these payments, and subsidised fares, may be increased over the period of the contract.

While Metro may have a monopoly for some public transport services, there are alternative transport options for many actual and potential customers. If fares for some services were significantly increased, many customers would find alternative arrangements and patronage for Metro would decline. The fact that Metro fares for most users are so heavily subsidised suggests that Metro is not in a position to misuse its monopoly power.

In practice, the Government will continue to have a major role in determining Metro fares as public bus transport is regarded as an important service for lower income households and other disadvantaged sectors of the community. Regardless of the information the Government may have, therefore, the level of fares will remain a decision for the Government.

The Regulator's cost of the most recent Metro investigation was approximately \$80 000. Metro Tasmania also incurred its own costs. In this context it could be argued that the investigation by the Regulator just adds another layer of unnecessary cost.

The Economic Regulator Act could be amended so that the Regulator is no longer required to perform this function. However, it would still remain necessary to have some form of oversight of the efficiency of Metro's operations and its pricing. Accordingly, an alternative option could be for the Department of State Growth (which has policy responsibility for Metro) to have oversight and provide advice, in conjunction with the Department of Treasury and Finance, to the Minister for Infrastructure and Treasurer. The Regulator could then provide an advisory role as required and have information gathering powers as may be necessary. The savings to Metro would then either require a smaller Community Services Obligation payment from the Government to Metro or a very small reduction in fares to customers.

**Proposal:**

*The Regulator ceases undertaking Metro pricing investigations. Instead, the Department of State Growth is responsible for prices oversight and providing advice on Metro's pricing, in conjunction with the Department of Treasury and Finance, to the Minister for Infrastructure and Treasurer, with the Regulator to provide an advisory role to the Departments as required.*

**MAIB pricing investigations**

The MAIB provides compulsory no-fault third party motor accident compensation in Tasmania. The Regulator is required to conduct investigations into the pricing policies of the MAIB every four years. In contrast to Metro, the MAIB is a self-funded scheme and is not subsidised by the Government.

The MAIB has estimated that the total cost of the most recent review was almost \$310 000, including the cost of the Regulator's investigation of around \$150 000. These reviews tend to

be more complex than the Metro investigations, mainly because of issues around re-insurance and future liabilities which are difficult to quantify and require actuarial advice. As a commercial insurance business, the MAIB would continue to be required to undertake its own actuarial work in the absence of any investigation by the Regulator.

Potentially, the MAIB is in a position to misuse its market power as it is a genuine monopoly and there is a legal requirement for vehicle owners to purchase insurance from the MAIB. This provides a strong case for some form of prices oversight, either by the Regulator setting maximum prices, as in the water and sewerage industry, or with the Government making the final decision on MAIB premiums. The risk here is that a Government might choose to set premiums at a very high level to provide large dividends to boost Government revenue, or set levels too low and put the solvency of the MAIB at risk.

There is nothing to prevent Governments setting very high premiums under the current arrangements. Governments have not taken this decision because in setting premiums they have sought to balance the advantages of large dividends with the impact on businesses and households of higher premiums, especially when cost-of-living pressures are a major concern. It is not evident that Governments would necessarily have any greater incentive to set higher premiums if the Regulator did not undertake any pricing investigations.

If pricing investigations ceased, there would not be sufficient information available to determine whether MAIB's operations are efficient according to industry benchmarks and whether the premiums are substantially above costs, including claims costs, unless these issues were examined under some other process, which could involve a role for the Regulator. While information on MAIB dividends is available, this may not reveal whether premiums are reasonable or not as these dividends tend to be influenced more by the investment returns than by the extent to which premiums in any year exceed MAIB's costs.

In cases where the MAIB considers that an increase in premiums is required, it may not be possible for stakeholder groups to accept that such an increase is reasonable if there is no detailed report, from a source that is perceived as being independent, that sets out the issues and supports such an increase.

If the Regulator ceased undertaking this activity, the Department of State Growth could be made responsible for providing advice, in conjunction with the Department of Treasury and Finance, to the Government on MAIB premiums. Again the Regulator could have an advisory role as required and with information gathering powers as may be necessary. However, the Departments would need to obtain detailed actuarial advice, and incur some of the costs the Regulator currently incurs. Otherwise, the advice from the Departments could lead to premiums being either too low as to risk insolvency, or too high resulting in unnecessarily high costs to the community. The costs for the Departments and the Regulator to prepare advice would need to be considered under this alternative option.

Again, the primary benefit would be the reductions in the Regulator's costs which, in turn, would save MAIB directly and would also lower its compliance costs. However, even if the MAIB passed on these savings to consumers in full, the savings to individual consumers are likely to be very small.

**Proposal:**

*The Regulator continues to undertake MAIB pricing investigations.*

## **Performance reporting on the electricity supply and the water and sewerage industries**

The Regulator undertakes annual performance reporting of the water and sewerage industry and the electricity supply industry. The annual water and sewerage report is required under the Water and Sewerage Industry Act. The Regulator has determined that an annual electricity supply industry report is consistent with the objectives of the Electricity Supply Industry Act.

There is a key difference between the electricity supply industry and the water and sewerage industry. Entrants are able to enter Tasmania's electricity supply industry, principally as generators or retailers and therefore they require information about the industry and would have some interest in reports, including performance reports, issued by the Regulator. All consumers are also contestable in the electricity supply industry. However, it is unclear what value potential entrants, or consumers, place on these reports.

By contrast, there is considerable less scope for entrants to operate in Tasmania's water and sewerage industry and consumers cannot choose who provides them with water and sewerage services.

The principal reason for this performance reporting has been asymmetric information; that is, the monopoly providers have more information about their services than customers and the Tasmanian community. Public reporting can be a powerful incentive for the industry to maintain and improve performance. An important feature of the report is that it presents a substantial amount of information on Tasmania's energy sector in a single document.

The 'Energy in Tasmania' report draws on annual performance reports and annual returns submitted by electricity and gas entities to the Regulator, together with information provided by the Department of State Growth on other fuels such as coal, wood and petroleum. Where applicable, the report also provides interstate comparisons.

Electricity entities are also required to provide information to the Australian Energy Regulator for its annual reports. In the case of the water and sewerage industry, TasWater is required to provide information to the National Water Commission for its national performance reports, to the Environment Protection Authority and to the Director of Public Health. Much of this information is required by the Regulator for its annual performance report.

The estimated annual cost to the Regulator of undertaking both of these reports is approximately \$160 000, which is met by regulated entities and then passed on to consumers.

It is proposed to remove the requirement for the Regulator to undertake these performance reports each year. These reports draw largely on information that is publically available. Other bodies such as the AER, the National Water Commission and the Environment Protection Authority cover the majority of the areas covered in these reports.

The main benefit of not providing these reports is the reduction in the Regulator's costs. The regulated entities have to provide much of this information to other regulators and so there is unlikely to be a material reduction in their own reporting costs.

Even if the savings made by the Regulator were passed on in full, it would have very little impact on prices of electricity, natural gas or water and sewerage, estimated to be less than \$1 a year for the average customer receiving these services.

There is a risk that if the Regulator no longer undertook the performance reporting, the level of service provision and degree of transparency and accountability of these regulated entities may decline. This might arise because the national reports do not focus so heavily on Tasmanian issues.

One option is the production of performance reports every three years or so. A second option is for the Regulator to produce a report if directed to by the Minister responsible for the Economic Regulator Act and the Electricity Supply Industry Act. This could occur, for example, if a major issue occurs such as an extended or widespread network failure or concerns over anti-competitive behaviour.

For water and sewerage, a further option is for the Regulator to include a performance report in the documentation it prepares under the price investigation process, which is expected to occur every five years. The Regulator would therefore take into account any major performance issues identified as part of the investigation. .

It would not be appropriate for the legislation to prevent the Regulator from producing an industry performance report for either industry at any other time. If the Regulator considers that a report is necessary and in the public interest, given the Regulator's statutory functions, such a measure would undermine the independence of the Regulator.

**Proposals:**

*The Regulator is only required to produce an industry performance report for the electricity supply industry if directed to by the Minister responsible for the Economic Regulator Act and the Electricity Supply Industry Act.*

*The Regulator is only required to produce industry performance reports for the water and sewerage industry shortly before each water and sewerage prices investigation, likely to occur every five years.*

**Interstate energy price comparisons**

In accordance with the objective of the Electricity Supply Industry Act for the Regulator to protect the interests of electricity customers, the Regulator prepares reports on natural gas and electricity prices available to small customers across Australian jurisdictions. These reports also examine the prices paid by customers entitled to a concession on their electricity bill and, for Tasmanian customers, the extent to which concessions reduce the impact of changes in electricity prices.

The AER's website and the ABS already provide information on electricity prices, though both organisations use a different measurement approach. Given these existing information services, the Regulator could cease providing these reports.

There would be a small saving in the Regulator's costs. However, the reports of the Regulator may provide more useful price comparisons than those prepared by the ABS and AER. There may be a risk that if they cease there is not a sufficiently robust framework to compare prices in Tasmania and therefore to provide information to stakeholders and the general public on this issue. Against this, it is becoming increasingly difficult to undertake meaningful interjurisdictional price comparisons due to the variations that exist in the availability of regulated energy prices across the various Australian states and territories.

There may be circumstances when information is required on how Tasmania's energy prices compare with prices in other Australian jurisdictions, such as if there are large price changes in Tasmania or some mainland jurisdictions. One option is for the relevant Minister to direct the Regulator to produce an energy price comparison report.

**Proposal:**

*The Regulator is required to produce interstate energy price comparisons only if directed to by the Minister responsible for the Economic Regulator Act and the Minister responsible for the relevant legislation that applies to the electricity supply industry or the gas industry.*

## Reporting on electricity network reliability

The Regulator aims to ensure that the interests of customers are not compromised by a low standard of service from the monopoly suppliers in the State. This is why the Energy in Tasmania report is supplemented by the inclusion of an annual reliability review. Reporting on the outcomes of this review, which is a legislative requirement, provides an evaluation of the reliability of the power system and assesses the outlook for reliability in the medium term, namely the following three to five years. The Report identifies the issues that will impact on the capacity of the power system to "keep the lights on".

From time to time specific aspects of industry performance are also investigated by the Regulator. For example, major incidents causing loss of power to consumers are closely monitored. Reports on the causes and consequential action are also publicly available.

The AER is expected to commence reporting on some of these areas. For example, the AER's service target performance incentive scheme is designed to influence a business, such as TasNetworks, to maintain or improve the quality of its services.

If the Regulator's responsibilities in relation to reporting on electricity network reliability were removed, the Regulator would no longer need to undertake an annual reliability review, or report on a range of electricity network performance outcomes or undertake electricity incident reporting. This would result in a saving in the Regulator's costs. However, due to the AER's reporting requirements, there may not be a material reduction to the costs of regulated entities.

If responsibility for monitoring and reporting on overall system reliability is left to the business entities and the AER, the issue is whether a range of risks to the robustness and security of energy supply in Tasmania could develop over time. If so, there may be an argument that reliability in the industry should continue to be periodically reviewed by a Tasmanian body to ensure that any industry-wide trends are being identified.

Again, it would not be appropriate for the legislation to prevent the Regulator from producing a report on electricity network reliability at any other time. If the Regulator considers that a report is necessary and in the public interest, given the Regulator's statutory functions, such a measure would undermine the independence of the Regulator.

### **Proposal:**

*The Regulator is required to prepare a report on electricity network reliability every three years or if directed to by the Minister responsible for the Economic Regulator Act and the Electricity Supply Industry Act.*

## Competitive neutrality arrangements

The objective of the competitive neutrality principles is the elimination of resource allocation distortions arising out of public ownership of entities engaged in significant business activities. These principles seek to prevent government businesses enjoying a competitive advantage over the private sector due to the fact that governments may subsidise certain activities and they generally face lower financing costs and no tax liabilities.

Part 6 of the Economic Regulator Act is designed to ensure that competitive neutrality principles are followed in Tasmania. This Part applies where a person believes that a public body has contravened any of the competitive neutrality principles. If that person is adversely affected by the alleged contravention and has discussed the alleged contravention with the

public body, that person may make a complaint to the Regulator. After conducting the investigation, the Regulator must determine whether the complaint is justified or not.

The number of competitive neutrality complaints each year varies. The estimated costs for the Regulator in a typical year are in the order of \$50 000 to \$100 000. Funding for this activity comes from the Consolidated Fund.

The Government has the capacity to direct a State Government entity to alter its behaviour if the Regulator upholds a competitive neutrality complaint. However, there is a deficiency in the powers of the Economic Regulator Act because the Government is unable to direct a council or an entity owned by local government in matters involving competitive neutrality in cases where a breach has been found by the Regulator. Enforcement powers could be introduced to reduce the incidence of repeated complaints about the same issue, such as the pricing of overnight camping facilities.

If enforcement powers were introduced, some councils may be concerned at the prospect of the Government having the power to interfere in the way local government operates its business activities.

Currently there is no significance test to determine whether an activity of a public body is large enough to warrant an investigation by the Regulator, unlike in some other states and territories. Instead, the criteria used by the Regulator focus more on the actual and potential competitive impact. A significance test could be adopted, such as the activity must generate a turnover of a minimum of \$2 million per year, to prevent investigations of very small activities and reduce the expenditure by the Regulator, and therefore the Government, on these investigations.

If a significance test were introduced, however, this would mean that some competitive neutrality complaints involving smaller business activities would not be investigated, even if these activities provide an unfair advantage to publicly-owned operators and therefore breach competitive neutrality principles.

**Proposals:**

*The Minister responsible for the Economic Regulator Act, with the agreement of the relevant Portfolio Minister, has the power to direct councils to take actions recommended by the Regulator when the Regulator has upheld a competitive neutrality complaint.*

*No significance test is applied with respect to competitive neutrality complaints.*

**Newspaper notifications**

Currently a number of Acts require the Regulator to publish notices in three local newspapers, such as notices of pricing investigations and associated hearings. This typically involves an annual cost of approximately \$10 000 to \$20 000. This may no longer be required as notices are published through website notification (with the current on-line subscription service) and media releases.

It is expected that there would be a low risk of some stakeholders not being aware of the Regulator's activities. Further, OTTER's Customer Consultative Committee is a good source of information exchange between key stakeholders, and includes groups such as Anglicare, TasCOSS and LGAT.

**Proposal:**

*The Regulator is not required to publish newspaper notices relating to its activities.*

## **Compliance powers of the Regulator**

The Regulator has a limited range of sanctions to ensure compliance by regulated entities in the electricity supply or gas industries. It can issue a written direction in cases where there are concerns over non-compliance but has no other sanctions other than the very costly and serious options of seeking a court-imposed fine or suspending or cancelling a licence and stepping in to take over operations. These last two options are so extreme that regulated entities may judge that they are not credible and therefore may have an incentive to not comply with their obligations.

Under the Water and Sewerage Industry Act, the Regulator may impose a monetary penalty up to 5000 penalty units (currently up to \$700 000) for the contravention of the Act or licence conditions, and up to 200 penalty units (currently up to \$28 000) for each subsequent day on which the contravention continues. However, the Regulator must consult, and consider any submission from the entity concerned before a monetary penalty may be imposed.

In other jurisdictions, economic regulators typically have mid-range sanctions in the form of administrative penalties they can impose on the entities. In terms of the electricity supply and gas industries, the Regulator considers that it should have the power to issue these penalties to encourage compliance without having to resort to very high cost and less timely actions. This would allow the Regulator to have the capacity to set a small or large penalty that can reflect the circumstances of a compliance breach, which would potentially have a more effective deterrent effect.

**Proposal:**

*The Regulator has the power to impose financial penalties in cases of material or sustained non-compliance by regulated entities in the electricity and gas industries.*

## **Extending the functions and powers of the Regulator**

Under the Economic Regulator Act, the Regulator may undertake inquiries relating to Local Government and State Government bodies on the direction of the Treasurer. These inquiries must, however, relate to or affect the pricing policies of these bodies. The Regulator has no information gathering powers in performing this function.

One issue is whether this function could be expanded to allow inquiries to be conducted to cover all aspects of the performance of these bodies, except perhaps where they relate to their statutory obligations in other areas, such as environmental protection or occupational health and safety.

A further issue is whether the Regulator should have information gathering powers that it can call on when conducting these inquiries.

The Regulator's role could also be expanded to provide advice to the Government on economic regulation in other areas across Government. The Regulator currently may conduct taxi fare methodology inquiries when requested by the Government. It could be asked to provide advice on, for example, irrigation pricing, an appropriate royalty regime for a natural resource or the fees to be charged, and the conditions that should be attached, for mining leases.

The primary benefit of expanding the Regulator's role is that it has expertise in economic regulation and pricing and this may also reduce the need for the Government to hire external consultants.

**Proposal:**

*There is no extension of the role of the Regulator into other areas.*

### **Other changes to the powers and functions of the Regulator**

The list of proposed changes to the role of the Regulator as set out above is not exhaustive. The Department of Treasury and Finance is interested in other potential changes to the powers and functions of the Regulator, including any alternative measures.

### **Timing and next steps**

The timeframe for the review is set out below:

December 2014 to January 2015 – consultation process. Treasury will hold discussions with the relevant businesses affected, such as Aurora, TasNetworks, TasWater, Metro and the MAIB, and also with government agencies, the Regulator, members of OTTER's Customer Consultative Committee and other interested parties and members of the public upon request. Written submissions are also sought from stakeholders and members of the public, to be emailed to Treasury at [economic.reform@treasury.tas.gov.au](mailto:economic.reform@treasury.tas.gov.au) by **30 January 2015**.

February 2015 – Treasury to prepare advice to the Government on recommended changes to the powers and functions of the Regulator, including a summary of stakeholder views.

Autumn 2015 session of Parliament – Legislation to amend the Economic Regulator Act and other Acts and regulations to be introduced into the Tasmanian Parliament.