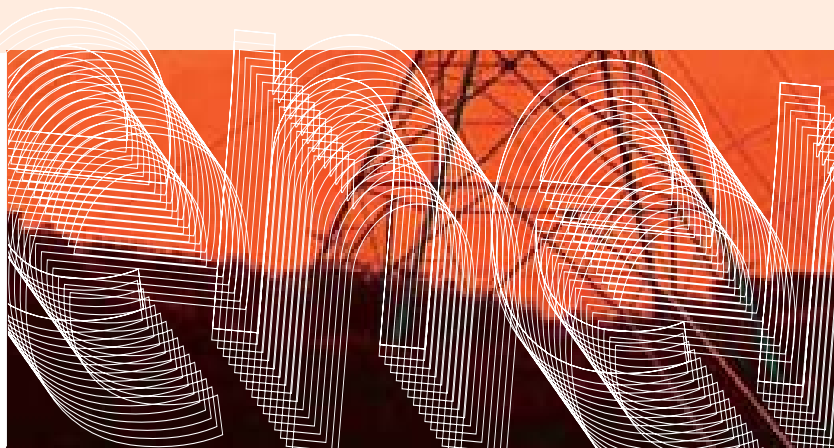


THE AUSTRALIAN ENERGY REGULATOR
(AER) BEGAN OPERATIONS ON 1 JULY 2005.

A NEW DIRECTION FOR ECONOMIC REGULATION OF AUSTRALIAN ENERGY MARKETS

STEVE EDWELL,
CHAIR, AER



This new independent regulatory body is responsible for the economic regulation of Australian energy markets and compliance with the electricity and gas rules at a national level. Households will benefit from energy market reforms that will encourage competition.

The AER comprises three statutorily appointed members: a full-time chairperson (myself), and two part-time members, one of whom is also required to be a full-time ACCC commissioner (Ed Willett) and a state/territory member (Geoff Swier).

A new framework for economic regulation

Until now there has been a fragmented and inconsistent approach to economic regulation across the states and territories, leading to unnecessary regulatory costs for businesses.

Once all the AER's functions are established, it will be a one-stop national regulator. This will mean consistent gas and electricity regulation across Australia. This streamlined regulatory process within Australian energy markets solves many of the problems raised by the Parer Energy Market Review and will benefit industry and consumers through more efficient regulation.

The infrastructure debate

What about comments that the Australian energy sector faces an apparent infrastructure crisis? Looking at the unprecedented levels of capital expenditure being approved by regulators and undertaken by participants, it is clear that we are far from a crisis.

For example, in electricity transmission about \$4.2 billion has been invested in just the first five years of the ACCC regulatory regime. To put this figure into perspective, this level of capital expenditure represents 30 per cent of the entire asset base of the networks in question.

The same is true of the Australian gas market. Far from being in a crisis, since 1997 the Australian gas industry has invested in five major transmission pipelines, significantly increasing access to new and existing gas reserves.

It is this sort of evidence that led the recent independent Export Infrastructure Taskforce to conclude that there is no infrastructure crisis.

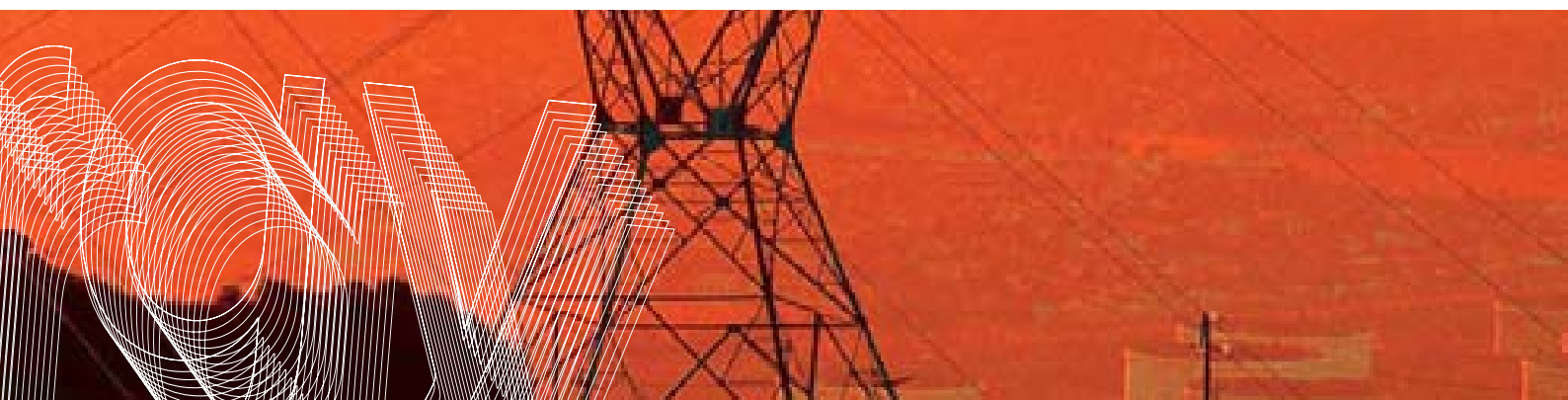
However, it is undeniable that Australia is experiencing a sustained period of economic growth, which in turn has led to sustained high levels of growth in demand for energy.

Regulatory guidelines

The goals of the AER are clear: increase the efficiency, transparency and predictability of regulatory decisions to ensure a streamlined and efficient process and a consistent framework across the jurisdictions. The rules governing a revenue determination should be clear to the industry well before any decision is made.

It is clear that one of the biggest strengths of the ACCC's approach to regulatory decisions has been its open and transparent consultation process.

The AER is keen to ensure that this form of consultation process is continued and is built upon.



IT IS VITAL TO ENSURE THAT THE REGULATORY REGIME CONTINUES TO BE MEET THE LONG-TERM INTERESTS OF CONSUMERS AND ENSURE THE LONG-TERM VIABILITY OF PARTICIPANTS.

For example, in Queensland, demand growth in electricity is running at twice the levels forecast four years ago. Significant infrastructure investment is therefore needed across the energy sector.

In light of this, everybody in the industry including the regulator should ask if the current regulatory regime is appropriate and whether it will deliver long-term security of supply for consumers, coupled with efficient pricing.

It is vital to ensure that the regulatory regime continues to meet the long-term interests of consumers and ensure the long-term viability of participants.

In other words, the methods used by the regulator should be apparent well in advance and not be changed halfway through. Accordingly, the AER published a compendium of regulatory guidelines for electricity transmission on 22 August 2005. The compendium is largely based on approaches developed by the ACCC, but draws all material together as a complete set of reference documents, including the statement of principles for regulation of electricity transmission services (SRP).

The compendium has been designed to evolve over time. The AER will monitor the effectiveness of these guidelines and review them as issues are raised by industry and other interested parties, and as circumstances, theory and best practice regulation develop.

The focus will remain on ensuring that consumers are able to share in efficiency gains and that the right incentives are placed on participants. Again, these reforms are about increasing the quality of regulation.

The consultation processes will only ever be as good as the input that is received. So far, industry participants have actively and effectively participated in consultation processes, consumer groups less so. One of the challenges is to encourage consumer groups to engage more effectively in the regulatory process.

Market monitoring and enforcement

To ensure a well-functioning electricity wholesale market, a robust surveillance, monitoring and enforcement mechanism is essential and the AER has assumed the responsibility for these from the National Electricity Code Administrator (NECA).

NECA emphasised voluntary compliance, an approach that would still seem appropriate, but one that needs to be complemented by a detailed monitoring of participant conduct and effective enforcement.

The AER is keen for a culture of corporate compliance to emerge. This is much better than an adversarial approach, with inherent costs and disruptions. The market does seem to have a reasonably good track record on compliance. When there is evidence of non-compliance, though, the AER will respond quickly and firmly and not hesitate to take enforcement action if the matter is serious enough.