AUSTRALIAN COMPETITION TRIBUNAL

Application by ETSA Utilities [2010] ACompT 5

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| Review from: | Australian Energy Regulator |
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| Parties: | **ETSA UTILITIES (ABN 13 332 330 749)** |
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| File number: | 4 of 2010 |
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| Judges: | **MIDDLETON J (DEPUTY PRESIDENT),****MR R DAVEY AND MR R SHOGREN** |
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| IN THE AUSTRALIAN COMPETITION TRIBUNAL |  |
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| RE: | APPLICATION UNDER SECTION 71B OF THE NATIONAL ELECTRICITY LAW FOR REVIEW OF A DISTRIBUTION DETERMINATION MADE BY THE AUSTRALIAN ENERGY REGULATOR IN RELATION TO ETSA UTLITITES PURSUANT TO CLAUSE 6.11.1 OF CHAPTER 6 OF THE NATIONAL ELECTRICITY RULES |
| BY: | ETSA UTLITITES (ABN 13 332 330 749)Applicant |

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| MEMBERS: | MIDDLETON J (DEPUTY PRESIDENT), MR R DAVEY AND MR R SHOGREN  |
| DATE OF PUBLICATION OF REASONS FOR DECISION: | 13 October 2010 |
| PLACE: |  |

**REASONS FOR DECISION**

1. On 14 September 2010, the Tribunal made the following announcement and directions:

***OTHER MATTERS:*** *The Tribunal has formed the view that a ground of review has been established for the purposes of section 71R(3) of the* National Electricity (South Australia) Law *in relation to the AER’s rejection of the Applicant’s claim for an addition to be made to its opening RAB in respect of easements extant as at 1 July 1999.*

*In these directions:*

*“category 1 easements” means registered power line easements in relation to ETSA Corporation’s distribution network as at 1 July 1999;*

*“category 2 easements” means registered padmount transformer easements in relation to ETSA Corporation’s distribution network as at 1 July 1999;*

*“category 3 easements” means deemed statutory easements arising from unregistered grants of easements by landowners in relation to ETSA Corporation’s distribution network as at 1 July 1999;*

*“category 4 easements” means deemed statutory easements arising from licences granted by landowners in relation to ETSA Corporation’s distribution network as at 1 July 1999;*

*“category 5 easements” means registered easements in relation to ETSA Corporation’s distribution network as at 1 July 1999 arising as a result of land subdivisions; and*

*all dollar figures are in dollars as at 1 July 1999.*

***THE TRIBUNAL DIRECTS THAT:***

*1. By 4pm on 5 November 2010, the AER file and serve any report addressing the following estimates relied upon by the Applicant:*

*(a) as to category 1 easements:*

*(i) the rate of $1949 per easement for acquisition costs;*

*(ii) the rate of $872/km for survey costs;*

*(b) as to category 2 easements:*

*(i) the rates of $2564 and $2052 per easement for acquisition costs;*

*(c) as to category 3 easements:*

*(i) the rate of $1282 per easement for acquisition costs;*

*(ii) the rate of $872/km for survey costs;*

*(iii) the total length of country easements;*

*(iv) the total length of metropolitan easements;*

*(d) as to category 4 easements:*

*(i) the rate of $605 for acquisition costs;*

*(ii) the rate of $872/km for survey costs;*

*(iii) the total length of country easements;*

*(iv) the total length of metropolitan easements;*

*(e) as to category 5 easements:*

*(i) the number of subdivisions containing an easement;*

*(ii) the average number of allotments in such subdivisions.*

*2. By 4pm on 17 November 2010, the Applicant file and serve any submissions in response to any report filed and served in accordance with paragraph 1.*

*3. The application be adjourned to not before 19 November 2010.*

1. It will be observed that the Tribunal formed the view that a ground of review had been established for the purposes of s 71R(3) of the *National Electricity (South Australia) Law* (‘the NEL’) in relation to the Australian Energy Regulator’s (‘AER’) rejection of the applicant’s claim for an addition to be made to its opening regulatory asset base (RAB) in respect of easements extant as at 1 July 1999.
2. The Tribunal now gives reasons for that view being formed.
3. The NEL is set out in the Schedule of the *National Electricity (South Australia) Act 1996* (‘the Act’) and, by the operation of s 6 of the Act, applies as a law of South Australia. Section 9 of the NEL gives the National Electricity Rules (‘the Rules’) the force of law in South Australia.
4. ETSA provides electricity distribution network services in South Australia and is registered as a distribution network service provider (‘DNSP’) under cl 2.5.1 of the Rules.
5. The AER is responsible for the economic regulation of electricity distribution network services provided by DNSPs, including ETSA. In particular, under Ch 6 of the Rules, the AER is responsible for determining the revenue that ETSA may earn from the provision by ETSA of electricity network services in South Australia. Prior to the AER assuming this responsibility in January 2008, the responsibility lay with the Essential Services Commission of South Australia (‘ESCOSA’).
6. Pursuant to cl 6.8.2 (in Ch 6) of the Rules (as modified by cl 11.26.2 of the savings and transitional rules in Ch 11 of the Rules), ETSA was required to submit, and on 1 July 2009 did submit, a regulatory proposal to the AER for consideration in accordance with the Rules (‘regulatory proposal’).
7. Pursuant to cl 6.10.1 of the Rules, the AER was required to make, and did make, a draft distribution determination in relation to the regulatory proposal entitled Draft Decision South Australia Draft Distribution Determination 2010-11 to 2014-15, dated 25 November 2009, and published on 30 November 2009 (‘the draft determination’).
8. On 14 January 2010, ETSA submitted a revised regulatory proposal to the AER (‘revised proposal’), pursuant to cl 6.10.3 of the Rules.
9. On 6 May 2010, pursuant to cl 6.11.1 of the Rules, the AER published its final distribution determination entitled: ETSA Utilities Distribution Determination 2010-11 to 2014-15, dated 4 May 2010 (‘the final determination’).
10. The AER’s reasons for the final determination are set out in its “Final Decision South Australia Distribution Determination 2010-11 to 2014-15”, dated May 2010.
11. In June 2010 ETSA applied for leave to review the final determination in respect of the following matters and was, pursuant to s 71B, granted that leave on 15July 2010:
	* + 1. Gamma: the decision by the AER, in calculating the estimated cost of corporate income tax pursuant to cl 6.5.3 of the Rules, to apply a value for the assumed utilisation of imputation credits (gamma) of 0.65; and
			2. RAB: the determination by the AER of the opening asset base pursuant to cl 6.5.1 of the Rules, in particular–
				1. the “valuation” of easements by the AER; and
				2. the failure by the AER to correct for a modelling error made by ESCOSA in its treatment of capital contributions used in calculating the 1999 RAB Value,

each of which is, or is an element of, a constituent decision pursuant to cl 6.12.1 of the Rules.

1. These reasons only deal with the question of the RAB, and the issue relating to the “valuation” of easements by the AER.
2. Pursuant to s 71P of the NEL, the Tribunal on review may affirm, set aside or vary the final determination or remit the matter back to the AER to make the final determination again with any direction or recommendation of the Tribunal.
3. The grounds set out in s 71C(1) are as follows:
4. *the AER made an error of fact in its findings of facts, and that error of fact was material to the making of the decision;*
5. *the AER made more than 1error of fact in its findings of facts, and that those errors of fact, in combination, were material to the making of the decision;*
6. *the exercise of the AER's discretion was incorrect, having regard to all the circumstances;*
7. *the AER's decision was unreasonable, having regard to all the circumstances.*
8. When considering the s 71C(1)(d) ‘unreasonable’ ground, the Tribunal has observed that the term ‘unreasonable’ does not just provide a basis for inferring the presence of one or more of the established grounds which render a decision ‘incorrect’ in the sense of the incorrect exercise of discretion, rather it provides a separate and distinct ground of review: *Application by EnergyAustralia* [2009] ACompT 8, at [63].
9. The term “findings of fact” in the context of s 71C(1)(a) and (b) is interpreted broadly, encompassing findings as to the existence of historical and present facts, opinions about the existence of future facts or circumstances, and opinions formed by the regulator based upon approaches to the assessment of facts or methodologies which it has chosen to apply.
10. ETSA submitted that, when regard is had to all of the circumstances, the AER in its final determination and final decision exercised its discretion incorrectly and made an unreasonable decision in relation to the value of easements.
11. Further, ETSA submitted that the AER made errors of fact which were (alone or in combination) material to the making of its decision under cl 7.3(b) of a 1999 Electricity Pricing Order ( ‘EPO’) made by the South Australian Treasurer pursuant to the *Electricity Act 1996* (SA), namely, the findings that:
	* + 1. on page 35 of the final decision, the “value” of the distribution network easements was already included in the RAB (whereas a valuation of the distribution network easements was not contained in Schedule 9 to the EPO and was not subsequently undertaken by ESCOSA in its 2005-2010 Price Determination);
			2. on page 35 of the final decision, ESCOSA’s assessment of the distribution network easements was a proper valuation for the purpose of the final determination and final decision (whereas ESCOSA merely perpetuated the $6m “allowance” for easements in the EPO which was formulated at a time when the data set necessary for a valuation of the distribution network easements was not available);
			3. on page 34 of the final decision, there was no convincing evidence of representations concerning the valuation of easements being made to bidders by the South Australian Government during the sale process of ETSA (whereas the first hand evidence of the State’s sales advisers, personnel of the Government-owned ETSA Utilities Pty Ltd, and the successful bidder demonstrates that such representations had been made on behalf of the State Government and relied upon by the successful bidder).
12. To correct these errors, ETSA sought an adjustment to the opening RAB as at 1 July 2005 of $116,161,569 based on the following calculations of indexed historic cost (IHC) for each of its categories of easements:

| **Easement Category** | **Number** | **Length (km)** | **Compensation Costs(as at 1/7/1999)** | **Acquisition Costs (as at 1/7/1999)** |
| --- | --- | --- | --- | --- |
| **Category 1**Registered Powerlines | Actual | Actual | Actual | (Estimate contained in the MFS 1996 Report valuation of compensation and acquisition costs) |
| Country | 5,099 | 3,870 | $1,390,629 | $1,949 per easement / $872 per km = $13,312,591 |
| Metro | 2,316 | 639 | $1,117,486 | $1,949 per easement / $872 per km = $4,847,661 |
| **Total** | $2,508,115 | $18,160,252 |
| **Category 2**Registered Padmount Transformers | Actual | N/A | Actual – only available as aggregate | Estimate derived from MFS 1996 Report as per the MFS 2009 Bridging Report |
| Commercial | 2,621 |  | (see total below) | $2,564 per easement = $6,720,244 |
| Metro | 5,508 | N/A | (see total below) | $2,564 per easement = $14,122,512 |
| Country | 398 | N/A | (see total below) | $2,052 per easement = $816,696 |
| **Total** | $141,066 | $21,659,452 |
| **Category 3**Statutory easement for powerlines – subtype A | Actual | Estimate from sample | Actual | Estimate derived from MFS 1996 Report as per MFS 2009 Bridging Report |
| Country | 17,269 | 20,368 | $96,629 | $1,282 per easement / $872 per km = $39,899,754 |
| Metro | 2,363 | 1,813 | $22,850 | $1,282 per easement / $872 per km = $4,610,302 |
| **Total** | $119,479 | $44,510,056 |
| **Category 4**Statutory easements for powerlines – subtype B | Actual | Estimate from sample  | Actual | Estimate derived from MFS 1996 Report as per MFS 2009 Bridging Report |
| Country | 8,187 | 3,974 | $39,316 | $605 per easement / $872 per km = $8,418,463 |
| Metro | 2,803 | 577 | $10,370 | $605 per easement / $872 per km = $2,198,959 |
| **Total** | $49,686 | $10,617,422 |
| **Category 5**Registered subdivision easements | Estimate | N/A | Not applicable | Actual costs of review and approval of plan of land division by ETSA – flat charge of $562 per plan and $20 per lot. |
| Subdivision | 3217 | - | - | $562 per plan + $20 per lot applied to 3217 plans and an estimated 36.5 lots per plan = $4,156,364 |
| **Total** | - | $4,156,364 |
| **Total compensation and acquisition costs** **as at 1 July 1999** | **$101,921,892** |
| **Total compensation and acquisition costs** **as at 1 July 2005** | **$123,427,569** |
| **Less $6 million indexed to 1 July 2005** | **$116,161,569** |

1. Questions arose as to the legislative context, including questions concerning the relationship between the *National Electricity (South Australia) Act 1996* (SA), the EPO, the NEL, the National Electricity Code which applied before 1 July 2005 (‘Code’) and the Rules.
2. An important threshold legal issue which arises in the context of these enactments and instruments is:

Did the AER have power under clause 7.3 of the EPO to make any adjustment to ETSA’s opening RAB as at 1 July 2005 in December 2004 dollars of $2,466m set out in the table in clause S6.2.1(c)(1) of the Rules?

1. The AER acknowledged that (assuming it had power to consider the relevant easements), it was open to the Tribunal to conclude that the AER incorrectly exercised its discretion in deciding not to consider in detail the valuation of the relevant easements submitted to it by the ETSA.
2. Notwithstanding the AER’s acceptance in the final decision of the proposition that cl 7.3(b)(iv) of the EPO conferred discretionary power on the AER to adjust ETSA’s RAB, the question whether cl 7.3(b) confers power to modify the RAB value specified in the Rules remained to be determined by the Tribunal for itself in this review proceeding.
3. Unless the Tribunal was satisfied that cl 7.3(b) is enlivened, the Tribunal could not proceed to determine the existence of any ground of review in relation to the AER’s conclusions on the relevant easements, or to make its own determination in lieu of the AER’s conclusion on this matter.
4. The Tribunal has had the advantage of detailed submissions on this threshold legal question by the AER. The following short summary does not do justice to the very well considered submissions. However, the Tribunal is clearly of the view that the AER had powers of adjustment of the opening RAB under cl 7.3 of the EPO.
5. This conclusion depends on whether the “context otherwise requires” for the purposes of cl 7 of Sch 3 to the NEL in its application to cl 1.11 of the EPO, so that the presumption in cl 7 should not be applied. If the context does not otherwise require, the effect of cl 7 is that the reference to the Code in cl 1.11 of the EPO will be taken to be a reference to the Rules, and the result of this construction will be that the AER (and the Tribunal) is required by cl S6.2.1(c)(1) of the Rules to apply the specified opening RAB as at 1 July 2005 to ETSA, and has no discretion in the matter. To the extent that cl 7.3 of the EPO might be inconsistent with cl S6.2.1(c)(1) of the Rules, cl 1.11 of the EPO makes it clear that the Rules must be applied.
6. That the context “otherwise requires” is to be found in the fact that after the Rules had commenced, various provisions of the *Electricity Act 1996* (SA) were amended to change references to the Code into references to the Rules (such as in s 35A), but the provision under which the EPO had been made, (s 35B(1)), was not similarly amended and was retained in its earlier form, referring to the “Code”.
7. As the AER submits the relevant question is whether, as at 1 July 2005 upon the replacement of the old National Electricity Law by the NEL, and upon the “remaking” of the Code in the form of the Rules, the context of cl 1.11 of the EPO “otherwise required”.
8. Although the amendments to the *Electricity Act 1996* (SA) came into force more than two years after the commencement of the NEL and the Rules, on 1 September 2007, nevertheless the selective amendment of references to the Code other than in s 35B(1) of that Act supports the conclusion that cl 1.11 of the EPO was intended to subordinate the EPO only to the Code, and not also to the Rules.
9. Therefore, the Tribunal is of the view that the AER did have a discretion in the matter.
10. As stated in the AER’s final decision at page 35, the AER did not consider the valuation submitted by ETSA in detail, instead adopting ESCOSA’s decision in favour of the $6m value. The Tribunal finds that the AER’s decision not to consider the valuation in detail was an incorrect exercise of discretion because:
	* + 1. the origin of the $6m figure showed it to be only a partial value of the relevant easements; and
			2. ESCOSA’s analysis had been largely responsive to the deprival valuation methodology advanced by ETSA at the time, whereas ETSA is now advancing a valuation based on what it claims to be an IHC methodology.
11. Having concluded as above, the Tribunal considered it appropriate to make the directions it did as set out above. This would allow a proper assessment to be made by the Tribunal. There is no question that upon forming the view that a ground of review had been established for the purposes of s 71R(3) of the NEL, that the Tribunal had the power to so direct and consider any report filed and served by the AER and any submissions made by ETSA.

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| I certify that the preceding thirty-three (33) numbered paragraphs are a true copy of the Reasons for Decision herein of the Honourable Justice Middleton (Deputy President), Mr RC Davey and Mr RF Shogren. |

Associate:

Dated: 13 October 2010