

# Economic Regulation Authority

 WESTERN AUSTRALIA

*Promoting fair prices, quality services and choice.*



# Public vs Private Infrastructure & Regulation

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# Overview

## Issues

Economic Regulation Authority

Some Economics

Private/Public Infrastructure & Regulation

Challenge for the future

# Introduction

Reflect on experience to date

Note major move to independent economic regulation

Provide feedback

Not offering policy prescriptions

# Part 1: Issues

What is the most efficient arrangement?

What are the pitfalls?

What role does regulation play?

Does regulation make a difference?

What forms of regulation work best?

Where to in future?

# Part 2: The Economic Regulation Authority

## Functions

- Administers access to monopoly infrastructure
- Licenses service providers
- Monitors & regulates markets
- Carries out inquiries (referred by government)

# Key Features of the ERA

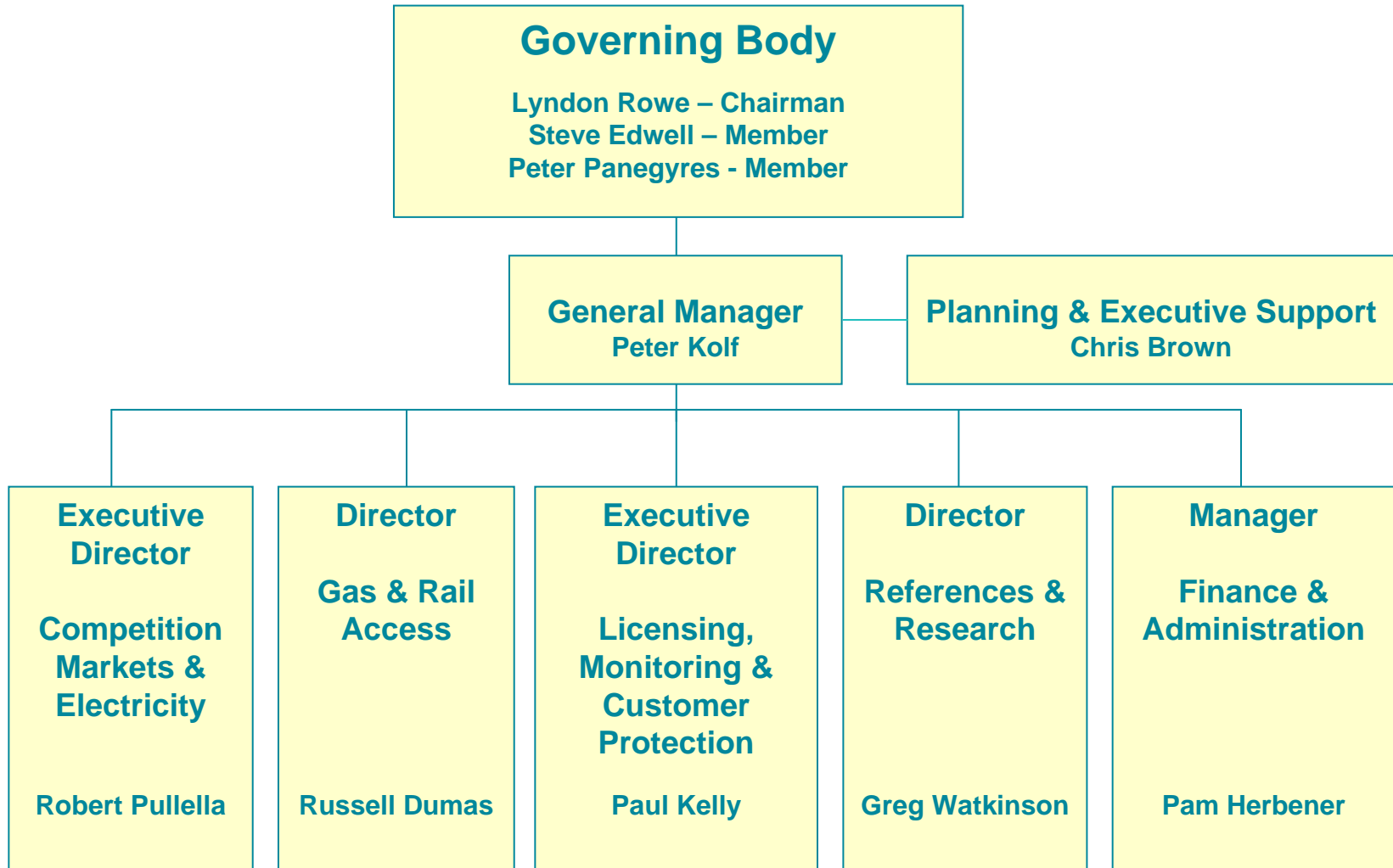
- Independence
- Transparency
- Consultation

# Objectives of Independent Economic Regulation

- Facilitate private sector provision of services
- Make best use of monopoly infrastructure
- Enhance competition upstream/downstream
- Consumer Protection and Fair Trading
  - Interface with Energy Ombudsman



# Economic Regulation Authority



# Objective & Matters to be Taken into Account

- No overriding objective

Key matters which the Authority must have regard to:

- Promoting outcomes that are in the public interest
- The interests of consumers, investors & service providers
- Encouraging investment in relevant markets
- Promoting competition & fair market conduct
- Preventing abuse of monopoly power
- Promoting transparency and public consultation

# New National Gas Law

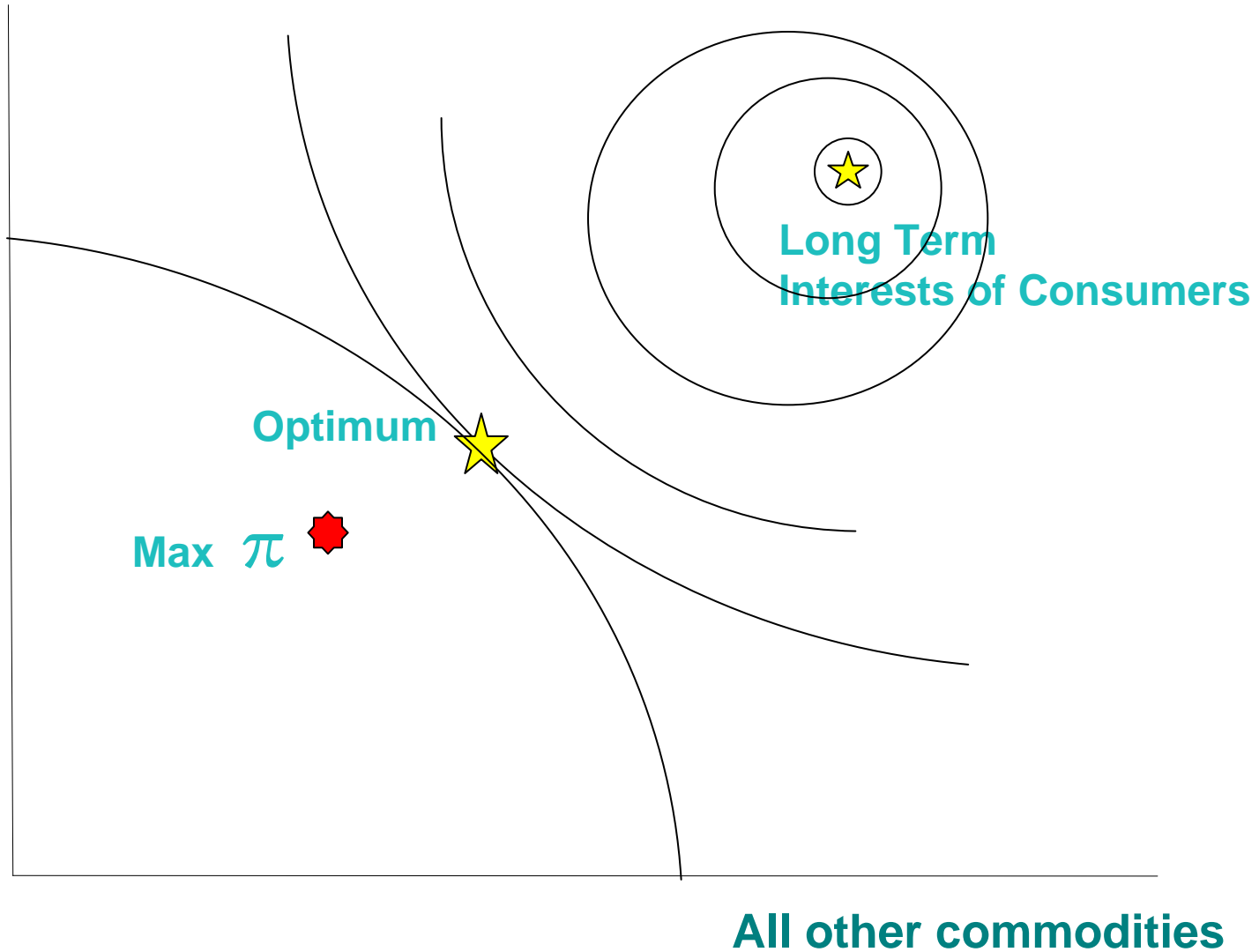
The objective of this Law is to promote efficient investment in, and efficient operation and use of, natural gas services for the **long term interests of consumers** of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.

## Part 3: Some Economics

### Economic Efficiency

- Productive efficiency
- Allocative efficiency
- Dynamic efficiency (long run)
  - Inefficient markets waste resources
  - Singularity
  - Does not address the distribution of income or wealth

# Electricity



# Objective Function

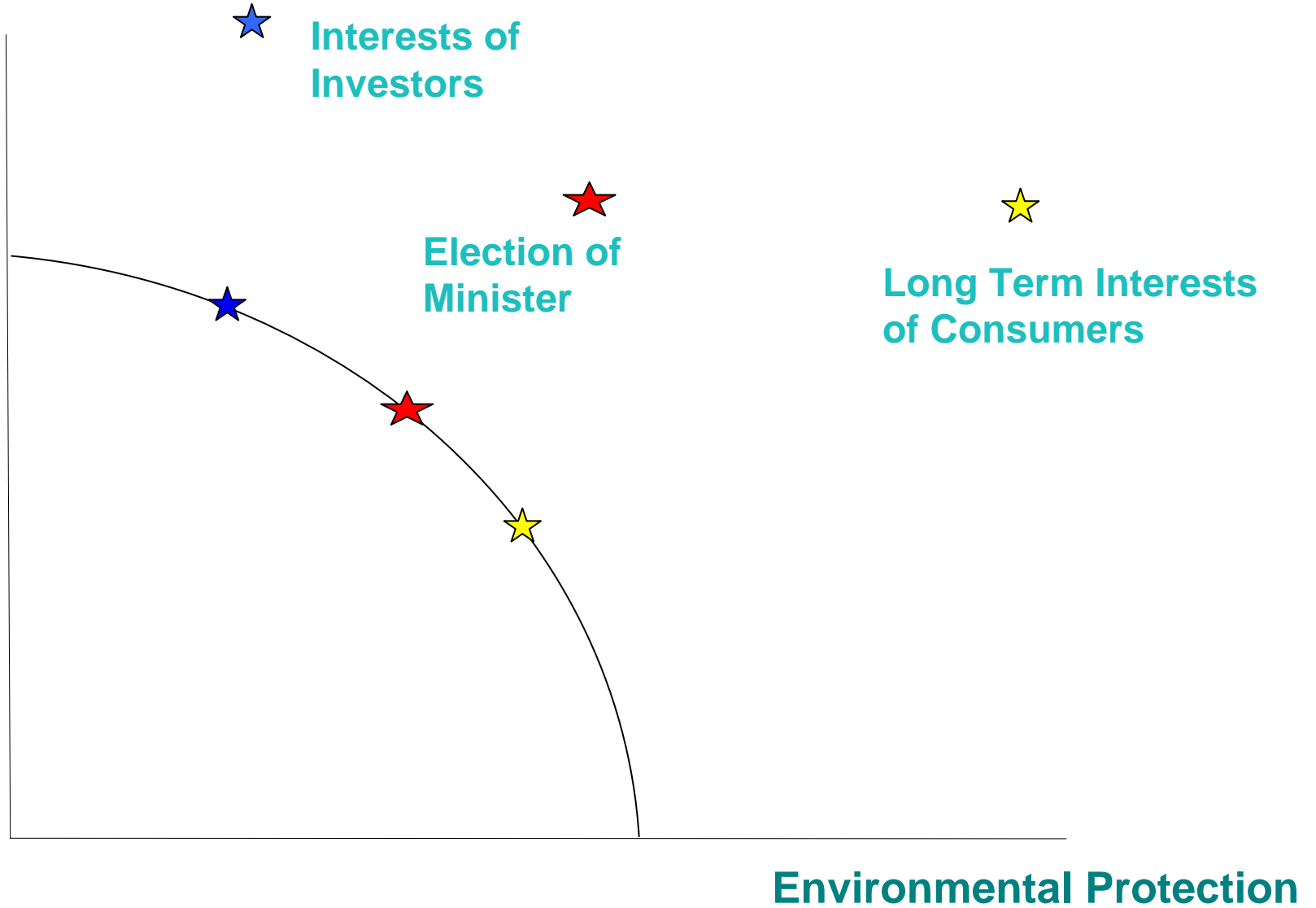
Maximise:

- Long term interests of consumers

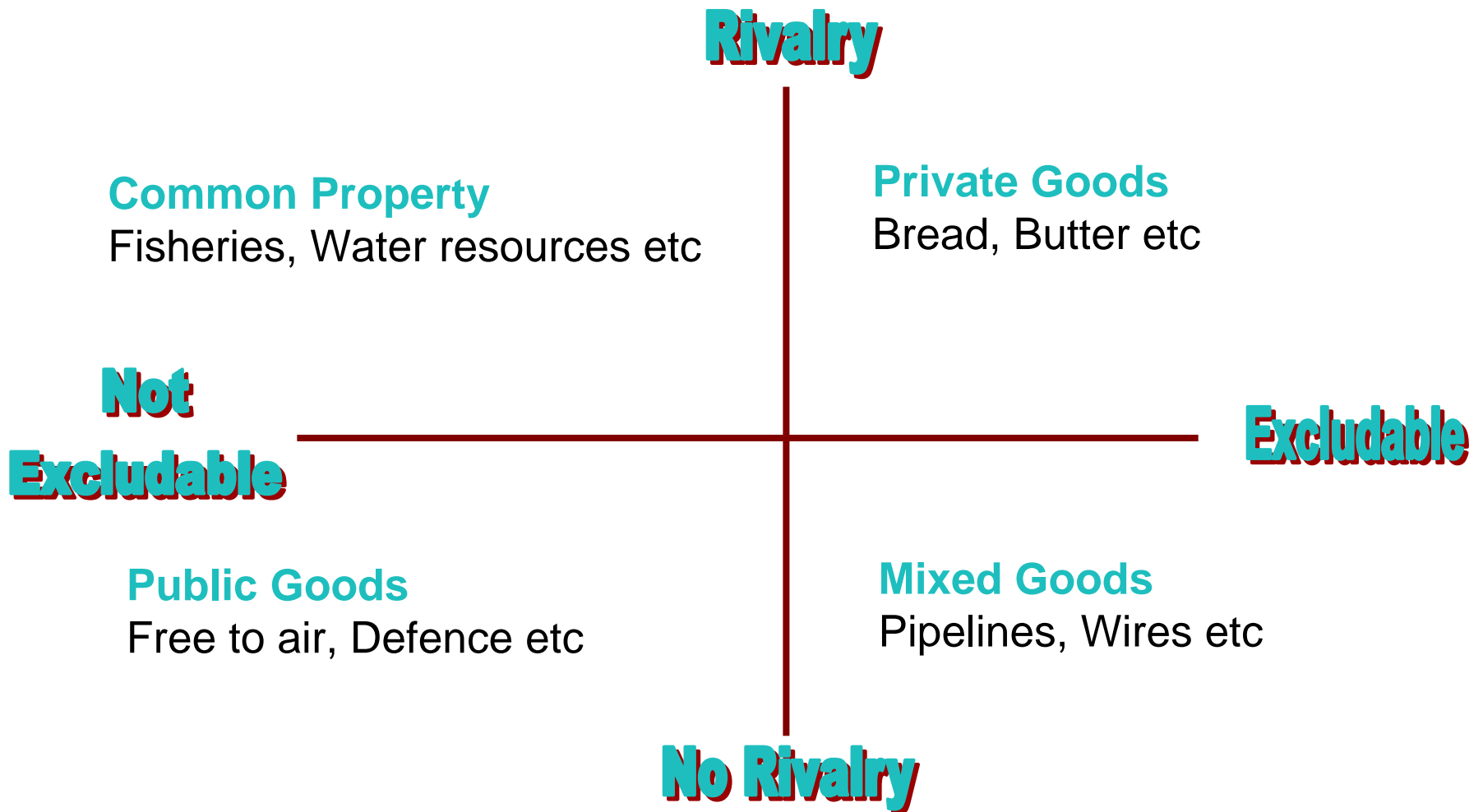
Subject to:

- Social advancement
- Environmental protection
- Economic prosperity
- Interests of investors & service providers
- Re-elect Minister

# Economic Prosperity



# Supply of Goods & Services





# Other Monopoly Factors

- Economies of scale
- Economies of scope
- Barriers to entry
  - infrastructure
  - legislative (legal)

# Externalities

- Environmental
- Technical
- Social

# Part 4: Private/Public Infrastructure

## Objectives of private sector participation:

- Economic efficiency
  - Continuous adjustment to changing circumstances
  - Decentralised decision making
  - Innovation
  - Low regulatory & administrative costs
  - Non pervasive regulatory frameworks
  - Minimisation of basis for dispute
- Equity
  - Fairness
  - Simple and easily understood rules

# Private Infrastructure

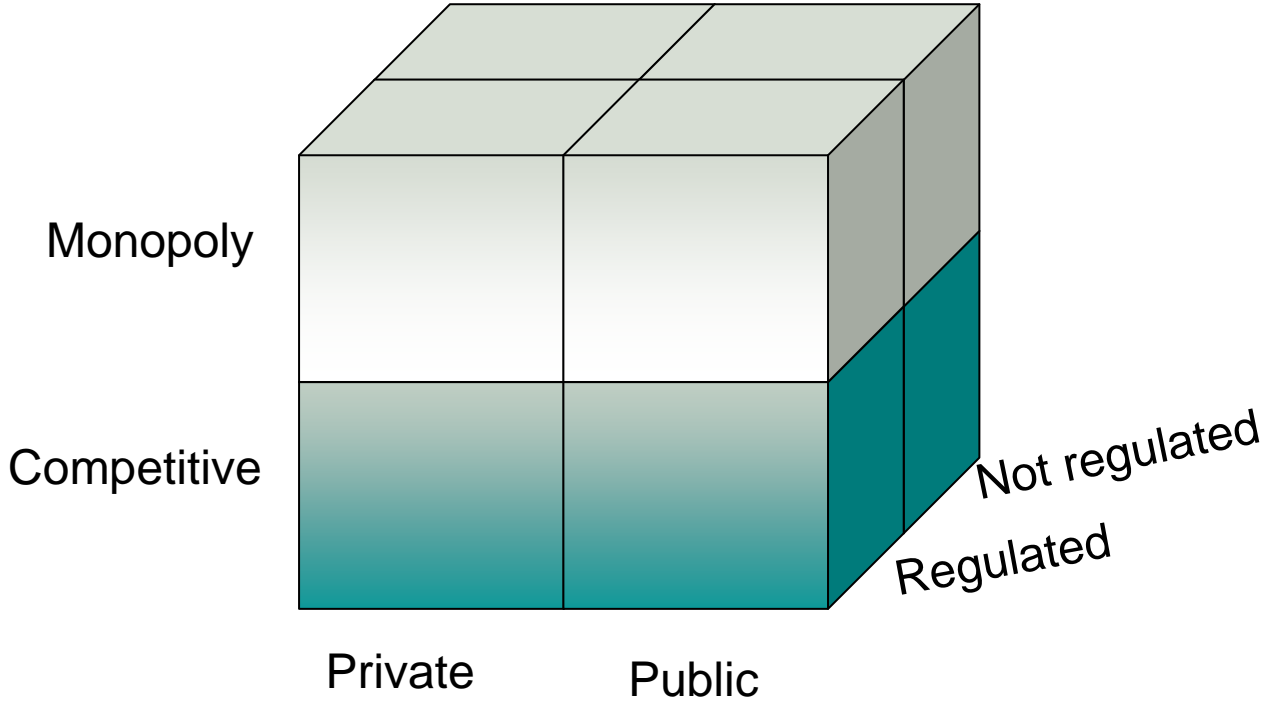
- Commercially driven
- Sees regulation as just another commercial burden
- More likely to test the regulatory envelope
- Has commercial incentive and legal obligations to behave as monopolist

Note: Edward Chamberlin: The Theory of Monopolistic Competition  
Harvard University Press 1965

# Public Infrastructure

- Is a form of regulation
- Executive government has direct influence
- Mix of commercial, social & political objectives
- Public corporations tend to be reasonably compliant
- Protective of monopoly rights

# Which works best?



# Monopoly the main problem

- A problem in either private or public sector
- Independent regulation of public sector may be more effective, but
- Social & political objectives of public sector inefficient
- The strong commercial focus of private sector may still provide better outcomes
- Regulation not always effective

# Bottleneck Infrastructure

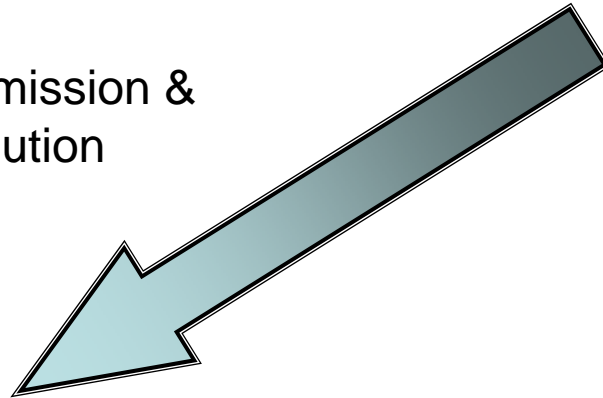
**Upstream**

Energy Resources,  
Water Sources,  
Electricity Generation

Transmission &  
Distribution

**Downstream**

Retail,  
Trading





# Isolate Monopoly Elements

## Market based regulation:

- Third party open access
- Structural separation
- Markets in contestable elements
- Artificial markets where possible
- Price or revenue cap if all else fails

# “What’s Yours is Mine”

## Open Access and the Rise of Infrastructure Socialism

Adam Thierer & Clyde Wayne Crews Jr.

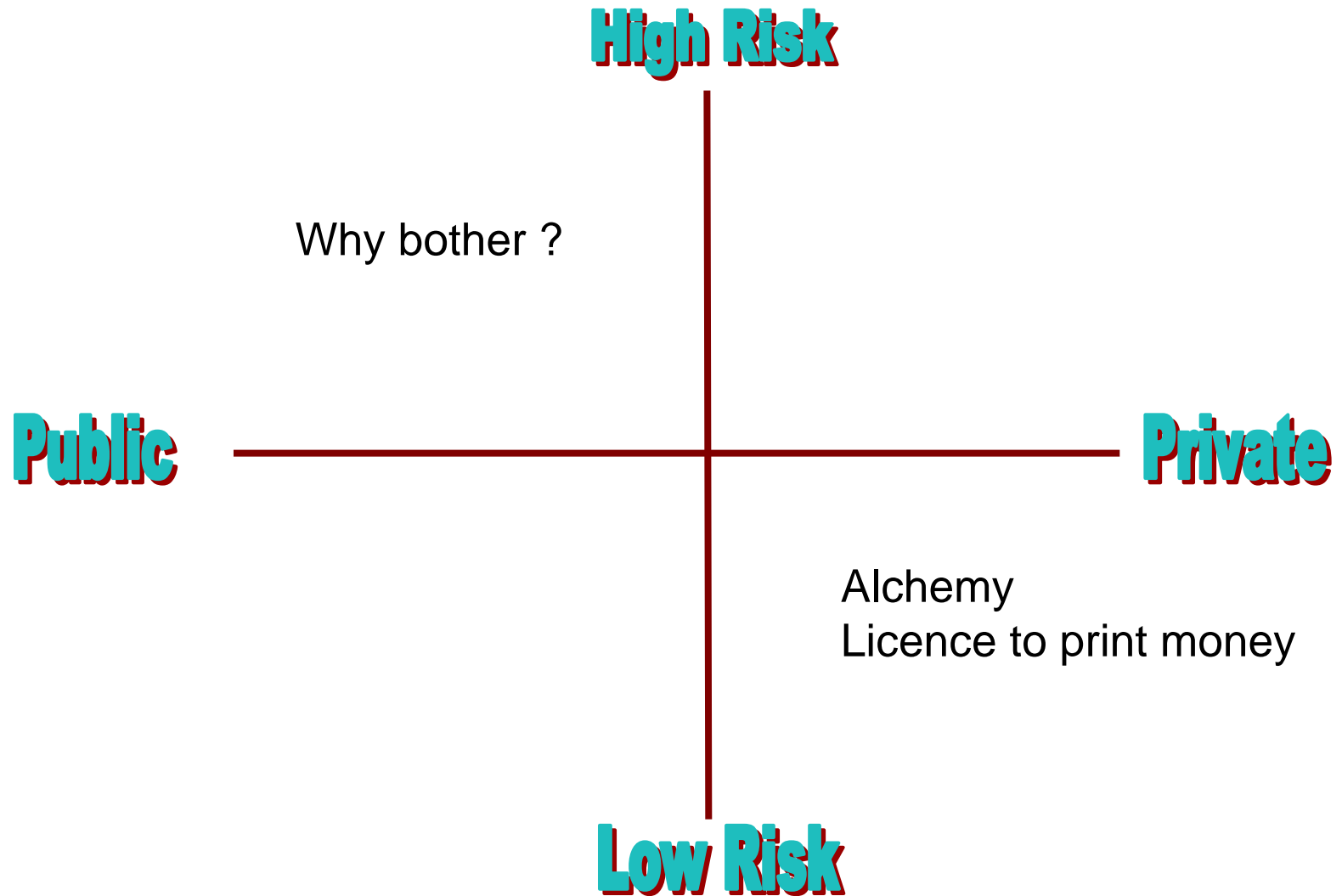
### Criticisms of Open Access:

- Ushers in bureaucratic processes that hinder competition
- Expands the role of government planning in markets
- Leads to litigation and high costs
- Discourages investment and innovation
- Turns networks into lazy public utility like vessels
- Creates mutant entities (ie artificial, that would not evolve naturally)
- **Regulation should not discourage network duplication**
- Regulation should not hinder bypass

# Competitive Tendering

- Privatisation
  - Government captures monopoly rents (tax)
- Competitive tendering of monopoly rights
  - Government captures monopoly rents (tax)
- Competitive tendering of works
  - Monopoly rents can be passed to consumers

# Allocation of Risk



# Performance of PPPs

Allen Consulting Group for Infrastructure Partnerships Australia 2007

- PPPs
  - Superior in both cost & time dimensions
  - Far more transparent than public projects
  - Performed better the bigger the project
- Australia likely to spend \$400 b next decade on infrastructure
- Significant benefits for all States to follow Victoria's, NSW's & Qld's lead in PPPs

# Challenge for the future

The challenge for the future is to increasingly identify and define boundaries within which individuals, companies and organisation operate pursuing their own objectives commercially without the need for detailed centralised systems of planning and control.

This has the potential to see a change in regulation from intrusive information intensive and administratively costly approaches to decentralised decision making through market based approaches.

ERA Annual Report 2006/07 p46

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**Independent Regulation and Advice**

[www.era.wa.gov.au](http://www.era.wa.gov.au)