

Asking The Law Question?

**Workshop on Network Issues
Distributed Generation
Australian CRC for Renewable Energy and the ESAA
UNSW – 27 May 2002**

Dr R.H.Stillman (UNSW)

1. Introduction

The aim of this discussion is to look at some of the common law principles inherent in the obligations owed by an electricity supplier to its customers in the market environment and the implications for embedded generation.

Basic to the issues raised is the following.

- (1) The case of *Electricity Supply Association of Australia v Australian Competition and Consumer Commission* [2001] FCA 1296B, in which an injunction was sought by ESAA to prevent the ACCC from publishing and disseminating its views on customer supply obligations.
- (2) The Trade Practices Act (1974) in respect of:
 - Section 4: definition of electricity as “goods”;
 - Section 52(1): in trade and commerce, conduct that is misleading, or deceptive, or is likely to mislead or deceive;
 - Section 71: implied undertakings as to quality or fitness – merchantable quality; and
 - Section 81: compensation for the recovery of loss or damage against any person involved in the contravention.

ESAA v ACCC was about statutory interpretation and the meaning of words. In effect it achieved nothing other than a disparity of opinions by eminent counsel. However, it does portend a future of operating in a less forgiving environment than the past, particularly as the immunities of the old franchised public utilities in policy and planning decisions no longer apply. Once embedded generation becomes part of the contractual chain it becomes subject to the same competing demands of cost, risk, service and liability as the privately owned or corporatised undertakings.

2. ESAA v ACCC

ESAA v ACCC involved a number of issues relating to the powers of the Commission in administrative law and the statutory obligations of TP Act (1974). Pertinent to the supply of electricity is the following.

1. ESAA had contented that the implied conditions do not apply to electricity supply contracts and even if they did they would not render a supplier liable for damage due to a power surges, brown outs or blackouts etc., so called “acts of god”, or the actions of third parties that are beyond the reasonable control of the supplier. The ESAA sought by way of declarations and injunctions to (1) prevent the ACCC from publicising and acting upon its view of s 71 and (2) vindicate the right of ESAA members to publish their own views of S 71.
2. The ACCC argued that s 71 – “quality and fitness” or “merchantable quality” was implied in conditions of electricity supply contracts. Hence, a breach of the

conditions placed on the electricity the supplier the onus of strict liability. As such the ACCC under its TPA defined charter was obliged to inform the public of the obligations the supplier owed to its customers.

3. The genesis of the ACCC view was in advice sought by the Electricity Industry Ombudsman, Victoria (EIOV). The response (October 1996) while guarded and qualified, indicated a concern with electricity companies misrepresenting, among other things, the effects of the implied conditions of 53(g) of the TP Act – “make a false or misleading representation concerning the existence, exclusion or effect of any condition, warranty, guarantee, right of remedy”. To quote:

“An action for damages..... does not appear to require the consumer to establish that the supplier was negligent in supplying or manufacturing the goods. Rather, the question is whether, at the time of supply, the goods were of merchantable quality and fit for the purpose. Apart from considering the question of “all other circumstances” in seeking to determine the merchantable quality of the electricity, the question whether the electricity was fit for the purpose appears to be a question of fact. The liability is not qualified as in the case of “merchantable quality”.

Therefore, I consider that it would be wrong to assert that the distribution companies are only liable for damage caused by power surges if the company itself is negligent. It rests on the distribution company to take precautions against uncontrollable events which may cause power surges, or perhaps insure against them. The distribution companies are contractually bound to supply electricity of merchantable quality and in a state which is fit for the purpose. How it does so is not the consumer’s concern”.

The ACCC view, strict liability, was accepted as the correct one to adopt for cases lodged with the regulator.

4. In an opinion given to the ACCC by Mr Archibald QC (February 1997) whether liability exists in cases in which power surges occur without fault on the part of distribution companies the following was stated.

“ It is preferable to approach the matter on this footing, rather than on the narrower footing of liability for surges caused by acts of God. Clearly..... power surges are often caused by events which although not acts of God, do not involve fault on the part of distributors” .

5. Given the definition in s 4 of the TP Act of “goods” and the character of the supplier-relationship for the delivery of electricity to customers must, it was said, be regarded as the supply of goods for the purposes of s 71 – “implied undertakings as to fitness of purpose”.

In relation to the requirement of merchantable quality the opinion went on to say:

“...that even the most diligent distributor is unable to ensure that at all times electricity will be supplied in a condition fit for the purpose for which it is required by the consumer does not, of itself, relieve the distributor of its contractual obligations to supply electricity of a quality which enable the electricity to be used for the purposes for which it is supplied (at least in circumstances in which exemption clauses are negated by operation of statutory provisions). While such circumstances may be “relevant” for the purposes of the definition in s 62 (2) of the TP Act (safety standards), I do not regard that factor as justifying the supply, with impunity, on some occasions of electricity in a form that is calculated (because of the surge) to cause harm to the customers property if not the customers person.”

Mr Archibald concluded:

“I therefore am of the opinion, on balance that electricity distribution companies which are subject to the operation of the TP Act are likely to be held for damage sustained by consumers in consequence of the power surges notwithstanding that the power surges are not referable to fault on the part of the distributors. Such consequence follows under s 71(1) because the excessive voltage associate with power surges renders that electricity not fit for the purpose for which such electricity is commonly acquired as it is reasonable to expect having regard to all the relevant circumstances.

It may also follow under s 71(2). Such a conclusion can, however, be no more than a view to the general result that may be expected to occur. The outcome in any particular instance in which a consumer suffers damage by reason of a power surge will, of course, depend upon the particular circumstances of the case."

Mr Archibald's opinion was circulated to regulatory bodies, supply companies, and ESAA.

6. In March 1997 United Energy Ltd provided the ACCC with the advice of Alex Chernov QC and James Peters. This advice assumed that s 71 (1) and (2) applied to electricity supply contracts but disagreed with the Archibald opinion as to whether a supplier would be liable for a breach of either the implied condition when a power surge caused damage. It did accept that a supplier could be held liable where its own negligence caused the surge.

7. In April 1997 Eastern Energy Ltd was provided with advice by J D. Heydon QC subsequently given to the ACCC. That advice was that:

- (i) the intention to be inferred from ss 68 – 73B of the TP Act (Contracts) was that the s 4 definition of "goods" so as to include electricity did not apply;
- (ii) if s 71(1) did apply to electricity then having regard to the relevant circumstances there was a reasonable prospect of persuading a court that electricity was of merchantable quality despite the occurrence of power surge.
- (iii) in relation to s 71(2), electricity that is subject only to surges that conform to what is to be expected from an overhead supply may well be held to be "reasonably fit" – not absolutely fit but meeting a standard of fitness that is reasonable in the circumstances.

This advice acknowledged that, while a supplier would probably not be in breach of s 71 because of a surge, it would depend on the circumstances.

8. Also in April 1997 Dennis Rose QC and John Emmerig advised ESAA that :

- (i) for the reasons given by Mr Heydon "electricity" was not "goods" for the purpose of s 71; but
- (ii) that, if it was, the implied conditions would not be breached if there were surges in supply due to causes other than a fault by the distributor.

9. In April 1997, the ACCC obtained further advice from Mr Archibald QC and Mr Scerri QC. That advice acknowledged the weight of the contrary opinions, but nonetheless confirmed the earlier Mr Archibald's earlier advice.

3. Duty of Care in Contract and Tort

Contract is private law-making by individuals involving economic exchange in a market environment in which the obligations owed by the parties are by mutual consent legally binding. In redressing a breach of contract, the law is concerned with the future outcome as if the contract had been performed whatever its economic consequences. That a contract deals with some future probability, whether it be an expectation of a profit¹, the recovery of an expense, or some reliance on an opportunity lost², the question in remedial law is – "has the plaintiff been wronged and if so what has been actually lost?"³

In contrast, tort law is community based law concerned with a breach of the duty of care which people within society owe to each other. Tort and criminal law have a common inheritance in revenge and deterrence. But, whereas a crime is an offense against the State, liability in tort is a civil matter which exists primarily to compensate the victim of the wrong by compelling the wrongdoer to pay damages for the harm done. To this extent remedial action in tort law seeks to restore the plaintiff to a past or “bad as old” state.

The question as to whether a negligent breach of a strict contractual duty is also actionable in the tort of negligence was answered in *Donoghue v Stevenson*⁴ (Figure 1) where the manufacturer breached his duty of care in respect of the quality of the ginger beer sold to the first buyer, a 3rd party. *Donoghue* had nothing to say where harm was purely economic. This was dispelled by the decision in *Hedley Byrne*⁵ where misleading information resulted in pure economic loss.

In *Bryan v Maloney*⁶ the High Court had to decide whether builders owe a duty of care in tort towards subsequent owners for the diminution in value of the property which occurs when a latent and previously unknown fault in a structure becomes evident? To determine this question it was necessary to decide whether builders owed a duty of care in tort in respect of such a loss to the clients with whom they are in contractual relations. The case suggested that in Australian law there was little or no concern if there was no rigid demarcation between tort and contract, and that the law of negligence encroached on the domain of contract. *Bryan* seems to support the view that if the ingredients which have in previous cases been considered to give rise to a duty of care in tort to avoid economic loss are present, such a duty should be recognised, irrespective of whether the plaintiff might already be adequately protected by possession of a contractual claim.

In summary.

1. Where negligent representation inducing an entry into a contract is actionable both in negligence and contract breach involving due care, damages are measured according to what the plaintiff's position would have been had there been no negligence.
2. When it comes to tortious conduct in the course of performance rather than tortious conduct inducing entry into the contract, and where both involve duties of care, then the wrong is the same and the plaintiff will be put in the same position as if there had been no negligence.
3. Where there is pure economic loss involving a contractual relationship the concept of a mutual assent to a legal relationship is subsumed into the assumption in tort that all persons are neighbours and are owed a duty of care.

4. Application

Three models can be used to represent the supply network. The term “quality of supply” is meant to mean any consistent failure of supply which detracts from some reasonably expected or regulatory reliability level.

- (1) The commercial market model is that relating the generator to the final consumer through the wholesale and retail markets – Figure 2A.
- (2) The system model shows the physical arrangement in which embedded generation feeds direct into the distribution network – Figure 2B
- (3) The legal model illustrates the contractual relationship between the various parties and the consumer. In the context of “quality of supply” the direct contractual relationship is between the network service provider and consumer – Figure 3.

1. The “retailer” is a broker of electricity and in essence can be treated as an agency selling a product which has been produced by another party. The analogy is that of an agent who sells on behalf of an insurance company⁷. The presumption is that as an independent entity, the retailer would have no knowledge as to how or in what state the electricity is delivered.

2. Although the embedded generator feeds directly into the distribution network and not the transmission system there is no means of differentiating between the quality of the electricity supplied by the embedded generator and that emanating from an indeterminate number of large generators. In law the embedded generator is too remote. Consequently, the responsibility for the quality of electricity supply remains with the network service provider.

The doctrine enunciated by the High Court in ***General Foods v Burnie Port Authority (1994)*** was that:

- where an occupier of land performs a dangerous activity, or allows someone else to do so, they owe a non delegatable duty of care to avoid a reasonable foreseeable risk of damage to the property or persons;
- they also stressed -
- that where the substance and activity posed a very high risk if it escaped the standard of care required amounts practically to a guarantee of safety.

3. Should the quality of supply deteriorate then in effect there is a breach of the conditions of the supply contract, implied or expressed. However, for a customer to succeed in an action for compensation for damage he or she would have to show :

- (i) what was within reasonable contemplation of the parties as to the implied or express terms of the supply contract as to the quality of supply; and
- (ii) what actual loss was suffered.

4. In contract law the breach is a reliance or expectation loss. The term expectation loss does not indicate that damages are payable simply for thwarted expectations, but rather for loss for non-performance of the contract. Even if the contract is not susceptible of specific performance, the customer is legally entitled to expect its performance.

5. Where damage to property arises from the breach, eg the diminution in some form of the quality of supply, this non-performance, is in effect, the loss of a contractual promise which in itself is a valuable right. That loss is compensated by an award of damages in money terms that represents the value of that right. Tort confers no right over and above the right to recover damages for loss sustained in consequence of the wrongful act involved⁸.

5. References

¹ *McRae v Commonwealth Disposals Commission* [1951] 84 CLR 377.

² *Commonwealth v Amman Aviation Pty Ltd*, [1991] 174 CLR 64

³ McHugh, Hayne and Callinan JJ: *Marks v GIO Holdings Limited*, [1998] HCA 699

⁴ (1932) AC.

⁵ *Hedley Byrne & Co Ltd v Heller and Partners Ltd* [1964] AC 562.

⁶ [1995] 69 ALJR 375

⁷ *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1.

⁸ Guadron J, *Marks v GIO Holdings Ltd* (1998) HCA 699.