B7 Electricity

B7.1 NCP commitments

State and Territory governments' electricity NCP commitments arise from the *Agreement to Implement the National Competition Policy and Related Reforms*, the *Competition Principles Agreement* (CPA) and other Agreements on Related Reforms for the Electricity Sector (Electricity Agreements).[1]

First, clause 4 of the CPA provides that, before introducing competition into a market traditionally supplied by a public monopoly and before privatising a public monopoly, governments will:

- remove from the public monopoly any responsibilities for industry regulation; and
- conduct a review of structural and competitive arrangements in the industry.

Second, the *Agreement to Implement the National Competition Policy and Related Reforms* requires that each participating State and Territory implement electricity reforms specified in the relevant Council of Australian Governments (COAG) agreements with the aim of establishing a competitive National Electricity Market (NEM) by 1 July 1999.

Third, the Electricity Agreements on the structure of the electricity industry commit jurisdictions, prior to their participation in the NEM, to have:

- structurally separated generation from transmission; and
- ring-fenced the retail and distribution businesses.

As early as 1994, COAG identified the main objectives for a fully competitive NEM to operate from 1 July 1999 as follows:

- the ability for customers to choose the supplier, including generators, retailers and traders, with which they will trade;
- non-discriminatory access to the interconnected transmission and distribution network;
- no discriminatory legislative or regulatory barriers to entry for new participants in generation or retail supply; and
- no discriminatory legislative or regulatory barriers to interstate and/or intrastate trade.

COAG supported these broad objectives in the April 1995 inter-governmental agreements that link NCP payments to the implementation of specified electricity

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39 NCP agreements on electricity are reproduced in the Council's *Compendium of National Competition Policy Agreements (June 1998).*

reforms. Subsequently, on 10 December 1996, the Prime Minister wrote to all Heads of Government seeking endorsement of a revised implementation timetable for national electricity reform. Under the 10 December 1996 timetable, participating jurisdictions agreed to:

- have the *National Electricity Code* (NEC) authorised by the Australian Competition and Consumer Commission (ACCC) (for the purposes of Part VII of the *Trade Practices Act 1974*[2]) and accepted as an industry access code by the ACCC (for the purposes of the undertaking provisions of Part IIIA of the *Trade Practices Act 1974)* by April/May 1997; and

- fully implement the market arrangements specified in the NEC by early 1998 requiring:

  - the National Electricity Market Management Company (NEMMCO) to have successfully installed and tested the information technology systems;

  - each jurisdiction to have promulgated and applied the National Electricity Law; and

  - NEMMCO and the National Electricity Code Administrator (NECA) to have assumed full operational responsibilities for the national market.

Achievement of the COAG objectives therefore requires the formal commencement of the NEM and participating jurisdictions (New South Wales, Victoria, South Australia and the ACT) to complete the transition to a fully competitive NEM, by 1 July 1999, to fulfil the second tranche NCP commitments.

The NEC also includes derogations where each participating jurisdiction has specified transitional provisions that will operate to ensure a smooth transition from the existing electricity industry regulatory arrangements to the NEM. Derogations from the NEC include technical requirements, contestability timetable,[3] transmission and distribution network connections and transmission losses. The derogations also enable jurisdictions to honour existing contracts which do not conform to the NEC.

Most of the derogations are scheduled to terminate on or before 31 December 2002, which means that they are largely a third tranche issue. However, for the second tranche assessment, NCP commitments require jurisdictions to have made sufficient progress to enable the year 2002 timetable to be met.

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40 Authorisation under Part VII of the TPA provides immunity from court action for certain types of arrangements or conduct that would otherwise be in breach of Part IV of the TPA.

41 Contestable customers in the retail market are those customers who can choose their supplier from the various licensed retailers operating in the market. The NEC requires each jurisdiction to nominate the persons that may register as a contestable customer under the NEC.

The National Electricity Market

The NEM is a wholesale market for the supply and purchase of electricity combined with an access regime for use of the transmission and distribution networks in New South Wales, Victoria, South Australia and the ACT. Queensland and Tasmania are expected to participate in the NEM upon interconnection with New South Wales and Victoria, respectively.

The NEM commenced on 13 December 1998 and is expected to increase efficiency in the electricity supply industry by introducing competition directly into the generation and retail sectors.

The principles of the NEM are set out in the NEC that consolidates new and existing interstate trading arrangements such as the wholesale market pool, technical standards and access to the network. Two new organisations, NECA and NEMMCO have been established to regulate and manage the NEM.

Market behaviour is regulated in a light-handed manner with market conduct and pricing oversight subject to national competition law administered by the ACCC. State and Territory regulators are responsible for the economic regulation of distribution services, contestability timetable, environmental standards, distribution and retail licence conditions, and health and safety. State and Territory regulators are currently responsible for the regulation of transmission services, however, the NEM arrangements provide for the ACCC to assume, on a progressive basis from 1 July 1999, the regulation of transmission services.

Conduct Code Agreement: reporting obligations

The *Conduct Code Agreement* requires that jurisdictions notify the ACCC of legislation that is reliant on section 51(1) of the TPA. Legislation reliant on this section is anti-competitive and this places an obligation on jurisdictions to demonstrate that such legislation satisfies clause 5 of the CPA. The Council is aware of two jurisdictions that have electricity industry related legislation reliant on section 51(1) of the TPA: Victoria and Tasmania.

B7.2 Progress against NCP commitments

Introduction

The NEM commenced on 13 December 1998 resulting in a competitive market for the supply and purchase of electricity in the participating jurisdictions, namely, New South Wales, Victoria, South Australia and the ACT. This satisfies the *Agreement to Implement the National Competition Policy and Related Reforms* requirement that each participating State and Territory must implement the required reforms to enable the establishment of a competitive NEM by 1 July 1999.

The ACCC received applications from:

- NECA and NEMMCO to authorise, under Part VII of the TPA, the proposed electricity wholesale market arrangements within the NEC; and

- NECA to accept, under Part IIIA of the TPA, an access code for the electricity transmission and distribution networks.

On 10 December 1997, the ACCC authorised the NEC. The ACCC accepted the NEC as an access code under the TPA on 16 September 1998. In making its authorisation and access decisions, the ACCC recognised that the current arrangements are an appropriate starting point but that significant deficiencies remain. When authorising the NEC, the ACCC imposed a number of conditions highlighting these deficiencies in the design of the NEM. These deficiencies include:

- market distortions due to price caps and floors;

- the potential for more commercially orientated solutions in areas such as reserve trader and ancillary services provision; and

- competition implications of various jurisdictional derogations such as generator technical standards.

The Council considers that the ACCC's authorisation and acceptance of the NEC signifies that the market arrangements specified in the NEC are an appropriate start to the NEM. But the Council also acknowledges that the ACCC's decisions were highly qualified, and improvements to the current arrangements are an ongoing requirement to facilitate the establishment of a satisfactory set of arrangements.

The Council notes that, in accordance with the Prime Minister's letter of 10 December 1996, NEMMCO and NECA have assumed full operational responsibilities for the national market.

Issues common to jurisdictions

Generally, the NEM is achieving its objectives. However, the Council accepts that implementation problems have had an impact on realising the full benefits of electricity reforms. To varying degrees, jurisdictions have encountered the following problems:

- timetable slippage in derogations (such as retail contestability) as a result of the delayed NEM start;

- implementing metering arrangements in relation to the introduction of retail contestability;

- inability to pass desired legislation; and

- understanding the operational responsibilities of NEMMCO and NECA.

Emerging NEM issues

Now that the NEM is operational, and competition in contestable services well established, some important issues are emerging which may require a reconsideration of reform policy, or raise questions about future compliance with NCP agreements. The Council will retain an ongoing interest in these issues – and anticipates that electricity reform will be a major focus of the third tranche assessment.

First, questions are being raised about the efficacy of NEC rules on the approval of regulated versus unregulated transmission interconnectors. This is a difficult issue. On the one hand, there appears to be growing interest in the construction of strategic unregulated interconnects (for example, the proposed unregulated connection between New South Wales and Queensland). On the other hand, many argue that the current rules for approving regulated interconnects are unworkable, citing experience with the proposed SANI regulated inter–connect between New South Wales and South Australia as an example. As a result, it is argued, regulated interconnects which are demonstrably in the public interest won't be constructed. The National Electricity Code Authority (NECA) pricing review is examining this issue. The Council would be concerned by any Government actions – outside the formal NEM processes – to impede construction of interconnectors.

Second, there are suggestions that publicly owned electricity generators have been competing on unfair terms with private generators. It is suggested that the publicly owned generators are not required to earn a commercial return on their assets and/or are subsidised in some way by their owner governments and, as a consequence, are gaining a greater share of the NEM market than they otherwise would. This is a competitive neutrality issue, since the claim is that businesses are attaining a market advantage derived solely from public ownership. However, no complaint has been lodged with the appropriate competitive neutrality complaints authority, and so the suggestions have not been tested.

Third, there have also been suggestions that States should revert to state–based markets and interstate trade in electricity should be abandoned. The Council would have serious concerns over any moves to restrict the operation of the NEM. The development of national markets in electricity services, and other utility services such as gas, is a cornerstone of NCP. NCP includes a mechanism to deal with any competitive neutrality problem, to the extent that it exists, and any inadequacies in this mechanism should be addressed directly.

Jurisdictions' ongoing commitments

Jurisdictions are at various stages with their electricity reform program. The Council considers that realistic and therefore achievable timetables are necessary to ensure effective and efficient implementation of NCP commitments. The electricity reforms adopted to date are a starting point against which the future electricity reforms will be measured.

The Council intends to closely monitor jurisdictions' ongoing progress against electricity reform commitments to ensure that an environment conducive to the introduction of competition is fostered. The Council's third tranche assessment will focus on the progress jurisdictions have made in achieving a fully competitive electricity market. The Council will focus on whether jurisdictions have achieved, or have an appropriate timetable to achieve, full retail competition. This will include contestability timetables, mechanisms to deal with issues such as metering and the ongoing effect of vesting contracts. The Council will also examine the continued appropriateness of any remaining derogations, recognising that while jurisdictions need mechanisms to allow for a smooth transition to a fully competitive market, derogations should only be in place for the minimum time possible to achieve a smooth transition.

The Council recognises that the establishment of the NEM and the structural reforms made by each jurisdiction are an important start to the creation of a fully competitive electricity market. However, considerable work remains to be done to see the full benefit of the reforms flow through to users and the Council will be considering, in its third tranche assessment, how well this has been achieved.

B7.2.1 NEM participating jurisdictions

New South Wales

Structural reform

In February 1995, the transmission activities of the government-owned vertically integrated electricity utility, Pacific Power, were separated to become the Electricity Transmission Authority (trading as TransGrid), with Pacific Power's activities confined to generation.

In early 1996, Pacific Power was separated into three independent, government-owned generation businesses known as Pacific Power, Delta Electricity and Macquarie Generation. Pacific Power is responsible for the State's entitlement of 58 per cent of the Snowy Mountains Hydro Electric Authority.

Twenty five distributors were amalgamated to form six State-owned corporations with the monopoly network functions being ring-fenced from retail services.

Regulatory reform

The Independent Pricing and Regulatory Tribunal (IPART) will regulate transmission pricing until 30 June 1999, when it will be regulated by the ACCC. IPART will continue to regulate distribution pricing and electricity tariffs for franchise customers until the retail market is fully contestable.

Interconnection with Queensland

A New South Wales Government-owned distributor and retailer, NorthPower, has commenced development of DirectLink, which is an interconnection to link the Tweed Valley to the New South Wales electricity grid. The project is scheduled for completion by January 2000.

TransGrid and Powerlink Queensland intend to build an interconnector between New South Wales and Queensland. This is due for completion in the year 2001.

National Electricity Law

Through the *Electricity Supply (NSW) Act 1995*, New South Wales has adopted the National Electricity Law.

Retail competition in electricity supply

From October 1996, customers who use in excess of 40GWh per year have been able to choose suppliers. As of 1 July 1998, customers in the range of 160MWh to 750 MWh per annum have been contestable. By 1 July 1999 businesses with many

small sites of 100MWh per annum and greater, will be able to aggregate their consumption to become contestable. Small customers who consume less than 160 MWh per annum will become contestable over a period commencing from 1 January 2001.

Assessment

The Council is satisfied that New South Wales has met its second tranche electricity reform commitments for the following reasons:

- New South Wales has met its structural commitments by restructuring the regulatory and operating sectors of the electricity sector;
- the separation of the natural monopoly (transmission and distribution) and competitive components (generation and retail) is consistent with the Electricity Agreements;
- New South Wales is continuing to pursue NorthPower's DirectLink interconnection and TransGrid/Powerlink's Queensland interconnector;
- New South Wales has promulgated and applied the National Electricity Law; and
- consistent with a competitive NEM, New South Wales is progressively allowing customers to choose their electricity supplier.

As part of the third tranche assessment, the Council intends to consider New South Wales' progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

Victoria

Structural reform

In October 1993, the Victorian Government reformed the State Electricity Commission of Victoria (SECV) into three separate businesses: Generation Victoria (generation); National Electricity (transmission); and Electricity Services Victoria (distribution).

National Electricity was separated into two businesses: the Victorian Power Exchange (administers the market and oversees the system control); and PowerNet Victoria (owns and maintains the transmission assets that form the physical network). Electricity Services Victoria was separated into five distribution businesses, each comprising an energy retailing arm and a regulated, local, geographic wires monopoly. Generation Victoria operated as an interim structure comprising five groups of power stations trading as independent, competing generators.

During the second half of 1995, all five distribution businesses were sold to the private sector. Subsequently, Victoria has privatised all wholly-owned generation businesses, its share of the Loy Yang B generator and its transmission utilities.

Regulatory reform

Victoria has established an independent economic regulator, the Office of Regulator General, who monitors price and service levels. The Office of Chief Electrical Inspector has been created to ensure industry compliance with set regulations, and auditing and monitoring of industry behaviour against statutory safety outcomes. An Energy Ombudsman has also been established to protect consumer interests and to resolve disputes between customers and energy businesses in the gas and electricity industries.

Conduct Code Agreement: reporting obligations

In accordance with clause 2(1) of the CCA, the Victorian Government has notified the ACCC of section 91AA of the *Electricity Industry Act 1993* which is new legislation that relies on section 51(1) of the TPA. Section 91AA of the *Electricity Industry Act 1993* will be repealed from 1 January 2001.

In accordance with clause 5 of the CPA, Victoria has reviewed the *Electricity Industry Act 1993*. This review was completed in January 1998. It is yet to be released as the Government is considering the recommendations.

National Electricity Law

The *Electricity Industry Act 1993* enables Victoria to apply the National Electricity Law to Victoria.

Retail competition in electricity supply

Customer thresholds for participation in the wholesale market have been, and will continue to be, progressively reduced. On 1 July 1996, approximately 2000 customers with annual consumption of at least 750 MWh became contestable. From 1 July 1998, customers with an annual consumption of at least 160 MWh became contestable. The final phase is scheduled for 1 January 2001, when all sites, including households, will be contestable.

Assessment

The Council is satisfied that Victoria has met its second tranche electricity reform commitments for the following reasons:

- Victoria has completed all its structural reform commitments through the structural separation of generation and transmission, and ring-fencing of retail and distribution businesses;

- Victoria has separated the regulatory role from the commercial aspects of the industry through the establishment of the Office of Regulator General;

- Victoria has promulgated and applied the National Electricity Law; and

- sufficient progress has been made with the contestability timetable such that all customers will become contestable on 1 January 2001.

As part of the third tranche assessment, the Council intends to consider Victoria's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

South Australia

Structural reform

On 1 January 1997, Optima (South Australian Generation Company) was separated from the Electricity Transmission South Australia (ETSA) Corporation.

During June 1998, the South Australian Government undertook a review of the restructuring of the South Australian electricity supply industry pursuant to clause 4 of the CPA. This review recommended that South Australian electricity sector be restructured into three separate generation companies: a transmission company; a single stapled ring-fenced distribution/retail company (with distribution and retail assets held in separate subsidiaries under a common holding company); and a separate gas trader.

On 12 October 1998, in accordance with the review recommendations, Optima was restructured into three new generation companies, namely, Optima Energy, Flinders Power and Synergen and a separate gas trader company was formed. The charters of the three government-owned generation companies contain provisions requiring them to operate on a competitive basis.

The remainder of the ETSA Corporation was disaggregated to form ElectraNet SA (transmission entity with ring-fenced system control), with the distribution and retail businesses maintained under a common holding company as stapled ring-fenced subsidiaries called ETSA Utilities Pty Ltd and ETSA Power Pty Ltd respectively.

Each of the businesses (with the exception of ElectraNet SA) were transferred to new Corporations Law companies.

The *Electricity Corporations (Restructuring and Disposal) Act* permits the long term lease of electricity generation, transmission and distribution assets, and the sale of associated assets.

Regulatory reform

South Australia proposed a range of new regulatory arrangements in conjunction with the structural reforms. These arrangements cover the following:

- an Electricity Ombudsman to deal with customer complaints;
- an Independent Industry Regulator, responsible for pricing, licensing and network access;
- an Electricity Supply Industry Planning Council;
- a Sustainable Energy Authority; and

· a Technical Regulator, responsible for safety and technical service requirements.

The legislative package to give effect these arrangements will be introduced into Parliament in June 1999. It is expected that the legislation will be passed in August 1999.

National Electricity Law

As lead legislator for the NEM, South Australia passed the *National Electricity (South Australia) Act 1996* in June 1996 and proclaimed the Act on 8 December 1998, providing for South Australia's entry into the NEM on 13 December 1998.

Retail competition in electricity supply

Since 20 December 1998, customers with an annual single site average load of at least 4GWh have been able to choose their own supplier. Customers with an annual usage of at least 750MWh and 160MWh will become contestable from 1 July 1999 and 1 January 2000 respectively. The remaining customers will become contestable on 1 January 2003.

Derogations

The South Australian government has lodged an authorisation application with the ACCC for the South Australian vesting contracts.

Assessment

The Council is satisfied that South Australia has met its second tranche electricity reform commitments for the following reasons:

· South Australia has separated the natural monopoly (transmission and distribution) and competitive components (generation and retail);

· South Australia's clause 4 review was rigorous and independent;

· the South Australian Government's announced intention to adopt the review recommendations ensures compliance with the Electricity Agreements and CPA obligations;

· South Australia has promulgated and applied the National Electricity Law; and

· the staged implementation of retail competition is in progress.

South Australia proposes to establish the regulatory bodies recommended in the clause 4 review by August 1999. The Council will undertake an interim assessment of South Australia's progress before 31 December 1999.

As part of the third tranche assessment, the Council intends to consider South Australia's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

Australian Capital Territory

Structural reform

ACTEW was corporatised on 1 July 1995. Progressively since 1995, the ACT government has implemented structural reforms consistent with those required by clause 4.

In preparation for the proposed sale of ACTEW, the ACT Government commissioned two reviews to determine the most appropriate structure and public benefit issues that would arise from privatisation. The Fay Richwhite Review (1998) examined risks and strategic issues in a changing business environment. The ABN AMRO/DGJ Projects Scoping Study of ACTEW (1998), considered structure and ownership options.

ABN AMRO/DGJ Projects recommended that the preferred course of action is to sell ACTEW as a multi-utility, however, if a sale does not proceed, the Government should continue to operate ACTEW as a multi-utility. A key issue raised in the scoping study is that under either public or private ownership, the Government should implement a full regulatory framework for electricity, water and sewerage. This could be achieved by broadening the regulatory powers of the independent pricing and access regulator, the Independent Pricing and Regulatory Commission (IPARC).

Regulatory reform

In 1995 when ACTEW was corporatised, the regulatory functions that were traditionally undertaken by the Electricians' Licensing Board (a public monopoly), were transferred to the Department of Urban Services.

Under the *Electricity Supply Act 1997*, the ring-fencing of electricity retail and distribution businesses is a licensing requirement (there are separate requirements for distribution and retailing). IPARC, the economic regulator, examines and tests the adequacy of ring-fencing in the context of its pricing references.

National Electricity Law

The relevant ACT legislation that gives effect to the National Electricity Law, the *Electricity (National Scheme) Act 1997*, was passed prior to the commencement of the NEM.

Retail competition in electricity supply

Since 28 June 1998, customers with an annual usage of more than 160 MWh at a single site are able to choose their retailer. A process, whereby all customers will be contestable, is scheduled for 1 January 2001.

Assessment

The Council is satisfied that the ACT has met its second tranche electricity reform commitments for the following reasons:

- since corporatisation of ACTEW in 1995, the ACT has implemented a number of structural reforms. These reforms include the separation of the regulatory and commercial functions of ACTEW, consideration of the appropriate commercial objectives of ACTEW and analysis of the merits of separating the potentially competitive elements of ACTEW;

- the ACT has promulgated and applied the National Electricity Law; and

- the ACT has made sufficient progress towards full customer contestability by 1 January 2001.

As part of the third tranche assessment, the Council intends to consider the ACT's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

B7.2.2 Proposed NEM participating jurisdictions

Queensland

Structural reform

In January 1995, the Queensland Government divided the Queensland Electricity Commission (QEC) into AUSTA Electric (generation) and the Queensland Transmission and Supply Corporation (QTSC). QTSC operated as a holding company for eight subsidiaries, comprising seven regionally-based electricity boards and the Queensland Electricity Transmission Corporation (trading as Powerlink Queensland).

On 1 July 1997, AUSTA Electric was separated into three independent and competing generation corporations:

- Stanwell Corporation;

- Tarong Energy Corporation; and

- CS Energy.

An engineering corporation, AUSTA Energy, was also established.

QTSC's subsidiaries were established as independent government-owned corporations. However, the retailing functions were removed from the distributors and three retail corporations were established.

In February 1999, the Queensland Government announced the following reforms to the electricity industry:

- the engineering corporation, AUSTA Energy is to be wound up;

- the establishment of an Electricity Monitoring Unit to address concerns about maintenance practices within the industry;

- the six separate regional distributors, which currently own Ergon Energy, will be amalgamated into a single corporation known as Ergon, with Ergon Retail operating as a subsidiary; and

- regional electricity councils are to be created across the State to provide direct community input to distribution corporations.

The restructure of the distribution corporations aims to reduce the number of reporting lines to shareholding Ministers, facilitate a more co-ordinated approach to regional development of the distribution sector, and provide a more workable arrangement for the ownership and business development of the retailing corporation.

Regulatory reform

It is not clear to the Council whether the Minister for Mines and Energy or the Queensland Competition Authority is the economic regulator in Queensland.

From 1 January 2002, the ACCC assumes the role of transmission pricing. However, this date may be brought forward in line with other jurisdictions.

Interconnection with New South Wales

Although Queensland is not physically linked to the NEM, it is currently operating the same market model as the NEC. Upon interconnection with New South Wales, Queensland intends to fully participate in the NEM.

Queensland has accelerated the completion of the Powerlink/Transgrid interconnector from the original date of October 2001 to January 2001. Interconnection may occur prior to January 2001 due to the construction of a private unregulated link.

National Electricity Law

Legislative amendments made to the *Electricity Act 1994* during 1997 gave effect to the establishment of a NEM.

Retail competition in electricity supply

Queensland has implemented the second stage of retail competition (for customers using greater than 4 GWh per year). Work is continuing on the implementation of the remaining tranches of contestability, with a view to having full retail contestability in January 2001.

Assessment

The Council is satisfied that Queensland has met its second tranche electricity reform commitments:

- Queensland has met its Electricity Agreements commitments by structurally separating generation from transmission and having separate distribution and retail companies, in preparation for its participation in the NEM;

- Queensland has reaffirmed its commitment to interconnect with New South Wales by 2000-01. The Council acknowledges that once Queensland is connected to the NEM it will become a full participant in the NEM; and

- implementation of the second stage of retail competition is on track to achieve full retail contestability in January 2001.

As part of the third tranche assessment, the Council will consider Queensland's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

Tasmania

Structural reform

On 1 July 1998, Tasmania structurally separated its vertically integrated public utility, the Hydro-Electric Corporation (HEC). The HEC has been separated into the following three businesses:

- Transend Networks Pty Ltd (Transend), a state-owned company that operates under the Corporations Law with responsibility for the transmission of electricity through the extra high voltage transmission network;

- Aurora Energy Pty Ltd (Aurora), a state-owned company that also operates under the Corporations Law with responsibility for the distribution of electricity (through the lower voltage networks) and retailing. Aurora has an exclusive retail licence for all of Tasmania, excluding the Bass Strait Islands; and

- HEC, a government business enterprise responsible for the generation of electricity and system control (ring-fenced) on mainland Tasmania. HEC is also responsible for generation, distribution and retailing on the Bass Strait Islands.

Structural review of the distribution/retail business

Prior to the establishment of Aurora, a CPA clause 4 review of HEC's distribution and retail businesses was conducted. In its final report of December 1997, the review committee made the following recommendations:

- prior to the introduction of competition, the distribution and retail businesses of the HEC should remain as an integrated entity, with ring-fencing (accounting separation) of the distribution and retail functions;

- when competition is introduced into the Tasmanian retail electricity market, the distribution and retail businesses of the HEC should be carried out by separate legal entities; and

- that there be no further disaggregation into multiple distribution and retailers.

The Tasmanian Government accepted the majority of these recommendations, particularly in relation to establishing appropriate regulatory arrangements for the

distribution/retail business. However, the Government did not accept the recommendation that distribution and retail should be conducted by separate legal entities when competition is introduced. The Government considered that ring-fencing would provide appropriate competitive safeguards. Consequently, Aurora was established as a single distribution/retail business.

Structural review of the HEC's generation activities and the system control function

A clause 4 review of HEC's generation business commenced in March 1999. The review team released an Issues Paper on 29 March 1999 and was required to report to the Government by 30 April 1999.

Regulatory reform

The independent Electricity Regulator is responsible for the regulation of electricity prices, ensuring that the regulatory framework is transparent, independent of government and co-ordinated within a single body.

A key objective of the Electricity Regulator is to promote efficiency and competition in the electricity supply industry, which means that the Electricity Regulator has obligations to ensure that the ring-fencing arrangements are effective in facilitating competition.

Third party access

The Tasmanian Government introduced the Tasmanian Electricity Code (TEC) from 1 July 1998 to provide for third party access to the Tasmanian transmission and distribution network.

Basslink

Tasmania has informed the Council that the Basslink (proposal to interconnect Tasmania with Victoria) is a fundamental part of the Tasmanian Government's energy strategy. The Basslink Development Board has been appointed to facilitate Basslink as a commercial opportunity in the NEM. The Board is acting as the notional proponent to progress key issues prior to the selection of a preferred proponent in February 2000. Two issues are the NEC rules for non-regulated interconnectors and the environmental and developmental approvals process. The Government's objective is to have Basslink commissioned in October 2002.

Through Basslink, the Government aims to:

- improve the security of electricity supply and reduce the exposure to drought conditions in Tasmania;
- provide Tasmania with access to electricity at prices determined competitively in the NEM;
- provide a means for electricity generated in Tasmania to be sold into the NEM;
- provide a new source of peak generating capacity in the NEM; and

- ensure that the cost of Basslink is minimised through a competitive selection process.

While Basslink will be built, owned and operated by the private sector, the Government has set a minimum link capacity of 200MW. The proponents are to determine other issues such as, the route and whether the link is to be developed as a regulated, non-regulated or hybrid interconnector under the NEC.

In the coming months, the Government will work with other jurisdictions and the NEM regulatory bodies to progress a number of structural and regulatory issues, including derogations and/or changes to the NEC associated with Tasmania's entry to the NEM.

National Electricity Law

The government has enacted the *Electricity – National Scheme (Tasmania) Act 1999* in preparation for becoming a NEM participant. This Act is the legislative vehicle for the adoption of National Electricity Law in Tasmania and is a precondition for Tasmania's entry to the NEM. The Government will proclaim the Act once the arrangements required for Tasmania's entry to the NEM are finalised.

Conduct Code Agreement: reporting obligations

In accordance with clause 2(1) of the CCA, the Tasmanian Government had notified the ACCC,[4] within 30 days of the legislation being enacted, of new legislation reliant on section 51(1) of the TPA. These electricity industry related Acts and their relevant sections are:

- *Electricity Supply Industry Act 1995* (section 44);
- *Electricity Supply Industry Restructuring (Saving and Transitional Provisions) Act 1995* (section 7); and
- *Electricity Supply Industry Amendment Act 1998* (section 49F(2)).

The *Electricity Supply Industry Act 1995* is scheduled for review in 1999 under Tasmania's Legislation Review Program and the *Electricity Supply Industry Amendment Act 1998* will be reviewed in conjunction with the review of this Act. The *Electricity Supply Industry Restructuring (Saving and Transitional Provisions) Act 1995* is currently being reviewed as part of the implementation of COAG's water reform agenda.

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42 The Commonwealth Treasurer was notified of the *Electricity Supply Industry Act 1995* and the *Electricity Supply Industry Restructuring (Savings and Transitional Provisions) Act 1995* as the ACCC had not yet been established.

Assessment

The Council considers that Tasmania's NCP commitments involve participating in the NEM if the Basslink eventuates, and conducting relevant CPA clause 4 reviews.

The Council is satisfied that Tasmania has met its second tranche electricity reform commitments for the following reasons:

- Tasmania has indicated a commitment to join the NEM by the end of the year 2002 if the Basslink proposal proceeds. In preparation for participation in the NEM, the Council considers that Tasmania has implemented the appropriate structural reforms required under the Electricity Agreements;

- as the TEC sets out a framework for third party access which has the potential to introduce competition into the Tasmanian electricity industry, Tasmania was required to undertake a clause 4 review of structural and competitive arrangements. The Council considers that the Government's decision to establish Aurora initially as a single distribution/retail business is consistent with the review recommendations. The review further recommended that following the introduction of competition, distribution and retail should be carried out by separate legal entities. As this separation has not yet been undertaken, the Council will assess the status of the distribution and retail businesses during the third tranche assessment; and

- the *Electricity Supply Industry Act 1995*, the *Electricity Supply Industry Restructuring (Saving and Transitional Provisions) Act 1995* and the *Electricity Supply Industry Amendment Act 1998* are to be reviewed as part of Tasmania's Legislation Review Program. The Council will consider the outcomes of these reviews in accordance with clause 5 the CPA, in the third tranche assessment.

The Council notes that the Tasmanian Government commenced a clause 4 review of the HEC's generation activities and system control function in March 1999. Tasmania advised the Council that the review team is required to report to the Government by 30 April 1999. The Council will assess this review in the third tranche assessment.

B7.2.3 Non-NEM participating jurisdictions

Western Australia

Structural reform

Western Australia is not a party to the Electricity Agreements, and consequently not a participant in the NEM, but is committed to applying competition policy in the electricity sector. Clause 4 of the CPA is relevant as Western Australia has introduced some competition by providing for third party access to Western Power's electricity transmission and distribution network.

In 1995, the State Energy Commission (SEC) was restructured into Western Power, Alinta Gas and the Office of Energy (OOE). The Western Australian Government also determined appropriate commercial objectives for Western Power in the context of its 1 January 1995 corporatisation.

Western Power's activities have been partially ring-fenced through the *Electricity Corporation Act 1994*, that requires Western Power to report annually on a segmented basis on the following:

- generation of electricity;
- transmission of electricity;
- interconnected distribution and sale of electricity in the state's south west;
- Pilbara interconnected system; and
- remote power systems.

Regulatory reform

The OOE is responsible for regulation of the electricity supply industry. These responsibilities include the licensing of electrical workers, authorising the supply of electricity, and regulating and monitoring the technical and safety aspects of the production, transmission, distribution and use of energy.

The *Electricity Corporation Act 1994* provides for third party access to Western Power's electricity transmission network.

Retail competition in electricity supply

Customers with a single site average load of at least 5 MW have been allowed to choose their own supplier from 1 July 1998. Since 1 January 1999 customers with an annual electricity consumption greater than 300 MWh have been contestable. The next stage involves Western Australia extending its contestable retail market to all customers with a single site average load of at least 1 MW from 1 January 2000.

Assessment

Western Australia's introduction of a third party access regime has the potential to introduce competition to the high voltage transmission system and distribution network, which gives rise to a NCP commitment under clause 4 of the CPA. Western Australia has advised the Council that the Minister for Energy has announced options for encouraging greater competition that will be considered. A clause 4 review of Western Power will be an integral part of these considerations.

The Council notes that Western Australia's progress in electricity reform is not as advanced as other jurisdictions, and intends to monitor future progress and the impact of competition on the Western Australian electricity supply industry, particularly during the third tranche assessment.

Northern Territory

Structural reform

The Northern Territory is not a participant in the NEM and has no obligations under the Electricity Agreements. However, clause 4 of the CPA is relevant to the Power and Water Authority (PAWA).

PAWA is a public monopoly established by the *Power and Water Authority Act* to provide electricity, water and sewerage services. In October 1998 the government undertook a review of PAWA. The review covered:

- future direction, structure, operations;
- regulatory and governance arrangements;
- separation of regulatory and commercial functions; and
- third party access arrangements.

The consultants recommended that the most effective competition model for PAWA was a regulated core business with a competitive periphery. (The competitive periphery involves the establishment of arrangements to provide competing electricity generators with access to customers and competitive tendering for inputs and significant system augmentation.)

The consultants also advised that there is merit in retaining the integration of PAWA's electricity, water and sewerage network and retailing businesses. This is due to the size of the Northern Territory market and existing economies of scale.

In its response on 1 December 1998, the Government decided to provide PAWA with an opportunity to achieve significant efficiency improvements under public ownership. The Government has indicated that it will revisit privatisation if the efficiency improvements are not achieved.

In response to the PAWA review, the following reforms are proceeding:

- over the next three years, electricity tariffs for commercial customers are to become progressively cost reflective;
- Territory-based arrangements are being developed to progressively open the electricity generation and retail markets to competition, commencing in the year 2000;
- competitive bids are to be sought when PAWA's electricity, water and sewerage systems require significant augmentation;
- regulatory functions are to be transferred from PAWA to relevant government agencies;
- an interdepartmental committee headed by Northern Territory Treasury has been established to consider the appropriate extent and form of economic regulation of electricity, water and sewerage services. In order to permit competition, the

regulatory arrangements will include an access regime to enable third parties to access electricity transmission and distribution networks; and

- PAWA's business has been reorganised along product lines comprising, among other things, power generation, transmission and distribution networks and retail services. This aims to separate the natural monopoly elements of transmission and distribution from the contestable elements of power generation and retail services.

The Northern Territory Government anticipates that the above reform program will take two to three years.

Assessment

The Northern Territory is not a NEM participant and therefore the only NCP commitments relevant to Northern Territory's electricity industry arise from clause 4 of the CPA. The Council considers that the review of PAWA, and the Government's response to this clause 4 review, is consistent with its NCP commitments.

The Council is satisfied that the Northern Territory Government has met its second tranche electricity reform commitments. However, the Council notes that the Northern Territory's progress in electricity reforms is not as advanced as other jurisdictions, and intends to monitor future progress and the impact of competition on the Northern Territory electricity supply industry, particularly during the third tranche assessment.