

# 6 Electricity

## Background

State and territory governments' electricity commitments under the National Competition Policy (NCP) 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). The CPA commitments relating to structural reform and legislation review are relevant to all jurisdictions, while the electricity agreements apply specifically to jurisdictions that are part of the national electricity market (NEM): New South Wales, Victoria, Queensland, South Australia and the ACT. The commitments are also relevant to Tasmania, which intends to enter the NEM in May 2005. The Australian Government is also a party to the agreements.

## National Electricity Market jurisdictions

The cornerstone of the agreed reforms under the electricity agreements is a commitment to establish a fully competitive NEM. While considerable progress has been made towards achieving a fully competitive NEM, the Council's past NCP assessments, the CoAG Energy Market Review (2002) (known as the Parer Review), CoAG, the Ministerial Council on Energy and the NEM Ministers' Forum have identified deficiencies in the electricity market. The Council noted in its 2003 NCP assessment that a coordinated approach by governments is required to most effectively address these market deficiencies, and that the Council would consider such an approach as part of its 2004 NCP assessment.

Other NEM-wide issues for consideration by the Council are jurisdictions' progress in meeting commitments in relation to derogations from the National Electricity Code and commitments to maximise the potential for competition in electricity retail markets. In addition, a number of governments have outstanding commitments in relation to particular reform measures - namely:

- New South Wales — the Electricity Tariff Equalisation Fund (ETEF)

- Queensland — full retail contestability and the Benchmark Pricing Agreement
- the Northern Territory and the ACT — legislation review and reform
- South Australia — inconsistent intra-NEM approval arrangements
- Tasmania — entry into the NEM.

Each of these specific areas is considered below.

## **National Electricity Market reform**

The Parer Review identified significant deficiencies in Australian electricity markets and made recommendations to address these deficiencies. The major findings and recommendations related to the industry's governance arrangements, market structure, transmission and interconnection, financial contract markets and demand-side participation concerns. The Council noted in its 2003 NCP assessment that all of the Parer Review's findings on the electricity sector relate to the general NCP commitment to establish a fully competitive NEM.

In December 2003, the Ministerial Council on Energy reported to CoAG its response to the findings and recommendations of the Parer Review, together with its reform policy objectives and recommendations. It agreed with the Parer Review's findings that substantial progress on energy market reform has been made in Australia and that significant benefits have arisen from that reform. It also concurred with the Parer Review findings that substantial policy issues remain to be resolved if the full benefits of market reform are to be realised. The Ministerial Council on Energy considered that a second phase of market reform is required (involving a coordinated response from governments) to capture those benefits.

It concluded that further reform should be undertaken to:

- strengthen the quality, timeliness and national character of governance of the energy markets, to improve the climate for investment
- streamline and improve the quality of economic regulation across energy markets, to lower the cost and complexity of regulation facing investors, enhance regulatory certainty and lower barriers to competition
- improve the planning and development of electricity transmission networks, to create a stable framework for efficient investment in new (including distributed) generation and transmission capacity
- enhance the participation of energy users in the markets, including through demand-side management and the further introduction of retail

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competition, to increase the value of energy services to households and business

- further increase the penetration of natural gas, to lower energy costs and improve energy services (particularly in regional Australia) and reduce greenhouse emissions
- address greenhouse emissions from the energy sector, in the light of concerns about climate change and the need for a stable long term framework for investment in energy supplies.

The following are key elements of the reform package that the Ministerial Council on Energy recommended to CoAG, as they relate to the electricity sector:

- *Governance* — subsume the NEM Ministers' Forum within the Ministerial Council on Energy, thereby establishing a single energy market governance body.
- *Economic regulation* — establish two new statutory commissions. The Australian Energy Market Commission (AEMC) will be responsible for rule-making and market development, and the Australian Energy Regulator (AER) will be responsible for market regulation. Initially covering electricity wholesale and transmission for the NEM, the responsibilities of the AEMC and AER will broaden to include gas transmission from 2005. By 2006, the AER will be responsible for regulating distribution and retailing (other than retail pricing), following the development of an agreed national framework.
- *Electricity transmission* — develop, implement and progress a new NEM transmission planning function, a regulatory test for transmission and a process for assessing wholesale market regional boundaries in 2004. Interregional financial trading arrangements are to be evaluated, and the review of transmission pricing arrangements is to be concluded for implementation in 2004.
- *User participation* — ensure jurisdictions in which full retail competition is operating align their retail caps with costs and periodically review the need for price caps. The Ministerial Council on Energy did not stipulate a date for the implementation of these reforms. It is to examine options for a demand-side response pool in the NEM and consider the costs and benefits of introducing interval metering.

Jurisdictions are sharing responsibilities for further developing and implementing of reform initiatives. Since December 2003 a significant number of public consultations have been held on the key reform initiatives. Legislation establishing the AER was passed through the Australian Parliament in June 2004. Legislation to establish the AEMC was passed through the South Australian Parliament in June 2004 but has yet to be applied in other jurisdictions.

The Council welcomes the Ministerial Council on Energy's commitment to progressing electricity sector reform. The Ministerial Council on Energy recommendations demonstrate an apparent willingness to address many of the market deficiencies highlighted in the Parer Review.

The Council noted in its 2003 assessment that many of the deficiencies in the electricity market identified by the Parer Review related to existing NCP reform commitments. The Ministerial Council on Energy reform program seeks to address these deficiencies in a coordinated and comprehensive manner.

There are a number of specific NCP commitments that remain outstanding which are considered in this assessment. These are discussed below.

## **Retail market competition**

The Parer Review discussed the importance of demand-side participation to the effective operation of the NEM. It noted the low level of demand-side involvement in the NEM, attributing it to demand inelasticity and consumers not facing cost-reflective retail prices. The review recommended the implementation of full retail contestability, the removal of price caps, a mandated interval meter roll-out and the introduction of pay-as-bid mechanisms to manage demand.

The Council considers the introduction of full retail contestability to be an essential component of the electricity reforms. It expressed this view in all previous NCP assessments of jurisdictions' compliance with the specific electricity commitments. Further, the Council notes that regulatory oversight of retail tariffs should be only a transitional arrangement and should cease when competition is sufficiently developed in retail markets.

The level of regulated tariffs for franchise customers is an important issue. If the level is set too low relative to underlying costs, it will impact on the development of competition in retail and generation. Further, if the regulated tariff is not cost reflective, new retailers cannot compete for franchise customers. These factors can combine to reduce scale economies for new entrants, increasing their costs and making it more difficult for them to compete.

In its December 2003 report to CoAG, the Ministerial Council on Energy recognised the importance of demand-side participation in achieving effective competition and maximising the benefits of market reform. It supports the further introduction of retail competition across the NEM, but guided by local circumstances and the need to protect consumers. The Ministerial Council on Energy recommended that in all jurisdictions in which full retail contestability is operating, retail price caps should be aligned with costs, and the need for the price caps should be reviewed periodically. It stated that it would examine the establishment of a demand-side response pool in the

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NEM. The Ministerial Council on Energy released a policy statement for user participation in August 2004.

The recommendations that retail price caps be aligned with costs and that the need for the caps be reviewed periodically are positive steps toward enhancing competition. The Council notes, however, that the Ministerial Council on Energy is not undertaking any reform program in relation to such issues but rather is focusing its retail market reform enquiries on user participation issues such as demand-side response pools and metering. The Ministerial Council on Energy did not commit to a date for implementing reforms of retail price caps although it has referred the matter to the AEMC for consideration once it is established.

All NEM jurisdictions other than Queensland have introduced full retail contestability while maintaining some form of regulatory prices oversight while markets are in transition to effective competition. The form of the regulatory pricing oversight and its potential impact on competition differs across each jurisdiction.

The Council considers it appropriate that decisions to extend retail price controls require the support of independent reviews as in New South Wales, South Australia and Victoria. Further, it is desirable that an independent regulator investigate and determine regulated tariffs as in New South Wales, South Australia and the ACT. In Victoria, the government has a reserve pricing power, although consultation with the state independent regulator has been usual. In Queensland, the government continues to determine regulated tariffs.

Community service obligations need to be delivered in a transparent and competitively neutral manner and not create barriers to entry for new retailers. Each NEM jurisdiction has rebate schemes intended to increase the affordability of electricity to particular sectors of the community, including pensioners, low income earners and those on life support systems. The government pays these rebates to either customers directly or retailers on behalf of customers. Provided rebates to retailers are paid in a competitively neutral manner, this rebate delivery method is transparent and does not distort competition in the retail market.

New South Wales and Queensland have mechanisms in place to manage the government's risk to fluctuating wholesale prices against the need to deliver uniform retail tariffs. These mechanisms are discussed in detail below.

## New South Wales

In New South Wales, following a ministerial reference in September 2003, the Independent Pricing and Regulatory Tribunal (IPART) determines the regulated retail tariff for small customers supplied under a standard form contract. Retailers are required to comply with the IPART tariff determination as a condition of their retail licences.

The New South Wales Government stated in its 2004 NCP annual report that it has a policy aim of reducing customers' reliance on regulated prices and that it views them as a transitional measure. In December 2003 it decided to extend the regulatory arrangements underpinning the regulated tariffs until 30 June 2007, on the basis that the retail market was not sufficiently competitive to protect the interests of small customers. The following factors were germane to the government's decision:

- The gradual introduction of competition has been demonstrably successful (notwithstanding the existence of regulated tariffs) with around 560 000 small energy customers accepting contestable supply terms and the number of retailers increasing since the start of full retail contestability.
- The regulated tariff has provided an essential consumer protection during the transition to full competition and should continue, given that a competitive market is still developing.
- Interjurisdictional discussions on the reform of energy market governance and regulatory arrangements are ongoing.
- The government considers regulated tariffs to be the most transparent transitional arrangement available, following an evaluation of alternative means to protect consumers.

In April 2004 IPART released its draft determination on electricity retail tariffs for the period 1 July 2004 to 30 June 2007. On behalf of IPART, PricewaterhouseCoopers conducted an independent analysis of the competitive offers available in the market. It concluded that competition is developing for small customers in New South Wales but cannot yet be considered effective.

In addition to extending the arrangements supporting regulated tariffs, the New South Wales Government extended the operation of the ETEF (discussed in detail below) until 30 June 2007.

The New South Wales Government also provides an energy rebate to eligible pensioners and those people who need to use a life support machine, such as dialysis. The rebate is made available through all New South Wales retailers.

## Victoria

The Victorian Government can, under its reserve pricing powers, override the franchised customer tariffs set by retailers. It is not required to refer the matter to an independent regulator, such as the Essential Services Commission for consideration before exercising its right of intervention. It has, however, sought the views of the Essential Services Commission in the past.

In its 2004 NCP annual report, the Victorian Government has stated that its 'goal is to have energy prices set by the market rather than regulation'. It has

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noted that it does not automatically exercise its reserve pricing power to constrain retailers' standard prices and that it has done so only where it has concluded that 'market power is being exercised and proposed retailer pricing was not justified'.

In December 2003 the Victorian Government announced a voluntary agreement with the privately owned energy retailers to lock in a pricing structure for four years. In its 2004 NCP annual report, it stated that the intent of the arrangement is to provide price certainty for Victorians, to strike a balance between protecting customers and ensuring a viable electricity industry, and to enable the continued progress of retail competition.

In June 2004 the Essential Services Commission released a report on the effectiveness of retail competition and the consumer safety net in gas and electricity. It concluded that competition is likely to become effective for a much larger proportion of small energy customers in the next few years. Until such time, residential customers in particular, should continue to have access to the minimum protections afforded by the retail code and a retail price benchmark such as that provided by the standing offer price arrangements. It further concluded that competition in the retail market overall, has developed such that a gradual rollback, and potentially the elimination, of retail price regulation should be considered. The Victorian Government is yet to respond to the commission's report, although it has stated that the need for continuing prices oversight will be assessed in light of the Essential Services Commission's final report and recommendations.

Victoria has a number of community service obligation schemes for electricity, including a network tariff rebate (which is intended to close the gap between electricity prices paid by country and city areas through the government's payment of a rebate to retailers on behalf of customers) that commenced on 1 April 2003. In addition, the Government provides a range of energy concessions and relief grants for electricity to low income groups, to help address fuel poverty.

## Queensland

Queensland has not introduced full retail contestability, although larger customers are contestable. From 1 July 2004 contestability was extended from the current threshold of customers using more than 200 megawatt hours per year to include those using more than 100 megawatt hours per year.

The Minister determines electricity retail prices for non-contestable customers charged by the three retailers operating in Queensland (ENERGEX, Ergon Energy and Country Energy). Customers within a particular class pay the same tariff across the state. In addition, the tariff structure includes special conditions for customers who are farmers in a drought declared area or whose properties are individually drought declared.

Other community service obligations include electricity rebates to eligible pensioners and seniors (administered by the franchise retailers on behalf of the Department of Communities), and to those on home based life support machines (administered directly by the Department of Communities).

## South Australia

Full retail contestability commenced in South Australia on 1 January 2003. As part of the consumer protection measures introduced to support the introduction of contestability, the South Australian Government conferred retail pricing powers on the Essential Services Commission of South Australia. The commission has the power to require that retailers justify any price increases for small customers on regulated tariffs, and it has reserve powers to cap such retail prices if it considers that electricity tariffs are excessive and unjustifiable. Further, the Electricity Act introduced the concept of a standing contract, which applied to small customers (those consuming less than 160 megawatt hours) unless they elect to transfer to a market contract.

Initially the standard contract provisions were to apply until July 2005, by which time the government will have undertaken a review of the effectiveness of the provisions and their continuing need. Following a review by IPART in March 2004 into the methodology used by the Essential Services Commission of South Australia (ESCOSA) in setting the standard contract price, the government has amended the standing contract provisions to implement a three year price path. ESCOSA is required to undertake a comprehensive public inquiry prior to setting the prices for the subsequent three years. Further, the government has extended the expiry date for the standing contract provisions from 1 July 2005 to a date to be fixed by proclamation.

To date, customer transfer numbers published by ESCOSA, indicate that small customers are increasingly taking advantage of retail competition with around 100,000 of the total small customer base of 740,000 having transferred (or in the process of transferring) to market contracts.

Retailers licensed to operate in South Australia are required to comply with the government's energy concession scheme. This requires retailers to deduct the concession amount from an eligible customer's account. The reduced amount is paid by the customer directly to the retailer with the amount of the concession then reimbursed by the government.

The government also developed a scheme offering a one-off \$50 electricity transfer rebate to energy concession recipients who switched from the standard contract to a market contract before 13 August 2004. Approximately 75,000 customers have taken advantage of the rebate.



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## The ACT

The ACT introduced full retail contestability on 1 July 2003. The ACT Government announced that it will allow a three-year transition period during which customers can remain with their existing supplier, ActewAGL Retail on a regulated tariff. The Independent Competition and Regulatory Commission determines the regulated tariff for franchise customers. In May 2003 the commission issued its final determination on retail prices for franchise customers and this determination will be in force until 30 June 2006. The ACT Government has advised the Council in its 2004 NCP annual report that the ACT Government will re-assess the continued need for the arrangements after the retail determination expires.

Electricity sector community service obligations under the ACT Concessions Program are delivered via a direct customer rebate. Rebates are payable to customers groups including pensioners and those on life support systems.

## Specific outstanding assessment issues

### New South Wales

#### The Electricity Tariff Equalisation Fund

In its 2003 NCP assessment, the Council detailed the nature of the ETEF in New South Wales. It concluded that the operation of the ETEF is likely to reduce liquidity in the financial and physical hedged market, which may increase the price of such financial instruments and increase the costs for other retailers, raising barriers to retail market entry. This view mirrors that expressed by the Parer Review.

New South Wales disputed these findings, arguing that the ETEF is a transparent mechanism through which the government delivers a community service obligation to price regulated electricity customers. Further, it stated that the ETEF was a transitional measure that was due to expire in July 2004, and that it would then examine the continued need for such an arrangement.

The New South Wales Government reviewed the continuing need for the regulated tariff and decided that the tariff should continue to apply until 30 June 2007. It stated in its 2004 NCP annual report that the decision to extend the application of the regulated tariff 'necessitated the continuation of the ETEF until 30 June 2007', and that the decision to extend the operation of the ETEF followed an examination of other options for minimising the risk to retailers. These options included the re-introduction of vesting contracts, the requirement that standard retailers buy electricity for regulated customers on behalf of the government and various market based processes. The

government's review of the ETEF built on an earlier review in 2001. The government concluded that there had been no developments that justified the move to a different risk management mechanism on the basis of greater effectiveness and efficiency. As such, it concluded that the ETEF should remain in place.

In relation to the effect of the ETEF on competition, the New South Wales Government has argued that there is no evidence that the ETEF has reduced energy related financial market trading activity. The Council previously considered in the 2003 NCP assessment the evidence in the state's 2003 NCP annual report. No new evidence has been submitted to the Council such that it needs to reconsider its conclusion that the ETEF is likely to reduce liquidity in the financial and physical hedged market.

The Council continues to be concerned about the extent to which the ETEF arrangements raise barriers to entry to new generation and adversely affects emerging retail competition. The Council considers the ETEF arrangements should be further considered within the context of the Ministerial Council on Energy retail market reform program.

## Queensland

### Full retail contestability

In the 2003 NCP assessment, the Council determined that Queensland had failed to meet its NCP obligation to introduce full retail contestability in electricity. Queensland agreed to consider the early introduction of contestability for customers consuming 100–200 megawatt hours per year (tranche 4A) and to undertake a further review of full retail contestability. The Council recommended a suspension of 25 per cent of Queensland's competition payments (10 per cent related to tranche 4A and 15 per cent related to the outcome of the wider review of full retail contestability).

In February 2004 the Queensland Government announced the extension of retail competition to tranche 4A customers. Contestability for tranche 4A customers commenced on 1 July 2004.

Queensland, however, has yet to complete the review of the costs and benefits of full retail contestability in accordance with its 2003 commitment. The government has commenced the review process by drafting terms of reference and engaging a consultancy firm to undertake the review. The government estimates that the review will be completed by the end of 2004, with a decision on the introduction of full retail competition anticipated in early 2005.

Consistent with the 2003 assessment, the Council considers that the Queensland government's decision to date, to not introduce full retail contestability, is in breach of its electricity commitments. The Council notes

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that Queensland will reconsider this decision following the 2004 review. The Queensland Government's response to this review will be considered by the Council in its 2005 assessment.

### The benchmark pricing agreement/long term energy procurement

In its 2003 NCP assessment, the Council considered the nature of the benchmark pricing agreement in Queensland, in light of the Parer Review concerns about the agreement's competitive effect. Queensland has advised the Council that the agreement is an example of an energy procurement arrangement designed to ensure retailers purchase wholesale electricity to supply the franchise customer load on a commercial and efficient basis. Queensland has introduced a new energy procurement arrangement referred to as long term energy procurement (LEP).

Under the LEP, the government benchmarks contracts purchased by the retailers supplying franchise load against a range of publicly available and retailer-specific data to ensure the retailers' contracts are efficiently priced. Risk is transferred to the retailers for exposure to the wholesale pool, thereby placing incentives on the retailers to actively manage pool price outcomes.

The LEP requires the retailers to enter the financial market and secure contracts for risk mitigation purposes (or face potential losses from remaining unhedged). Queensland has argued that the energy procurement arrangement supports the development of wholesale contract market mechanisms because it requires the retailer to bid for financial contracts and encourages generators to offer contracts, reinforcing and enhancing the underlying liquidity in the market. The arrangement is competitively neutral in that the retailer can choose its preferred counterparty, irrespective of whether that counterparty is government or privately owned.

In essence, the government negotiates a supply contract with retailers on behalf of the franchise load. The arrangement focuses on benchmarking of contracts and attempts to replicate outcomes that would occur in an effectively competitive market. The actual purchasing and hedging of energy remain the sole responsibility of the retailers.

The Council does not consider that the LEP has an anticompetitive effect. The continued need for such an arrangement will be dependant on the introduction of full retail contestability and the role of regulated retail tariffs. These issues will be considered by the Ministerial Council on Energy in the context of its retail market reform program.

## South Australia

### Licensing arrangements

In its 2003 NCP assessment, the Council expressed continuing concern about the potential for overlap between the NEM regulatory processes for new interconnects and South Australia's licensing requirements for new transmission companies. This issue arose in the context of the SNI interconnect project, which was approved through NEM regulatory processes but also subject to a customer benefits test under South Australian licensing arrangements.

As discussed, the Ministerial Council on Energy's reform program provides for the harmonisation of regulatory arrangements across jurisdictions. A single national energy regulator (the Australian Energy Regulator) and rule making body (the Australian Energy Market Commission) are scheduled to commence operation by the end of 2004. Implementation of the new governance arrangements and regulatory harmonisation will likely address regulatory inconsistencies such as that encountered in the SNI interconnect project.

## Tasmania

### National Electricity Market participation

Tasmania is scheduled to enter the NEM on 29 May 2005. Basslink is scheduled to be commissioned in November 2005. To facilitate Tasmania's entry into the NEM, a suite of structural and regulatory arrangements have been developed. Key milestones that have been achieved to date include:

- the Australian Competition and Consumer Commission's authorisation of the proposed NEM entry transition arrangements
- the formalisation of arrangements with the existing NEM jurisdictions for Tasmania to become a participating jurisdiction
- membership of the National Electricity Code Administrator (NECA) and the National Electricity Market Management Company Limited (NEMMCO)
- the passing of legislation required to adopt the National Electricity Law and apply the National Electricity Code in Tasmania;
- amendment of the *Electricity Supply Industry Act 1995* (see below for details)

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- memoranda of understanding between the Tasmanian Government, the state-owned electricity businesses and NEMMCO that govern the NEM entry process.

The *Electricity Supply Industry Act 1995* was amended in April 2003 to establish the framework required to facilitate Tasmania's entry to the NEM and provide for the introduction of retail contestability over four years, commencing six months after Basslink is commissioned. The reform legislation introduced a suite of structural and regulatory arrangements, including:

- transferring certain functions and powers in relation to transmission pricing from the Office of the Tasmanian Energy Regulator to the ACCC
- formalising the appointment of the Office of the Tasmanian Energy Regulator as the state's jurisdictional regulator under the National Electricity Code
- establishing a head of power to enable the development of detailed arrangements for the introduction of retail competition in Tasmania
- enabling Transend Networks, as system controller, to enter into agreements with NEMMCO which will enable NEMMCO to perform the system controller functions in Tasmania.

Tasmania has obtained authorisation from the ACCC for a number of derogations to the National Electricity Code to accommodate the transitional entry into the NEM. The derogations include vesting contract arrangements between Aurora Energy and Hydro Tasmania covering non-contestable customer load. The derogations are due to expire two years after Tasmania enters the NEM.

In relation to retail contestability, Tasmania proposes that the first tranche — covering around 19 customers consuming in excess of 20 gigawatt hours per year — will be introduced on 1 July 2006. The remaining stages are scheduled to occur at annual intervals, with full retail contestability scheduled from 2010 following a positive cost–benefit assessment. Table 6.1 sets out the timetable for retail competition.

**Table 6.1:** Tasmania's retail contestability timetable

<i>Introduction of contestability*</i>	<i>Electricity consumption (Gigawatt hours per year)</i>	<i>Approximate number</i>	<i>Indicative customer type</i>
1 July 2006	20	10	Mineral processors
1 July 2007	4	54	Large industrial facilities and commercial complexes
1 July 2008	0.75	295	Medium factories and smaller commercial complexes
1 July 2009	0.15	1030	Small factories and large offices
1 July 2010	Less than 0.15	230 000	Small business and domestic customers

\*Dates are subject to completion of Basslink in late 2005.

The Council is satisfied with Tasmania's progress in implementing measures to participate in the NEM. While a number of measures have yet to be implemented, progress suggests that Tasmania, once Basslink is commissioned, will be at least substantially ready to participate in the NEM. The Council will assess further progress in its 2005 NCP assessment.

## The ACT

### Legislation review and reform

At the time of the 2003 NCP assessment, the ACT had one outstanding legislation review matter relating to electricity. That matter has now been addressed with the enactment of the *Construction Occupations (Licensing) Act 2003* on 11 March 2004.

## Code derogations

In its 2003 NCP assessment, the Council expressed concern that derogations from the National Electricity Code could fragment the NEM, reducing its effectiveness and limiting the scope for competition. For this reason, derogations to the code are warranted only when necessary to provide a smooth transition to the NEM or when related to unique characteristics within a particular jurisdiction — for example, derogations relating to Tasmania's entry into the NEM, metrology procedures following the introduction of full retail contestability, and recognition of the separation of transmission ownership and operation in Victoria.

Derogations must be authorised by the ACCC, which assesses the public benefit against the likely competitive detriment under the *Trade Practices Act*

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1974. In applying this test, the ACCC considers not only the public interest associated with the particular derogation, but also the competitive impact of the derogation on the NEM as a whole. The Council considers that the broad focus of the ACCC's authorisation test provides a satisfactory balance between the need for flexibility in dealing with transitional arrangements and the broader need for consistency to facilitate competition within the NEM.

## **Non-National Electricity Market jurisdictions**

As outlined, the CPA commitments relating to structural reform and legislation review are relevant to Western Australia's and the Northern Territory's electricity sectors.

### **Western Australia**

In its 2003 NCP assessment, the Council noted that the Western Australian Government had endorsed all of the recommendations of the independent Electricity Reform Task Force, including the indicative reform timetable. The agreed program and timetable included:

- the vertical disaggregation of Western Power into generation, networks (transmission and distribution) and retail entities, and the establishment of a fourth entity, the Regional Power Corporation, with responsibility for electricity supply in the north west interconnected system and Western Power's non-interconnected systems, by 1 July 2004
- the establishment of a bilateral contracts market with an associated residual trading market
- the mitigation of Western Power's generation market power through the auctioning of its capacity, a requirement that it participate in the residual trading market, and restrictions on its ability to invest in new or replacement fossil fuelled generation plant
- the retention of uniform tariffs and retail price caps
- the implementation of retail contestability for all customers above 50 megawatt hours per year from 1 January 2005, then full implementation once the other reforms have been completed
- the development of an electricity access code (to be administered by an independent regulator) by 1 January 2004 and the operation of the new access framework and licensing regime by 1 January 2005.

The *Electricity Industry Act 2004* was passed on 8 April 2004 and the *Electricity Legislation Amendment Bill 2004* on 23 September 2004. The legislation implements many of the reform initiatives to which the government has committed. In particular, it contains provision for the development of a wholesale market for the South West Interconnected System, an independent licensing regime for electricity industry participants, a third party electricity access code, and consumer protection measures.

Further implementation measures in each of these areas include the following:

- *An industry licensing regime.* The independent Economic Regulation Authority commenced on 1 January 2004. It is responsible for utilities regulation in Western Australia. The *Electricity Industry Act 2004* specifies procedures in relation to granting licences, including terms and conditions that the authority may impose, licence exemption conditions, and licence amendment, transfer, enforcement and cancellation procedures.
- *Third party access.* A new electricity access code that provides for third party access to electricity networks in Western Australia is being developed consistent with the principles in clause 6 of the CPA. The access code will be operational by the end of 2004.
- *A wholesale market.* The wholesale electricity market is scheduled to commence from July 2006. A Market Rules Development Group has been set up to help develop market rules for the wholesale market. The market rules were proclaimed on 30 September 2004. Transitional arrangements will be developed to assist independent power producers to compete until the market is fully implemented.
- *Top up and spill.* New electricity balancing and trading arrangements have been established as the first stage of progression to the new wholesale market. The arrangements allow independent generators to manage load balancing requirements and to trade on a limited basis.
- *Independent market operator.* The government is in the process of establishing an independent market operator — a new entity independent of Western Power. The independent market operator will operate the wholesale market by the end of 2004.
- *Consumer protection.* Consumer protection measures will include the implementation of a customer service code, standard supply contracts, consumer connection policies and an energy ombudsman scheme, and the imposition of retailer of last resort obligations on Western Power.

In addition, retail contestability thresholds for electricity are being progressively lowered. In July 2001 the threshold was lowered from an average load of at least 1 000 kilowatt (or 8 760 megawatt hours per annum) to an average load of 230 kilowatt (or 2 000 megawatt hours per year) at a single site. On 1 January 2003, contestability was extended to customers



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using an average load of at least 34 kilowatt (or 300 megawatt hours per year). This represented an increase in the number of contestable customers from 450 to around 2 500, meaning contestability has been extended to approximately 50 per cent of Western Power's total sales.

The government initially had a target of introducing full retail contestability from 1 January 2005. In its 2004 NCP annual report, Western Australia has noted that the Electricity Reform Task Force has recommended a delay in the implementation of full retail contestability until such time as competition develops in the generation and wholesale markets. The task force proposed that the threshold for contestability be reduced to 5.7 kilowatt average load (50 megawatt hours per year) on 1 January 2005. The government has accepted this recommendation and will introduce the next tranche on 1 January 2005. The Council accepts that implementation of other key reforms (including the establishment of a generation wholesale market) should appropriately precede the introduction of further contestability.

Western Australia has made substantial progress in implementing electricity sector reform. However, it has failed to implement an essential aspect of the reform package recommended by the Electricity Reform Task Force and accepted by the government — namely, the structural separation of Western Power into generation, networks and retail entities in the south west interconnected system, and the establishment of a regional power entity for Western Power's north west interconnected system and non interconnected system. In its final report to government, the task force referred to the recommendations for Western Power's disaggregation and for the establishment of the wholesale market as '[t]he most significant recommendations of the Task Force'. It noted too that '[c]entral to the proposed structural change is the disaggregation of Western Power'.

The Electricity Corporation Bill 2003, required to implement the disaggregation of Western Power, was introduced into the Legislative Assembly in October 2003. The Bill progressed to a second reading in the Legislative Council before being withdrawn, with publicised opposition making it evident that the Bill would not pass a third reading.

The government has stated in its 2004 NCP annual report that it continues to be committed to the disaggregation of Western Power and intends to reintroduce the disaggregation legislation following the next election. The passage of the legislation and the implementation of the restructuring reforms would satisfy Western Australia's CPA clause 4 obligations. The Council will review the position in its 2005 NCP assessment.

The Council considers Western Australia's failure to implement the structural reforms recommended by the Electricity Reform Task Force and accepted by the Government to be a serious breach of its obligation under CPA clause 4. The Council is mindful, however, of the substantial progress made by Western Australia in implementing other key aspects of the reform program.

## The Northern Territory

At the time of the 2003 NCP assessment, the Northern Territory had one outstanding legislation review matter relating to electricity — namely, section 19 of the *Power and Water Corporation Act 2002*.

The section provides the corporation with an exemption from the payment of local government rates. The Northern Territory advised for the 2003 assessment that the section had not yet been repealed because complexities regarding the local government funding arrangements were yet to be resolved. Until such time, the corporation will continue to pay local government rate equivalents through the Northern Territory's tax equivalent regime. It has done so since 1 July 2001, and the arrangements satisfy competitive neutrality requirements.

**Table 6.2: Review and reform of electricity-related legislation**

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
New South Wales	Electricity (Pacific Power) Act 1950	Provides for the constitution of Pacific Power and to define its principal objectives, powers, authorities, duties and functions. Amends and repeals certain other Acts.	Not for review, as the Government has established new state-owned corporations from Pacific Power's generation and transmission businesses.	The Act was repealed by the Pacific Power (Dissolution) Act 2003, assented to on 30 June 2003.	Meets CPA obligations (June 2003)
	Electricity Safety Act 1945	Provides for the development of electricity supply; confers certain powers, authorities, duties and functions on the Energy Corporation of NSW; provides for the regulation of the sale and hiring of electrical apparatus and amends certain Acts.	<p>Review completed in March 2002.</p> <p>The review recommended that:</p> <ul style="list-style-type: none"> <li>the legislation be retained;</li> <li>government intervention regarding consumer electrical articles and installations is warranted and should be retained; and</li> <li>the provisions applying to the safety of second-hand consumer electrical articles be retained.</li> </ul>	<p>The Government approved the review's recommendations in May 2002.</p> <p>There are no NCP-related changes to the legislation.</p>	Meets CPA obligations (June 2003)

(continued)

Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
New South Wales (continued)	Electricity Supply Act 1995	Regulates the supply of electricity in the wholesale and retail markets; sets out the functions of persons engaged in the conveyance and supply of electricity  The Act does not contain anti-competitive provisions.	Review will be undertaken after trends in the fully contestable retail market become clear.	Extensive amendments were made to the Act in late 2000 to facilitate the introduction of full retail contestability for all electricity customers in NSW from 1 January 2002.	Meets CPA obligations (June 2003)
	Electricity Transmission Authority Act 1994	Constitution of the New South Wales Electricity Transmission Authority		Act repealed.	Meets CPA obligations (June 2001)
	Energy Administration Act 1987 (Electricity-related provisions)	Constitution of the Energy Corporation of New South Wales	Review completed.	Licence and approval requirements repealed.	Meets CPA obligations (June 2001)
Victoria	Electricity Industry Act 1993	Implements electricity industry reform	Review completed.	Act replaced by the Electricity Industry Act 2000. The Electricity Industry (Residual Provisions) Act 1993 contains remaining provisions relevant for historical purposes.	Meets CPA obligations (June 2001)

(continued)

Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
Victoria (continued)	Electricity Industry Act 2000	Implements electricity industry reform	Assessed against NCP principles at introduction. Assessment found the Act's provisions to be consistent with NCP principles, that is they do not restrict competition, but rather underpin existing competition and facilitate its introduction for domestic and small business customers.		Meets CPA obligations (June 2001)
	Electric Light and Power Act 1958			Act repealed and replaced by the Electricity Safety Act 1998.	Meets CPA obligations (June 2001)
	Electricity Safety Act 1998	Safety standards for equipment, licensing of electrical workers	Assessed against NCP principles at introduction. Assessment found the restrictions justified in the public interest on public safety and consumer protection grounds. Act addresses consumers' inability to detect hazardous products and assess the competency of tradespeople.	Restrictive provisions retained.	Meets CPA obligations (June 2001)

(continued)

**Table 6.2** continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
Victoria (continued)	Electricity Safety (Equipment) Regulations 1999	Standard-setting and approval requirements for electrical equipment	Assessed against NCP principles at introduction. Assessment found the restrictions justified in the public interest on public safety and consumer protection grounds. Regulations address consumers' inability to detect hazardous products.	Restrictive provisions retained.	Meets CPA obligations (June 2001)
	Snowy Mountains Hydro- Electric Agreements Act 1958			Act repealed.	Meets CPA obligations (June 2001)
	State Electricity Commission Act 1958		Scoping study has shown that the Act does not restrict competition.		Meets CPA obligations (June 2001)

(continued)

Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
Queensland	Electricity Act 1994	Conduct requirements, restrictions on trading activities, Ministerial pricing powers	Review of non-safety provisions completed in April 2002. Review made nine recommendations. Government accepted all recommendations with legislative amendments to be implemented in regard to six of the recommendations, departmental reviews for a further two and ongoing implementation of existing processes in regard to the remaining recommendation.	Legislative amendments to give effect to recommendations relating to non-safety provisions were assented to in May 2003 in the Electricity and Other Legislation Amendment Act 2003.	Meets CPA obligations (June 2003)

(continued)

Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
Western Australia	Electricity Act 1945 – Part 1 of 2	Regulations concerning mandated supply, determination of interconnection prices, restrictions on the sale/hire of non-approved electrical appliances, uniform pricing	Initial review completed in 1998. The review recommendations have been superseded by wider reform of the electricity industry.	Repealed by the Electricity Legislation Amendment Act 2004.	Meets CPA obligations (October 2004)
	Electricity Corporation Act 1994	Exclusive retail franchise of Western Power, entry restrictions for generation, competitive neutrality restrictions	Initial review completed. Further review was conducted as part of wider electricity sector reform.	Some minor competitive neutrality advantages have been removed by the Statutes (Repeals and Minor Amendments) Act 1998.  Generator entry restrictions removed by the establishment of the electricity market, licensing regime and access code under the Electricity Industry Act 2004 and Electricity Legislation Amendment Act 2004.  Retail contestability to be gradually introduced.	Meets CPA obligations (October 2004)

(continued)



Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
South Australia	Electricity Act 1996	Restrictions on market entry and market conduct	Review completed in September 2000. No reforms recommended as Act facilitates regulation of electricity supply in conjunction with other national electricity market reforms	No reform required	Meets CPA obligations (June 2003)
	Electricity Corporation Act 1994	Restrictions on market entry and market conduct	Review completed in September 2000. No reforms recommended as Act facilitates establishment of state owned corporations in SA in conjunction with other national electricity market reforms.	No reform required	Meets CPA obligations (June 2003)
	National Electricity (South Australia) Act 1996	Restrictions on market entry and market conduct	Review completed in September 2000. No reforms recommended as sole object is to implement a national electricity market. Review process: consultation with other jurisdictions.	No reform required	Meets CPA obligations (June 2003)

(continued)

Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
Tasmania	Electricity Supply Industry Act 1995	Conduct requirements, exclusive retail provisions, tariff-setting procedures	Review completed in late 2001.	Review recommendations were either enacted or are redundant following passage of legislation enabling Tasmania's entry into the NEM.	Meets CPA obligations (June 2003)
	Electricity Consumption Levy Act 1986			Act repealed.	Meets CPA obligations (June 2001)
ACT	Hydro-Electric Commission Act 1944, Hydro-Electric Commission (Doubts Removal) Act 1972 and Hydro-Electric Commission (Doubts Removal) Act 1982			Acts repealed and replaced by the Electricity Supply Industry Act 1995 and the Electricity Supply Industry Restructuring (Savings and Transitional Provisions) Act 1995.	Meets CPA obligations (June 2001)
	Utilities Act 2000	Licensing requirements, restrictions on business conduct	The Act's introduction followed public consultation and review of both existing regulatory arrangements and principles for effective regulation.	Restrictive provisions retained. Other Acts amended or repealed include the Electricity Supply Act 1997, the Electricity Act 1971, the Energy and Water Act 1988 and the Essential Services (Continuity of Supply) Act 1992.	Meets CPA obligations (June 2001)

(continued)

Table 6.2 continued

Jurisdiction	Legislation	Key restrictions	Review activity	Reform activity	Assessment
Northern Territory	Electricity Act		Act reviewed as part of a broad review of the Power and Water Authority, and under a departmental review.	Act repealed and replaced by the Electricity Reform Act, the Electricity Networks (Third Party Access) Act and the Utilities Commission Act.	Meets CPA obligations (June 2001)
Northern Territory (continued)	Power and Water Authority Act		Review completed.	Act was replaced by the Power and Water Corporations Act from 1 July 2002. All electricity-related amendments made except for the removal of GOC's local government rate exemption (s.19). There is no specific timetable for repeal of s.19. GOC to continue to pay local government rate equivalents through the Territory's Tax Equivalent Regime until complexities regarding the existing local governments funding arrangements are resolved. GOC began paying local government rate equivalents on 1 July 2001.	Does not meet CPA obligations (June 2004)