Australian Energy Market Commission

Draft Rule Determination

Obligations of Network Service Providers (Connection Applications)

Rule Proponent
Energy Solutions Australia Pty Ltd

15 February 2007

Signed: .....

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Chairman
For and on behalf of
Australian Energy Market Commission

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AEMC 2007, *Obligations of Network Service Providers (Connection Applications),* Draft Rule Determination, 1 February 2007, Sydney.

About the AEMC

The Council of Australian Governments, through its Ministerial Council on Energy, established the Australian Energy Market Commission (AEMC) in July 2005 to be the Rule maker for national energy market. The AEMC is currently responsible for Rules and policy advice covering the National Electricity Market. It is a statutory authority. Our key responsibilities are to consider Rule change proposals, conduct energy market reviews and provide policy advice to the Ministerial Council as requested, or on the AEMC's initiative.

Contents

1. Summary

On 14 July 2006, the Australian Energy Market Commission ("the Commission") received a Rule change proposal from Energy Solutions Australia Pty Ltd ("Energy Solutions"). The proposal sought to oblige network service providers to establish comprehensive contact information registers of contestable service providers and connection applicants for distribution to certain parties.

In accordance with section 99 of the National Electricity Law ("NEL") the Commission has made this draft Rule determination outlining the reasons for its draft decision not to make the proposed Rule. For the purposes of the draft Rule determination, the Commission has not been satisfied that the proposed Rule will or is likely to contribute to the achievement of the national electricity market objective as required by the Rule making test specified in section 88 of the NEL. This draft Rule determination sets out the reasons for the Commission's decision.

The Rule proposed by Energy Solutions contemplated amending clauses 5.2.3 and 5.3.3 of the Rules. The proposed Rule would have imposed additional obligations on network service providers to:

1. Maintain a register of parties (name and contact details) who had advised the network service provider that they were able to provide contestable services including the contestable construction of, and the ownership and operation of related distribution and/or transmission network infrastructure.
2. Subject to the consent of the connection applicant, register the applicant's contact details and make them available to the parties registered to provide contestable services.
3. Distribute the register of contestable service providers to connection applicants (within ten days after the receipt of a connection enquiry).

Energy Solutions contended that incumbent network service providers presently enjoy a competitive advantage in the provision of contestable network services by virtue of their unique position, which is not available to other competitors. Specifically, since a party wishing to establish a connection must first contact the relevant incumbent provider, it is privy to information regarding potential commercial opportunities that other providers may not be. This was said to result in an "uneven playing field", to the detriment of other contestable network service providers.

The proposed amendments to the Rules were viewed by Energy Solutions as a means of reducing this informational advantage and the perceived associated competitive disadvantage. It reasoned that increasing the availability of information by establishing publicly available registers administered by incumbent providers would deliver benefits by invigorating competition in the market for contestable network services, thereby advancing the national electricity market objective.

During the consultation period, the Commission received sixteen submissions, the majority of which did not support the Rule change proposed by Energy Solutions. In reaching its draft decision the Commission gave careful consideration to the arguments

put forward in submissions, and undertook its own analysis where appropriate. Under the rule making test contained in section 88 of the NEL, the Commission must be satisfied that the proposed Rule will or is likely to contribute to the achievement of the national electricity market objective, namely:

> *"The national electricity market objective is to promote efficient investment in, and efficient use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system."*

In assessing the Rule proposal against this objective, the Commission has reached the following conclusions:

- there is currently insufficient evidence that the identified informational advantage represents a significant impediment to competition to warrant the imposition of the proposed Rule requirements on network service providers;
- there is currently insufficient evidence to support the claim that the proposed Rule will *enhance* competition for contestable network services;
- numerous firms registered on jurisdictional websites are ostensibly ready and able to provide contestable network services, thus competitors clearly exist and appear to be vying with incumbent providers in spite of the identified information advantage;
- many of the concerns expressed by the proponent and in submissions about the potential competitive advantage of the incumbent network service provider are removed through clause 5.3.3(b)(3) of the Rules, which requires network service providers to inform connection applicants when a service is contestable, particularly considering that:
  - the customers seeking to connect to a network – particularly the transmission network – will very often by large and well-resourced corporations well versed in such matters;
  - the proposed Rule would, in some cases, appear to needlessly duplicate information that is *already provided* in many state jurisdictions – particularly as it relates to contestable distribution connection works; and
  - the various state-based licensing arrangements would presumably result in a relatively small number of readily identifiable prospective service providers offering to contest the *ownership and operation* of network infrastructure (as distinct from its construction), reducing any informational advantage as it relates to these services;
- the proposed Rule is likely to impose significant regulatory and administrative costs on network service providers that will be required to construct and maintain comprehensive registers, with no obvious offsetting benefits;
- the potential accreditation and legal costs that would confront incumbent network service providers will likely be considerable;
- the proposal appears to entail a significant element of duplicity that impinges on existing jurisdictional arrangements, which may needlessly inflate costs and cause unnecessary confusion and uncertainty;

- the administrative role contemplated by the proponent is not one that should appropriately be assigned to incumbent network service providers; and
- the additional costs associated with the proposed Rule may inefficiently impact on network users through higher network service charges in a non-transparent fashion.

The Commission is therefore not satisfied that the potential benefits of the proposed Rule change would outweigh the potential costs associated with the scheme. Accordingly, the Commission's draft decision is that the Rule proposed by the proponent is unlikely to contribute to the national electricity market objective, as required by law. On this basis, and in accordance with section 99 of the NEL, the Commission's draft decision is to not make the proposed Rule. The remainder of the draft Rule determination outlines the Commission's reasons for its draft decision in detail.

The Commission welcomes submissions on its draft Rule determination. The closing date for submissions is **30 March 2007.**

The Commission requests that all submissions lodged be signed by the person making the submission or, if the submission is from an entity, by an authorised representative of the submitting entity.

An original signed hard copy of the submission must be sent to:

Australian Energy Market Commission
PO Box H166
Australia Square NSW 1215

A copy of the signed submission may also be sent electronically to submissions@aemc.gov.au or by fax to (02) 8296 7899. Submissions received by the Commission in any other manner, or after the closing date, will be considered at the Commission's discretion.

Under section 101 of the NEL, any interested person or body may request that the AEMC hold a pre-determination hearing in relation to the draft Rule determination. Any request must be made in writing and received by **22 February 2007.**

2. Energy Solutions' Rule proposal

On 14 July 2006, the Australian Energy Market Commission ("the Commission") received a Rule change proposal from Energy Solutions Australia Pty Ltd ("Energy Solutions"). The proposal sought to broaden the obligations placed on network service providers in relation to connection applications involving the provision of contestable services. If implemented, it would require incumbent network service providers to establish comprehensive contact information registers of contestable service providers and connection applicants for distribution to certain parties.

The proponent made two subsequent submissions elaborating on certain aspects of the initial proposal and issues raised by other respondents.[1] This section contains a summary of the proposed Rule change and the supporting arguments presented by Energy Solutions.

2.1. Summary of the Rule proposal

Chapter 5 of the Rules contains a framework for facilitating connection to transmission and distribution networks. A party wishing to connect must, in the first instance, lodge a connection enquiry with the relevant incumbent network owner. Clause 5.3.3 places a number of obligations on network service providers responding to a connection enquiry. Of principal importance for present purposes is the obligation to inform a connection applicant if any requested service is contestable in the relevant participating jurisdiction.[2] In the Rules, the term contestable is defined as:[3]

> *"a service which is permitted by the laws of the relevant participating jurisdiction to be provided by more than one Network Service Provider as a contestable service or on a competitive basis".*

Energy Solutions maintained that since a party wishing to establish a connection must first contact the relevant incumbent provider, it is privy to information regarding potential commercial opportunities that other providers may not be. Chapter 5 of the Rules was therefore argued to bestow a competitive advantage upon incumbent network service providers, resulting in an "uneven playing field". Energy Solutions argued that incumbent network owners enjoyed the following competitive advantages in the provision of contestable network services:

- Strategic value and availability of information: *"The incumbent owner has information (regarding potential commercial opportunities) that has been obtained from its unique position, and which is not likely to be available to the competitive market as a whole".*[4]
- Identity of applicants: *"The incumbent network owners have a competitive advantage through knowing the identity of potential customers (i.e. Connection Applicants)*

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1 Energy Solutions Australia, Submissions, 8 August 2006 and 13 October 2006.
2 National Electricity Rules, Version 12, Clause 5.3.3(b)(3).
3 National Electricity Rules, Version 12, Chapter 10, page 786.
4 Energy Solutions Australia, Rule Proposal, 14 July 2006, page 4.

whereas providers of contestable services are required to identify these potential customers through their own devices and at their own cost".[5]

- Costs associated with obtaining information: *"The new entrant may need to expend considerable resources just to identify potential customers. In contrast, the incumbent will have to have obtained that information at little or no cost".*[6]
- Timeliness of information: *"The new entrant is at a competitive disadvantage even when it finally identifies the potential customer. That is because of the time delay associated with that process. In a worst case scenario the customer may have already contracted with the incumbent network owner".*[7]
- Easier to contract with incumbent: *"Connection Applicants are faced with the issue of identifying (often unknown) competing service providers at the same time that they are required to deal with a myriad of other (often complex) issues. In that situation the easiest solution is for the Connection Applicant to simply contract with the incumbent network owner".*[8]

The proposed Rule change consequently sought to expand the obligations placed on incumbent network service providers by Chapter 5 with a view to reducing the identified information advantage and the perceived associated competitive disadvantage. Specifically, the proposed Rule sought to amend clauses 5.2.3 and 5.3.3 by requiring network service providers to:

1. Maintain a register of parties (name and contact details) who had advised the network service provider that they were able to provide contestable services including the contestable construction of, and the ownership and operation of related distribution and/or transmission network infrastructure.
2. Subject to the consent of the connection applicant, register the applicant's contact details and make them available to the parties registered to provide contestable services.
3. Distribute the register of contestable service providers to connection applicants (within ten days after the receipt of a connection enquiry).

Energy Solutions claimed that establishing publicly available registers would deliver benefits through an enhancement of competition in the market for contestable network services, furthering the national electricity market objective. Energy Solutions foresaw benefits to connection applicants such as:[9]

- potential for innovation;
- freedom of choice;
- potential for lower prices;
- greater variety in the scope of services offered; and
- greater flexibility in the commercial terms and conditions.

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5 Ibid, page 4.
6 Energy Solutions Australia, Submission, 8 August 2006, page 2.
7 Ibid.
8 Energy Solutions Australia, op cit, page 4.
9 Energy Solutions Australia, 8 August 2006, page 2.

In sum, Energy Solutions claimed that the proposed Rule would contribute to the achievement of the national electricity market objective through:[10]

- the promotion of efficient investment in electricity services;
- improved incentives for efficient network investment and for competitive supply of network services;
- reduction in the potential exercise of market power in the provision of network services by the incumbent network owners; and
- greater scope for the provision of contestable services.

The Commission's assessment of Energy Solutions' proposal is presented in section 4 of this draft Rule determination.

2.2. Request to expedite

In its initial proposal, Energy Solutions requested that the Commission treat the proposed Rule change as non-controversial and therefore eligible for expedition under section 96 of the NEL. The proponent did not explain why it considered the Rule proposal was non-controversial.

To be expedited on the grounds that it is non-controversial, a proposed Rule change must be "unlikely to have a significant effect on the national electricity market", ie must be considered non-significant in its effect on the National Electricity Market as a whole. Powerlink[11] and EnergyAustralia[12] argued that the proposed Rule change would have a significant impact on market participants. Accordingly, each submitted that Energy Solutions' request that the proposal be treated as non-controversial should be rejected. Powerlink stated in its submission[13]:

> *"The proposed Rule would require Network Service Providers to establish and maintain a new register of parties claiming to provide contestable services. This is a new obligation that does not currently exist in any form. Powerlink believes that a proposed Rule which imposes a new obligation on parties, and which has been submitted to the Commission without prior consultation with all of the affected parties should not be considered non-controversial".*

The Commission's analysis supported the contention by EnergyAustralia and Powerlink that the proposed Rule change could significantly impact market participants. If implemented, the Rule would impose new and significantly wider obligations on network service providers with regards to processing connection applications. Accordingly, the Commission concluded that the proposed Rule change was not non-controversial and elected not to expedite the process.

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10 Energy Solutions Australia, 14 July 2006, page 5.
11 Powerlink, Submission, 27 July 2006.
12 EnergyAustralia, Submission, 18 August 2006.
13 Powerlink, Submission, 27 July 2006.

3. Draft Rule Determination

In accordance with section 99 of the NEL, the Commission's draft decision is to not make the proposed Rule. On balance, the Commission is not satisfied that, under section 88 of the NEL, the Rule proposed by Energy Solutions will or is likely to contribute to the achievement of the national electricity market objective and therefore does not satisfy the Rule making test. In making this draft Rule determination, the Commission has taken into account:

- its powers under the NEL to make the proposed Rule;
- submissions received; and
- the national electricity market objective and statutory Rule making test.

Each of these matters is discussed below. A detailed discussion of the Commission's reasons for the draft Rule determination is provided in section 4.

3.1. Commission's power to make the Rule

The Commission is satisfied that the subject matter of the proposed Rule falls within the Commission's Rule making powers as set out in section 34 of the NEL. Specifically, clause 34(1)(c) of the NEL states that the Commission may make Rules for or with respect to regulating:

> *"the activities of persons (including registered participants) participating in the national electricity market or involved in the operation of the national electricity system".*

In its initial submission, EnergyAustralia claimed that the proposal inappropriately impinged upon jurisdictional contestability arrangements. It questioned the powers of the Commission to consider the proposed Rule, opining that:[14]

> "*Whilst section 34 of the NEL confers a broad jurisdiction upon the AEMC, a rule of this nature must relate to the operation of the wholesale market and the networks which form the national electricity system. The rule goes beyond operational matters and beyond that required to facilitate access to the networks and extends into the operation of a competitive market for contestable services."*

As outlined in section 2.1 above, contestable services are defined in the Rules as those services that have been deemed by jurisdictional arrangements to be provided on a competitive basis. A corollary of this classification is that any monopoly status is removed for those particular services, thereby exposing them to prospective competition. However, whilst the proposal relates to services for which formal price regulation does not apply, it will nonetheless significantly impact "the activities of persons participating in the national electricity market", particularly incumbent network service providers.

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[14] EnergyAustralia, Submission, 18 August, page 2.

Incumbent network service providers have an existing obligation under the Rules to inform connection applicants whether a service being sought is contestable.[15] The proposal by Energy Solutions sought to broaden this obligation to include the compilation and administration of contact registers for distribution to certain parties. When considered in this light, the Commission believes that the proposal effectively constitutes an extension to the current information obligations under the Rules. It is therefore satisfied that the subject matter of the proposed Rule falls within the scope of section 34 of the NEL, and thus the Commission's Rule making powers.

3.2. Assessment against the national electricity market objective

Under the Rule making test in the NEL, the Commission must be satisfied that the proposed Rule will or is likely to contribute to the enhancement of the national electricity market objective. The national electricity market objective contained in section 7 of the NEL states:

> *"The national electricity market objective is to promote efficient investment in, and efficient use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system."*

The Rule making test is contained in section 88 of the NEL, and states:

> *"(1) The AEMC may only make a Rule if it is satisfied that the Rule will or is likely to contribute to the achievement of the national electricity market objective".*
>
> *"(2) For the purposes of subsection (1), the AEMC may give such weight to any aspect of the national electricity market objective as it considers appropriate in all the circumstances, having regard to any relevant MCE statement of policy principles".*

Energy Solutions' proposed Rule change sought to promote competition in the provision of contestable services by alleviating an information advantage perceived to favour incumbent network service providers. It reasoned that incumbent providers are presently unfairly advantaged since they are oftentimes privy to information regarding potential commercial opportunities that other providers may not be. It considered that its proposed Rule change would deliver benefits by "levelling the playing field", allowing contestable providers to compete more effectively and thereby advancing the national electricity market objective.

The Commission wholeheartedly supports the promotion of competition in energy markets. Indeed, in its recent review of the Rules relating to the economic regulation of transmission revenues the Commission sought to introduce competition wherever market circumstances allowed, and took steps to roll back prescriptive regulation wherever feasible.[16] However, before the Commission can conclude that a Rule will indeed promote competition and potentially further the national electricity market objective, it must be satisfied that:

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15 National Electricity Rules, Version 12, Clause 5.3.3(b)(3).

16 Australian Energy Market Commission, 2006, Rule Determination, National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 No. 18.

- a significant and sustained market failure has been identified that warrants regulatory intervention, eg, an ostensible hindrance to competition;
- the proposed Rule change will deliver benefits by addressing the identified market failure, eg, through the promotion of competition; and
- the potential costs associated with the proposed Rule change do not outweigh the deliverable benefits.

On the basis of the information provided in submissions, and its own analysis, the Commission is not satisfied that the proposed Rule change meets these fundamental criteria.

First, the Commission is not persuaded that the Rule change proposal submitted by Energy Solutions identifies a significant market distortion that warrants regulatory intervention. Neither the proponent nor the submissions provided cogent evidence that the present provision contained in clause 5.3.3(b)(3) of the Rules is inadequate. No submission demonstrated to the Commission's satisfaction that alternative providers are disadvantaged to such an extent that they are unable to compete effectively with incumbent providers for custom. Moreover, several factors suggest that the extent of the informational advantage - and thus the impact on competition – is likely to be minimal, including:

- the customers seeking to connect to a network – particularly the transmission network – will very often be large and well-resourced corporations well versed in such matters;
- the proposed Rule would, in some cases, appear to duplicate information that is *already provided* in many state jurisdictions;
- a large number of firms registered on various jurisdictional websites are ostensibly ready and able to provide contestable network services, and evidence exists that competition is occurring; and
- the various state-based licensing arrangements would presumably result in a relatively small number of readily identifiable prospective service providers offering to contest the *ownership and operation* of network infrastructure (as distinct from construction), reducing any asymmetry as it relates to these services.

The Commission is consequently not satisfied that a demonstrable market benefit exists. An important part of the competitive process is buyers searching and competitors undertaking marketing and similar activities to attract custom. The mere fact that it may be more difficult for alternative service providers to identify prospective customers (and vice versa) does not in itself justify a Rule change – there must be evidence that this difficulty is *inhibiting effective competition*. For the reasons outlined above, the Commission is not convinced that there is evidence of an ostensible market failure in this regard.

Second, the Commission has reached the view that the proposed Rule change is likely to entail significant additional costs. The administration of potentially heavily populated proposed registers will likely be an onerous, costly task for incumbent network service providers that will divert significant organisational resources. The proposed Rule

would also duplicate a number of other arrangements *already in place* in other jurisdictions. Moreover, were such a scheme to be implemented, a more efficient approach would seem to be for a *single independent body* to maintain a *single* register. Indeed, the Commission considers that it would be inappropriate for network service providers to assume responsibility for the mooted registers, particularly in light of the potential accreditation and legal liability issues created.

On balance, the Commission therefore considers that the potential costs of the scheme contemplated by the proposed Rule change would significantly outweigh any potential benefits it may deliver in the market for contestable network services. Accordingly, on the strength of the arguments set out in submissions and its own analysis, the Commission is not satisfied that, under section 88 of the NEL, the Rule proposed by Energy Solutions will or is likely to contribute to the achievement of the national electricity market objective. Its draft decision is therefore to not make the proposed Rule.

A more detailed assessment of the Energy Solutions' proposal is presented in section 4 of this draft Rule determination.

3.3. Consultation

Energy Solutions Australia submitted its Rule change proposal on 14 July 2006 and lodged supplementary submissions on 8 August 2006 and 13 October 2006. [17]

During the preliminary assessment stage the Commission received four submissions from other parties. Submissions from Bovis Lend Lease and AGL Hydro lent support to the arguments presented by the proponent. Conversely, a submission received from EnergyAustralia opposed the proposed Rule change and the request for expedition. A submission from Powerlink also disagreed that the proposal was non-controversial and opposed the request for expedition.

A section 95 notice was published on 14 September 2006, with submissions due on or before 16 October 2006. In total, sixteen submissions were received, the majority of which opposed Energy Solutions' proposed Rule change. Several submissions stated that even if the Commission did see merit in Energy Solutions proposal, in practice, network service providers were inappropriate bodies to administer the type of registers contemplated in the proposal. Other submissions gave qualified support to the proposal provided the scheme was not too onerous.[18]

There was no request for a public hearing.

The following respondents lodged submissions in relation to Energy Solutions' proposed Rule change:

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17 Energy Solutions' most recent submission clarified that its proposal was intended to encompass the situation where a party other than an incumbent network owner took *ownership* of connection works (see: Energy Solutions Australia, Submission, 13 October 2006). Whilst its proposal does cover this scenario, it clearly also includes – intentionally or otherwise - the contestable *construction* of related distribution and/or transmission network infrastructure.

18 AGL Hydro, Submission, 31 August, 2006; Origin Energy, Submission, 23 October 2006.

- Powerlink (27 July 2006);
- Energy Solutions Australia (8 August 2006 and 13 October);
- EnergyAustralia (18 August 2006 and October 2006);
- Bovis Lend Lease (29 August 2006);
- AGL Hydro (31 August 2006);
- AGL Electricity (Distribution) (16 October 2006);
- Country Energy (16 October 2006);
- Electricity Transmission Network Owners Forum (16 October 2006);
- Energy Networks Association (16 October 2006);
- Electricity and Water Ombudsman of NSW (16 October 2006);
- Integral Energy (16 October 2006);
- Metropolis Metering Assets (16 October 2006);
- Origin Energy (23 October 2006); and
- Victorian Energy Networks Corporation (VENCorp) (16 October 2006).

Section 107 notices were published by the Commission on 7 December 2006, 21 December 2006 and 1 February 2007 extending the period for assessment of the proposal by the Commission. These extensions allowed the Commission to complete a comprehensive assessment of the complex issues raised in the proposal and submissions.

4. Commission's analysis

The Rule proposed by Energy Solutions sought to extend the obligations placed on incumbent network service providers by requiring the establishment and maintenance of contact information registers of contestable service providers and connection applicants. As such, its implementation would place significant further requirements on incumbent network service providers.

It is generally accepted that the best way to maximise economic benefits for society is through the operation of competitive markets. For this reason, regulation should only be applied where a demonstrable and sustained market failure has been identified. Moreover, any intervention should be the minimum necessary to address the identified market distortion. Finally, regulation must necessarily bestow benefits that outweigh the associated regulatory costs. Accordingly, in analysing the proposed Rule, the Commission has examined:

1. the potential *benefits* of the proposal, including the nature and extent of the perceived market failure the proposal is intended to address; and
2. the potential additional *costs* to network service providers and network customers, including:
    a. the extent of duplication of existing jurisdictional arrangements; and
    b. the administrative practicability of network service providers establishing and maintaining contact information registers.

The remainder of this section presents the Commission's detailed analysis and conclusions in relation to each of these issues. In undertaking its analysis, the Commission has carefully considered the issues identified by the proponent, and by respondents in submissions.

4.1. Potential benefits of the proposed Rule

Energy Solutions contended that incumbent network service providers enjoy a strategic advantage with respect to the provision of contestable services by virtue of favourable access to customer information. Specifically, since a party wishing to establish a connection must first contact the relevant incumbent provider, it is privy to information regarding potential commercial opportunities that other providers may not be. This was said to be of key strategic value, resulting in an "uneven playing field", to the detriment of other contestable network service providers.

The primary source of economic benefits was said to stem from a reduction in this informational advantage.[19] The central premise of the proposal was that the Rules as

[19] The complexity of connection services typically sought was said to provide a further incentive for connection applicants to contract with incumbent providers. Specifically, since connection applicants must identify alternative providers whilst simultaneously dealing with myriad other complex issues, the "easiest solution" is claimed to be to contract with the incumbent. However, assuming that is indeed the case, it is not obvious how the proposed Rule change is intended to address this issue, if indeed it is addressable at all – contracting

presently formulated significantly hinder connection applicants and alternative service providers from meeting and interacting in the marketplace. Improving the availability of information regarding the identity of contestable service providers and connection applicants was therefore thought to be capable of alleviating this difficulty. In turn, this was expected to promote competition in the market for contestable network services and advance the national electricity market objective.

4.1.1. Submissions

The Commission was interested in gauging from respondents, and in particular from contestable service providers, the extent of the supposed market failure and its impact on the market in which contestable services are provided. Four submissions identified with the perceived problem highlighted by Energy Solutions.

- Bovis Lend Lease stated that it was interested in opportunities to build, own and operate both transmission and distribution network services. However, it argued that incumbent network owners had information not generally available to the market, regarding the identity of parties who required contestable services. It stated that the issues raised by the Energy Solutions were "real and substantive" and inhibited the competitive provision of contestable services.[20]
- AGL Hydro indicated that contracting with providers other than the incumbent was difficult due to both a lack of service providers and the difficulty of interfacing contestable works with existing assets of the incumbent. It stated that it had encountered a wide range of experiences when dealing with incumbent providers, ranging from "excellent support" to "take it or leave it" offers. It also considered the issues raised by Energy Solutions were "real and substantive".[21]
- Origin Energy outlined that its experiences in negotiating the connection of generation assets had been "generally satisfactory". It agreed that there was an informational advantage that favoured incumbents and that the negotiation process can be "one-sided" due to a lack of alternative service providers.[22] The submission highlighted that since the Rules already require an incumbent to advise an applicant whether a service is contestable, there is a "natural incentive to seek out any alternative service provider in order to obtain a better deal". It saw the key issue as being whether the applicant can easily identify and contact alternative providers.[23]
- Metropolis Metering Assets concurred with the assessment of Energy Solutions that under the Rules incumbent network owners are provided with a competitive advantage.[24]

However, a number of other submissions did not support the proposed Rule change and saw little obtainable benefit through its implementation.

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with the incumbent will likely always be the "easiest solution" irrespective of whether a register is provided.

20 Bovis Lend Lease, Submission, 29 August 2006.

21 AGL Hydro, Submission, 31 August 2006.

22 It is unclear from Origin's submission whether this lack of options was *absolute* or merely *perceived* due to a lack of information surrounding potential alternative service providers.

23 Origin Energy, Submission, 23 October 2006.

24 Metropolis Metering Assets, Submission, 16 October 2006.

- Integral Energy considered that information asymmetry would not be substantially addressed through the provision of names and contact details of service providers. It considered that this information would be imperfect as connection applicants would continue to incur costs in seeking the particulars and detailed costs of service provision.[25]
- The Electricity Transmission Network Owners Forum ("ETNOF") opined that the types of customers that usually sought connection to the transmission network were substantial developers. As such, those types of customers could generally be considered to have the resources and know-how to be able to source engineering and other services and apply considerable countervailing negotiating power.[26]
- The Energy Networks Association ("ENA") considered that there was no competitive benefit to be derived from the proposed Rule change. It stated that the provision of connection services is a competitive industry and it is ultimately the choice of the customer how much she/he wants to test the competitiveness of connection services. It expressed the view that incumbent service providers should not be forced to undertake an agency relationship on behalf of their competitors. It thought the proposal would likely result in less innovation and less effective competition in the market.[27]
- AGL Electricity ("AGLE") similarly indicated that, in its view, the proposed Rule change would likely have the effect of reducing competition in the market for contestable services relative to existing arrangements.[28]

Finally, a number of submissions agreed with the *general sentiment* of the proposed Rule change, but disagreed with the proposed method of implementation. In particular, a number of proposals that believed a Rule change might deliver benefits indicated that it would nonetheless be inappropriate for incumbent network service providers to maintain registers in the manner contemplated by the proposal.[29]

4.1.2. Commission's assessment

The Commission is not persuaded that the Rule change proposal submitted by Energy Solutions identifies a significant market distortion that warrants regulatory intervention. Whilst the Commission agrees that the Rules currently bestow a favourable information advantage on incumbent providers, it is not currently convinced that this advantage represents a significant impediment to competition. In the Commission's view, neither the proponent nor the submissions provide cogent evidence that the present provision in the Rules is inadequate.

Clause 5.3.3(b)(3) *already* requires an incumbent to inform an applicant when a service is contestable. This clearly reduces the potential competitive advantage of the incumbent

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25 Integral Energy, Submission, 16 October 2006.
26 ETNOF, Submission, 16 October 2006.
27 ENA Submission, 16 October 2006.
28 AGLE, Submission, 16 October 2006.
29 See: Energy & Water Ombudsman NSW, Submission, 16 October 2006; Origin Energy, Submission, 23 October 2006; VENCorp, Submission, 16 October 2006. Those submissions *opposing* the Rule proposal expressed similar sentiments. See further discussion in section 4.2.1 below.

network service provider and creates an obvious incentive for customers to seek out alternative service providers in search of a better deal. Whilst two connection customers indicated in submissions that they had nonetheless "experienced difficulties" negotiating connections with incumbent network service providers, neither indicated they were unaware of the existence of alternative providers, or unable to locate them.[30]

More generally, no submission demonstrated to the Commission's satisfaction that alternative providers are disadvantaged to such an extent that they are unable to compete effectively with incumbent providers for custom. In fact, several factors – most of which were raised in respondents' submissions - suggest that the extent of the informational advantage (and thus the impact on competition) is likely to be minimal, including:

- The customers seeking to connect to a network – particularly the transmission network – will very often be large and well-resourced corporations well versed in such matters. As ETNOF highlighted in its submission, such parties would likely not need the Rules to be augmented to ensure adequate rivalry for their business.[31]
- The proposed Rule would, in some cases, appear to needlessly duplicate information that is *already provided* in some state jurisdictions – particularly as it relates to contestable distribution connection works. The incremental benefit of replicating publicly available information is likely to be minimal at best whilst unnecessarily inflating costs.[32]
- A large number of firms registered on jurisdictional websites are ostensibly ready and able to provide contestable network services, thus competitors clearly exist and appear to be vying with incumbent providers in spite of the identified information advantage. The Commission notes, for example that:
  - there are several hundred accredited service providers listed on the NSW Department of Energy, Utilities and Sustainability ("DEUS") register;[33]
  - in 2005 in South Australia, 25% of all contestable underground residential development work was undertaken by distribution service providers other than the incumbent, ETSA Utilities;[34] and
  - in NSW a large proportion of customer connection work is performed by parties other than the incumbent network provider, for example in the 2006/06 financial year EnergyAustralia undertook only 13% of new connection work internally,[35] and Integral Energy undertook less than 1% of new connection works on its network.[36]

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30 Origin Energy, ibid, AGL Hydro, ibid.

31 ETNOF, Submission, 16 October 2006, page 4.

32 The *cost* impact of the duplicative aspect of the proposed Rule change is elaborated upon in section 4.2.2 below.

33 See: http://www.deus.nsw.gov.au.

34 ESCOSA, *Discussion Paper: Contestable Augmentation of the Distribution Network,* June 2005, page 8.

35 EnergyAustralia Network Performance Report 2005/06, 31 October 2006, page 11.

36 Integral Energy Network Performance Report 2005/06, 31 October 2006, page14.

- The various state-based licensing arrangements would presumably result in a relatively small number of readily identifiable prospective service providers offering to contest the *ownership and operation* of network infrastructure (as distinct from its construction). This would likely result in few, if any information asymmetries for these particular contestable distribution or transmission connection services.

On balance, the Commission is neither satisfied that a demonstrable market benefit exists, nor persuaded that the identified informational advantage represents a problem requiring regulatory intervention. An important part of the competitive process is buyer's searching and competitors undertaking marketing and similar activities to attract custom. The mere fact that it may be "more difficult" for alternative service providers to identify prospective customers (and vice versa) does not in itself justify a Rule change – there must be evidence that this difficulty is *inhibiting effective competition*.

The Commission has been presented no compelling evidence that competition is currently being stifled, whilst several other factors suggest the impact on competition is likely to be minimal. In the absence of self-evident economic benefits, the Commission considers it unnecessary and inappropriate to require the costly diversion of resources of incumbent network businesses to the managerial and administrative requirements of registers. The following section elaborates further upon the likely costs intrinsic to the proposed Rule change.

4.2. Potential costs of the proposed Rule

The Rule change proposed by Energy Solutions clearly entails a number of additional costs. The establishment and maintenance of contact information registers is itself a costly exercise that will divert significant organisational resources, particularly staff. However, in the longer term a more significant cost may well be managing the potential legal liabilities that may arise from administering such lists. Fundamental issues also surround the efficiency of the proposed arrangements from an administrative standpoint and the novelty of the registers themselves.

4.2.1. Submissions

The majority of submissions did *not* support the proposed Rule in the form presented by Energy Solutions. A fundamental concern expressed by opponents to the proposal was the potential cost burden imposed on network service providers charged with establishing and administering the scheme.

- Integral Energy stated that the maintenance of the proposed registers would add to the administrative cost to network service providers, which would ultimately passed on to consumers. It added that network service providers would also incur higher risks from increased legal exposure.[37]
- ENA identified a number of additional costs that it believed would result from implementing the proposed Rule change.[38] It claimed that these additional costs inherent in such a scheme would be significant and ultimately borne by all electricity consumers, effectively resulting in: "*the smearing of the cost of a*

[37] Integral Energy, Submission, 16 October 2006, page 2.
[38] ENA, Submission, 16 October 2006, page 2.

marketing function for a contestable service in a non-transparent and inefficient manner across all network users". These costs were said to far outweigh any potential benefit.[39]

- AGLE outlined similar reservations regarding the respective costs and benefits of the proposed change. In gauging the likely cost of the scheme, it indicated that the expected number of connection applications in a year would, in its view, be considerable and the number of contractors to be accredited by the network service provider for which accreditation will need to be maintained would also "not be small".[40]

Another consistent sentiment expressed by many respondents was that network service providers are inappropriate bodies to administer the type of scheme proposed by Energy Solutions.[41] A common argument was that it would amount to incumbent providers carrying out a marketing role and/or effectively discharging a regulatory function. The Commission was also warned of likely attribution issues and the potential liability risk faced by network service providers for third party damages.

- ETNOF expressed the view that the proposal would amount to forcing a network service provider to become a forum for the marketing of the services of other parties. A further concern was that the maintenance of the registers could carry the implication that the network service providers were endorsing the contestable service providers as being capable of performing these services. ETNOF claimed that network service providers would have neither the knowledge nor the capacity to acquire that knowledge. In its view, any such register should properly incorporate a certification and auditing process. However, it did not consider these to be appropriate functions for a network service provider.[42]
- ENA similarly maintained that the proposal would require network service providers to act as managers and administrators of a contestable services scheme. ENA also stated that it was not clear from the proposal how the network businesses were to ascertain whether the contestable service providers would have the requisite skills and experience for performing any type of connection work.[43]
- EnergyAustralia likewise claimed that it would be inappropriate for network service providers to be responsible for administering a scheme that "facilitates a competitive market for contestable services".[44] It also highlighted a number of other concerns, including:
    - since the incumbent providers themselves would most likely be on such registers, a perception of preferential treatment may be created;

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39 ENA, op cit, page 3.
40 AGL Electricity, Submission 16 October 2006.
41 EWON, Submission, 16 October 2006; Country Energy, Submission, 16 October 2006; AGL Electricity, Submission, 16 October 2006; ETNOF, Submission, 16 October 2006; EnergyAustralia, Submission, October 2006, VENCorp, Submission, 16 October, 2006; ENA, Submission, 16 October.
42 ETNOF, op cit.
43 Energy Networks Association, ibid.
44 EnergyAustralia, Submission, 18 August 2006.

- in situations where errors occurred in the register details, or where an alternative provider had not received many referrals from the list, allegations of competitive misconduct may arise; and
- the proposal has a potentially wide ambit that could cover all changes to transmission and distribution connections and potentially capture works ranging from the construction of a transmission line through to the installation of a three phase air conditioner in a domestic residence, or any other residential works where the meter box is modified.

In its view, the culmination of these factors rendered it "totally inappropriate" for such an obligation to be imposed on network service providers.[45]

- The Electricity & Water Ombudsman of NSW ("EWON") expressed similar concerns, noting that if providers were required to manage such lists there would be unnecessary potential for administrative error or failure, which might disadvantage consumers.[46]
- VENCorp did not support the proposed Rule change in its present form on the grounds that it would place network service providers at risk of legal liabilities and damages. It indicated that this might occur if, for example, a third party sustained damages as a result of relying on a list provided by the network service provider.[47]
- Even Origin Energy whilst ostensibly supporting the proposal, questioned whether there was a solution that would be less onerous on incumbent network service providers and "thus more practical and acceptable to all parties".[48]

A number of respondents queried the *efficiency* of the proposed scheme and in particular, the *novelty* of the mooted registers. Many respondents thought that the proposed Rule would, in some cases, needlessly duplicate arrangements already in place in other jurisdictions, unnecessarily inflating costs.

- AGLE provided a high level summary of jurisdictional arrangements presently in situ in New South Wales, Victoria, South Australia and Queensland that it claimed would provide for more effective competition for connection services than the proposed Rule. Citing this overlap, it claimed the proposed Rule would lead to unnecessary costs and confusion for customers seeking to connect.[49]
- Integral Energy stated that the proposed Rule change failed to recognise existing NEM jurisdictional arrangements for accreditation of service providers of contestable services and the institutional processes to accommodate them.[50]
- EWON referred the Commission to the jurisdictional arrangements in place in New South Wales for the competitive provision of contestable services facilitated by the Department of Energy, Utilities and Sustainability ("DEUS").[51]

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45 EnergyAustralia, Submission, October 2006.
46 EWON, Submission, 16 October 2006, page 1.
47 VENCorp, Submission, 16 October 2006.
48 Origin Energy, Submission, 23 October 2006.
49 AGL Electricity, Submission, 16 October 2006, page 1.
50 Integral Energy, Submission, 16 October 2006, page 2.
51 EWON, Submission, 16 October 2006, page 1.

- Country Energy opined that the proposed Rule change would create duplication in the market, which it considered to be an "undesirable and unnecessary outcome" that would lead to increased costs, inefficiencies and disputes. It also referred the Commission to the jurisdictional arrangements in place in New South Wales facilitated by DEUS.[52]

A number of respondents argued that in addition to overlapping with *existing arrangements*, the newly created registers would overlap *with each other*. Since every network service provider would be required to maintain a register of contestable service providers, it was claimed that multiple contestable service providers would naturally seek to register with multiple network service providers. The result, it was argued, would be duplicative and wasteful. Submissions lodged by ENA, ETNOF, Country Energy, EnergyAustralia and AGLE argued that the proposed scheme would be inefficient in this respect.

For this reason, a number of respondents argued that if the Commission nonetheless saw merit in the proposed scheme that a more efficient approach would be for a *single independent body* to maintain a *single register*.[53] A central list was thought to provide the distinct advantage of consistency for consumers and providers alike. In contrast, no submission expressly concluded that a network service provider is an appropriate custodian of such a list. Submissions elaborated that more appropriate bodies might include NEMMCO[54], the ACCC[55], the AEMC[56] or the relevant regulator or government agency in each jurisdiction.[57]

4.2.2. Commission's assessment

The Commission believes that many of the criticisms raised in the submissions are cogent. It has reached the draft view that the establishment and administration of the proposed registers will likely be an onerous, costly task for incumbent network service providers. The management of potentially heavily populated registers seems likely to divert significant organisational resources, with additional costs likely including:[58]

- staff and other resources to maintain registers and ensure ongoing compliance;
- managing legal liabilities that may arise from administering the lists;
- diversion of resources within call centres; and
- re-training across relevant operations and customer service areas.

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52 Country Energy, Submission, 16 October 2006, page 1.

53 EWON, Submission, 16 October 2006; Origin Energy, Submission, 23 October 2006; VENCorp, Submission 16 October 2006; Country Energy, Submission, 16 October 2006; ETNOF, Submission, 16 October 2006; ENA, Submission, 16 October 2006; EnergyAustralia, Submission, 18 August 2006.

54 ETNOF, Submission, 16 October 2006, page 3.

55 ETNOF, Submission, 16 October 2006, page 3; ENA, Submission, 16 October 2006, page 2.

56 ETNOF, Submission, 16 October 2006, page 3.

57 VENCorp, Submission, 16 October 2006, page 2.

58 The Commission notes, for example, that there are several hundred accredited service providers listed on the NSW Department of Energy, Utilities and Sustainability ("DEUS") register.

The Commission concurs with the numerous submissions that highlighted the potential for the proposed Rule to extensively duplicate a number of other arrangements *already in place* in other jurisdictions. Several submissions highlighted the jurisdictional arrangements in place in New South Wales facilitated by DEUS. The Commission also notes that some jurisdictions, including Victoria and South Australia incorporate tendering requirements to facilitate competition for certain contestable services. In addition, Powercor – Victoria's largest distributor - currently provides a register of recognised contractors available to undertake customer initiated augmentation works.[59]

Consequently, in the Commission's view the proposed Rule change would appear to clearly involve an element of needless replication for no obvious benefit. Table 1 below summarises some of the existing jurisdictional arrangements that would be at least partly duplicated by the proposed Rule change.

Table 1. Examples of Existing Jurisdictional Arrangements

NSW	The *Electricity Supply Act* states that new or expanded connection to the network is required to be funded by customers, and as such they are contestable. However, work can only be performed by Accredited Service Providers ("ASPs"). Accreditations are administered by the Department of Energy, Utilities and Sustainability ("DEUS") and cover various transmission and distribution works. A register of ASPs is available on the DEUS website.[60]
VIC	*Electricity Industry Guideline No.14* requires that licensed distributors call for tenders to perform construction works from at least two other persons, unless the customer and provider agree that tenders do not need to be called. Network providers are required to adopt and observe tendering policies consistent with those in the Guideline. Powercor, Victoria's largest distributor also has a list of recognised contractors available on its website.[61]
SA	Under the *Electricity Distribution Code*, network providers are required to inform the customer of their right to call for tenders. Tendering can be called for both design and construction of distribution connection assets and extensions.
QLD	Contestability is neither mandated nor precluded by the *Electricity Act 1994*. However, in practice, incumbent providers have used electrical contractors to undertake works and advertised tenders on their websites.

The Commission has likewise reached a draft view that the construction and maintenance of multiple, largely identical registers by multiple providers is likely to be inefficient, diverting a considerable aggregate level of resources across all network service providers. The Commission agrees with the argument that were such a scheme to be implemented a more efficient approach would be for a *single independent body* to maintain a *single register*. Indeed, the Commission has reached a draft view that it is

[59] See: http://www.powercor.com.au.
[60] See: http://www.deus.nsw.gov.au/index.asp.
[61] See: http://www.powercor.com.au.

inappropriate for network service providers to administer the type of scheme proposed, especially in light of the potential accreditation and legal liability issues created

Specifically, network service providers would presumably need to undertake some form of vetting process to ensure that registered providers were accredited and thus had the requisite qualifications in each jurisdiction to work on network systems.[62] This in turn could conceivably place providers at risk of legal damages if, for example, a connection applicant sustained damages after relying on a register maintained by the provider. It is for these reasons that the management of accreditation schemes has, quite rightly, largely been a matter for *individual jurisdictions*.

In the Commission view, imposing further obligations through the Rules without a wider policy framework would not only increase the risk of duplication, confusion and complexity, but would also be ill advised without input from the jurisdictions themselves. On balance, the accreditation concerns and potential legal costs highlighted in submissions suggest that it would be inappropriate for network service providers to be encumbered with the responsibilities contemplated by the proponent. Again, were such a scheme to be implemented, the vetting of applicants is a task more appropriately undertaken by a *single independent entity*.

The Commission has therefore reached a draft view that the proposed Rule change is likely to entail significant regulatory and administrative costs - particularly for incumbent network service providers – with few, or indeed any offsetting benefits. The likely accreditation and potential legal costs that would confront incumbent network service providers may also be considerable. In addition, the proposal appears to entail a significant element of duplicity that may needlessly inflate costs. Finally, the Commission is not convinced that the administrative role contemplated by the proponent is one that should appropriately be assigned to network service providers.

In sum, there is a high likelihood that the proposal would result in significant additional costs that may be passed through to network users in a non-transparent and potentially inefficient manner. As section 4.2 outlined, the proposed Rule change appears to entail few, if any self-evident economic benefits that might off-set these costs.

4.3. Commission's draft decision

In accordance with section 99 of the NEL, the Commission's draft decision is to not make the proposed Rule. Based upon the strength of the arguments set out in submissions and its own analysis, the Commission is not satisfied that, under section 88 of the NEL, the Rule proposed by Energy Solutions will or is likely to contribute to the achievement of the national electricity market objective. Specifically, the Commission considers that

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62 This might be particularly challenging for contestable *construction* of network infrastructure since the number of prospective service providers could be considerable. Accreditation issues are likely to be less significant for the *ownership and operation* of network infrastructure, since there are likely to be fewer prospective providers. However, as noted in section 4.1.2 above, these providers are readily ascertainable by virtue of the various state-based licensing regimes. For example, a list of all energy licences issued in Victoria is publicly available on the ESC website (http://www.esc.vic.gov.au). In other words, there is arguably no significant informational advantage and thus no obvious benefit to be obtained from the proposed Rule change for these particular services.

the potential costs of the scheme contemplated by the proposed Rule change would significantly outweigh any potential benefits that might arise.