24 February 2012

Mr Chris Pattas
General Manager, Network Operations and Development Branch
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Email: AERInquiry@aer.gov.au

Dear Mr Pattas

RE: ELECTRICITY DISTRIBUTION RING FENCING GUIDELINES REVIEW

CitiPower and Powercor Australia (**the Businesses**) welcome the opportunity to make this submission to the Australian Energy Regulator (**AER**) following the release in December 2011 of the *Electricity Distribution Ring-fencing Guidelines Review Discussion Paper.*

Victoria has had in place *Electricity Industry Guideline No. 17 Electricity Ring Fencing* (**EIG17**) since October 2004. The cited aim of the EIG17 was to limit the ability of vertically integrated Distribution Network Service Providers (**DNSP**s) to discriminate against upstream and downstream competitors. Since its inception the Businesses are not aware of a single breach of compliance with EIG17. The absence of any identified breaches and/or enforcement actions under EIG17 demonstrate that the current Victorian arrangements have proven effective. In addition to being effective, they have achieved this objective without incurring structural, reporting or administrative costs that have characterised other regulatory instruments put in place by regulators around Australia.

A single set of national ring-fencing guidelines is unnecessary given that a national approach already exists under the *Competition and Consumer Act 2010* (CCA). The AER has not cited any examples of breaches of the CCA as it relates to vertically integrated businesses, to suggest it is ineffective in limiting the ability of vertically integrated DNSPs to discriminate against upstream or downstream competitors.

The Businesses believe that Australian electricity consumers are well protected from any adverse impact of vertical integration of DNSPs by section 50 of the **CCA**. Section 50 of the CCA prohibits the acquisition of shares or assets by a corporation where the acquisition would have the effect or likely effect of substantially lessening competition in a market. The provision is designed to have general application across the economy, including the electricity industry.

The nature and extent of any vertical integration is one of the matters that the Australian Competition and Consumer Commission (**ACCC**) must take into account in determining whether an acquisition would have the effect or likely effect of substantially lessening competition.[1] The ACCC's *Merger Guidelines*, November 2008 make plain that, in assessing the competition effects of a vertical acquisition, the ACCC will take into account any incentive and ability that the acquirer has to discriminate in favour of an upstream or downstream business.[2]

In circumstances where laws are in place to ensure anticompetitive vertical integration does not occur, the rationale for an additional regulatory overlay to address any issues associated with vertical integration in the energy sector is unclear. The policy objective behind section 50 is to protect the competitive process for the benefit of consumers. The same objective would presumably also underlie any measures to address the potential issues associated with the more specific scenario currently contemplated, namely, vertical integration in the electricity industry. There have been no instances of section 50 of the CCA failing to apply to vertical integration in the electricity industry.

The significance of section 50 of the CCA in addressing any adverse impact of industry integration (both horizontal and vertical) is evident in Victoria in the *Electricity Industry Act 2000* (Vic) (**EIA**). At present, section 68 of the EIA prohibits (subject to certain exceptions) a person from holding a controlling interest in two or more distribution, generation or transmission companies or a substantial interest in three or more distribution, generation or transmission companies. One of the exceptions provided for in the EIA (see section 68(8)) is that the Essential Service Commission of Victoria has the power to determine that it is satisfied that the ACCC has considered the proposed acquisition and that the ACCC has notified the acquiring party that it does not propose to intervene under section 50 of the CCA.

The approach under the EIA in its current form recognises the pivotal role of section 50 of the CCA in preventing anticompetitive acquisitions (including vertical acquisitions) in the electricity industry. It also both limits the potential for regulatory duplication and facilitates consistency in competition regulation.

In further recognition that section 50 is the appropriate mechanism by which to ensure any competition concerns associated with vertical integration in the energy sector are addressed, the Victorian Government has accepted submissions of interested parties that, in light of the CCA, the cross-ownership provisions in the EIA are not required. The Government has foreshadowed that these provisions will be repealed at the commencement of the National Energy Customer Framework in Victoria (expected to be 1 July 2012).[3].

The Businesses would welcome the opportunity to discuss any of the matters raised in this submission. If you have any questions, please contact Stephanie McDougall on (03) 9683 4518 or by email at smcdougall@powercor.com.au.

Yours sincerely

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[1] Section 50(3)(i) of the CCA.

[2] See, for example: ACCC, *Merger Guidelines,* November 2008, pp27-30.

[3] See the Department of Primary Industries' decision paper, *The National Energy Customer Framework in Victoria*, available at: http://www.dpi.vic.gov.au/energy/about/legislation-and-regulation/national-energy-customer-framework/the-national-energy-customer-framework-in-victoria.

Brent Cleeve
MANAGER REGULATION