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**Australian
Competition &
Consumer
Commission**

Applications for Authorisation

Comalco Limited

in relation to Gladstone Power Station

Date: 19 November 1999

Application No
A40078
A40079
A40080

Commissioners:
Fels
Martin
Jones
Bhojani

File no:
CA99/488

Summary

On 29 July 1999 Comalco Limited lodged three applications (A40078, A40079 and A40080) for authorisation in relation to electricity generated by the Gladstone Power Station (GPS) and supplied to Boyne Smelter Limited through the National Electricity Market (NEM).

The applications were lodged under sections 88(1) and 88(8) of the Act.

The GPS joint venture seeks to amend certain previously authorised agreements to accommodate the introduction of the NEM. Those agreements have not yet been finalised by the applicant. The agreements, together with a number of other agreements relate to the expansion of the Boyne Island aluminium smelter, were authorised by the Commission in 1994.

In its submission in support of the current applications Comalco claims that the amended arrangements would not have a negative impact on competition or otherwise contravene the TPA. The existing agreements and proposed amendments, including the role of Queensland Power Trading Corporation (QPTC) under the Interconnection and Power Pooling Arrangement, are merely designed to:-

- preserve, to the extent possible, the financial arrangements that underpinned the acquisition of GPS;
- ensure that QPTC can take its energy entitlement from GPS; and
- provide QPTC with some flexibility as to when GPS will be dispatched.

Comalco also submits that the existing agreements have resulted in significant past and ongoing public benefits.

Comalco further submits that the amended arrangements have little or no anti-competitive impact in any relevant market.

The Commission takes the view that in the material before it that the anti-competitive effect of the agreements is not likely to have changed and it accepts that public benefits previously accepted by the Commission continue to flow from the arrangements. However, it has not seen the final version of the agreements and authorisation is subject to the applicant providing the Commission with signed agreements so that if any such agreement or agreements depart(s) materially from the outline of the agreement provided by the applicant the Commission may review that aspect of the determination.

List of Abbreviations

| | |
|---------|--------------------------------------------------------|
| BSL: | Boyne Smelters Limited |
| CAL: | Comalco Aluminium Limited |
| CPA: | Capacity Purchase Agreement |
| CPS: | Collinsville Power Station |
| EGA: | Exempted Generation Agreement |
| GAL: | Gladstone Aluminium Limited |
| GPS: | Gladstone Power Station |
| IPPA: | Interconnection and Power Pooling Agreement |
| MPPA: | Master Power Purchase Agreement |
| NEC: | National Electricity Code |
| NEM: | National Electricity Market |
| NEMMCO: | National Electricity Market Management Company Limited |
| NRGGOS: | NRG Gladstone Operating Services Pty Ltd |
| OMA: | Operation and Maintenance Agreement |
| QAL: | Queensland Aluminium Limited |
| QEC: | Queensland Electricity Commission |
| QETC: | Queensland Electricity Transmission Commission |
| QGC: | Queensland Generation Corporation |
| QIEM: | Queensland Interim Electricity Market |
| QSO: | Queensland System Operator |
| QPTC: | Queensland Power Trading Corporation |
| QTPTC: | Queensland Transitional Power Trading Corporation |
| QTSC: | Queensland Transmission and Supply Corporation |
| TPA: | Trade Practices Act |
| TPC: | Trade Practices Commission |

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1. Introduction

1.1 On 29 July 1999 Comalco Limited (Comalco) lodged three applications for authorisation with the Commission in relation to electricity generated by the Gladstone Power Station (GPS) and electricity supplied to the National Electricity Market (NEM) and to Boyne Smelter Limited (BSL).

1.2 Application A40078 was made under section 88(1) of the *Trade Practices Act* (the Act) for an authorisation to make and give effect to a contract or arrangement or arrive at an understanding, where a provision of the proposed contract, arrangement or understanding would be, or might be, an exclusionary provision within the meaning of section 45 of the Act.

1.3 Application A40079 was made under section 88(1) of the Act for an authorisation to make and give effect to a provision of a contract, arrangement or understanding, which provision has the purpose, or has or may have the effect, of substantially lessening within the meaning of section 45 of the Act.

1.4 Application A40080 was made under section 88(8) of the Act for an authorisation to engage in conduct that constitutes, or may constitute, the practice of exclusive dealing within the meaning of section 47 of the Act.

1.5 It was requested that any authorisation granted be expressed to apply to a person who becomes a party to the agreement after they are amended or after authorisation is granted, as provided under section 88(10) of the Act.

1.6 Comalco described the contract, arrangement or understanding, referred to in paragraph 1.2 as relating to the Interconnection & Power Pooling Agreement (IPPA) being part of the joint venture agreement relating to the GPS. It described the contract, arrangement or understanding, referred to in paragraph 1.3 as concerning joint venture agreements relating to the GPS.

1.7 The Commission was requested to authorise all contracts, arrangements, understandings, practices, acts or things made, given effect to, carried on or done under (or in relation to) the proposed arrangements.

2. Background

Australia's aluminium industry

2.1 The major raw material used in the production of aluminium is alumina which is extracted from the ore, bauxite, by a refining process.

2.2 Bauxite mines in Australia are operated by:

Alcoa of Australia Limited in the Darling Ranges, WA;

Comalco at Weipa, Qld;

Nabalco Pty Ltd at Gove, NT; and

Worsley Aluminium Pty Ltd at Mt Saddleback, WA .

2.3 There are six alumina refineries in Australia. In Western Australia the Kwinana, Pinjarra and Wagerup refineries are owned and operated by Alcoa. Also in Western Australia is the Worsley refinery which is owned by Reynolds Australia Alumina Limited (50%), Shell Company of Australia (37.5%), Kobe Alumina Associates (Australia) Pty Ltd (10%) and Nissho-Iwai Alumina (2.5%). The Gove alumina plant is managed by Nabalco.

2.4 Queensland Alumina Limited (QAL) operates the world's largest alumina refinery, located near Gladstone.

2.5 There are six aluminium smelters in Australia, located at:

Bell Bay, Tasmania;

Boyne Island, Queensland;

Point Henry, Victoria;

Portland, Victoria;

Kurri Kurri, NSW; and

Tomago, NSW.

The applicant

2.6 Comalco was formed in 1960 following the discovery of large bauxite deposits at Weipa, in Queensland. It is a supplier of bauxite, alumina and primary aluminium to world markets.

2.7 In addition to its wholly owned bauxite mine at Weipa, Comalco is a member of a consortium which owns a bauxite mine (its production entitlement is 4%) at Boké, Guinea, West Africa.

2.8 Comalco's bauxite refining interests are in QAL (30.3%) and Eurallumina SpA, Italy (26.9%). Comalco has a total entitlement to over 1.2 million tonnes of alumina each year.

2.9 Comalco owns and operates the smelter at Bell Bay and it has a substantial interest (79.36%) in a smelter in New Zealand. It is also part of two joint ventures associated with the smelter at Boyne Island near Gladstone.

2.10 The arrangements relating to its Gladstone operations are the subject of these applications. Comalco described the applications as being in respect of certain existing arrangements and proposed amendments to those arrangements in relation to electricity generated by the GPS and supplied to the Boyne Island aluminium smelter (the Smelter) and the National Electricity Market (NEM).

2.11 The agreements relating to GPS and the Smelter have been the subject of authorisations in:

- 1979 – the formation of joint venture for the construction and operation of the Smelter; and
- 1994 – the expansion of the Smelter and the formation of a joint venture for the acquisition and operation of GPS.

2.12 The GPS joint venture seeks to amend certain previously authorised agreements to accommodate the introduction of the NEM and comply with the National Electricity Code (NEC) and the Queensland-specific exemptions to the NEC (Queensland derogations).

2.13 The Queensland derogations provide for the continuation of certain agreements in force prior to the introduction of the NEM and allow the appointment of a State entity as the “Nominated Generator” for those privately-owned generators, such as GPS, with “Exempted Generation Agreements” (EGAs). A Nominated Generator acts as a virtual generator, trading the electricity of an actual generator (or generators) in the NEM. Queensland has appointed the Queensland Power Trading Corporation (QPTC) to perform this function.

2.14 The role of QPTC as the Nominated Generator for GPS means that certain agreements, most notably the IPPA, must be amended. The proposed amendments to the IPPA would essentially “ring-fence” GPS by having QPTC:

- register as the Nominated Generator for GPS under the NEC;
- prepare forecasts for GPS's electricity output;
- develop and submit dispatch offers concerning GPS's available capacity with the objective of achieving overall dispatch in accordance with the forecast;
- supply electricity generated by GPS to BSL and the NEM;
- provide electricity from the NEM to BSL;
- continue to pay GPS capacity and energy charges; and
- receive all revenue in relation to GPS-generated electricity supplied to the NEM.

Previous authorisation applications

2.15 Comalco formed a joint venture in 1979 for the construction and operation of an aluminium smelter on Boyne Island, Queensland. The joint venture, BSL, is an incorporated entity currently comprised of Comalco and several Japanese companies, including related or subsidiary entities (BS joint venturers). In 1979, Comalco (on behalf of the BS joint venturers) applied for and received authorisation.

2.16 In late 1993, Comalco and Comalco Aluminium Limited (CAL) applied for authorisation to expand the Smelter by constructing a third potline. Because of the substantial investment involved in this expansion and the critical importance of maintaining an adequate and economical supply of electricity, Comalco formed a second (unincorporated) joint venture (comprised of many of the same members of the BS joint venture as well as NRG Energy Inc., a US power company) to acquire and operate GPS (GPS joint venture). Comalco and CAL (on behalf of the GPS joint venture) sought authorisation for the new agreements and amended arrangements. Authorisation was granted by the Trade Practices Commission (TPC) on 3 March 1994.

Original (1979) Authorisation for the Construction and Operation of the Smelter

2.17 The original authorisation, applied for in 1979, related to the arrangements for the construction and operation of a large aluminium smelter in close proximity to an alumina refinery operated by QAL.¹ QAL's refinery, the largest in the world and located in Gladstone, Queensland, supplies the BS joint venturers with alumina through the Comalco subsidiary, CAL.²

2.18 The 1979 authorisation included arrangements for the establishment of a joint venture as well as agreements relating to alumina supply, tolling, conversion services, management and technical services, and long term power supplies.

2.19 The trade practices issues concerned exclusive alumina supply arrangements between CAL and the BS joint venturers and a requirement that the BS joint venturers, other than Comalco, export their share of the Smelter's aluminium output.³ In approving the applications for authorisation, the TPC saw the joint venture as essentially geared towards the export market and unlikely to proceed without these restrictions.

2.20 The TPC viewed the economic development of Australian natural resources as the primary public benefit, which might not otherwise have taken place in the absence of the joint venture. Under the circumstances, the TPC was satisfied that the proposed arrangements would result or be likely to result in a benefit to the public and that this benefit would outweigh any anti-competitive detriment that arose from the arrangements.

Additional (1994) Authorisation for the Smelter Expansion and Operation of GPS

2.21 In the early 1990s, Comalco and the BS joint venturers decided that an increase in plant size would allow the joint venture to take advantage of substantial (additional) economies of scale. By constructing a third potline, it was estimated that production at the

¹ The Smelter was initially referred to as the "Gladstone Smelter" and the joint venture was known as "Gladstone Aluminium Limited" (GAL). GAL's original participants included a US Company, Kaiser Aluminium, which later sold its interest to Comalco. GAL subsequently changed its name to BSL. For convenience, all discussions relating to the Smelter joint venture refer only to BSL.

² CAL receives alumina from QAL pursuant to a tolling arrangement, where alumina is sent from the refinery to the Smelter via a 9km conveyor belt system.

³ Aluminium produced at the Smelter is actually delivered to the BS joint venturers (other than Comalco) at agreed overseas ports.

Smelter would increase by 200,000 tonnes, which would mean a total annual capacity of approximately 460,000 tonnes.⁴

2.22 The Smelter's expansion was conditional on the acquisition of GPS because of the importance of maintaining a secure and cost effective supply of electricity.

2.23 The expansion of the Smelter and the acquisition and operation of GPS necessitated the amendment of previously authorised arrangements and the negotiation of several new agreements. Comalco and CAL applied for and received authorisation in relation to the new and amended arrangements on 3 March 1994.

2.24 No application for authorisation was made for the actual acquisition of GPS. State Crown immunity applied as the vendor was the Queensland Electricity Commission (QEC). In any event, the purchase could not have substantially lessened competition, as the vendor was the sole electricity generator in the State.

Smelter Agreements

2.25 The expansion of the Smelter required the modification and termination of various agreements as well as the execution of entirely new arrangements. Certain existing Smelter agreements were modified to reflect the term of the GPS agreements and take into account the different participants in the expanded Smelter arrangements.⁵ The agreements relating to power supply were terminated whilst two new agreements concerning tolling and technology were reached.⁶

GPS Agreements

2.26 The following agreements were addressed in the submission supporting the applications for authorisation:

- a) the State Agreement, which dealt with issues relating to the support of the State, such as the continuous supply of electricity to the Smelter, the issue of a licence to the GPS joint venturers and the provision of credit support in respect of QEC;⁷
- b) the Joint Venture Agreement, which provided generally for the GPS joint venturers to associate themselves as an unincorporated joint venture for the acquisition and operation of GPS;
- c) the IPPA between the GPS joint venturers and QEC, which provided for:

⁴ Since the third potline has come on line, the Smelter's capacity has increased to 490,000 tonnes.

⁵ Some of the BS joint venturers did not participate in the expansion whilst others established new companies to participate in the expansion.

⁶ The First Expansion Tolling Agreement dealt with the conversion of alumina to aluminium by BSL in the third potline and the new Technology Agreement involved the supply of core reduction technology for the third potline.

⁷ The parties did not seek authorisation for the State Agreement based on the principle of State Crown immunity.

- i. the connection of GPS and BSL to the Queensland transmission grid;
 - ii. security of power supply to the Smelter;
 - iii. transmission of power from GPS to the Smelter;
 - iv. power pooling arrangements whereby:
 - A) QEC's basic entitlement to energy from GPS was determined on the basis of cost-based merit order;
 - B) the GPS joint venturers acquired electricity from QEC to supply the Smelter if insufficient GPS generating units were dispatched to meet the Smelter load; and
 - C) GPS supplied energy in excess of the Smelter's requirement to QEC;⁸
 - v. the allocation of the capacity of GPS between BSL and QEC; and
 - vi. certain arrangements in respect of coal procurement by the GPS joint venturers;
- d) the Capacity Purchase Agreements (CPAs) pursuant to which the GPS joint venturers made capacity available to QEC;
- e) a Master Power Purchase Agreement (MPPA) between the GPS joint venturers and BSL setting the price and other terms for the sale of electricity from the GPS joint venturers to BSL, and subsidiary Power Purchase Agreements in respect of Block A (first and second potlines) and Block B (third potline);
- f) an Operation and Maintenance Agreement (OMA) pursuant to which NRG Gladstone Operating Services Pty Ltd (NRGGOS) was appointed as operator of GPS;
- g) the Power Sales Administration Agreements pursuant to which NRGGOS was also appointed to administer the power contracts (described in paragraphs (c), (d) and (e)) on behalf of each GPS joint venturer;
- h) the Coal Supply Agreements under which QEC supplied coal (acquired pursuant to long term contracts with Curragh Queensland Mining Limited and Callide Coalfields Pty Limited) to the GPS joint venturers; and
- i) a Rail Haulage Agreement with Queensland Rail.

Australian Electricity Industry

2.27 There have been significant changes to the Australian electricity industry since the previous applications for authorisation were granted in 1994. Prior to 1990, the supply of

⁸ The arrangements referred to in paragraphs (B) and (C) are known variously as "capacity support" and "economy interchange".

electricity in each State and Territory was dominated by a single State-owned authority (or combination of authorities) responsible for the generation, transmission and distribution of electricity.

2.28 In anticipation of the introduction of the NEM, many State and Territory governments restructured their electricity industries. The integrated authorities in the eastern and southern States were dismantled and the new electricity entities were either corporatised or, in the case of Victoria, privatised.

2.29 The restructuring of the Queensland industry was part of a gradual process beginning with the break up in 1995 of Queensland's vertically integrated governmental electricity organisation, known as QEC, and leading to the introduction of the Queensland Interim Electricity Market (QIEM) in January 1998. The QIEM was to operate until either the NEM came into effect or until 31 December 1998, whichever occurred earlier.

2.30 The NEM came into effect on 13 December 1998 after the NEC received authorisation from the Commission in October of that year. Queensland has participated in the NEM from its commencement.

Queensland Electricity Industry

Pre-1995 Regulatory Structure

2.31 Until 1995 Queensland had a State-owned electricity authority known as QEC. QEC was wholly responsible for the generation and transmission of electricity.

2.32 Electricity generation was based on a cost based merit order system, meaning that QEC estimated electricity demand and then dispatched the lowest cost generators first, gradually moving to higher cost generators, until demand was satisfied.

2.33 The agreements surrounding the acquisition and operation of GPS, including the IPPA, were negotiated in the context of this regulatory framework.

1995-1997 Regulatory Structure

2.34 In January 1995, QEC was separated into three corporatised (government-owned) entities: the Queensland Generation Corporation (QGC), the Queensland Transmission and Supply Corporation (QTSC) and the Queensland Electricity Transmission Corporation (QETC).⁹

2.35 QGC was responsible for operating the State-owned electricity generators located on eleven separate sites throughout Queensland.

2.36 QTSC and its subsidiary, QETC, were responsible for the transmission, distribution and retail functions associated with the supply of electricity. System Control, an operating division of QETC, was responsible for the commitment and dispatch of all generators in accordance with economic dispatch and cost based merit order. This ensured dispatch of the lowest cost available generation capacity.

⁹ The authorised GPS agreements were novated in favour of the relevant corporatised entity at that time. Comalco notified the Commission of the novation on 18 January 1995.

2.37 As a result of this restructuring:

- QTSC became the counter party to the IPPA and CPAs;
- where the original IPPA contained an obligation that could only be performed by a generator or transmission entity, the IPPA was amended so that QTSC was obliged to procure performance of that obligation by QGC or QETC; and
- QGC became the counter party to several agreements, including the Callide and Curragh On-Sale Agreements for the supply of coal, the Power Station Sale Agreement and certain intellectual property arrangements.

1997-1998 Regulatory Structure: the QIEM

2.38 In mid 1997, QGC was disaggregated into three (government owned) generating entities: Stanwell Corporation Limited (Stanwell), Tarong Energy Corporation Limited (Tarong) and CS Energy Limited (CS Energy) in preparation for the NEM.¹⁰

2.39 In January 1998, the State of Queensland created the QIEM, an interim wholesale electricity market where these three generators and one 'virtual' generator submitted dispatch offers and traded electricity.

2.40 The virtual generator, QPTC,¹¹ was created out of QTSC, and competed with the three government owned generators by submitting dispatch offers on behalf of certain privately-owned generators.

2.41 QETC, also known as Powerlink, retained responsibility for the high voltage transmission grid (ie, the infrastructure used to transmit electricity from generators to regional distributors) under the QIEM. QETC also had responsibility for managing the QIEM through a ring-fenced entity known as the Queensland System Operator (QSO).¹²

2.42 The restructuring of the Queensland electricity industry meant that:

- QPTC replaced QTSC as the counter party to the IPPA, CPAs and other power related arrangements;
- the Callide and Curragh On-Sale Agreements for the on-sale of coal were novated to CS Energy and Stanwell respectively; and
- the remaining obligations under the Power Station Sale Agreement, Power Station Intellectual Property Arrangements, and some minor support documents, were novated to AUSTA.

National Electricity Market

2.43 The NEM, which is governed by the NEC, creates:

¹⁰ A fourth company, AUSTA Energy Corporation Limited (AUSTA), received those assets of QGC relating to engineering services. AUSTA is expected to cease operations by the end of 1999.

¹¹ Until July 1999, QPTC was known as the Queensland Transitional Power Trading Corporation (QTPTC).

¹² When the QIEM ended, the functions of QSO were taken over by the National Electricity Market Management Company Limited (NEMMCO).

- a competitive wholesale market for the purchase and supply of electricity;
- an open access regime that provides for non-discriminatory access to electricity networks; and
- a transparent and nationally consistent legal and regulatory framework.¹³

2.44 Under the NEM generators of different types, with different management approaches and using different network configurations compete with one another. Generators compete by submitting offers to supply electricity (dispatch offers) to a central co-ordinator, NEMMCO.

2.45 NEMMCO also receives bids for the purchase of electricity (dispatch bids) from retail electricity suppliers (and certain qualified end user customers).

2.46 NEMMCO then matches dispatch offers to dispatch bids, taking the lowest priced offers first and progressively accepting higher priced offers until demand is satisfied.

2.47 This process of matching dispatch offers and bids is called the "spot market". The price received by particular generators or paid by particular wholesale electricity consumers is the "spot price". Because electricity cannot be stored, the spot price may fluctuate dramatically over a particular day or week as the market adjusts to variations in demand and changes in the availability of generating plant.

2.48 The introduction of the NEM has had several consequences for the contractual arrangements relating to GPS. Specifically, the start of the NEM has meant that:

- QPTC may no longer assure the dispatch of GPS in accordance with the cost-based merit order system;
- Queensland State-owned generators are no longer required by regulation to operate in accordance with a cost-based merit order;
- the data on which pricing of energy interchange was calculated is no longer available; and
- purchasing coal from a competing generator is not seen as desirable.

Queensland Derogations: Exempted Generation Agreements

2.49 The actual operation of the NEM varies in each State and Territory pursuant to derogations specific to that jurisdiction. These jurisdictional derogations were designed to allow for an orderly transition to the NEC's requirements from State and Territory based arrangements and preserve as much as possible pre-existing contractual arrangements like the IPPA.

2.50 The Queensland derogations permit, among other things, the appointment of a State entity as the Nominated Generator for certain privately owned electricity generators with pre-existing contractual arrangements, referred to as EGAs. The functions of a Nominated Generator include submitting dispatch offers on behalf of privately owned generators and otherwise assuming the role of a generator for the purposes of the NEM.

¹³ Although the NEM is generally consistent among the participating States and Territories, certain deviations from the NEC specific to each State or Territory, known as derogations, are permitted. The Queensland derogations are discussed below.

2.51 Queensland has appointed QPTC as Nominated Generator. Thus, under the proposed amendments, QPTC would represent GPS in the NEM. QPTC would also be the “Market Customer” in respect of the Smelter’s load under the proposed amendments.

2.52 The Queensland derogations have been constructed to allow QPTC to become a market participant to the fullest extent possible whilst maintaining the essential commercial arrangements between QPTC and GPS.

2.53 Under a set of temporary arrangements, QPTC has acted as the Nominated Generator for GPS in the QIEM and NEM. The GPS joint venturers entered into the temporary transitional arrangements until such time as the parties could conclude negotiations for permanent alternative arrangements. Under the transitional arrangements:

- QPTC registered as the “Generator” in respect of GPS;
- QPTC makes offers for dispatch of GPS in accordance with a specified bidding protocol;
- QPTC delivers the Smelter design load to GPS at BSL connection points; and
- payments between the GPS joint venturers and QPTC are determined in accordance with the IPPA and CPAs.¹⁴

¹⁴ The pricing mechanism contained in the IPPA and CPAs is based on data from the merit order system, which is no longer available after the restructuring of QEC. Consequently, the parties agreed to use average capacity support and economy interchange prices based on historical data during the transitional period.

3. The applications

3.1 The following description of the applications is based on material presented in the submission from Comalco.

3.2 Authorisation is sought for certain existing agreements and proposed amendments to those agreements which may raise issues under section 45 and/or section 47 of the *Trade Practices Act 1974* (Cth) in relation to electricity generated by the GPS and supplied to the Smelter and the NEM.

3.3 Authorisation is sought under section 88(1) for those agreements that may constitute: an exclusionary provision; an arrangement with the purpose or effect of substantially lessening competition; or a “price fixing” agreement.

3.4 Authorisation is sought under section 88(8) for those amended agreements that may contravene section 47 as an exclusive dealing practice. Although some of the agreements contain exclusive provisions with suppliers or customers, they constitute a relatively small portion of the market that would be affected by such provisions.

3.5 The GPS joint venture seeks to amend certain previously authorised agreements to accommodate the introduction of the NEM and comply with the NEC and the Queensland derogations.

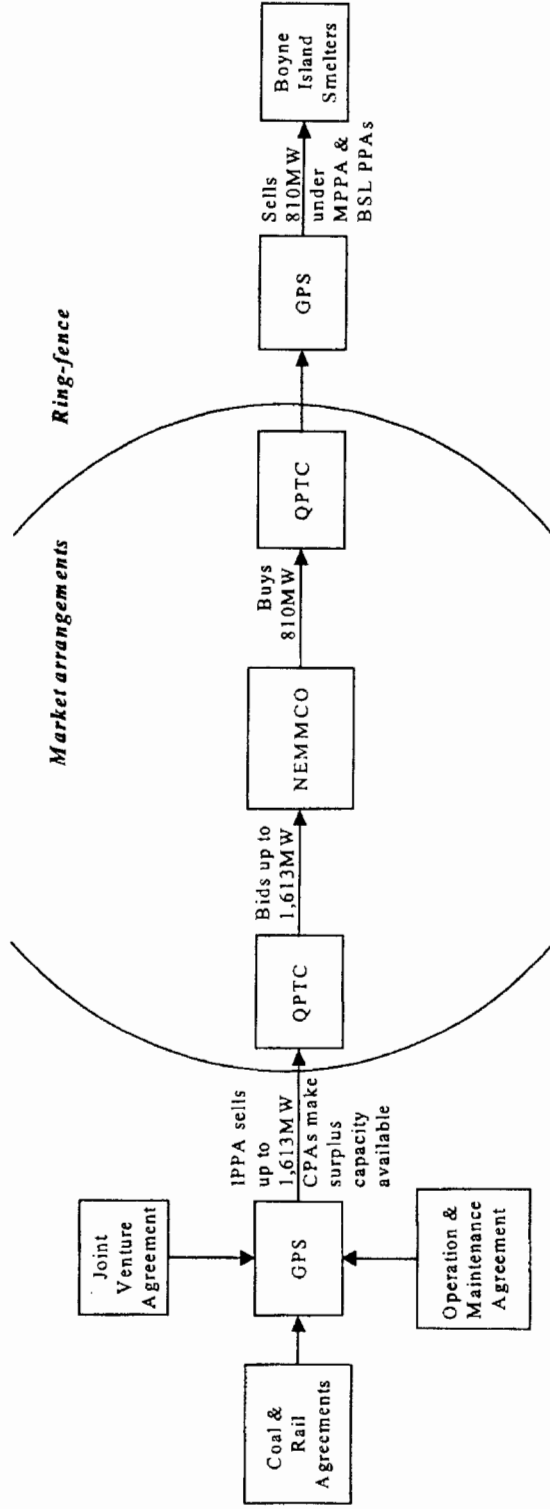
3.6 The GPS agreements for which authorisation is sought are the following:

- Joint Venture Agreement;
- IPPA;
- CPAs;
- Power Purchase Agreements;
- OMA;
- Power Sales Administration Agreements;
- Coal Supply Agreements; and
- Rail Haulage Agreement.¹⁵

A diagram of the interrelationships of the agreements follows:

¹⁵ Although authorisation is sought for all of the above arrangements, many of the amendments are not significant and only reflect changes made to the IPPA. However, because of the overall changes to the structure of the electricity market, authorisation is being sought for all of the above referenced agreements.

**Structure for the GPS/BSL/QPTC
core contracts ...**



Joint Venture Agreement

3.7 The GPS Joint Venture Agreement permitted the GPS joint venturers to form an unincorporated joint venture for the acquisition and operation of GPS. Under the amended arrangements, the GPS joint venturers will reach arrangements or understandings regarding their participation having the following effect:

- (a) GPS generated electricity will be offered at the same (or similar) prices; and
- (b) all of GPS generated electricity supplied to the wholesale pool will be through the Nominated Generator.

3.8 Authorisation of the Joint Venture Agreement is sought under section 88(1).

Interconnection and Power Pooling Agreement

3.9 As mentioned earlier, the role of QPTC as the Nominated Generator for GPS means that certain agreements, most notably the IPPA, must be amended. The proposed amendments to the IPPA would essentially “ring-fence” GPS by having QPTC:

- register as the Nominated Generator for GPS under the NEC;
- prepare forecasts for GPS's electricity output;
- develop and submit dispatch offers concerning GPS's available capacity with the objective of achieving overall dispatch in accordance with the forecast;
- supply electricity generated by GPS to BSL and the NEM;
- provide electricity from the NEM to BSL;
- continue to pay GPS capacity and energy charges; and
- receive all revenue in relation to GPS-generated electricity supplied to the NEM.

3.10 To accommodate the requirements of the NEM, the existing arrangements must be amended to reflect the changes in the regulatory framework. The existing contractual arrangements relating to GPS are largely based on Queensland's regulatory regime prior to the introduction of the QIEM, when the dispatch of electricity involved a merit order system (based on cost as opposed to dispatch offers). The IPPA in particular will require significant modification, including:

- deeming QPTC to be the Nominated Generator in respect of GPS for the purposes of the NEC;
- making QPTC, as the Nominated Generator, responsible for submitting dispatch offers of GPS's available capacity to the NEM and receiving revenues from the NEM;
- requiring dispatch offers submitted by QPTC to reasonably accord with agreed forecasts;¹⁶
- requiring QPTC to make specified payments to GPS if the operation of GPS differs materially from the forecasts;

¹⁶ Under the amended IPPA, QPTC would be required to maintain an overall level of commitment and dispatch of GPS that is equivalent to the entitlement of QPTC and BSL together to energy under the cost based merit order dispatch rules.

- having QPTC acquire (through the NEM) the energy required to supply the Smelter up to the limits specified in the IPPA;
- modifying the pricing provisions between QPTC and GPS as the information on which pricing for the energy interchange was calculated will no longer be available to QPTC;¹⁷ and
- because QPTC would have responsibility for the dispatch of GPS, protecting the Smelter against poor heat rates caused by excessive operation of GPS at light loads.

3.11 As part of the amendment process, the IPPA will also be amended to enable the Smelter access to additional electricity from the NEM (via QPTC) through a separate QPTC-BSL agreement.

3.12 The Smelter arrangements (as authorised in 1994) are not significantly affected by the introduction of the NEM and will not be materially altered as part of the restructuring of the parties' arrangements. The only likely amendments to the Smelter Power Purchase Arrangements are amendments that will reflect, on a back-to-back basis, changes to the IPPA pricing and security of supply arrangements. Thus, apart from the changes to the Power Purchase Arrangements, the agreements involving the Smelter will remain in effect and, accordingly, further authorisation is not being sought for those arrangements.

3.13 The proposed amendments to the IPPA may raise potential competition issues in one of the following ways:

- QPTC, as the Nominated Generator, would make dispatch offers in respect of GPS capacity sold in the NEM;
- QPTC would compensate the GPS joint venturers on the same terms for sales of electricity in the NEM, over dispatch of GPS and wilful default;
- GPS joint venturers would continue to supply BSL on the same terms, pay and receive a common price for capacity support and economy interchange energy and (in the case of financial default by QPTC) direct QPTC as to how GPS capacity should be bid.

Appointment of QPTC as the Nominated Generator

3.14 The NEC, which has been authorised by the Commission, specifically permits Queensland to appoint a single State entity as a Nominated Generator. As the Nominated Generator, QPTC would trade electricity purchased from GPS in the NEM as a whole and not separately for individual joint venturers. Comalco submitted that such provisions might raise issues under section 45 as an exclusionary provision (as defined in section 4D of the TPA) or as an agreement that substantially lessens competition, or under section 45A as price fixing. The arrangements might possibly raise issues under section 47 as well. Having a single entity, QPTC, as the Nominated Generator could be regarded as lessening competition between the GPS joint venturers for the acquisition of "Nominated Generator services" in contravention of section 45 of the TPA.¹⁸ QPTC is not specifically compensated for acting as

¹⁷ Under the amended IPPA, the modified pricing mechanisms for capacity support and economy interchange energy are intended to approximate the prices that would have existed had the existing mechanisms continued.

¹⁸ It is not clear whether these services are "acquired" under the TPA, but for the purposes of this submission we have assumed that they are.

the Nominated Generator for GPS. Comalco suggested that the arrangements could also conceivably fall within the definition of exclusive dealing in section 47(2), as QPTC will provide various services related to its role as Nominated Generator to the GPS joint venturers on an exclusive basis.

3.15 Authorisation is sought under section 88(1) and section 88(8).

Compensation on Same Terms for Sales of Electricity in the NEM, Over Dispatch of GPS and Wilful Default

3.16 Comalco said that compensating the GPS joint venturers on the same terms for sales of electricity in the NEM, over dispatch of GPS and wilful default might raise theoretical issues relating to price fixing under section 45A or a substantial lessening of competition under section 45 and in relation to compensation for over dispatch and/or wilful default on the same terms.

3.17 Authorisation is sought under section 88(1).

Sale of Energy to BSL on Same Terms, Payment and Receipt of Common Price for Energy Interchange and Direction of QPTC Bids Where Financial Default Occurs

3.18 Under the proposed amended agreements (as under the existing arrangements) GPS joint venturers will sell electricity to the Smelter on the same terms and conditions, pay and receive a common price for energy interchange and (in the case of financial default by QPTC) direct QPTC's bids of GPS generated electricity in the NEM.

3.19 Authorisation is sought under section 88(1).

Capacity Purchase Agreements

3.20 The CPAs provide for the sale of energy by the GPS joint venturers to QPTC (in separate contracts on the same or similar terms). As under the arrangements authorised in 1994, each GPS joint venturer will make the "contract capacity" available to QPTC, which is the difference between GPS's total capacity and the capacity required to supply the Smelter. The contract capacity is approximately 509 MW.¹⁹

3.21 Comalco submitted that, as in the 1994 authorisation, under the CPAs sales of capacity and energy by each of the GPS joint venturers to QPTC will be on the same terms, raising issues in relation to sections 45 and 45A.

3.22 Authorisation is sought under section 88(1).

Power Purchase Agreements

3.23 The MPPA defines the general conditions under which electricity is purchased by BSL. Sitting under the MPPA are two long-term take-or-pay power purchase agreements with the GPS joint venturers (Block A and Block B). The Block A agreement relates to

¹⁹ The proposed amendments to the CPAs will reflect changes to the IPPA, such as the provisions relating to indemnity and force majeure.

electricity purchases for two of the Smelter's potlines, while the contract for Block B provides electricity for the third potline.

3.24 The MPPA will change on a back-to-back basis with the amendments to the IPPA. The most significant amendments to the MPPA relate to those IPPA changes concerning:

- the basis for calculating capacity support and economy interchange payments; and
- the security of supply provisions.

3.25 Authorisation is sought under section 88(1).

Operation and Maintenance Agreement

3.26 The OMA, as under the previously authorised arrangements, provides for the appointment of an operator to manage GPS on a day to day basis.²⁰ The proposed amendments modify the OMA to reflect changes made in the IPPA in relation to the provision of forecast data and one or two technical matters.

3.27 Authorisation is sought under 88(1) and 88(8).

Power Sales Administration Agreements

3.28 The OMA does not give the operator (ie, NRGGOS) the authority to sell capacity or energy on behalf of the GPS joint venturers. However, under the Power Sales Administration Agreements (NRGGOS has a separate agreement with each GPS joint venturer) NRGGOS, subject to direction by the relevant GPS joint venturer, administers the IPPA, the CPAs and the BSL Power Purchase Agreements on behalf of the GPS joint venturer. The only changes to these agreements are those necessary to reflect changes in the IPPA and related agreements. It is necessary on a practical level for the operation of GPS that there be a single operator. The GPS joint venturers will continue the appointment of NRGGOS and continue to jointly pay NRGGOS.

3.29 Authorisation is sought under section 88(1).

Coal Supply Agreements

3.30 Under the initial arrangements, the GPS joint venturers had entered into two long term agreements with QEC for the supply of coal from the Curragh and Callide mines (On-Sale Agreements). These agreements established the price to be paid for coal by the GPS joint venturers.

3.31 Following the 1997 disaggregation of QGC and the establishment of the QIEM, the GPS joint venturers began negotiations with a view to entering into a coal supply agreement directly with the Callide Mine, in lieu of the Callide On-Sale Agreement.²¹ Under the new

²⁰ NRGGOS will continue to act as the operator for GPS under the amended arrangements.

²¹ The GPS joint venturers are not currently negotiating a new arrangement with the Curragh Mine in the light of ongoing litigation between Stanwell Corporation and the Curragh Mine. The On-Sale Agreement relating to the Curragh Mine remains in effect.

Callide Coalfields Purchase Agreement and the Curragh On-Sale Agreement (authorised in 1994), the joint venturers pay a common price for coal purchases.

3.32 Authorisation is sought under section 88(1).

Rail Haulage Agreement

3.33 The Rail Haulage Agreement provided that each GPS joint venturer enter into an umbrella agreement with Queensland Rail for the transport of coal (for use by GPS) by rail. Transport by rail is the only feasible means of shipping coal in Queensland because under the *State Transport Act 1960* (Qld) the carriage of coal by road is restricted for distances over 8km. Queensland Rail is the only provider of rail transport in the State of Queensland.

3.34 The only changes to this Agreement are those necessary to reflect the changes in the Callide Coalfields Purchase Agreement, discussed above.

3.35 Authorisation of this conduct is sought under section 88(1) and section 88(8).

4. Statutory tests

4.1 These applications were made under sub-section 88(1) of the Act (in respect of arrangements, provisions of which may be exclusionary provisions, or may have the effect of substantially lessening competition, within the meaning of section 45 of the Act), and sub-section 88(8) of the Act (in respect of conduct that would or may constitute exclusive dealing). The Act provides that the Commission shall only grant authorisation if the applicant satisfies the relevant tests in sub-sections 90(6), (7) or (8) of the Act.

4.2 Sub-sections 90(6) and (7) provide that the Commission shall grant authorisation only if it is satisfied in all the circumstances that:

- the provisions of the subject arrangements or conduct have resulted or would result or be likely to result, in a benefit to the public; and
- that the benefit outweighs the detriment to the public constituted by any lessening of competition that has resulted, or would result or be likely to result, from the arrangements or conduct.

4.3 Sub-section 90(8) provides that the Commission shall grant authorisation in relation to an application under sub-sections 88(1) or 88(8) only if it is satisfied in all the circumstances, that the exclusionary provision or exclusive dealing conduct has resulted, or is likely to result, in such a benefit to the public that the arrangements should be allowed to be given effect to, or the conduct should be allowed to take place.

4.4 Whilst there is some variation in the language between sub-sections 90(6), (7) and (8) the Commission adopts the view taken by the Trade Practices Tribunal (the predecessor of the Australian Competition Tribunal) that in practical application the tests are essentially the same.

4.5 In deciding whether it should grant authorisation, the Commission must examine the anti-competitive aspects of the arrangements or conduct, the public benefits arising from the arrangements or conduct, and weigh the two to determine which is the greater. Should the public benefits or expected public benefits outweigh the anti-competitive aspects, the Commission may grant authorisation or grant authorisation subject to conditions.

4.6 If this is not the case, the Commission may refuse authorisation or alternatively, in refusing authorisation, indicate to the applicant how the applications could be constructed to change the balance of detriment and public benefit so that authorisation may be granted.

5. The submissions

5.1 Comalco lodged a submission in support of the applications. A copy of that submission is on the public register. That submission is briefly outlined below.

5.2 The Commission sought comments on the applications from a range of parties. Submissions were received from the following:

- Boyne Smelters Limited
- Queensland Power Trading Corporation Limited
- NRG Asia-Pacific Ltd
- State Development
- Rio Tinto Limited
- Tarong Energy
- Powerlink Queensland

A copy of each of the submissions is on the public register. A summary of the submissions appears below.

5.3 Brief submissions were lodged by NRG, State Development and Rio Tinto in support of the applications.

5.4 QPTC comments that in order to comply with the requirements of the NEC for each generator to be represented by a single market participant the QPTC will be responsible for bidding the entire output of GPS into the NEM and for ensuring that the entire requirements of the smelter are met from within the NEM. To the extent that output of GPS matches (or exceeds) the requirements of the smelter, the QPTC is largely insulated from fluctuations in the pool price within the NEM.

5.5 QPTC also submits that in the event of a mechanical or electrical failure, the GPS will not be able to generate sufficient output to cover the requirements of the smelter and QPTC will be required to meet any electricity shortfall by purchases from the NEM. In this context there is essentially no difference from the existing arrangements between the GPS joint venturer and QPTC except that QPTC may be called upon to purchase make-up electricity from the NEM at the prevailing pool price rather than directly from the existing state owned generators.

5.6 QPTC goes on to say that a significant proportion of the aluminium produced at the smelter is traded internationally in competition with other aluminium producers. This is an important source of overseas income for Australia and it is considered essential that the existing relationship between GPS and the smelter be maintained to ensure the continuing viability of the smelter in an international market-place.

5.7 QPTC notes that the proposed amended agreements allow QPTC to make its own decisions about how the output of GPS is bid into the market subject only to existing undertakings as to the technical safety of generating plant and preserving the commercial

position of the GPS joint venture. However, if QPTC is in default of payments to the GPS joint venture then the joint venture may step into this role to the extent of the default. While it may be posited that the undertaking given by QPTC to the GPS joint venture amount to limitations upon the behaviour of QPTC in the market, it is believed that any such limitations are only marginally more restrictive than would be the case for a market generator bidding in its own right. It is intended that the QPTC should have the maximum capacity to trade as a market participant while meeting its obligations to the GPS joint venturers. To this end, significant modifications to the IPPA are proposed to allow QPTC to submit dispatch offers in the NEM reasonably in accord with forecasts prepared by QPTC and agreed with the joint venturers. Participants in the NEM will require QPTC to compete with the other three existing State owned generators in Queensland, with generators in New South Wales when the interconnection between Queensland and New South Wales is completed and subsequently the privately owned generators that have recently been announced.

5.8 The submission of Tarong Energy raises a number of issues. It notes that until CS Energy or Stanwell Corporation commission more capacity in the Central Queensland region – a net export region, QPTC has the largest capacity. Furthermore, it also has substantial contractual arrangements post 2001 with the BS joint venturers. Together with limited transmission capacities to north and south Queensland, the arrangements could have substantial long term impact on the operation of the market.

5.9 Tarong submits that the agreements between the State Government, its various GOC and the BS joint venturers, should be unwound. This would free the Government and its GOCs from contractual commitments not designed for the competitive market, and give the BS joint venturers the opportunity to participate in the market directly as both a generator and customer. Such negotiation is likely to require time to complete. While waiting for the outcome of the negotiations an interim authorisation may be required to allow QPTC to participate in the NEM.

5.10 Tarong is particularly concerned about the impact on the market as a result of QPTC having to dispatch the power station 'to reasonably accord with agreed forecast' and 'to make specified payments to GPS if the operation of GPS differs materially from the forecasts'. It adds the forecast of power station operation pattern and energy production in the competitive market is subject to a great deal of uncertainty. Having QPTC offering GPS subject to preset medium term constraints could result in the station being offered into the market in an uncompetitive way, distorting the market's efficiency.

5.11 Tarong submits the arrangements:

- Lock in the Queensland Government as a market participant in the NEM (via one of its generating entities)
- Do not give the BS joint venturers the opportunity to participate in and profit from the NEM
- Are long term

5.12 It further submits that if the Commission proposes to authorise the applications the authorisation should have a review date and that date should be within 12 months of the Queensland/NSW Interconnector (QNI) being operational.

Submissions of Comalco

5.13 Comalco submits that the amended arrangements would not have a negative impact on competition or otherwise contravene the TPA. The existing agreements and proposed amendments, including the role of QPTC under the IPPA, are merely designed to:-

- preserve, to the extent possible, the financial arrangements that underpinned the acquisition of GPS;
- ensure that QPTC can take its energy entitlement from GPS; and
- provide QPTC with some flexibility as to when GPS will be dispatched.

5.14 It is also submitted that the existing agreements have resulted in significant past and ongoing public benefits. In assessing the public benefits of the amended arrangements, the Commission must consider the interdependent relationship between the expansion and operation of the Smelter and the acquisition and operation of GPS. The Smelter's expansion, which was conditioned on the acquisition of GPS, enhanced its ability to compete internationally and increased Australia's exports and export income. Apart from the Smelter, the acquisition and operation of GPS has led to substantial public benefits in the form of a large capital expenditure program and improved operational and environmental performance.

5.15 The amended arrangements, by providing QPTC with flexibility to trade the output of GPS in the NEM, would result in additional public benefits. GPS is a significant generator of electricity in Queensland both in terms of its size and efficiency. Allowing QPTC to trade in the NEM using GPS's electricity output would create a substantial competitor to the three other large Queensland electricity generators and thus increase competition across the State for the benefit of all electricity users.

Past and Ongoing Benefits Related to the Smelter

5.16 The expansion of the Smelter provided significant value to the Australian economy in the form of:

- substantial capital expenditures, including the construction of new works;
- increased employment in relation to the construction and operation of the Smelter and in support industries;
- more revenues for local, state and national governments; and
- greater efficiency and competitiveness in aluminium smelting.

Substantial Capital Expenditures

5.17 In the 1993 submission, it was estimated that during the construction phase the total capital expenditure would amount to \$930 million. It was further estimated that \$66 million of the \$930 million figure would be spent in the Gladstone/Fitzroy region with an estimated regional flow-on effect of \$86 million. The total flow-on effect was estimated at \$834 million.

5.18 The actual expenditure during the 1995-97 construction phase was over \$1.13 billion. Approximately 45% of the project cost was spent in Queensland, 33% in other parts of Australia and 22% overseas. Of the approximately \$400 million spent on equipment, about 40% of the purchases were made in Australia.

Increased Employment

5.19 The Smelter expansion required a substantial construction workforce, amounting to in excess of 400,000 man hours. During peak construction there were over 1,300 people working on the Smelter expansion whilst over the life of the project there were approximately 4,000 people involved. After construction was completed, the operational workforce increased by an additional 350 full time jobs.

More Revenues for Local, State and National Governments

5.20 The Smelter expansion has also meant significant benefits for national, state and local governments. The Commonwealth Government, for example, receives increased tax revenue from the expanded Smelter. The third potline which came fully on-line in November 1997, increased the Smelter's annual operating expenditure by approximately \$400 million, resulting in an increase to gross national product.²²

5.21 The expansion has also enhanced Australia's aluminium exports by approximately \$500 million per annum (through increasing the Smelter's output by an additional 230,000 tonnes of aluminium per year²³ for a total of 490,000 tpa).

5.22 The increased output of the Smelter has also added to gross state product. In both cases, the dominant flow-ons occurred in the metals, metal products and electricity sectors, which relate to the main purchases of alumina from the existing QAL refinery operation and electricity from GPS.

More Efficient and Internationally Competitive Smelter

5.23 The TPC's 1994 authorisation recognised that the most significant public benefit from the expansion of the Smelter would be:

the further development of an efficient, internationally competitive aluminium smelter, through an increase in the value of exports and an overall development of the Australian economy.

5.24 The addition of the third potline enhanced the Smelter's operating efficiency in the increasingly competitive aluminium smelting market. Specifically, the expansion has lowered the unit cost of production by around 18%. This improvement stems from productivity gains of more than 40%, an increase in energy efficiency, better usage of raw materials, further economies of scale and improved overall performance.

Past, Ongoing and Future Benefits Concerning the Gladstone Power Station

5.25 The benefits associated with the Smelter were (and are) integral to the acquisition and operation of GPS because the cost and reliability of power supply is crucial to producing aluminium at world competitive prices. The strategic purpose for the acquisition of GPS was to provide, for at least 30 years, a block of power for the Smelter expansion at an internationally competitive price and extend the power supply arrangements to the existing Smelter for at least a further 30 years.

²² The contribution to gross national product was estimated to be \$341 million in the 1993 submission. Two-thirds of that figure was expected to remain in Queensland.

²³ The rated capacity of Line 3 since the 1993 submission has increased from 200,000t/year to 230,000t/year.

5.26 As a consequence of this interdependence, any assessment of the amended arrangements, which are designed to preserve the risk allocation among the parties, should consider the public benefits of the Smelter expansion in the context of the GPS joint venture.

Substantial Capital Expenditure

5.27 GPS is also undergoing an on-running \$187 million plant refurbishment program to ensure continuing reliable operation of GPS over its 30 year plus life. This expenditure is timed to coincide with accumulated age and service hours applicable to each unit of GPS. To date, the GPS joint venture has spent \$170 million in this area.

Secure, reliable and competitively priced power supply for the Smelter

5.28 The acquisition and refurbishment of GPS and entry into the GPS contractual arrangements has provided a secure and reliable supply of electricity to the Smelter. The power purchase arrangements also provide power at a price that enables the Smelter to be internationally competitive.

Improved Environmental Performance

5.29 Following the acquisition, the GPS joint venturers have spent additional funds on refurbishment of the plant. A comprehensive plant improvement program was developed to ensure that GPS met the environmental standards specified in the State Agreement. The program, amounting to about \$90 million of the refurbishment expenditure, had three priority areas – reduction of chimney stack particulate emissions, reduced nitrogen oxide (NO_x) emissions and control of coal dust and drainage effluent. As a result of these efforts the production of hazardous pollutants has decreased by an average of 95% for particulate emissions and 33% for NO_x emissions.

The NEM and Wholesale Competition in Electricity

5.30 The extent of benefits arising out of the NEM, however, is a function of the number of generators supplying energy to the wholesale market. Quite simply, the more generators involved the greater the benefits. In its grant of authorisation for the NEC, the Commission noted that ensuring competitive benefits arise from the NEM is dependent upon:

[e]stablishing more generation businesses to compete in the market [which] should make it more difficult to exercise market power as it results in capacity demanded being distributed among competing businesses.

5.31 As noted earlier, GPS is a significant electricity supplier in Queensland with lower operating costs than many other generation plants in the State. Its current capacity is 1,680 MW out of a total of 8,273 MW for all of Queensland. Based on GPS's ability to provide competitively priced electricity, its inclusion via QPTC in the NEM will inure to the benefit of the NEM as well as the State of Queensland. Queensland in particular can expect enhanced competition and a more efficient electricity market as a consequence of QPTC bidding GPS's electricity production in the NEM. The added flexibility QPTC has in being able to submit competitive bids for GPS on a day to day basis will further add to these market efficiencies.

5.32 Comalco made the following submissions in relation to the likely effect on competition of each of the agreements.

Joint venture agreement

5.33 Authorisation was previously sought and granted under section 88(1) for any possible lessening of competition, contrary to section 45 of the TPA, resulting from the formation of the joint venture. It was noted in the submission supporting the applications for authorisation that the joint venture did not involve any lessening of competition because, in the absence of the joint venture, there would be no competition between the GPS joint venturers in any relevant market.

Interconnection and power pooling agreements

5.34 Exclusionary provisions under section 4D apply only where parties to a contract are “competitive with each other”. The GPS joint venturers should not be considered in competition with one another for the purposes of electricity supply. Thus, these arrangements would not contravene section 45 as an exclusionary provision or section 45A as price fixing.²⁴ For similar reasons such an arrangement is very unlikely to raise any issue under section 45 as a contract or provision that substantially lessens competition.

5.35 Also, it is submitted that the appointment of QPTC as the Nominated Generator does not raise an issue under section 45.

5.36 QPTC is not specifically compensated for acting as the Nominated Generator for GPS; however, even the implicit compensation of QPTC by the GPS joint venturers on the same terms would not constitute price fixing under section 45A or substantially lessen competition for the purposes of section 45. Section 45A, which prohibits price fixing between companies in competition with one another, provides an exemption in section 45A(4) for the collective acquisition of goods or services by parties to a contract, arrangement or understanding. This arrangement is also unlikely to contravene section 45 because, as indicated above, the joint venturers are not in competition with one another for the generation of electricity.²⁵ Thus, any compensation to QPTC will not have the effect of substantially lessening competition in any market.

5.37 Comalco submits that the arrangements could also conceivably fall within the definition of exclusive dealing in section 47(2), as QPTC will provide various services related to its role as Nominated Generator to the GPS joint venturers on an exclusive basis. However, there are no other potential suppliers that could be foreclosed from this market, except for other State entities, as a result of the “exclusive” arrangement.

Capacity purchasing agreements

5.38 As in the 1994 authorisation, under the CPAs sales of capacity and energy by each of the GPS joint venturers to QPTC will be on the same terms, raising issues in relation to sections 45 and 45A.

²⁴ The arrangements would also not contravene section 45A as price fixing because section 45A(2) provides an exemption for the joint supply of goods and services produced pursuant to a joint venture.

²⁵ Even if the Commission viewed NRG Energy as competing with the other GPS joint venturers in the supply of electricity, the limited capacity of CPS would mean that any lessening of competition would not be *substantial* for the purposes of section 45.

5.39 It is submitted that these arrangements, as in 1994, do not substantially lessen competition in the market for the supply of electricity because the arrangements are a necessary element of the GPS joint venture. Thus, without these arrangements the GPS joint venture would not be supplying electricity in Queensland.

Power Purchase Agreements

5.40 The effect of the arrangement is the same as discussed under the IPPA and CPAs above. Since the GPS joint venturers would not be competitors in the absence of the joint venture arrangements, including the MPPA and Block A and Block B agreements, it is submitted that competition would not be substantially lessened by these arrangements.

Operation and Maintenance Agreement

5.41 Under the OMA the GPS joint venturers could be said to acquire all operating and maintenance services from NRGGOS in contravention of section 47(2). However, because the GPS joint venturers are not in competition with one another and given the importance of a single operator as a practical matter, there is no substantial lessening of competition as a result of the arrangement.

Power Sales Administration Agreements

5.42 These agreements could potentially raise an issue under section 45 because the contracts contain the same or similar terms. However Comalco says, as a practical matter, it is necessary to have a single set of rules for administering the relevant agreements. Again, as stated earlier, these arrangements are a necessary part of the GPS joint venture, without which the individual joint venturers would not require the services covered by these contracts.

Coal Supply Agreements

5.43 The joint venturers pay a common price for coal purchases. The collective acquisition exemption pursuant to section 45A(4) applies. The agreements also do not substantially lessen competition because, but for the joint venture, the GPS joint venturers would not be competitors for the acquisition of coal.

Rail Haulage Agreement

5.44 The arrangements would not substantially lessen competition in contravention of section 45 because, absent the joint venture, the joint venturers would not acquire such services.

5.45 It is also submitted that the Rail Haulage Agreement does not contravene section 47 as an exclusive dealing arrangement because the Agreement does not substantially lessen competition. Such an arrangement is unlikely to substantially lessen competition unless other potential providers of transport services are foreclosed from a significant percentage of the market for such services.

Summary of Comalco's submissions

5.46 For the reasons set out above, it is submitted that the amended arrangements would have little or no anti-competitive effect in any relevant market. In any event, the substantial past, ongoing and future public benefits associated with the existing agreements and proposed

amendments outweigh any lessening of competition. Consequently, the parties seek authorisation as outlined above.

Comalco's comments on Tarong Energy submission

5.47 In relation to Tarong's submission that QPTC's dispatch of the GPS using an agreed upon forecasting formula may distort the operation of the NEM, Comalco says these forecasts will be used as part of GPS's operational and management planning as well as for coal procurement. It adds the dispatch forecasts may be reviewed and adjusted each month for changes in circumstances. In addition Comalco says the forecasts are longer term monthly and annual forecasts meaning that QPTC is effectively free to compete in the NEM on a day to day basis.

5.48 In relation to Tarong's comment as to the amount of capacity available to bid into the NEM Comalco submits that the proposed arrangements do not affect whether QPTC will bid GPS's capacity into the NEM but merely how the amount of electricity available for dispatch will be calculated.

5.49 Comalco challenges the suggestion of Tarong that any authorisation granted should be reviewed after the Queensland-New South Wales interconnection. It notes the expansion of BSL and refurbishment of GPS were undertaken as a long term investment and having a review date so soon after the contracts have been entered into defeats the purpose of the authorisation. Comalco adds that in its submission the limited potential for anti-competitive harm is not related to the QNI.

Submission of Powerlink Queensland

5.50 In its submission of 5 November 1999 Powerlink comments that one of the purposes of the NEM is to provide an open access regime for non-discriminatory access to electricity networks. Under the current transmission pricing arrangements Powerlink provides access to loads in return for payment of TUOS charges. (Powerlink is a Government Owned Corporation completely separate to QPTC.)

5.51 Powerlink goes on to say that the arrangements in the IPPA require access to be provided for up to 810MW of load at BSL at charges specified in the IPPA. It then refers to the separate QPTC-BSL agreement (see paragraph 3.11 of this determination) that will enable the smelter to access additional electricity and says that its understanding of this arrangement is that it deals with energy only and not access to transmission lines. Powerlink submits that the Commission may wish the arrangements in relation to the additional power to be provided in a transparent manner.

Response of Comalco

5.52 In Comalco's response of 12 November 1999 it indicates that the agreement referred to by Powerlink does not form part of the applications for authorisation and it does not believe the points raised impact on the applications. It adds that Comalco and Powerlink are still negotiating for BSL transmission access beyond the IPPA and that agreement will be submitted to ERU/ACCC for approval if necessary.

6. The Commission's evaluation

6.1 The Commission's evaluation of the applications is in accordance with the statutory tests as set out in section 4 of this determination.

6.2 In granting authorisation in 1994, the TPC determined that the public benefits were likely to result from the proposed expansion of the Smelter. It considered

The main benefit to the public that the [TPC] sees flowing from the joint venture is the economic development of Australian natural resources that might not otherwise take place. It cannot be assumed that, if the joint venture does not go ahead, the prospective overseas participants would obtain their requirements of aluminium from smelters using Australian bauxite or alumina as feedstock; many other countries have large reserves of bauxite and/or refining and smelting capacity.

6.3 The TPC said that the public is likely to benefit through the further development of an efficient, internationally competitive smelter. In the TPC's view, the public was likely to benefit through an increase in the value of exports and the overall development of the Australian economy.

6.4 Further the TPC accepted that

the proposed expansion of the Boyne smelter and the acquisition of the Gladstone Power Station are interdependent, and that the public benefits attributable to the expansion and operation of the smelter are also attributable to the acquisition and operation of the Power Station.

6.5 The TPC was unable to decide on the information before it that the proposed arrangements were likely to result in a reduction in the cost of electricity to Queensland consumers. It added, however, that any such reduction would be a benefit. There is no material in the current applications that would allow the Commission to draw any conclusions on this issue.

6.6 The TPC also noted that the public would benefit to the extent that the plant proposed decreased the level of environmental pollution associated with its operation. In this regard the Commission notes the submission of Comalco that there has been significant improvement in pollution control in recent years with an average reduction in particulate submissions of 95% and in NO_x emissions of 33%.

6.7 In its 1994 determination the TPC considered that

many of the proposed arrangements relating to the expansion and operation of the Boyne smelter and the acquisition and operation of the Gladstone Power Station are unlikely to lessen competition. ... The Commission also considers that the electricity and power pooling arrangements will have the effect of maintaining the QEC's existing monopoly in the Queensland wholesale market for electricity, despite the sale of the Gladstone Power Station. The Commission considers that it is unfortunate that the sale of the Power Station will not be used to facilitate a greater degree of competition in this market.

6.8 Although the TPC considered some of the arrangements to be anti-competitive, it also considered that there was likely to be substantial public benefit from the joint venture.

6.9 Tarong Energy raised a number of competition issues in relation to the applications. Comalco has responded to those issues and its response is outlined in chapter 5 of this

decision. The only comment that the Commission wishes to raise is in respect of Tarong's suggestion that any authorisation should be reviewed 12 months after the Queensland-New South Wales Interconnection becomes operational. That will be discussed later.

6.10 While the introduction of the NEM has altered the competitive environment in which certain of the agreements operate, it seems to the Commission that in the context of the proposed amendments to the arrangements there will be no increase in the likely anti-competitive effect and, in fact, to some extent the likely anti-competitive effect may be reduced as a consequence of the introduction of the NEM. The Commission also notes the submission of Comalco that the low operating costs of GPS (partly a result of the increased efficiency stemming from the improvements implemented by the GPS joint venture) will make GPS generated electricity an important part of the wholesale market and thus encourage greater competition among generators in Queensland. It also notes Comalco's submission that the amended arrangements will provide QPTC with greater flexibility to trade GPS's output into the NEM and that would provide greater public benefit. While the Commission can draw no conclusions from the material before it as to Comalco's submissions, if its claims are correct the amended agreements are likely to result in an increase in competition.

6.11 As mentioned earlier Comalco submits that the existing agreements have resulted in significant past and ongoing public benefits and in assessing the current applications, the Commission must consider the interdependent relationship between the expansion and operation of the Smelter and the acquisition and operation of GPS. The Commission accepts that submission. On the information before it considers that the public is likely to have benefited in a number of respects and that those benefits will continue with the proposed amendments.

6.12 In broad terms an efficient, internationally competitive smelter has been developed. It has benefited Australia through an increase in exports and the overall development of the Australian economy. More specifically the Commission accepts that the expansion of the smelter has provided benefit and continues to provide benefit in the following terms:

- Substantial capital expenditure – actual expenditure on the construction phase was over \$1.13billion. Approximately 45% of the project cost was spent in Queensland, 33% in other parts of Australia and 22% overseas. Of approximately \$400 million spent on equipment, about 40% was spent in Australia
- Increased employment in relation to the construction and operation of the smelter and in support industries – during peak construction there were over 1300 people working on the project and after construction there were an additional 350 full time jobs
- More revenue for local, state and national governments – the third pot line came fully on-line in November 1997. This increased the smelter's annual operating expenditure by approximately \$400 million resulting in an increase in gross national product. The expansion also enhanced Australia's aluminium exports by \$500 million
- Greater efficiency and competitiveness in aluminium smelting – Comalco claims efficiency increased resulted in lower the unit cost of production by around 18%.

6.13 The Commission is satisfied that the proposed amendments and arrangements satisfy the relevant tests. The Commission is also satisfied on the basis of its consideration that there is no reason to limit the time frame of the authorisation as suggested by Tarong Energy.

6.14 Comalco asks the Commission to authorise all contracts, arrangements, understandings, practices, acts or things made, given effect to, carried on or done under (or in relation to) the proposed arrangements. However, the Commission notes that the proposed amendments and arrangements between the BS joint venturers and the GPS joint venturers (and others) are not yet completely finalised. On that basis the Commission would wish to consider the agreements once finalised to ensure that there is no material inconsistency between the outline of agreements provided in the applications and the agreements as signed.

7. Determination

7.1 For the reasons outlined in Chapter 6, the Commission concludes that it is appropriate to grant authorisation to make the arrangements as set out in the outlines provided by Comalco Limited in respect of applications A40078, A40079 and A40080.

7.2 Authorisation is granted on condition that Comalco provide a copy of all signed agreements that are the subject of the determination on the basis that where any agreement(s) depart(s) materially from the outline provided as part of the applications, the Commission may review that aspect of this determination.

7.3 As provided for in section 88(10) the proposed authorisation will apply to or in relation to any persons who become parties to the arrangements the subject of this determination on or after the date on which the authorisation is granted.

7.4 On 21 October 1999 the Commission issued a draft determination proposing to grant authorisation to applications A40078, A40079 and A40080 in respect of the conduct outlined by the Comalco Limited. There was no request for a pre-decision conference pursuant to section 90A of the Act to be held in respect of the draft. The Commission therefore affirms its draft determination.

7.5 This determination is made on 19 November 1999. If no application for a review of the determination is made to the Australian Competition Tribunal, it will come into force on 11 December 1999. If an application for review is made to the Tribunal, the determination will come into force:

- where the application is not withdrawn – on the day on which the Tribunal makes a determination on the review; or
- where the application is withdrawn – on the day on which the application is withdrawn.