



Public Competition Assessment

18 December 2006

Origin Energy Limited - proposed acquisition of Sun Gas

Introduction

1. On 9 August 2006, Origin Energy Limited (**Origin**) provided a submission to the Australian Competition and Consumer Commission (**ACCC**) seeking informal clearance to acquire both Sun Retail and Sun Gas.
2. The ACCC decided not to oppose the acquisition of Sun Retail on 11 October 2006. Origin subsequently acquired Sun Retail.
3. In relation to Sun Gas, on 11 October 2006 the ACCC advised Origin that, on the basis of its preliminary assessment, it considered that the proposed acquisition would be likely to substantially lessen competition in the relevant markets. No announcement of the decision of 11 October 2006 was made because Origin indicated publicly from the outset that it was prepared to contemplate offering undertakings in relation to the acquisition of Sun Gas if the ACCC considered there to be competition concerns. The ACCC and Origin subsequently engaged in discussions regarding possible undertakings.
4. On 27 November 2006, the Queensland Government announced that AGL was the winning bidder for Sun Gas. In light of this announcement, discussions between the ACCC and Origin Energy Limited regarding possible undertakings were discontinued. The purpose of Public Competition Assessments is to advise the market as to the ACCC's consideration on certain matters.
5. The ACCC made its decision on the basis of the information provided by the merger parties and information arising from its market inquiries. This Public Competition Assessment outlines the basis on which the ACCC has reached its decision on the proposed transaction, subject to confidentiality considerations.

Public Competition Assessment

6. To provide an enhanced level of transparency and procedural fairness in its decision making process, the ACCC issues a Public Competition Assessment for all transaction proposals where:
 - a merger is rejected;

- a merger is subject to enforceable undertakings;
 - the merger parties seek such disclosure; or
 - a merger is approved but raises important issues that the ACCC considers should be made public.
7. This Public Competition Assessment has been issued because the ACCC considered that Origin Energy Limited's proposed acquisition of Sun Gas raised significant competition concerns and an undertaking would be required.
 8. By issuing Public Competition Assessments, the ACCC aims to provide the market with a better understanding of the ACCC's analysis of various markets and the associated merger and competition issues. It also alerts the market to the circumstances where the ACCC's assessment of the competition conditions in particular markets is changing, or likely to change, because of developments.
 9. Each Public Competition Assessment is specific to the particular transaction under review by the ACCC. While some transaction proposals may involve the same or related markets, it should not be assumed that the analysis and decision outlined in one Public Competition Assessment will be conclusive of the ACCC's view in respect of other transaction proposals, as each matter will be considered on its own merits.
 10. Many of the ACCC's decisions will involve consideration of both non-confidential and confidential information provided by the merger parties and market participants. In order to maintain the confidentiality of particular information, Public Competition Assessments do not contain any confidential information or its sources. While the ACCC aims to provide an appropriately detailed explanation of the basis for the ACCC decision, where this is not possible, maintaining confidentiality will be the ACCC's paramount concern, and accordingly a Public Competition Assessment may not definitively explain all issues and the ACCC's analysis of such issues.

The parties

The acquirer: Origin Energy Limited

11. Origin is a public company with interests in electricity, natural gas and LPG retailing, LPG production and distribution, electricity generation and the management of natural gas networks.
12. Origin is one of only two retailers of natural gas to 'non-contestable' customers in south-east Queensland.¹ It is proposed that Full Retail Contestability (FRC) be introduced on 1 July 2007.

The target: Sun Gas

¹ Non-contestable gas customers in Queensland are those that use less than a prescribed amount (1 TJ of gas) per year.

13. Sun Gas is the gas retailing arm of Energex and, prior to its sale to AGL, was Government-owned. Sun Gas supplies gas in Queensland to residential customers and large industrial users as well as to a small number of customers in Victoria and New South Wales.
14. The vast majority of Sun Gas' customers are located to the south of the Brisbane River in the Allgas distribution area.
15. As can be seen from the above descriptions, Origin and Sun Gas are the only two retailers of natural gas to 'non-contestable' customers in south-east Queensland.

Market Definition

16. The ACCC considered the relevant market was the market for the retailing of gas in south east Queensland. The ACCC noted the possibility that the market may be geographically wider, but decided that it was appropriate, in this instance, to confine the market to the south east Queensland region due to the presence of a number of significant barriers to retailing gas in this region, specifically:
 - a. the low levels of gas uptake in south-east Queensland;
 - b. the need to overcome positions of incumbency; and
 - c. the need to obtain sufficient supplies of gas on the Roma to Brisbane Pipeline (RBP), which was capacity constrained.

Timing

17. The following table outlines the timeline of key events in this matter.

Date	Event
09-Aug-2006	ACCC commenced review under the Merger Review Process Guidelines. Market inquiries commenced
04-Sep-2006	Closing date for submissions from interested parties
27-Sep-2006	ACCC requested further information from Origin. Timeline suspended.
11-Oct-2006	ACCC advised Origin that it had serious competition concerns & an undertaking would be required.
12-Oct-2006	ACCC gave Origin further time to make corporate decisions and seek information.
27-Nov-2006	AGL announced as winning bidder for Sun Gas. Discussions between the ACCC and Origin re possible undertakings were discontinued.

Market inquiries

18. The ACCC conducted market inquiries with a range of industry participants, including competitors, potential competitors, input suppliers, industry bodies, other regulatory agencies and other interested parties.

19. Horizontal and vertical integration competition concerns were raised by a number of market participants. In particular, market participants were concerned that if Origin acquired Sun Gas, it would have 100% of the non-contestable gas customers in south east Queensland in the period leading up to and beyond FRC. Further, market participants were concerned that even if Origin gave an undertaking to divest Sun Gas, the ability of the acquirer to prepare for FRC might be limited given the short period before FRC, leading to competitive detriment.

Competition analysis

20. The ACCC noted that the acquisition would have been likely to result in an increase in vertical integration between Origin's gas producing and gas retailing functions. The ACCC considered that competition in production and retailing was the critical issue in analysing whether concerns arose from this increase in vertical integration.
21. It was found that competition from other suppliers existed at the production level. However, the only pipeline that transports natural gas into south east Queensland is the Roma to Brisbane Pipeline (RBP). Market inquiries revealed that the RBP was fully constrained with no spare capacity and was likely to remain so for a considerable amount of time.
22. Post-acquisition, Origin would have been the only retailer of gas to residential customers in the relevant market. Due to the capacity constraints being experienced by the RBP, the ACCC considered the prospect of new entry that would be capable of constraining the merged entity was not very likely. As such, the ACCC had serious competition concerns in this regard.
23. The ACCC also noted that Origin and Sun Gas have both been very significant retailers of gas to industrial customers that took gas from the RBP. Post merger, the ACCC was concerned that the likelihood of existing and new entry constraining the merged entity was low, again due to capacity constraints on the RBP.
24. The ACCC took into consideration the likelihood that full retail contestability would occur on 1 July 2007 and considered that the maintenance of a competitive dynamic in this context was critical.
25. The ACCC noted that Origin and Sun Gas also retailed gas to large customers not connected to the RBP. Market inquiries revealed that in these areas it was likely that the merged entity would have faced sufficient competition from a number of other gas retailers and producers such that competition concerns were unlikely to arise.

26. The ACCC also noted that the proposed acquisition would have increased the vertical integration between Origin's gas retailing operations and its position as the operator of the natural gas distribution networks owned by Envestra Limited. In addition Origin is a significant shareholder in Envestra. However, because Origin was already a vertically integrated network operator and retailer, the proposed acquisition would have been unlikely to have given Origin any additional ability to engage in anticompetitive behaviour.

Undertakings

27. At the commencement of the ACCC's assessment of the matter, Origin raised the possibility of providing undertakings in relation to the proposed acquisition of Sun Gas. The ACCC and Origin subsequently engaged in significant discussions regarding undertakings. During the course of these discussions, the ACCC had regard to the need for Sun Gas to adequately prepare for FRC on 1 July 2007 and the level of control that Origin would have had over Sun Gas during the term of any hold separate period prior to any divestment.

Conclusion

28. Discussions regarding the proposed undertakings were discontinued when it was announced that AGL had entered into an arrangement to acquire Sun Gas.