



ELECTRICITY INDUSTRY ACT 2000
APPLICATION FOR A GENERATION LICENCE

Horizon Energy Holdings Ltd
ARBN 078 377 527

CMS Generation Horizon Energy Holdings Ltd
ARBN 078 377 372

Horizon Energy Investment (No 2) Pty Ltd
ACN 078 121 187

NRGenerating Holdings (No. 4) B.V.
ARBN 073 074 530

Loy Yang Power Management Pty Limited
ACN 077 985 758

and

Loy Yang Marketing Management Company Pty Limited
ACN 105 758 316

NOTICE OF DECISION

8 April 2004

SUMMARY

In accordance with the provisions of section 19 of the *Electricity Industry Act 2000* (**the EI Act**) the Essential Services Commission (**the Commission**) has decided to grant a licence to generate electricity for supply or sale in Victoria to be held jointly by the following applicants:

- CMS Generation Horizon Energy Holdings Ltd ARBN 078 377 372
- Horizon Energy Holdings Ltd ARBN 078 377 527
- NRGenerating Holdings (No 4) BV ARBN 073 074 530
- Horizon Energy Investment (No 2) Pty Ltd ACN 078 121 187
- Loy Yang Power Management Pty Limited (**LYPM**) ACN 077 985 758 and
- Loy Yang Marketing Management Pty Limited (**MMCo**) ACN 105 758 316.

This follows the revocation of the electricity generation licence by the Commission and currently held by:

- CMS Generation Horizon Energy Holdings Ltd
- Horizon Energy Holdings Ltd
- NRGenerating Holdings (No. 4) B.V.
- Horizon Energy Investment (No 2) Pty Ltd
trading on behalf of the above mentioned entities as Loy Yang Power; and
- Loy Yang Power Management Pty Ltd as the agent of Loy Yang Power.

Note: These entities are collectively known as the Loy Yang Power Partnership.

With the exception of MMCo, that is an additional licensee, the new licensees are the same entities listed on the previous licence, but now have a new ownership structure. The primary function of LYPM on behalf of the other licensees is to be responsible for generating electricity, whilst MMCo will be responsible for the dispatching and marketing activities of Loy Yang Power. The roles and responsibilities of LYPM and MMCo are outlined in the attached **Schedule**.

This new ownership and operational structure does not contravene the EI Act as it relates to ‘cross – ownership’ or ‘prohibited interests’. These matters have been dealt with separately in the decision by the Federal Court of Australia dated 19 December 2003 at **FCA 1525** and the *Electricity Industry (Prohibited Interest) Regulations 2003* (**the Regulations**).

The decisions to revoke the existing licence and to grant a generation licence to the applicants do not take effect unless and until the applicants inform the Commission that completion of the sale of the shares in each company that comprises the Loy Yang Power Partnership to GEAC CoOp. The sale of the shares is between GEAC Operations Pty Ltd (a wholly owned subsidiary of the Great Energy Alliance Pty Ltd) and the current owners of the Loy Yang Power Station under which GEAC will acquire 100 percent ownership of each entity constituting the Loy Yang Power Partnership.

BACKGROUND

Requirement to obtain a licence

1. Section 16 of the EI Act provides that a person must not engage in the generation of electricity unless the person is -
 - the holder of a licence authorising that activity; or
 - exempted from the requirement to obtain a licence in respect of that activity.

Entitlement to apply for a licence

2. Section 18 of the EI Act provides that a person may apply to the Commission for a licence authorising one or more of the following activities as specified in the licence -
 - (a) to generate electricity for supply or sale;
 - (b) to transmit electricity;
 - (c) to distribute or supply electricity; or
 - (d) to sell electricity.

The applicants

3. The joint applicants (**the applicants**) that will operate the Loy Yang Power Station (and mine) are:
 - CMS Generation Horizon Energy Holdings Ltd ARBN 078 377 372
 - Horizon Energy Holdings Ltd ARBN 078 377 527
 - NRGenerating Holdings (No 4) BV ARBN 073 074 530
 - Horizon Energy Investment (No 2) Pty Ltd ACN 078 121 187
 - Loy Yang Power Management Pty Limited (LYPM) ACN 077 985 758
 - Loy Yang Marketing Management Company Pty Limited (MMCo) ACN 105 758 316

Loy Yang Marketing Management Company Pty Ltd (MMCo) as already cited, is the additional applicant for the licence to generate electricity

4. The Commission has been advised that there will be no change to the Loy Yang Power Partnership and that (in addition to MMCo) those entities will remain the holders of the licence. This is possible because the total shareholdings in the four entities:

- CMS Generation Horizon Energy Holdings Ltd
- Horizon Energy Holdings Ltd, NRGenerating Holdings (No. 4) B.V.
- NRGenerating Holdings (No 4) BV ARBN 073 074 530
- Horizon Energy Investment (No 2) Pty Ltd

will be purchased by the Great Energy Alliance Corporation Pty Ltd (**GEAC**) through its wholly owned subsidiary Great Energy Alliance Corporation Operations Pty Ltd (**GEAC OpCo**).

5. The shares in GEAC are owned and controlled by the following entities:

SHAREHOLDER	EQUITY CONTRIBUTION
The Australian Gas and Light Company (AGL)	35.0 %
The Tokyo Electric Power Company, Inc. (TEPCO)	35.0 %
Commonwealth Bank of Australia (CBA)	14.5 %
Motor Traders' Association of Australia Superannuation Fund Pty Ltd	11.2 %
Westscheme Pty Ltd	4.3 %

6. The following entities have a holding company, Loy Yang Marketing Holdings Pty Ltd (**MM Hold Co**), which has a wholly owned subsidiary in the form of the additional licensee, Loy Yang Marketing Management Company Pty Ltd (MMCo).

SHAREHOLDER	EQUITY CONTRIBUTION
Tokyo Electric Power Company International BV (TEPCO)	49.97 %
Commonwealth Bank of Australia (CBA)	26.32 %
Motor Trades' Association of Australia superannuation fund Pty Ltd	17.11 %
Westscheme Pty Ltd	6.60 %

7. GEAC, (and in particular, AGL) is quarantined from any involvement in this entity and cannot exercise any influence over MMCo and its dispatching and marketing activities.
8. Section 16 of the EI Act provides that a person must not '*engage*' in the generation, transmission, distribution or retailing of electricity without a licence, unless the person is specifically exempt. The Commission has decided pursuant to section 16 of the EI Act that both MMCo and LYPM, which have split their functions, are engaged in activities that require that they both be licensed.

The application

9. On 29 December 2003, and following a decision on 19 December 2003 in the Federal Court of Australia, the applicants formally applied for a licence to generate electricity for supply and sale in Victoria. The applicants provided the Commission with details of each entity's background, structure, and experience in the energy industry.
10. The application also included a statement of the applicants' ability to comply with all applicable codes and guidelines upon granting of the generation licence.

Advertising the application

11. The Commission complied with the requirements of section 19(6) of the EI Act by publishing a notice in *The Age* newspaper on 8 January 2004 inviting interested persons to make submissions to the Commission in respect of the application by the close of business on 23 January 2004. By letter dated 8 January 2004 the Commission also wrote directly to each licensed entity and stakeholders inviting them to make a submission in respect of the application. Invitations to comment were also sent to the members of the Commission's Customer Consultative Committee and other interested parties.
12. The Commission did not receive any submissions in respect of the application.

Provisions relating to the Commission's decision

13. Section 19(1) of the EI Act provides that, subject to sub-section (2) the Commission may grant or refuse the application for a generation licence for any reason it considers appropriate, having regard to the objectives of the Commission under the EI Act and under the *Essential Services Commission Act 2001* (the ESC Act).
14. The objectives specified under section 10 of the EI Act are -
 - (a) to the extent that it is efficient and practicable to do so, to promote a consistent regulatory approach, between the electricity industry and the gas industry; and
 - (b) to promote the development of full retail competition.
15. Section 8 of the ESC Act provides that –
 - (a) In performing its functions and exercising its powers, the primary of objective of the Commission is to protect the long-term interests of Victorian consumers with regard to the price, quality and reliability of essential services.
 - (b) In seeking to achieve its primary objective, the Commission must have regard to the following facilitating objectives:
 - (i) To facilitate efficiency in regulated industries and the incentive for efficient long-term investment;
 - (ii) To facilitate the financial viability of regulated industries;
 - (iii) To ensure that the misuse of monopoly or non-transitory market power is prevented;
 - (iv) To facilitate effective competition and promote competitive market conduct;
 - (v) To ensure that regulatory decision making has regard to the relevant health, safety, environmental and social legislation applying to the regulated industry;
 - (vi) To ensure that users and consumers (including low-income or vulnerable customers) benefit from the gains from competition and efficiency; and
 - (vii) To promote consistency in Regulations between States and on a national basis.
16. Section 19(2) of the EI Act provides that the Commission must not grant an application for a generation licence unless the Commission is satisfied that subject to sub-section (4) the applicant has the technical capacity to comply with the conditions of the licence.

Section 19(4) states –

The Commission does not have to be satisfied as to the applicant's technical capacity to comply with the conditions of the licence at the time it is issued if –

- (a) the activities specified in the licence are not likely to be commenced to be carried out within the next following 12 months; and*
- (b) the application is granted subject to such conditions as are determined by the Commission relating to further approval of the applicant's technical capacity or approval of future facilities necessary for the carrying out of the activities.*

CONSIDERATION OF THE APPLICATION

General approach

17. Consistent with its objectives under the ESC Act and the requirements of the EI Act for granting a licence, the Commission is of the view that unless there are good reasons to the contrary, its approach should be to grant a licence to an applicant. The principal grounds on which the Commission might refuse an application would be to protect the interests of customers, or if it believed that the licensee did not have the technical capacity to comply with the conditions of the licence or the licensee did not satisfy the cross-ownership provisions provided in the EI Act.
18. The granting of a licence to the following entities is consistent with the matters raised in paragraph 17:
 - CMS Generation Horizon Energy Holdings Ltd ARBN 078 377 372
 - Horizon Energy Holdings Ltd ARBN 078 377 527
 - NRGenerating Holdings (No 4) BV ARBN 073 074 530
 - Horizon Energy Investment (No 2) Pty Ltd ACN 078 121 187
 - Loy Yang Power Management Pty Limited ACN 077 985 758
 - Loy Yang Marketing Management Company Pty Limited ACN 105 758 316

ISSUES

Technical Capacity

19. The applicants have provided particulars in the application of their technical capacity to comply with the conditions of the licence and the following points should be noted:
 - there will be no change in the current personnel employed or engaged to operate and manage the generation and related activities at Loy Yang, except that 12 personnel previously employed on behalf of the Loy Yang Power Partnership will be transferred to and employed by MMCo, which has the primary operational functions. These persons will, amongst other things, be responsible for directing the operations of the Power Station, undertaking the dispatch and marketing activities and managing the relationships with the regulators.

- the Commission has been advised that MMCo has applied for an Australian Financial Services Licence that confirms the transfer of 12 personnel from the Loy Yang Power partnership to MMCo. It is understood that ASIC will grant the financial services licence following settlement of the purchase and the grant of the licence by the Commission.
 - a services deed will be operational between LYPM and MMCo to allow MMCo to call on expertise and / or personnel as and when required from LYPM including IT, Human Resources, procurement, legal / insurance services and other non – core activities.
 - a comprehensive risk management strategy has been developed
20. The applicants have confirmed familiarity with the operation of the National Electricity Code and will continue and maintain registration and compliance with NEMMCO.

Cross-ownership and ‘prohibited interest’ issues

21. The issues of cross - ownership and ‘prohibited interest’ have been considered and dealt with by other means. This includes the making of the *Electricity Industry (Prohibited Interest Regulations) 2003* (the Regulations). The impact on competition through cross – ownership was also considered in the matter of *Australian Gas Light Company v. Australian Competition and Consumer Commission* [2003] FCA 1525. This reference is located at http://www.austlii.edu.au/au/cases/cth/federal_ct/2003/1525.html.
22. The matter of prohibited interests is addressed by sections 68(3) and (4) of the EI Act and the subsequent making of Regulations at sections 61 and 119 of the EI Act. The Regulations are binding on the Commission. Section 3(2) of the Regulations ensures that operation of the EI Act is varied in the matter of cross – ownership and prohibited interests. The Regulations have the effect of increasing the permissible limit of economic interest from 20 % to 35 % in a corporation. AGL has a 35 % interest in GEAC.

Compliance with Codes and Rules

23. Victorian electricity generation licences require licensees to comply with all applicable provisions of the Distribution Code and the System Code.
24. The Commission notes that generation licences also include a requirement to comply with all relevant laws.

DECISION

25. The Commission is satisfied that -
- the applicants have the technical capacity to comply with the conditions of the licence to be granted; and
 - the granting of a licence would not be inconsistent with the EI Act.

26. Having regard to the objectives specified in section 10 of the *Electricity Industry Act 2000* and section 8 of the *Essential Services Commission Act 2001*, the Commission has decided to revoke the existing licence and to grant a generation licence to the applicants. This does not take effect unless and until the applicants inform the Commission that completion of the sale of the shares to GEAC OpCo has occurred. In making its decision to grant the applicants a generation licence, the Commission also requests that the applicants provide confirmation of the granting of an Australian Financial Services Licence by the Australian Securities and Investments Commission.

The sale of shares is to GEAC Operations Pty Ltd (a wholly owned subsidiary of the Great Energy Alliance Pty Ltd) by the current owners of the Loy Yang Power Station under which GEAC will acquire 100 percent ownership of each entity constituting the Loy Yang Partnership. The new licensees are:

- CMS Generation Horizon Energy Holdings Ltd ARBN 078 377 372
- Horizon Energy Holdings Ltd ARBN 078 377 527
- NRGenerating Holdings (No 4) BV ARBN 073 074 530
- Horizon Energy Investment (No 2) Pty Ltd ACN 078 121 187
- Loy Yang Power Management Pty Limited ACN 077 985 758; and
- Loy Yang Marketing Management Pty Limited ACN 105 758 316.

A copy of the licence forms an attachment to this decision.

SCHEDULE

The relevant responsibilities of MMCo & LYPM

The relevant responsibilities of MMCo are to be as follows:

- determination and management of the scheduling of the availability of the power station
- determination and management of trading, dispatch and rebidding and contracting strategies
- placement of dispatch offers, rebids and ancillary services offers
- negotiating, entering into and managing electricity derivative contracts or power purchase agreements
- dealing with all relevant regulators
- managing Partnership assets in relation to dispatch and marketing activities
- significant management responsibilities including reporting to the Partnership on trading activities, ensuring audits of financial statements and submitting annual budgets to the Partnership.

The relevant responsibilities of LYPM are to be as follows:

- generating electricity from the Power Station at the quantities and the times determined by NEMMCO following bids, if any, by MMCo
- acting in accordance with instructions from NEMMCO
- monitoring and reporting on the need for improvements and maintenance to the Power Station and Mine
- maintenance of the Power Station and the Mine at times determined in conjunction with MMCo
- significant management responsibilities including maintenance plans and providing breakdown of operating costs to the Partnership.

Undertakings to the ACCC and / or the Federal Court of Australia - AGL

The Federal Court of Australia [see FCA 1525] determined that the acquisition would not substantially lessen competition if AGL complies with a number of undertakings to the ACCC and / or the Federal Court of Australia. The undertaking given by AGL provides, amongst other things, the following:

- AGL's interest in Loy Yang must not exceed 35 percent
- that the Partnership appoints MMCo to be solely responsible for undertaking Dispatch and Marketing Activities as the agent of the Partnership. The Consortium Agreements must provide that any dealings with MMCo and AGL will be at arm's length and that AGL will not participate in the appointment or supervision of the executive management of MMCo
- that AGL is prohibited from having an economic interest in MMCo
- that AGL will not otherwise be involved in the Dispatch and Marketing Activities of Loy Yang
- that AGL will not have access to confidential customer information or confidential generator information.

The aforesaid undertaking also includes provision for a detailed Risk Management Policy.