



# **DRAFT**

# **Amended Ring-fencing**

# **Guideline**

## **Explanatory Statement**

July 2017

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Inquiries about this publication should be addressed to:

Australian Energy Regulator  
GPO Box 520  
Melbourne VIC 3001

Tel: 1300 585165

Email: [AERInquiry@aer.gov.au](mailto:AERInquiry@aer.gov.au)  
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## Request for submissions

Interested parties are invited to make written submissions to the Australian Energy Regulator (**AER**) regarding this paper by the close of business on **15 August 2017**.

Submissions should be sent electronically to: [ringfencing@aer.gov.au](mailto:ringfencing@aer.gov.au).

Alternatively, submissions can be mailed to:

Mr Chris Pattas  
General Manager, Networks  
Australian Energy Regulator  
GPO Box 520  
Melbourne VIC 3001

We prefer that all submissions be publicly available to facilitate an informed and transparent consultative process. Submissions will be treated as public documents unless otherwise requested. Parties wishing to submit confidential information are requested to:

- clearly identify the information that is the subject of the confidentiality claim
- provide a non-confidential version of the submission in a form suitable for publication.

All non-confidential submissions will be placed on our website at [www.aer.gov.au](http://www.aer.gov.au). For further information regarding our use and disclosure of information provided to us, see the ACCC/AER Information Policy, June 2014 available on our website.

Enquiries about this paper, or about lodging submissions, should be directed to [ringfencing@aer.gov.au](mailto:ringfencing@aer.gov.au).

## Shortened forms

Shortened Form	Extended Form
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
DNSP	distribution network service provider
Guideline	Australian Energy Regulator, Electricity Distribution Ring-Fencing Guideline, November 2016
NER or the rules	National Electricity Rules
TNSP	transmission network service provider

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# Definitions

Terms	Definitions
affiliated entity	<p>in relation to a DNSP, means a legal entity:</p> <ul style="list-style-type: none"><li>(a) which is a direct or indirect shareholder in the DNSP or otherwise has a direct or indirect legal or equitable interest in the DNSP</li><li>(b) in which the DNSP is a direct or indirect shareholder or otherwise has a direct or indirect legal or equitable interest</li><li>(c) in which a legal entity referred to in paragraph (a) or (b) is a direct or indirect shareholder or otherwise has a direct or indirect legal or equitable interest</li></ul>
contestable electricity services	<p>means:</p> <ul style="list-style-type: none"><li>(a) other distribution services and</li><li>(b) other electricity services.</li></ul>
electricity information	<p>means information about electricity networks, electricity customers or electricity services, excluding aggregated financial information, or other service performance information, that does not relate to an identifiable customer or class of customer</p>
existing service	<p>in relation to a DNSP means a type of service that the DNSP was providing on 1 December 2016</p>
information register	<p>means the register established and maintained by a DNSP under clause 4.3.5 of the Guideline</p>
law	<p>means any law, rule, regulation or other legal obligation (however described and whether statutory or otherwise)</p>
legal entity	<p>means a natural person, a body corporate (including a statutory corporation or public authority), a partnership, or a trustee of a trust, but excludes staff in their capacity as such</p>
NEL	<p>means, for the purposes of the application of this Guideline in a participating jurisdiction, the National Electricity Law set out in the schedule to the National Electricity (South Australia) Act 1996 (SA), as applied by the participating jurisdiction and subject to any modification made to the National Electricity Law by that jurisdiction</p>

NER	means, for the purposes of the application of this Guideline in a participating jurisdiction, the rules called the National Electricity Rules made under Part 7 of the National Electricity Law, subject to any modification made to the National Electricity Rules by that jurisdiction
non-distribution services	(a) transmission services and (b) other services
office	Means, as the case may be: (a) a building (b) an entire floor of a building or (c) a part of a building that has separate and secure access requirements such that staff from elsewhere in the building do not have unescorted access to it
office register	Means the register established and maintained by a DNSP under clause 4.2.4(a) of the Guideline
officer	in relation to a legal entity (such as a DNSP) means: (a) a director or company secretary of the legal entity (b) a person who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the legal entity or (c) a person who has the capacity to affect significantly the legal entity's financial standing
other distribution services	means distribution services other than direct control services  note: this includes negotiated distribution services and distribution services that are not classified
other electricity services	means services for the supply of electricity, or that are necessary or incidental to the supply of electricity other than: (a) transmission services or (b) distribution services
other services	means services other than: (a) transmission services or (b) distribution services
regional office	means an office that has less than 25,000 customer connection points within a 100 kilometre radius of that office

staff of an entity (such as a DNSP), includes:

- (a) employees of the entity
- (b) direct or indirect contractors to the entity (whether the contractors are individuals or corporate or other entities)
- (c) employees of direct or indirect contractors to the entity
- (d) individuals (including secondees) otherwise made available to the entity by another entity

staff position in relation to a DNSP or a related electricity service provider, means a position within the organisational staffing structure of the DNSP or related electricity service provider (as the case may be) that involves the performance of particular roles, functions or duties.

staff register means the register established and maintained by a DNSP under clause 4.2.4(b) of the Guideline

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# 1 About the Ring-fencing Guideline amendment

We published our Electricity Distribution Ring-fencing Guideline (**Guideline**) on 30 November 2016. Since that time, we have become aware of some aspects of the Guideline that could benefit from being made clearer or otherwise revised to avoid unintended consequences. This Explanatory Statement provides an explanation as to the changes we are proposing to make.

The Guideline has yet to be fully implemented by distribution network service providers (**DNSPs**). While the Guideline came into effect on 1 December 2016, full compliance is not required until 1 January 2018. This thirteen month period is referred to as the implementation period. During this period, DNSPs have been assessing their compliance with the Guideline and the steps needed to achieve compliance. We have been actively encouraging DNSPs to share with us their plans to achieve compliance by no later than the end of the implementation period. During this implementation period, in which we have been consulting with DNSPs and industry more generally, we have identified and received suggestions that some revisions to the Guideline may be desirable.

This Explanatory Statement is only concerned with these proposed amendments to the Guideline. For an explanation of the Guideline as a whole (which is otherwise unaffected by these proposed changes), refer to the Explanatory Statement that accompanied our Guideline in November 2016. These documents can be found on the AER's website.

This Guideline amendment process is only intended to address the need for improved clarity and to address unintended consequences stemming from the way the Guideline is presently drafted. We do not intend to reconsider the scope or intent of the Guideline or to look at any broader changes. This is because insufficient time has passed to warrant a review of whether or not the Guideline is working as intended. Our intention is that the Guideline amendments be limited to addressing the issues outlined in this document.

## 1.1 Background to the Ring-fencing Guideline

Ring-fencing is the identification and separation of regulated monopoly business activities, costs and revenues from those that are associated with providing services in a contestable market. Ring-fencing obligations that apply to DNSPs generally require the separation of the accounting and functional aspects of regulated distribution services from other services provided by the DNSP.

The Guideline sets out the obligations a network business must abide by to separate its regulated monopoly services from any services it may seek to offer to contestable markets. As noted by the Australian Energy Market Commission (**AEMC**), the following types of behaviours by DNSPs result in harm that ring-fencing aims to avoid:<sup>1</sup>

- cross-subsidising an affiliate's services in contestable markets with revenue derived from its regulated services

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<sup>1</sup> AEMC, *National Electricity Amendment (Expanding competition in metering and related services) Rule 2015*, December 2015, p. 399.

- discrimination in favour of a DNSP's related electricity service provider operating in a contestable market
- providing related electricity service providers with access to commercially sensitive information acquired through provision of regulated services
- restricting access of other participants in contestable markets to infrastructure services provided by the DNSP, or providing access on less favourable terms than to its related electricity service providers.

We expect the Guideline will aid development of competitive markets where competition is feasible and support efficient, incentive-based regulation of monopoly networks where competition is not feasible.

## 1.2 Rule Requirements

The Guideline is made and amended under clause 6.17.2 of the National Electricity Rules (**NER**).

Clause 1.5 of the Guideline also allows us to amend the Guideline from time to time in accordance with clause 6.17.2 of the rules and the distribution consultation procedures.

Clause 6.17.2(d) of the NER states that:

*In developing or amending the Distribution Ring-Fencing Guidelines, the AER must consult with participating jurisdictions, Registered Participants, AEMO and other interested parties, and such consultation must be otherwise in accordance with the distribution consultation procedures.*

The distribution consultation procedures at clause 6.16 of the rules state we must publish the amended Guideline, an explanatory statement and an invitation for written submissions, allowing no less than 30 business days for submissions to be provided. Within 80 business days of commencing consultation, we must publish our decision with reasons, and the amended Guideline itself.

### 1.3 Indicative timetable

Event	Date
AER publishes Draft Amended Guideline and Explanatory Statement, invitation for written submissions	4 July 2017
Submissions close (30 business days after invitation)	15 August 2017
AER publishes final Amended Guideline	October 2017
NER deadline for publishing the final Amended Guideline (80 business days from commencement of consultation process)	24 October 2017

## 2 Proposed amendments and reasons

This section sets out issues that have been raised in our discussions with DNSPs as they have worked to implement the Guideline. Some of these issues stem from concerns that the Guideline, as written, should be amended to address the following unintended effects:

- the definition of a 'related electricity service provider' includes all affiliates, not just those that provide electricity services
- in event of an emergency, a DNSP may not be able to support other DNSPs to help restore power to customers because of restrictions on the branding of these services.

Other issues stem from specific practical scenarios identified by DNSPs where we consider that additional exceptions to the requirements of the Guidelines are reasonable, having regard to the practicalities of compliance and the very low levels of harm (if any) that are likely to arise from non-compliance.

### 2.1 Proposed changes

The proposed revisions are set out in the sections below.

#### 2.1.1 Revised definition of 'Related Electricity Service Provider'

A number of DNSPs raised concerns with us in regard to the way that a related electricity service provider (RESP) is defined. The Guideline states that a:

"Related Electricity Service Provider, in relation to a DNSP, includes:

- (a) an affiliated entity of the DNSP; and
- (b) the part of the DNSP that provides contestable electricity services."

It was intended that the term RESP be defined so as to include those parts of the DNSP that offer contestable electricity services and a DNSP's affiliates that offer contestable electricity service. As worded at present, the definition of RESP includes an affiliate entity even if the affiliate does not offer electricity services.

In addition, the definition of a RESP captures a DNSP that is related to another DNSP through ownership. We propose to revise this definition so that a RESP only includes those parts of the DNSP or an affiliate that offer contestable electricity services. To take account of the fact that a DNSP that is affiliated with a DNSP may also provide contestable electricity services, the revised definition of a RESP excludes the part of the affiliated DNSP that provides direct control services or prescribed or negotiated transmission services.

The revised definition is proposed to be:

"Related Electricity Service Provider, in relation to a DNSP, includes:

- (a) an affiliated entity of the DNSP; and
- (b) the part of the DNSP;

that provides contestable electricity services, but excludes a part of an affiliated entity that provides direct control services."

We also propose to make a minor amendment to clause 3.1(d)i. to clarify that a DNSP is able to allow a TNSP to use the DNSP's assets to provide transmission services, and to allow another DNSP to use the DNSP's assets to provide distribution services, where the other requirements of that clause are satisfied.

## 2.1.2 Branding

It was intended that the Guideline would prevent a DNSP from using its brand name to offer contestable electricity services. This obligation aimed to avoid any confusion that might be created from a DNSP providing electricity services that are available in contestable markets and that are not regulated by the AER. However, as written, the provision unintentionally extends the restriction to all services offered by an affiliate of the DNSP, not just electricity services. We therefore propose to revise clause 4.2.3(a) of the Guideline, by adding additional references to "contestable electricity services" to make our original intentions clear. We also propose to revise clause 4.2.3(a)iii of the Guideline to make it clear that the DNSP can continue to promote its own services as long as the other requirements of clause 4.2.3(a) are satisfied.

A further issue we have considered is how the branding restrictions in the Guideline could affect operation of the AER's Shared Asset Guideline. In some limited circumstances, a DNSP is permitted to make simultaneous use of assets in the regulatory asset base (RAB) to generate unregulated revenues (as contemplated in the shared asset provisions in clause 6.4.4 of the NER). Where this additional use would not materially prejudice the use of the assets to provide direct control services, we consider it reasonable for the part of a DNSP that provides those other distribution services to be able to use those assets, even if they are branded as assets involved in the supply of direct control services by a DNSP. There are very few examples of these sorts of shared assets. A prime example is the unused capacity of a pole or conduit that can be rented to, say, other utilities. In these limited circumstances, we consider it reasonable for a DNSP to retain existing branding of these assets (if any) and to be able to undertake ancillary activities (such as invoicing) using the DNSP's direct control service brand.

We therefore propose to include an additional provision (new clause 4.2.3(b)iii.) in the Guideline so that the branding requirements of the guideline do not prevent such use of the DNSP's direct control service brand. The exception will not be available in relation to assets, such as trucks, where the use of the asset for both purposes is not simultaneous. Further, the exception will also not be available for the use of that brand by an affiliated entity of the DNSP. The wider range of services that can be provided by an affiliated entity of the DNSP means that the affiliated entity would have greater opportunities (than the DNSP itself) to gain an unfair advantage over its competitors by using the DNSP's direct control service brand in connection with services that are not direct control services. Overt use of a DNSP's brand to promote the services associated with the use of shared assets would not be consistent with the intent of this exception to the branding obligations.

### 2.1.3 Emergency response

There are times when significant network outages occur and DNSPs are called on to provide support to other DNSPs, for example, as a result of severe weather events. The Guideline contains provisions to facilitate staff and asset sharing in these emergency response circumstances. However, the branding provisions may unintentionally constrain this activity. We propose to include an additional provision (new clause 4.2.3(b)iv.) in the Guideline so that the Guideline's branding requirements do not restrict such cooperation.

### 2.1.4 Information disclosure

Clause 4.3.3 requires that a DNSP must not disclose confidential information to any person, including a RESP, unless specific criteria are met. These provisions around disclosure of information by a DNSP were intended to include exceptions in certain specific circumstances, such as where there is a necessity for disclosure or where explicit informed consent has been obtained from the customer to whom the information relates.

Based on our discussions with DNSPs as they have worked to implement the Guideline, we have identified additional situations where we consider that disclosure is appropriate (without the need for the information to be shared under clause 4.3.4). These are:

- disclosure that is necessary to enable another legal entity to provide its own services, where the information is requested by or on behalf of a customer or prospective customer of that legal entity.<sup>2</sup> This recognises that, in some circumstances, the relevant customer may not otherwise be dealing with the DNSP directly. It is intended that the exception will apply where the customer makes the request to the other legal entity, rather than to the DNSP, and where the customer makes the request via a developer or other intermediary.<sup>3</sup>
- disclosure to facilitate co-operation in responding to severe weather events or other emergencies beyond a DNSP's reasonable control.<sup>4</sup>
- disclosure for research purposes, provided that the person or entity doing the research does not then disclose the information to a related electricity service provider of the DNSP.<sup>5</sup>

We propose to amend clause 4.3.3, and to make some consequential amendments to clauses 4.3.4(a), (c) and (e), so that these additional types of disclosure are permitted under clause 4.3.3 and do not trigger the information sharing requirements of clause 4.3.4.

To provide greater transparency of the circumstances in which a DNSP discloses information to an affiliated entity, we also propose to amend clause 4.3.3(g) so that

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<sup>2</sup> Clause 4.3.3(d)

<sup>3</sup> This exception is intended to enable the DNSP to disclose information where the customer is the customer of any other legal entity, not just an affiliated entity of the DNSP. Clause 4.1 of the Guideline will continue to apply in relation to any disclosure of information by the DNSP permitted by this exception.

<sup>4</sup> Clause 4.3.3(e)

<sup>5</sup> Clause 4.3.3(f)

information can only be disclosed under clause 4.3.3(g) where a related electricity service provider has requested the disclosure, rather than on the DNSP's own initiative.

### **2.1.5 Staff sharing registers**

In broad terms, the Guideline requires a DNSP to separate staff involved in regulated services from those involved in contestable services. However, staff who do not have access to electricity information are exempted from this requirement. Staff who have access to electricity information may also be shared where those staff do not have an opportunity to use that electricity information to engage in conduct that is contrary to the intent of the Guideline.

Clause 4.2.4 currently requires DNSPs to include on their staff and office registers the position descriptions of corporate staff exempt from the non-sharing obligations. However, we consider the types of corporate positions that may be shared are relatively intuitive and well understood as a matter of usual corporate and commercial practice. We consider that this obligation is therefore likely to be unnecessarily burdensome to DNSPs. We propose to remove this requirement from clause 4.2.4(b) by including an exemption for 4.2.2(b)i.b.

### **2.1.6 Sharing of information**

With respect to information registers, clause 4.3.5 requires a DNSP to include all legal entities (including RESPs) who request access to confidential information shared with a RESP on their information register. However, clause 4.3.4 says that a DNSP is only required to disclose information where the legal entity is competing, or is seeking to compete, with the DNSP or a RESP of the DNSP in relation to the provision of contestable electricity services. We propose to amend 4.3.5(a) to exclude affiliates of a DNSP who are legal entities but not RESPs and therefore do not provide contestable electricity services.

### **2.1.7 Obligations on contractors to DNSPs**

Clause 4.4.1 is concerned with conduct of service providers to DNSPs. The clause currently has the effect that any new agreement between a DNSP and a service provider must contain provisions that require the service provider to comply with the co-location, staff sharing, information sharing and branding obligations of the Guideline. This means that even agreements for services that are unrelated to the provision of regulated (direct control) services would be affected. For example, security services, cleaning services, etc., must include clauses for all of the relevant ring-fencing provisions. We propose to amend clause 4.4.1(a) so that this obligation is limited to agreements for the provision of services to the DNSP that enable or assist the DNSP to supply direct control services.

## **2.2 Other minor changes**

### **2.2.1 Legal separation - additional examples of exempt services**

Clause 3.1 of the Guideline requires a DNSP to provide distribution services only. Non-distribution services therefore must be provided by a different legal entity. A number of exceptions are provided where a DNSP provides services in-house that are not subject to

this requirement for separation. We propose to add exceptions for regulatory services, which are commonly found within regulated businesses that provide advice on compliance and other regulatory related issues affecting DNSPs, and for the provision of corporate services (more generally) to entities other than related electricity service providers.

For consistency, we also propose to make minor amendments to clauses 4.2.1(b)i.c. and 4.2.2(b)i.c. of the Guideline (which relate to staff and office separation) to make it clear that those clauses apply in relation to regulatory services.

### **2.2.2 Typographical changes**

A number of minor typographical changes have been made to improve the Guideline. These changes are shown in mark-up in the revised version of the Guideline.