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Via email: [Ringfencingguideline2016@aer.gov.au](mailto:Ringfencingguideline2016@aer.gov.au)

Dear Chris

**Re: Draft Ring-fencing Guideline**

AusNet Services is pleased to have the opportunity to contribute to the draft phase of the Australian Energy Regulator's (AER) development of the ring-fencing guideline (**Draft Guideline**) for Distribution Network Services Providers (DNSPs).

Emerging end-user facing markets for energy related services are the catalyst for this ring-fencing review. The AER notes in its Explanatory Statement accompanying the Draft Guideline that (p 10):

The current guidelines were designed to support the structural separation of retail, transmission, distribution and generation. The current guidelines do not adequately account for new and emerging technologies like solar PV, network energy storage or market reforms around metering and other service contestability.

In revising the ring-fencing framework, in our view, customer interests should be the central focus in accordance with the national electricity objective. In pursuing this focus, it is critical to acknowledge that networks have an important role in integrating and developing emerging technologies within the distribution system. The ability of the DNSP to innovate and respond to the developing needs of the market is essential for the safety and reliability of the network. It is important then, that the DNSP's ability to facilitate the evolution of the electricity sector is not compromised through the new ring-fencing arrangements.

In reviewing the Draft Guideline we have identified various constraints on DNSP activities that may inadvertently impact on the efficiency of providing distribution services and therefore, do not promote customer interests. We understand that such impacts may not be intended, and therefore we encourage the AER to clarify the ring-fencing guideline to address these concerns.

Our earlier submission suggested that the development of the guideline should be guided by a central focus on customer outcomes, based on the principles of proportionality and functionality. We believe these remain the key guiding principles to inform the finalisation of the guideline.

Our detailed submission is attached. We look forward to continuing to engage with the AER in the guideline development process. If you have any queries regarding our submission we would be pleased to discuss these with you.

Yours sincerely,

Alistair Parker



**Executive General Manager – Regulated Energy Services**

# AusNet Services – Submission on the AER’s Draft Ring-fencing Guideline

## 1. Structure of this submission

AusNet Services is pleased to have the opportunity to contribute to the draft phase of the Australian Energy Regulator’s (**AER**) development of the ring-fencing guideline (**Draft Guideline**) for Distribution Network Services Providers (**DNSPs**) under Rule 6.17 of the National Electricity Rules (**NER**).

The submission includes the following sections:

**Section 2** of this Submission proposes a short set of criteria informed by best-practice regulatory principles, against which we have framed our feedback on the Draft Guideline.

**Sections 3 to 6** of this Submission respond to each of the key components of the Draft Guideline including:

- Legal separation requirements in clauses 3.1 (**section 3**);
- Non-discrimination requirements in clause 4.1 (**section 4**);
- Functional separation requirements in clause 4.2 (**section 5**); and
- Other provisions including accounting separation, information disclosure, waivers, compliance and enforcement and transitional requirements (**section 6**).

## 2. Criteria for the development of the ring-fencing guideline

In our submission to the AER on its preliminary positions paper, we proposed a set of principles to inform the AER’s development of the Draft Guideline. We have refined these principles, informed by the Council of Australian Governments’ (**COAG**) Best Practice Regulation Guide, to provide the following criteria.

### **Principle 1: Maintain a primary focus on the achievement of customer interests**

The development of the ring-fencing guideline must, first and foremost, remain focussed on achieving the best possible outcomes for customers – which means promoting economic efficiency and productivity, increasing consumer choice and quality, as well as lowering prices.

These considerations must sit ahead of, and not secondary to, achieving certain market structures or other competition-related outcomes.

Accordingly, caution should be applied to ring-fencing measures which may have the effect of:

- reducing economies of scale and scope of DNSPs and/or unduly increasing costs to DNSPs and therefore prices for end-users; and
- constraining innovation, decreasing choice or quality of service.

In our view, such outcomes are contrary to the achievement of the national electricity objective set out in s 7 of the National Electricity Law (**NEL**).

### **Principle 2: Apply a cost/benefit test to determine appropriate ring-fencing measures**

The ring-fencing measures should accord with the cost-benefit test for regulation – that is, additional regulation should only be imposed when the costs of regulation are less than the benefits, and is therefore, in the long-term interests of consumers. In pursuing the right balance of market intervention, we consider that the ring-fencing measures should:

- attempt to identify the least-cost measure necessary to address the particular harms identified by the AER (i.e. cross subsidisation and discriminatory behaviour); and
- avoid a “one-size” fits all approach, affording flexibility to deal with legitimate differences between DNSPs’ functions and operations.

### **Principle 3: Use clear and unambiguous language to minimise uncertainty**

To enable DNSPs and other stakeholders to understand the implications of the ring-fencing measures, and for the benefit of the AER administering the ring-fencing guideline, the guideline should:

- use terms and concepts consistently, and in accordance with the DNSP's regulatory framework (including the NER and the NEL); and
- use clear and unambiguous language, which is not subject to misinterpretation.

We have used the above criteria to frame our feedback and propose amendments on the Draft Guideline, whilst preserving the AER's policy position.

Accordingly, this submission should be read together with the AusNet Services' proposed amendments to the Draft Guideline set out in **Attachment A**.

## **3. Legal separation requirements**

### **3.1 Overview of Draft Guideline**

Clause 3.1 of the Draft Guideline provides that DNSPs are required to be a separate legal entity and are prevented from providing "non-network services" other than through a related body corporate if it incurs costs in providing services in this category above a \$500,000 annual threshold. "Non-network service" is not a defined concept under the NER or under the Draft Guideline.

The AER's rationale for clause 3.1 is to "*separate [a DNSP's] regulated network services from the unregulated services [a DNSP] (or a related body corporate) offer to a competitive market*" (Explanatory Statement, p 1).

The Draft Guideline specifies that clause 3.1 is not subject to a waiver process.

### **3.2 Assessment of the AER's approach and proposed solutions**

#### **(a) The requirement that DNSPs must only provide "network services" is too narrow, and is inconsistent with the range of services provided for under the NER**

"Network services" is defined under the NER as a "distribution service associated with the conveyance, and controlling the conveyance of electricity through the network".<sup>1</sup> More broadly, "distribution service" under the NER means "a service provided by means of, or in connection with, a distribution system".<sup>2</sup>

By definition then, network services is a narrower definition, representing a type of distribution service – including, direct control services, comprising standard control and alternate control services. However, DNSPs provide a much broader range of distribution services. Beyond "network services", DNSPs provide:

- **Shared asset services** – DNSPs provide services in other industries, such as leasing space on poles and in duct systems for use by telecommunications service providers.
- **Non-network solutions for remote regions** – for example, remote area power systems installed in lieu of replacing aged assets with traditional poles and wires to maintain the distribution service.
- **Metering services** – DNSPs in Victoria currently provide Type 5 and 6 meters and associated metering data services as regulated services.
- **Recoverable works** – DNSPs provide services such as repairing the distribution network after damage to restore or maintain electricity supply.<sup>3</sup>

<sup>1</sup> "Network services" means "transmission services" or "distribution services" "associated with the conveyance, and controlling the conveyance of electricity through the network" (NER, Chapter 10).

<sup>2</sup> "Distribution system" means a "distribution network, together with the connection assets associated with the distribution network, which is connected to another transmission or distribution system" (NER, Chapter 10).

<sup>3</sup> AER, Final Framework and approach for the Victorian Electricity Distributors, Regulatory control period commencing 1 January 2016, 24 October 2014, p 19. In AER's Framework and Approach Paper for Victorian DNSPs, the AER recognised that only a distributor may perform these types of repairs on its assets, which it classified as distribution services.

- **Laboratory and HV testing services** – Services provided by a DNSP to other DNSPs using specialist equipment that would be inefficient for all DNSPs to maintain.
- **Other services** – such as sharing of spare equipment for other DNSPs or providing assistance to other DNSPs in times of emergency (i.e. providing a DNSP with access to office and field staff, restoration plant) and other advisory services.

The above services fall within the definition of a “distribution service” since they are services which are provided in connection with a distribution system, but would not fall within the narrower scope of “network services”.

**Box 1: Example – DNSPs commonly provide network support activities to other DNSPs**

A DNSP holds a spare zone substation transformer, for the event of loss of an in-service transformer. Without the spare, if such an event occurred, an urgent repair or replacement would be required but this could take many months. Supply reliability for customers served from the zone substation would be degraded during this period.

An adjoining DNSP has zone substations, which are designed so that the spare transformer of the first DNSP could provide the backup for it as well. Sharing the spare transformer would be a substantial cost saving.

This sharing arrangement would require a commercial arrangement between the DNSPs, with the first DNSP, which owns the spare transformer, providing a service to its neighbour. Arguably the service is not a ‘network service’, as the service provided is not ‘electricity conveyance’, which is the basis of that term.

**Conclusion:** Under the Draft Guideline, a DNSP would be precluded from providing this service (and instead, would have to rely on the allowance under clause 3.1(b)).

In our view, clause 3.1(a), which prevents DNSPs from providing the full range of distribution services, is at odds with the NER, and therefore, the policy position of the guideline.

Specifically, in the Explanatory Statement (p 23), the AER recognises that:

A DNSP must be able to provide **all distribution services, regulated and unregulated**, as well as regulated transmission services (where relevant), in order to meet its obligations under the NER. (Emphasis added)

The practical effect of clause 3.1 of the Draft Guideline will be to require a related body corporate of the DNSP to provide the broader range of distribution services, which exceed the threshold under clause 3.1(b). This outcome is problematic because a related body corporate cannot provide distribution services – it does not control or operate the network assets, which are necessary or otherwise incidental to the provision of such services.

Accordingly, in our view, the operation of clause 3.1 as currently drafted will undermine the efficient utilisation of DNSP’s core capabilities, skills and expertise and result in a loss of economies of scale and scope otherwise available to DNSPs.

In addition, the legal separation requirements will also have other unintended impacts, which are inconsistent with the NER.

Clause 3.1(a) is inconsistent with the Shared Asset Guideline administered by the AER which provides DNSPs with incentives to utilise network assets in the most efficient manner, including by using those network assets to also provide (i) distribution services that are not classified; or (ii) services that are not distribution services. By preventing a DNSP from providing such services, the AER would compromise the efficiency incentives promoted by the Shared Asset Guideline – which ultimately will result in a loss of benefits to end users.

To address the above issues, we have proposed the following solutions.

**Proposed solution: Amend clause 3.1(a) to provide that DNSPs “may provide distribution services” but “must not provide any energy-related services”**

- Given the narrow definition of network services, we propose that clause 3.1(a) be amended to refer to “distribution services”. To do otherwise, would restrict a DNSP from undertaking activities which the NER only permits a DNSP to provide.
- We have also amended the prohibition on the provision of “non-network services” to replace it with the concept of “energy-related services” and tied this term to the remit of

the NEL – that is, “electricity services” other than distribution services. The term “energy-related services” will cover services “necessary or incidental to the supply of electricity to consumers of electricity” including the generation of electricity and the sale of electricity.

Tying the definitions in the guideline to concepts used in the NER and the NEL ensures that there is consistency with the broader regulatory framework and provides certainty to DNSPs and other stakeholders in the application of these guidelines.

Our suggested drafting amendments to the restrictions in clause 3.1(a) and (b) ensure that DNSPs are not prevented from providing other services which are not within the scope or objective of the guideline.

For example, DNSPs should be able to provide other services such as gas or water services, which do not cause any relevant concerns for competition in downstream energy markets.

**Box 2: Example – DNSPs which participate in more than one regulated service**

This example involves the synergistic management of an unregulated, non-distribution service of the DNSP. Some other DNSPs are, or operate within, entities that also provide other regulated utility services that cannot be identified as ‘network services’ or ‘distribution services’. These services may include gas and water distribution. It would appear that there is no harm caused by these services remaining within a common entity, and therefore should not be subject to the legal separation requirements.

Other services (which are not electricity services within the definition of the NEL) which DNSPs should be able to continue to provide or participate in include, for example:

- participating in legitimate economies of scope and scale activities which are available to it because it is a member to a corporate group (such as joint procurements of equipment, financing, insurance, or outsourcing arrangements e.g. call-centres);
- utilising core asset management skills and expertise to provide non-distribution services such as managing a third party’s power system – for example, a standalone power system established within the DNSP’s distribution area where availability of alternative service providers is not likely; or
- investing in, and commercialising the results of, business innovation and improvements, for the benefit of the DNSP and other stakeholders. For example, commercialising intellectual property developed by the DNSP is unlikely to be classified as a network or distribution service, but the value derived through network innovation and investment should be able to be commercialised by DNSPs for the benefit of end-users.

We consider that if the guideline is to be read to restrict such services it will result in an elimination of economies of scope and scale, as well as demonstrated business synergies, and, ultimately disincentivise DNSPs from investment and innovation, impacting customers both directly and indirectly.

In our view, the types of “services” referred to above do not fall within the policy intent of clause 3.1 or cause any mischief which these guidelines are intended to minimise. Therefore, we have amended clause 3.1(a) and (b) to make clearer that the restrictions imposed are directed to relevant “electricity services” as defined under the NEL, so that business activities, which do not raise concerns for competition in electricity markets, will not unintentionally be captured.

**(b) The absence of a waiver process is inflexible**

The Draft Guideline provides that the legal separation requirement is not subject to any waiver process.

We consider that the absence of a waiver to clause 3.1 is unnecessarily inflexible and is likely to result in significant restructuring costs to DNSP and their related parties.

We have set out below two examples where DNSPs utilise their core capabilities, skills and expertise to provide non-distribution services.

**Box 3: Example – Mt Baw Baw**

AusNet Services operates a stand-alone power system, which serves the community at Mt Baw Baw village, an alpine resort in Victoria. The service is subject to Victorian licensing exemption and is not part of the NEM. As the regional DNSP AusNet Services is able to deploy its field resources to manage the assets. The arrangement ensures that an appropriately skilled workforce is available locally and able to provide a timely response in the event of supply outages.

As a stand-alone system, i.e. not connected to a network in the NEM, the Mt Baw Baw supply is not recognised as any service by the NER. The proposed legal separation provision, limiting the DNSPs services to provision of 'network services', or broader definitions including 'distribution services' would prohibit AusNet Services as DNSP from providing this service.

There may be potential feasible solutions involving reassignment of certain services to a related body corporate, however there are also potential impediments to achieving such an outcome. A waiver of clause 3.1 is the practical solution in this instance.

The Draft Guideline will require the divestment of the above kinds of activities to a separate legal entity, despite the more flexible position afforded under the functional separation requirements.

This may result in significant costs – such as, potential increased tax obligations, treatment of concerns raised in relation to financial funding arrangements and potential need to revise existing agreements, legal costs, potential to trigger technical redundancies and employment agreement impacts, and forcing the opening of commercial contracts to be re-negotiated. In the case of taxation impact, this would include stamp duty payable on asset transfers into new entities. Whilst tax relief may be granted by the Australian Taxation Office (ATO), our internal assessment to date, is that this is not certain and an early decision by the ATO on such matters would not normally be expected.

The potential costs to DNSPs in unravelling pre-existing arrangements such as those described above are real and significant. Conversely, the associated benefits cannot be immediately identified – unless a case-by-case approach is taken by the AER. Accordingly, the failure to afford a waiver for clause 3.1 fails the cost/benefit test for regulation.

**Proposed solution: Amend the guideline to provide a waiver to the legal separation requirements**

- Consistent with the principle that the ring-fencing guideline should avoid a “one-size fits all” approach, we consider that clause 3.1 should be subject to waiver. Specifically, we consider that the AER should grant a waiver where the DNSP can demonstrate that the costs of separating out certain services from the DNSP will outweigh any benefits associated with ring-fencing.

**(c) The proposed exemption threshold is arbitrary and should reflect the size and scale of DNSPs**

We agree there is a need for an exemption provision to enable DNSPs to be able to operate their business effectively and efficiently. However, the proposed cap of \$500,000 is arbitrary and for reasons set out below, not a sufficient amount.

The AER rejected the use of a threshold determined as a percentage of annual average revenue because it considered that this would (Explanatory Statement, p 24):

...create inconsistencies across DNSPs, and could result in materially adverse effects on the markets for contestable services.

Therefore, the AER concluded that “...a threshold based on a fixed dollar value would achieve a more balanced outcome” (Explanatory Statement, p 24).

We consider the AER’s reasoning above does not sufficiently support the \$500,000 allowance because:

- The statement that a “one percent of annual average revenue” threshold could result in materially adverse effects on markets for contestable services is unsupported.

The Transmission Ring-Fencing Guidelines provide that a TNSP is permitted to carry on “related businesses” which attract revenue of up to 5 per cent of the TNSP’s total annual revenue. So far as we are aware, there have not been any material market distortions in those relevant markets to date, as a result of that form of threshold being used.

- In addition, there seems to be no rational basis for selecting \$500,000. This allowance is severely insufficient given the size and complexity of networks’ operations – for example, it is well below the median housing prices of most major capital cities in Australia. Placed into a network services context, the cost of a single bulk mail out to a DNSPs customers’ would be likely to exceed this amount.

The purpose of clause 3.1(b) should not be merely to capture those services which ‘fall through the cracks’ of the legal separation requirement. Most importantly the allowance should be a sufficient amount to ensure that the provision does not constrain the ability of DNSPs to continually and meaningfully adapt their networks, in circumstances where the demand for such services may lag market understanding and classification of such services. For example, trials provided for under the Demand Management Incentive Allowance or separately initiated by the DNSP to enable it to understand how Distributed Energy Resources (**DER**) interact with or utilise networks, facilitating optimal network operation and investment. Such trials conducted by DNSPs and involving new technologies are critical to releasing the full potential of DER for individuals, networks and markets.

In light of the above, the \$500,000 allowance is insufficient for DNSPs to be able to engage in the provision of any other electricity services, which may be necessary or incidental to its core distribution services.

#### **Proposed solution:**

##### **Increase the allowance for energy-related services which a DNSP may provide, in accordance with the size and scale of its network**

- For reasons provided above, we consider that the allowance for DNSPs to incur costs associated with “energy-related services” should be increased to ensure that the DNSP can continue to invest and innovate in its network and associated services.
- We have provided a mechanism similar to the one which exists in the TNSP ring fencing guidelines (i.e. 1% of annual revenue requirement) which scales the allowance to reflect the size and scale of the network business.

##### **However, exclude from the allowance any contestable metering services consistent with the Power of Choice Review**

- In accordance with the “Expanding competition in metering and related services” rule change, which underpins the need for ring-fencing guideline, we have carved out from the cap on expenditure related to energy-related services, the provision of contestable metering services. We have defined “contestable metering services” in accordance with concepts recognised in the NER. We agree with the AER that only a related body corporate of the DNSP should be able to provide such services, subject to Victorian DNSPs being able to continue to deploy regulated metering services as distribution services.

## **4. Non-discrimination obligations**

### **4.1 Overview of Draft Guideline**

Clause 4.1(a) of the Draft Guideline seeks to prevent a DNSP providing preferential treatment to its related body corporate or its customers “in connection with the supply of distribution services or non-distribution services”.

Clause 4.1(b) provides a list of non-exhaustive obligations to address potential discrimination, with the Draft Guideline stating a DNSP must, in summary:

- deal with its related bodies corporate on an arm's length basis;

- deal with competitors of its related body corporate(s) on substantially the same terms and conditions as those for its related entity;
- avoid providing information that the DNSP has obtained through its dealings with a competitor of its related body corporate that may advantage the latter;
- avoid advertising or promoting the services of its related body corporate; and
- have independent and separate branding for its distribution services and non-distribution services.

Clause 4.1 is also not subject to any waiver process.

## 4.2 Assessment of the AER's approach and proposed solutions

### (a) Clause 4.1 results in market intervention unrelated to the objectives of the ring-fencing guideline

Clause 4.1(a) provides that a DNSP:

... must not discriminate (either directly or indirectly) between its related body corporate (including customers of its related body corporate) and competitors of its related body corporate (including customers of a competitor of its related body corporate) in connection with the supply of distribution services or non-distribution services.

The AER explains that the basis for the non-discrimination obligations in its Explanatory Statement (p 34):

In the absence of these provisions, there is a risk of a DNSP's related bodies corporate gaining an unfair advantage over its competitors in the markets for competitive or contestable energy-related services...

We agree with the AER that the focus of the non-discrimination obligations should be on promoting competition in downstream contestable energy-related markets. That is, the non-discrimination obligations should prevent a DNSP from unfairly leveraging its natural monopoly position *in the provision of distribution services* to favour its related parties operating in related markets.

However, the Draft Guideline has potential scope to intervene in markets unconnected to the objectives of the ring-fencing guideline.

In particular, clause 4.1(a) seeks to regulate market behaviour beyond monopoly services provided by a DNSP (i.e. distribution services) to *any other service* provided by the DNSP (i.e. non-distribution services). The Explanatory Statement does not explain the need for an unconstrained obligation, though the AER does acknowledge that "this is a broad obligation" (Explanatory Statement, p 4).

In our view, clause 4.1 is not sufficiently targeted to the potential harms which this ring-fencing guideline is intended to address – that is, the potential for the DNSP, in connection with the provision of monopoly services, to favour its related body corporate over competitors. This objective is confirmed by the AER, noting that (Explanatory Statement, p 13):

... a DNSP could **restrict access to its monopoly assets**, favouring its affiliate over competitors. What this means is that a DNSP, a related body corporate or another service provider could gain an unfair advantage that limits the potential development of competitive markets, which can provide customers with better services and choices and at lower price. (Emphasis added)

Accordingly, the non-discrimination obligations are too broad, and instead should be explicitly directed to the markets where the DNSP has ability to exercise monopoly power – that is, distribution services only.

Similar comments apply to clause 4.1(b) which purportedly binds a DNSP irrespective of the type of services it is providing, as well as clause 4.1(b)(v) and (vi) which binds the DNSP even where a related body corporate may not be providing an energy-related service.



**Proposed solution:**

**Confine the scope of clause 4.1 to markets where a DNSP can leverage its monopoly power in favour of its related body corporate**

To address the comments made above, clause 4.1(a) should be directed towards prohibiting a DNSP from discriminating in connection with “providing distribution services” in respect of a related body corporate and its competitors. This ensures that the non-discrimination obligations do not creep into markets which are not the focus of this ring-fencing guideline. Similar amendments should be made to clause 4.1(a)(i), (ii) and (iii) to limit its operation to the provision of distribution services.

In addition, to minimise any ambiguity, clauses 4.1(v) and (vi) should also be qualified by tying the restrictions on promotion and branding to the provision of “energy-related services” by a related body corporate. This would ensure consistency with the formulation of clause 4.1(iv).

**(b) In addition, some aspects of clause 4.1(b) may be open to interpretation**

Other aspects of clause 4.1(b) which we consider could be clarified include the following:

- Clause 4.1(b)(ii) requires a DNSP to provide services on equal terms and conditions as between a related body corporate and its competitors, while clause 4.1(b)(iii) requires the DNSP to provide the same quality of service to its related body corporate and its competitors.

Basically, clauses 4.1(b)(ii) and (iii) may have the unintended effect of requiring strict equivalency in terms and conditions, even where there may be legitimate circumstances which drive different commercial terms. The terms and conditions (e.g. price) generally *inform* reasonable differences in the quality, reliability and timeliness of the service. For example, a competitor of a related body corporate may wish to pay more, to get a quicker or more reliable service from the DNSP. However, the current formulation of the guideline would prevent a DNSP reasonably negotiating differentiated commercial terms in such circumstances.

- Clause 4.1(vi) refers to “independent and separate” branding which would preclude a level of secondary branding, which we expect is not the intention of the AER.

**Proposed solution: Minor amendments to aspects of clause 4.1(b)**

We have drafted amendments to clause 4.1(b) to:

- Amalgamate clauses 4.1(b)(ii) and (iii) to simplify and clarify the drafting in accordance with commercial practical outcomes; and
- Amend clause 4.1(b)(vi) to replace the words “separate and independent” to “materially distinct” which would require material differentiation between branding, whilst enabling some secondary branding.

## **5. Functional separation requirements**

### **5.1 Overview of Draft Guideline**

The Draft Guideline provides for functional separation obligations in two areas:

- physically separating a DNSP’s offices for provision of the ring-fenced distribution and transmission services from its service providers or its related bodies corporate; and
- preventing staff sharing between a DNSP and staff of its related bodies corporate who are involved in the provision or marketing of contestable energy-related services.

The Draft Guideline notes that separate offices means different buildings.

The AER provides some common exceptions to locational and staff separation – including for staff who are not involved in:

- the provision of energy-related services; or

- provision of any direct control services or regulated transmission services and who therefore do not have access to information about electricity customers and services.

The exceptions for staff sharing are broader, and additionally permit staff sharing for: senior executives of both the DNSP and the related body corporate; and staff who are involved in the provision of DNSP's negotiated distribution services and unregulated distribution services.

Finally, the AER imposes limitations on a DNSP's ability to remunerate staff based on the performance of a related body corporate.

The functional separation requirements may be subject to waiver.

## 5.2 Assessment of the AER's approach and proposed solutions

### (a) The physical separation requirements are inconsistent with DNSPs' legitimate operations

Clauses 4.2.1 and 4.2.2 are inconsistent with one another, and read together, do not accord with DNSPs' legitimate businesses operations. Specifically, the practical effect of clauses 4.2.1 and 4.2.2(iv) will involve:

- placing staff that provide direct control services and regulated transmission services in a different office from staff that provide other distribution and transmission services (e.g. unregulated or negotiated services);
- but, enabling sharing of staff who provide distribution services, albeit not in the same location.

The unintended consequences of the Draft Guideline are demonstrated below.

#### **Box 5: Example – Scenario demonstrating separation of AusNet Services' Networks Strategy Team**

AusNet Services staff supports its electricity networks in a neutral manner – that is irrespective of service classification. So, for example, the networks strategy team, who develop the strategies for best practice asset management to achieve service and safety obligations and annual plans to put these into effect, operate across both electricity distribution and transmission networks.

Under clause 4.2.1, the networks strategy team would need to be physically split into different buildings depending on whether staff members are involved in the provision of regulated services or unregulated/negotiated electricity network services. That said, under clause 4.2.2(iv) the network strategy team for distribution network services (irrespective of classification) could be jointly resourced, however, as above, just not in the same location.

#### **Box 6: Example – Scenario where AusNet Services' control centre serves electricity distribution and transmission networks, as well as its gas distribution network**

Another example is AusNet Services' personnel who serve the gas distribution network as well as its electricity networks. For example, AusNet Services employ staff to operate in its control centre to provide services across the electricity networks and gas network including incident and emergency management response staff and system management.

AusNet Service's gas distribution services would not be classified as distribution services in the context of this ring-fencing guideline, as such services are subject to a separate national energy law. However, given the undefined nature of "energy-related services", the Draft Guideline could be interpreted in these circumstances to require a separate control centre for its gas network and negotiated / unregulated electricity networks services, from the control centre serving regulated electricity network services.

Both of the examples above demonstrate that the Draft Guideline will undermine and constrain incentives to establish efficiencies and cost-saving aggregation of services and people. Instead, DNSPs will be required to duplicate resources across its regulated services resulting in significant cost increases which will ultimately be borne by consumers.

While a waiver may be obtained in these circumstances, in our view, reliance on a waiver to undertake business as usual functions is inefficient, and reflects the fact that the Draft Guideline

is not sufficiently targeted to the specific concerns around discriminatory behaviour identified by the AER.

**Proposed solution: Provide parallel exceptions for location separation and staff sharing**

- The constraint on co-location should be directed to “energy-related services” as defined in the context of the NEL (and described further above in this submission). This will ensure that unintended consequences such as in Example 6 above are avoided.
- The same exceptions for staff sharing should apply for office separation. In AusNet Services’ view there is no logical reason to have differing (and more limited) exceptions applying to locational separation. As highlighted in Example 5 above, this inconsistency will lead to inefficient service provision and duplication in costs, which ultimately will be borne by customers. Accordingly, we have proposed to delete the exceptions in clause 4.2.1(b) and provided that the same exceptions which apply for staff sharing equivalently apply to office separation.
- In addition, we have suggested other minor amendments to provide for consistency and clarify in the exceptions under clause 4.2.2(b) including to:
  - inserted the word “directly involved” in clause 4.2.2(a) and (b)(i) consistent with its use by the AER in this clause, and remove the word “customer and services” – “services” is too broad;
  - expanded clause 4.2.2(ii) to incorporate “officers” – i.e. directors and company secretaries should also be exempt; and
  - clarified the language in clause 4.2.2(iii) to refer to staff who do not “in the normal course, have direct access to information” and reinforced the scope of this provision by expanding the examples of corporate services provided.

**(b) The staff sharing exception in clause 4.2.2(b)(iv) should also apply to equivalent transmission services**

The Draft Guideline limits permitted staff sharing in clause 4.4.2(b)(iv) to negotiated/unregulated distribution services, to the exclusion of staff sharing for negotiated/unregulated transmission services.

The drafting of the Draft Guideline on this matter is explicit, however it is an inconsistent treatment to limit the sharing of staff to a subset of the transmission service categories. This would impinge on the efficient and effective provision of services across the network service spectrum, and can only be to the detriment of network customers.

For example, there is no harm from staff in the distribution network strategy team from also providing that service for assets which are providing an un-regulated transmission service. For example, as explored in our submission to the AER’s Preliminary Position Paper, the contestable provision of new transmission services in Victoria relies on skill sets held across the broader business of the service provider to provide cost effective services. The resource sharing from this arrangement creates operational efficiencies that flow through as benefits to consumers of regulated services.

While this guideline is not intended to bind TNSPs, we consider that for hybrid networks, such as AusNet Services, it should be made clear that a DNSP is not prevented from utilising staff that provide transmission services for a related body corporate.

**Proposed solution: Maintain operational synergies between DNSP/TNSP businesses**

- References to distribution services in clause 4.2 should also apply to equivalent transmission services for hybrid DNSP/TNSPs. We have addressed this in the Definitions and Interpretation section of our mark-up in Attachment A.
- This change will avoid further duplication of resources and increases in costs, to enable DNSs to continue to utilise resourcing synergies which exist with any related transmission business.

**(c) The requirement for the DNSP to occupy a different building from its related body corporate is disproportionate to address concerns raised by the AER**

Clause 4.2.1 requires “independent and separate” offices for direct control services (and regulated transmission services) from the operation of energy-related services. The Draft Guideline makes clear that this requires offices in different buildings. We understand this requirement is aimed to “keep apart a DNSP from its affiliates offering services into competitive markets” and “prevent the businesses and employees from mixing and sharing, inadvertently or otherwise, commercially sensitive information” (Explanatory Statement, p 37).

We consider that requiring building separation is a disproportionate response to achieve the above objectives – particularly given that security technology advances displace the need for such locational separation. Corporate offices commonly have secure access floors. If a DNSP occupied a multi-floor commercial space, it could separate staff on different floors and prevent unauthorised access by using security passes. Alternatively, single floors could also be separated into two or more secure office spaces requiring pin-code or security pass access.

Such security measures provide the same benefits of building separation by preventing the comingling of ring-fenced staff with other staff, while avoiding the costs and resource implications for DNSP and its related bodies corporate which arise with the stricter form of separation required by the AER.

**Proposed solution: Amend clause 4.2.1 to require physical separation, rather than building separation**

- We consider that clause 4.2.1 should be amended to require a DNSP to operate “physically separate and secure offices”.

**(d) The restriction on the remuneration of staff goes too far**

Clause 4.2.2(c) provides that a DNSP must not remunerate or incentivise staff based on a related body corporate’s performance. The broad application of this clause will disenfranchise staff from participating in group-wide employee share schemes.

Generally speaking, there are relevantly two types of parent company incentive schemes, which are offered by companies, such as DNSPs.

There are incentive payment schemes, which are a common part of the employees’ remuneration. These schemes generally comprise rewards based on performance against the employees’ individual accountabilities and also on the business corporate performance, such that there is a sense of sharing with employees.

The other example is the group-wide employee share schemes, which provide a similar function, supporting staff association with the company as an employer of choice. For example, at AusNet Services, staff members have the opportunity to participate in a share investment plan, which is for shares in the listed, head company.

Both of these schemes would be prohibited under the Draft Guideline, disenfranchising less-senior staff, skilled workers, administrative staff etc., including all those employees who are able to operate across businesses under clause 4.2.2(b). In our view, this outcome is unjustified and goes beyond the ring-fencing policy intent to minimise discriminatory behaviour.

**Proposed solution: Limit the scope of clause 4.2.2**

- We consider that this clause should be confined to addressing the particular harms that the AER is attempting to minimise – in particular, to reinforce the integrity of the separation requirements and the non-discrimination obligations.
- Accordingly, we propose amendments to clause 4.2.2 to prohibit remuneration or incentive arrangements which would encourage conduct which is otherwise prohibited by the Guideline. This ensures that the provision more clearly achieves the AER’s policy.
- Alternatively, we consider that the restriction should explicitly carve out share or equity schemes or plans relating to a related body corporate for the benefit of all staff that can be shared under clause 4.2.2(b) (not just limited to senior executives).

## 6. Other provisions

### 6.1 Establishing and maintaining separate accounts

In summary, clause 3.2 requires DNSPs to maintain separate accounts as between a DNSP and its related bodies corporate and prevents any cross-subsidisation as between distribution services and other services.

We have suggested minor changes to this clause, in accordance with comments made elsewhere in this submission and to improve the readability of the clause.

#### **Proposed solution: Minor amendments to clause 3.2**

- Amend clause 3.2.2(a) to more clearly express the prohibition on any cross-subsidisation.
- Remove references to “non-distribution services”, which is an undefined term, and replace it with “other services”, which preserves the intent of the AER.

### 6.2 Information access and disclosure

Clause 4.3 requires a DNSP to, in summary:

- to keep information confidential and only use it for relevant purposes and obtain consent from relevant customers before disclosing information to any party; and
- to provide access to information on equal terms to a related body corporate and its competitors.

In our view, the obligations around keeping information confidential and obtaining consent (in clauses 4.3.1 and 4.3.3 respectively) are unnecessary because such requirements result in:

- duplication with existing privacy law requirements and general confidentiality obligations existing at law which all DNSPs are bound by; and
- results in potential inconsistency with comprehensive requirements in the NER for use and disclosure of metering data.

Accordingly, in our view, these clauses may result in conflicts with existing legal requirements, and may otherwise result in uncertainty for DNSPs.

We also consider that clarifying amendments could also be made to clause 4.3.2 to:

- re-focus the clause on preventing discriminatory provision of information, rather than equal terms. Similar comments made above in relation to clause 4.1(b)(ii) and (iii) apply. That is, different terms for access to information may be reasonably justifiable depending on the particular circumstances – for example a competitor of a related body corporate may pay more for the same data, but which is required to be prepared on a more disaggregated basis; and
- consistent with the objectives of the guideline, limit the operation of the clause to apply where a related body corporate provides energy-related services.

#### **Proposed solution: Simplify the information access and disclosure provisions**

Our suggested amendments to this section to address the above comments include to:

- delete clauses 4.3.1 and 4.3.3 and amend clause 4.3.2 to reframe in the context of the non-discriminatory obligations and to confine scope to “energy-related services”; and
- in addition, we have included a clarifying note which provides that nothing in this clause authorises a DNSP to provide access to information which is not permitted by law or regulation.

### 6.3 Waiver provisions

The AER has power under clause 5.2.1 to make a decision to either grant or refuse to grant the waiver, and under clause 5.3 it may revoke or vary a waiver.

We consider that there is a lack of transparency in the AER's decision making process under the waiver process. For example:

- There is no prescribed time-frame for the AER to make a decision in respect of a waiver process.
- While the AER has discretion around publishing its decision on a waiver application under clause 5.2 or a revocation / variation of a waiver under clause 5.3, there is no explicit requirement for the AER to provide the DNSP with reasons for its decision. We consider this is a minimum requirement consistent with administrative law principles.
- Where the AER varies or revokes a waiver decision, the AER is currently not required to consider an appropriate transition for the DNSP to implement the changed requirements. In our view, the AER should be consulting with the DNSP to provide for a transitional period to minimise any unintended non-compliance or other consequences.

**Proposed solution:**

To address the above issues, we have amended the Draft Guideline accordingly:

- We consider that the AER's decision under clause 5.2.1 should be made within 40 business days of receiving the application, consistent with the pass through provisions in the NER (e.g. NER, clause 6.6.1(e)). Also consistent with existing provisions of the NER, if the AER does not notify the DNSP of its decision within that timeframe, the AER is taken to have approved the waiver application.
- The AER should be required to provide reasons to the DNSP for any decision made under clause 5.2 or 5.3 so that a DNSP can consider the reasonableness of the AER's decision.
- The AER should also be required to provide for an appropriate transition period for any revocation or variation to a waiver to enable the DNSPs to make adjustments to its operations to comply with any changed circumstances.
- In addition, consistent with submissions made above, we consider that clauses 3.1 as well as 4.2 should be subject to waiver. Accordingly, we have proposed amendments to clause 5 to incorporate additional cross-references.

## **6.4 Compliance and enforcement**

### **(a) The timing of the first annual compliance report should be made clear**

We have also proposed minor changes to clause 6.2.2 to make clear that the first annual compliance report will not be required until after the end of the full first regulatory year post 1 December 2016.

For example then, AusNet Services' first annual compliance report will be due on 30 April 2018 (since our regulatory period ends 31 December). We consider this change is consistent with the AER's intention.

**Proposed solution:**

Minor changes be made to clause 6.2.2(b) to make clear that the first annual compliance report will not be required until a whole year of the ring-fencing guidelines have been in place.

### **(b) The AER should provide guidance as to the treatment of costs incurred in complying with the ring-fencing guideline**

The Draft Guideline and the Explanatory Statement do not address the treatment of, and responsibility for, costs incurred in implementing the separation measures.

The ring-fencing guideline is a regulatory step change, and compliance with its obligations will require DNSPs to make changes to the way they operate. The costs of doing so are likely to be material.

In our view, the change in regulatory obligations would constitute a regulatory change event and the costs incurred should be recoverable through an associated mechanism.

The NER provides that cost recovery as a pass-through event requires the amount to be advised within 90 days of the event, however aspects of implementation may occur over a 12 month period. Treatment as separate events is unlikely to provide a fair and reasonable outcome as individually the amounts may not satisfy the 1% of revenue trigger.

**Proposed solution:**

The AER should clarify how cost recovery should be treated for the purpose of the ring-fencing guideline. The AER should also ensure that costs incurred will not impact on the operation of regulatory incentive mechanisms such as the Efficiency Benefits Sharing Scheme.

## **6.5 Transitional provisions**

The Draft Guideline provides for a:

- a 12-month transition period for clause 3.1 (legal separation); and
- a 6-month transition period for clauses 4.2.1 (physical separation/co-location) and 4.2.2 (staff sharing).

The scope of transition relief described above does not give sufficient regard for the potential complexity and time involved for DNSPs to bring themselves into compliance with the ring-fencing arrangements.

For example, it may take some time before a DNSP can identify potential new office space, negotiate new commercial leases, and physically relocate staff and systems. In our experience, relocation of offices can take approximately 9-12 months, from identifying possible lease options to completion of the relocation.

Once staff and systems are relocated, AusNet Services will need to implement written protocols and training to ensure compliance with the staff sharing requirements. Therefore, an earlier implementation of clause 4.2.2, before clause 4.2.1, would be impractical.

There is also no transition period specified for clauses 3.2 (cost allocation), 4.1 (non-discrimination obligations) and clause 4.3 (Information access and disclosure). In our view immediate compliance is unreasonable given that:

- the transition period for cost allocation process should align with the transition for legal separation, since accounts and associated cost allocation measures will need to be restructured in accordance with changed corporate structure;
- DNSPs will need time to prepare and implement protocols for the behavioural-type obligations contained in clauses 4.1 and 4.3, and conduct training to minimise compliance breaches by staff; and
- more specifically, in our experience, branding changes can also take a significant amount of time to implement.

**Proposed solution:**

We have specified more reasonable timeframes for transition periods including:

- 12 months for legal separation, cost allocation requirements (clauses 3.1 and 3.2);
- 12 months for the functional separation requirements (clause 4.2) as well as branding changes (clause 4.1(b)(vi)); and
- 6 months for the other non-discrimination and sharing of information requirements (clauses 4.1 and 4.3)

We have also included a clause which provides an appropriate transition period for any change in service classification which materially impacts on the DNSP's ability to comply with the guideline.

**ATTACHMENT A –  
Proposed amendments to AER's Draft Guideline**





# **DRAFT**

# **Ring-Fencing Guideline**

## **Electricity Distribution**

August 2016

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# 1 Nature and authority

## 1.1 Application of this guideline

This Electricity Distribution Ring-fencing Guideline (**Guideline**) is made under clause 6.17.2 of the National Electricity Rules (**NER**).

Under clause 6.17.1 of the **NER**, this **Guideline** is binding on all **Distribution Network Service Providers (DNSPs)**.

The objectives of this **Guideline** are to promote the ~~National Electricity Objective~~ **national electricity objective** by providing for the accounting and functional separation of the provision of ~~direct control~~ **distribution services** by **DNSPs** from ~~the provision of~~ other services provided by them, or by their **related bodies corporate**. ~~it~~

This Guideline includes obligations on **DNSPs** targeted at:

- cross-subsidisation, with provisions that aim to prevent a **DNSP**:
  - providing ~~non-network~~ **energy-related services** that could be cross-subsidised by its **network distribution services**; or
  - inefficiently inflating its prices for **direct control services** ~~and regulated transmission services~~, and
- discrimination, with provisions that aim to:
  - prevent a **DNSP** providing an inappropriate competitive advantage to its own service providers or **related bodies corporate** which provide ~~competitive or contestable~~ **energy-related services**; and
  - ensure a **DNSP** treats and protects information it acquires appropriately.

This **Guideline** commences on 1 December 2016- (Commencement Date).

## 1.2 Confidentiality

The **AER** will assess confidentiality claims by **DNSPs** arising under this **Guideline** in accordance with its **Confidentiality Guideline**, the **Competition and Consumer Act 2010** and the National Electricity Law (**NEL**).

## 1.3 Definitions and interpretation

In this **Guideline**:

- The words, phrases and abbreviations presented in bold **such as this** have the meaning given to them in the **NER**- or as specified below:
  - **energy-related services** means:
    - (a) subject to paragraph (b), any electricity service (as defined under NEL) other than distribution services; and

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(b) any **distribution service** which is a **contestable metering service**.

▪ a **contestable metering service** means any of the following services, if required to be provided on a contestable basis:

1) the provision, installation and maintenance of a **metering installation**; or

2) **metering data services**.

- For the purposes of clause 4.2 specifically, if a **DNSP** or a **related body corporate** of a **DNSP** is also a **Transmission Network Service Provider (TNSP)** any reference to:

▪ **distribution service** is to be read as a reference to “**distribution service or transmission service**”;

▪ **direct control service** is to be read as a reference to “**direct control service or prescribed transmission service**”; and

▪ “**negotiated distribution services and unregulated distribution services**” is to be read as a reference to “**negotiated transmission services and unregulated transmission services**”.

For the avoidance of doubt, this **Guideline** binds the **DNSP** only, and any references to **transmission services** which are incorporated as a result of the above, does not bind any **TNSP**.

- The words ‘shall’ and ‘must’ indicate mandatory requirements, unless the overall meaning of the phrase in which one of these words appears, is otherwise.
- Explanations in this **Guideline** about why certain information is required are provided for guidance only. They and do not limit or expand in any way the **AER**’s objectives, functions or powers.

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## 1.4 Process for revisions

The **AER** may amend or replace this **Guideline** from time to time to meet changing needs, in accordance with clause 6.17.2 of the **NER** and the **distribution consultation procedures**.



## 2 Relationship with other regulatory instruments

This **Guideline** should be read in conjunction with:

- (a) The decision in the **AER's distribution determination** on the classification of the **distribution services** to be provided by a **DNSP** in a **regulatory control period**, in accordance with clauses 6.2 and 6.12.1(1) of the **NER**;
- (b) Clause 6.15 of the **NER**, the **Cost Allocation Guideline** and the **AER-approved Cost Allocation Methods (CAM)**;
- (c) Clause 6.4.4 of the **NER** and the **Shared Asset Guideline**; and
- (d) ~~A Regulatory Information Instrument~~ A regulatory information instrument served on a **DNSP** by the **AER** under section 28F of the **NEL**.

Together, these instruments achieve the desired ring-fencing outcomes in the long term interest of consumers.

The **AER's** service classification decision determines the nature of the economic regulation, if any, applicable to a **DNSP's** specific **distribution services**. The classification affects the application of obligations in clause 4.2 of this **Guideline**.

The **Cost Allocation Guideline** and a **DNSP's CAM** relate to the allocation and attribution of its costs between its **distribution services**. They complement the obligations in clause 3.2.2 of this **Guideline**, which relate to the allocation and attribution of a **DNSP's** costs between **distribution services** and ~~non-distribution~~ other services.

The **Shared Asset Guideline** enables the adjustment of a **DNSP's** revenues that it can recover from its **distribution services** where its **CAM** no longer accurately reflects how its assets are used. The shared asset mechanism therefore modifies the effect of the **CAM**.

~~The Regulatory Information Instruments~~ The regulatory information instruments can require a **DNSP** to provide information to the **AER** and to have this information certified and audited. This can include information that is subject to ring-fencing obligations under this **Guideline**.

## 3 Prevention of cross subsidies

### 3.1 Legal separation

- (a) A **DNSP** must be a legal entity and, subject to clause 3.1(b), ~~must only~~ a DNSP may provide network distribution services; and must not provide any energy-related services.
- (b) A **DNSP** may incur costs of up to ~~\$500,000~~ 1% of its annual revenue requirement (identified and allocated in accordance with clause 3.2.2) in any regulatory year for

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providing ~~non-network energy-related services~~ (other than **contestable metering services**).

(a) A **DNSP** must not provide ~~non-network energy-related services~~ where doing so would involve the **DNSP** incurring such costs in excess of ~~\$500,000~~ **1% of its annual revenue requirement** in any regulatory year.

(c) For the avoidance of doubt, ~~clauses~~ **clause** 3.1(a) and ~~3.1~~ (b) do not prevent a **related body corporate** of a **DNSP** from providing ~~non-network energy-related~~ services.

(d) For the avoidance of doubt, clauses 3.1(a) and 3.1(b) do not prevent a **DNSP** and a **TNSP** being the same legal entity.

(e) A **DNSP** ~~cannot~~ **may** apply for a waiver of the obligations set out in ~~clauses~~ **clause** 3.1(a) and ~~3.1~~ (b).

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## 3.2 Establish and maintain accounts

### 3.2.1 Separate accounts

(a) A **DNSP** must establish and maintain appropriate internal accounting procedures to ensure that it can demonstrate the extent and nature of transactions between the **DNSP** and its **related bodies corporate**.

(b) The **AER** may include a requirement in a **regulatory information instrument** for a **DNSP** to:

- i. provide its internal accounting procedures to the **AER**;
- ii. report on transactions between ~~the~~ **DNSP** and its **related bodies corporate**.

(c) A **DNSP** cannot apply for a waiver of the obligations set out in ~~clauses~~ **clause** 3.2.1(a).

### 3.2.2 Cost allocation and attribution

(a) A **DNSP** must not allocate or attribute to **distribution services** any costs ~~that properly relate which are not directly attributable to non-the provision, or are not incurred in providing~~ **distribution services**.

(b) A **DNSP** must allocate or attribute costs to **distribution services** in a manner that is consistent with the **cost allocation principles** and its approved **CAM**, as if those cost allocation principles and **CAM** otherwise applied to the allocation and attribution of costs between **distribution services** and ~~non-distribution~~ **other** services.

(c) A **DNSP** must demonstrate to the **AER** whenever it provides financial information to the **AER** in accordance with a **regulatory information instrument** how it meets the obligation in ~~clauses~~ **clause** 3.2.2(a) and ~~3.2.2~~ (b).

(d) A **DNSP** cannot apply for a waiver of the obligations set out in this clause 3.2.2.

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## 4 Non-discrimination

## 4.1 General obligations to not discriminate

- (a) A **DNSP** must not discriminate (either directly or indirectly) between its **related body corporate** (including customers of its **related body corporate**) and competitors of its **related body corporate** (including customers of a competitor of its **related body corporate**) in connection with the supply of **distribution services** ~~or non-distribution services~~.
- (b) Without limiting the scope of 4.1(a), this provision requires a **DNSP** to, in connection with the supply of **distribution services**:
- deal or offer to deal with its **related body corporate** as if its related body corporate was not a related body corporate of the **DNSP**;
  - deal or offer to deal with competitors of its **related body corporate** (including customers of those competitors) on substantially the same terms and conditions, (including in relation to quality, reliability and timeliness of service), as those for its **related body corporate** (including customers of its **related body corporate**);
  - ~~provide substantially the same quality, reliability and timeliness of service to competitors of its **related body corporate** (including customers of its **related body corporate**), as it provides to its **related body corporate** (including customers of those competitors);~~ ~~[Deleted]~~;
  - not provide information to its **related body corporate** that the **DNSP** has obtained through its dealings with a competitor of the **related body corporate** that may advantage the **related body corporate** in the provision of ~~competitive or contestable energy-related~~ **services**;
  - not advertise or ~~promote the energy-related~~ **services** provided by its **related body corporate**; and
  - have ~~independent and separate~~ materially distinct branding for its **distribution services** from the branding of **energy-related services** provided by a related body corporate that provides non-distribution services.
- (c) A **DNSP** cannot apply for a waiver of the obligations set out in clause 4.1.

## 4.2 Specific obligations for functional separation

### 4.2.1 Physical separation/co-location

- (a) A **DNSP** must operate ~~independent and physically~~ separate and secure offices for the provision of ~~direct control services and regulated transmission services~~ from the offices from which any of its separate service providers or **related bodies corporate** provides ~~other energy-related~~ **services**. For ~~example~~ avoidance of doubt, a **DNSP** ~~must~~ does not need to operate in a different building, ~~and but must~~ prevent staff from mixing in the normal course of undertaking work activities.
- ~~(b)~~ The obligation set out in clause 4.2.1(a) is subject to the following exceptions:
- ~~Office accommodation for staff of its separate service providers or related bodies corporate that do not provide energy-related services; or~~

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- viii. ~~Office accommodation for staff who are not directly involved in the provision of **direct control services** and regulated **transmission services** and who therefore do not have access to information about electricity customers and services, such as staff who exclusively perform corporate services, for example in payroll and human resources; or~~
- ix. ~~(b) Any arrangements agreed through the waiver process set out in Section 5 of this Guideline.~~ clause 4.2.2(b).

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## 4.2.2 Staff sharing

- (a) A **DNSP** must ensure that its staff directly involved in the provision of a **direct control service**, ~~or a regulated transmission service~~ are not also directly involved in the provision or marketing of a competitive or contestable **energy-related service** by a **related body corporate**.
- (b) The ~~restriction~~ restrictions set out in ~~clause~~ clauses 4.2.21(a) ~~does~~ and 4.2.2(a) do not apply to:
- A member of staff who is not directly involved in the provision of **energy-related services**; or
  - A member of staff who is a senior executive or officer of both a **DNSP** and a **related body corporate**; or
  - A member of staff who is not directly involved in the provision of any **direct control services** ~~or regulated transmission services~~, and who therefore ~~does~~ does not in the normal course of its duties, have direct access to information about electricity customers ~~and services, such as~~, (for example staff who exclusively perform corporate services, for example in such as, but not limited to, administrative, accounting or payroll and, human resources, information technology support services or legal services for the DNSP and its related body corporate); or
  - A member of staff who is involved in the provision of a **DNSP's negotiated distribution services** and **unregulated distribution services**; or
  - Any arrangements authorised through the waiver process set out in Section 5 of this **Guideline**.
- (c) A **DNSP** must not remunerate or otherwise incentivise its staff ~~(other than a staff member who is a senior executive of both the DNSP and a related body corporate) based on the performance of a related body corporate to engage in behaviour or conduct which is prohibited by this Guideline.~~

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## 4.3 Information access and disclosure

### 4.3.1 Protection of information

~~A DNSP must keep information provided by a customer, prospective customer or service provider for **direct control services** and/or regulated **transmission services** confidential. The DNSP must only use this information for the purpose for which that information was provided.~~

[\[Deleted\]](#)

### 4.3.2 Sharing of information

Where a **DNSP** acquires information in providing **direct control services**, ~~it must not discriminate on the basis for, or the terms and/or regulated transmission services, and shares conditions on which, it provides access to~~ that information (including information derived from that information) ~~withas between~~ a **related body corporate**, ~~it must provide access to that information (including the derived information) on an equal basis with third parties competing with the~~ which provides **energy-related services** and competitors of that related body corporate.

To avoid doubt, nothing in this clause authorises a **DNSP** to provide access to information to either a **related body corporate** who provides **energy-related services** or competitors of that **related body corporate**, where it is not permitted to do so by law or regulation.

### 4.3.3 Disclosure of information

~~A **DNSP** must not disclose information acquired in providing **direct control services** or regulated **transmission services** (including information derived from that information) to any party, including a **related body corporate**, without obtaining the explicit informed consent of the relevant customers or prospective customers to whom the information relates.~~

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#### 4.3.4 No waiver

A **DNSP** cannot apply for a waiver of the obligations set out in this clause 4.3.

## 5 Waivers

### 5.1 DNSP's application for a waiver

A **DNSP** may apply in writing to the **AER** for a waiver of its obligations under ~~clause~~clauses 3.1 and 4.2 of this **Guideline**. An application for a waiver must include all information and materials necessary to support the **DNSP**'s application, including:

- (a) ~~The~~Details of the service, or services, in relation to which the **DNSP** is requesting the waiver;
- (b) Whether the waiver being sought relates to ~~the physical separation/co-location obligation in clause 4.2.1 and/or to the staff sharing obligation in clause 4.2.2 and the reason that the DNSP is requesting the waiver;~~
  - i. ~~The~~the legal separation requirement in clause 3.1;
  - ii. the physical separation/co-location obligation in clause 4.2.1; and/or
  - iii. the staff sharing obligation in clause 4.2.2,  
and the reason that the DNSP is requesting the waiver.
- (c) Details of the costs associated with the **DNSP** complying with ~~clause 4.2~~clauses 3.1 and/or 4.2 (as applicable) if the waiver is refused and how these costs will vary if the waiver is granted;
- (d) Whether the **DNSP** seeks the waiver to apply to the current **regulatory control period**, the next **regulatory control period** or both;
- (e) Any additional measures that the **DNSP** proposes to undertake in conjunction with the waiver; and
- (f) The reasons why the **DNSP** considers the waiver should be granted with reference to the matters set out in clause 5.2.2, including, but not necessarily limited to, the benefits, or likely benefits the grant of waiver would bring to electricity consumers.

### 5.2 AER's consideration of a waiver application

#### 5.2.1 Requirement to consider a waiver

- (a) The **AER** must consider an application under clause 5.1, and may subject to this clause, grant, or refuse to grant, the waiver subject to such conditions as the **AER** considers necessary.
- (a) The **AER** must provide the **DNSP** with its decision (including reasons) in respect of an application for a waiver within 40 business days of receiving an application under

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clause 5.1. If the AER does not provide notice of its decision within that time, the AER is taken to have approved the DNSP's waiver application.

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## 5.2.2 Matters AER will consider

- (a) In considering an application under clause 5.1, and deciding whether to grant, or refuse to grant, the waiver, the **AER** may consider any matter it considers relevant but will have regard to at least:
- the ~~National Electricity Objective~~national electricity objective;
  - the potential for cross-subsidisation and discrimination if the waiver is granted or refused; and
  - whether the benefit, or any likely benefit, to electricity consumers of the DNSP's compliance with ~~clause 4.2~~clauses 3.1 and/or 4.2 (as applicable) would be outweighed by the cost to the DNSP of complying with that obligation.

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## 5.2.3 The AER's assessment of the waiver application

- (a) When the **AER** receives an application under clause 5.1 it:
- may reject the application without further consideration if it considers that the application has been made on trivial or vexatious grounds;
  - may request any further information that it considers is necessary for it to consult on, and/or make a decision on, the application;
  - may invite public submissions on the application; and
  - may impose such conditions as it considers appropriate when granting a waiver.
- (b) If the **AER** undertakes a public consultation process it may publish its decision ~~that~~ explain on its website to explain the reasons to grant, or refuse to grant, a waiver.
- (c) The **AER** may publish the terms and conditions of any waiver that is granted.

## 5.2.4 Form of waiver

The **AER** may grant a waiver to:

- apply to one or more ~~DNSP~~DNSPs;
- apply for the DNSP's current **regulatory control period**, the next **regulatory control period** or both; and
- be made subject to such terms and conditions as the **AER** considers appropriate.

## 5.3 Reviewing a waiver within a regulatory control period

- (a) The **AER** may review a waiver within a **regulatory control period** if it considers that it may no longer be required. The **AER** may vary or revoke a waiver, having regard to the matters set out in clause 5.2.2. Subject to clause 5.3(c), if the **AER** varies or revokes a waiver it must provide notice of its decision to the **DNSP** and provide reasons.

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- (b) The **AER** may if it considers appropriate:

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~~(d)~~i. \_\_\_\_\_ conduct such consultation as it considers appropriate; in determining whether a waiver is still required; and

~~(e)~~ publish its decision on its website that explains the reasons to vary or revoke the waiver;

~~(f)~~ii. publish or the terms and conditions of any varied waiver that is granted; and

~~(g)~~(c) considerThe **AER** must, in consultation with the **DNSP**, provide an appropriate transition for the **DNSP** to implement the AER's newany decision made under clause 5.3(a).

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## 6 Compliance and enforcement

### 6.1 Maintaining compliance

A **DNSP** must establish and maintain appropriate internal procedures to ensure it complies with its obligations under this **Guideline**. The **AER** may require the **DNSP** to demonstrate the adequacy of these procedures upon reasonable notice. However, any statement made or assurance given by the **AER** concerning the adequacy of the **DNSP's** compliance procedures does not affect the **DNSP's** obligations under this **Guideline**.

### 6.2 Compliance reporting

#### 6.2.1 Annual compliance report

- (a) A **DNSP** must prepare an annual ring-fencing compliance report and submit it to the **AER**. The annual compliance report must identify and describe, in respect of the regulatory year to which the report relates:

- a.i. all measures a **DNSP** has taken to ensure compliance with ~~(all)~~ its obligations under this **Guideline**;
- b.ii. any breaches of this **Guideline** that relate to the **DNSP**; and
- c.iii. all ~~non-network energy-related~~ services provided by the **DNSP**, and all associated activities undertaken by the **DNSP**, in accordance with clause 3.1(b).

- (b) The annual compliance report must be accompanied by an assessment of compliance by a suitably qualified independent authority.

- (c) Annual compliance reports may be made publicly available by the **AER**.

#### 6.2.2 Timing of annual compliance reporting

- (a) ~~Subject to clause 6.2.2(b), a~~ **DNSP** must submit to the **AER** an annual compliance report within 4 months of the end of the regulatory year to which the compliance report relates.

- (b) A **DNSP** will not be required to start reporting on its compliance with this **Guideline** until the end of the first full regulatory year after ~~this Guideline commences~~ the Commencement Date.

#### 6.2.3 Reporting by AER

The **AER** may publish reports from time to time about **DNSPs'** compliance with this **Guideline** on the basis of information provided to it under this clause 6.2.2.

### 6.3 Compliance breaches

A **DNSP** must notify the **AER** in writing within five business days of becoming aware of a material breach of its obligations under this **Guideline**. The **AER** may seek enforcement of this **Guideline** by a court in the event of any breach of this **Guideline** by a **DNSP**, in accordance with the **NEL**.

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## 6.4 Complaints and investigations

At any time, the **AER** may require a **DNSP** to provide a formal response to particular complaints or concerns about compliance with this **Guideline**.

### 7 Appendix A – Transitional arrangements

(a) Despite clause 1.1:

~~(c) The obligation set out in clause 3.1(a) commences on a date that is 12 months after the commencement date provided in clause 1.1; and~~

i. ~~The the~~ obligations set out in clause 3.1, 3.2, 4.1(b)(vi) and 4.2 commence on a date that is 12 months after the **Commencement Date**; and

~~(d)ii.~~ the remaining obligations in clauses 4.2-1 and 4.2-23 commence on a date that is six months after the ~~commencement date provided in clause 1.1~~ **Commencement Date**.

(a) Where the **distribution determination** of the relevant **DNSP** results in a change to the classification of **distribution services** provided and that change materially affects the **DNSP's** obligations under this **Guideline**, the **DNSP** must implement changes to comply with the changed obligations within 12 months after the commencement of the relevant **distribution determination**.

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