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AER Draft Ring Fencing Guideline- Exposure Draft

The Australian Energy Council (the Energy Council) welcomes the opportunity to make a submission to the Australian Energy Regulator's (AER) Draft Ring Fencing Guideline - Exposure Draft (the Exposure Draft).

The Energy Council is the industry body representing 21 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

The Energy Council is concerned that the AER has made significant changes to the Draft Ring Fencing Guidelines through the Exposure Draft. Although we are pleased the AER has dropped the provision that allowed distribution network service providers (DNSP)'s to directly provide non network services to the value of \$500,000, we are concerned that waivers from legal separation obligations are now permitted.

The Energy Council is also concerned that the AER has made these changes without consulting with the broader market and providing a proper understanding for the reasons for these changes.

Removal of threshold

The Energy Council supports the AER's decision to abolish the proposed \$500,000 threshold that allows DNSPs to provide some limited non-network services directly. There has been little evidence to suggest why the threshold was ever necessary. The Energy Council previously raised concerns in the submission to the AER's Draft Guidelines that the materiality threshold of \$500,000 could have had an adverse effect on the market for Behind the Meter (BTM) contestable energy services. The Energy Council therefore supports the AER's decision as the retention of the threshold would have undermined the ring-fencing policy objectives.

Waivers for legal separation, cross promotion and co-branding

The Energy Council does not support the decision to permit waivers for legal separation, cross promotion and co-branding. This is in practice an acceptance of the contention that implementing measures to ensure DNSP's operate in contestable markets on a level playing field somehow constrains network efficiency and this places a greater cost on customers than the incremental benefits of highly competitive markets. The DNSPs provide regulated monopoly services. Waivers do not apply to the delivery of these monopoly services. Waivers provide economies of scope for DNSP owners.

The regulated entity is the entity that is ring fenced from other activity, not the other way around. Accordingly, it is the Energy Council view that legal separation and an absolute prohibition on cross promotion and co-branding is the minimum ring fencing requirement.

The Exposure Draft contemplates the circumstances in which a waiver may be legitimately required because of a jurisdictional requirement that compels a network to provide services that do not satisfy the definition of distribution services under the guideline. The example cited is Ergon Queensland's requirement to supply rural communities not connected to the National Electricity Market (NEM). Where such a community service obligation exists, and is required by law, then to the extent that the AER ring fencing guideline is inconsistent with the obligation and the law, the Energy Council submits that the threshold test has been met for a waiver to be made. These are however very limited and entirely apparent cases. The Energy Council contends that this threshold test should be the only circumstance in which a waiver application can be made or granted.

When waivers apply to legal separation, the Energy Council submits that consultation becomes more critical. Clause 5.4 should therefore be worded as the AER "must" publish reasons for granting or refusing waivers, terms and conditions of waivers for transparency and confidence in the process. All waivers should be subject to consultation to ensure that the AER is informed to come to an opinion around 5.3.2 (a) iii - the likelihood of impact to competition will only be exposed through a consultation process.

Staff sharing

The Energy Council does not support the decision to permit a DNSP to share staff or offices. Physically separating a DNSP's offices from its service providers or related bodies corporate and preventing staff sharing between a DNSP and its related body corporate would guard against the normal flow of information between DNSPs and their affiliates providing contestable services. Allowing waivers will lead to DNSPs to compromising the non-discrimination provisions that apply in the AER ring fencing guidelines.

We also oppose the decision to exclude an 'officer' (a director or company secretary) from the requirement for DNSPs to ensure staff involved in the provision of direct control services are not also involved in the provision of other distribution services or other electricity services. These staff members will have access to important information, including financial, strategic and other planning documents that relate to network and other services.

Furthermore, the definition of 'confidential information' appears too narrow, excluding aggregated financial information and other service performance information. The latter, for example, could identify where behind the meter services could offer value and augment network operations. This would be of value to market participants but the Exposure Draft does not seem to prevent its disclosure or sharing with an affiliate.

Interim waivers

The Energy Council does not support the decision to permit interim waivers. An interim waiver appears to be a default position that the AER may use if a decision cannot be made to refuse a waiver under 5.3.1. Further an interim waiver is allowing a DNSP a period of unchecked, unimpeded provision of contestable services without consideration of harm or impact. We are concerned that interim waivers are not subject to any test of the National Electricity Objective (NEO), cross subsidisation or discrimination or costs to consumers (including the impact to competition).

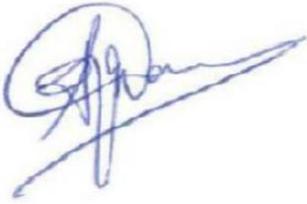
We are also concerned that these waivers do not have a mandatory expiry date and that the interim waiver could also apply to legal separation. Legal separation waivers are complete and require a reasonable amount of time to grant a waiver.

Finally, the Energy Council would welcome more clarity from the AER about its administration of the Guideline. For example, the Exposure Draft indicates the AER 'may' include a requirement for a DNSP to provide its internal accounting procedures and report on transactions with an affiliate in a regulatory information instrument. It also states that the AER 'may' publish reports from time to time about DNSPs' compliance with the Guideline.

We encourage the AER to closely monitor compliance and to be transparent in its operations. This means monitoring transactions between DNSPs and affiliates as a matter of course and more generally, providing regular information to the market about its administration of the Guideline. This will promote greater confidence in its effectiveness and therefore, in the potential for effective competition in the market for contestable services.

Any questions about our submission should be addressed to Panos Priftakis, Policy Adviser by email to panos.priftakis@energycouncil.com.au or by telephone on (03) 9205 3115.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'S. McNamara', with a long horizontal stroke extending to the right.

Sarah McNamara
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Australian Energy Council