

30 January 2020

Ms Sarah Proudfoot
General Manager, Consumers and Markets
Australian Energy Regulator
GPO Box 521
Melbourne VIC 3001

Dear Ms Proudfoot

Re: Review of transmission ring-fencing arrangements

Australian Energy Operations (**AEO**) welcomes the opportunity to respond to the Australian Energy Regulator's (**AER**) discussion paper on transmission ring-fencing arrangements.

AEO is a contestable transmission business that constructs, owns and operates electricity transmission assets, specialising in connecting generation assets and load requiring assets to the existing electricity network.

We support the AER's intention to update and strengthen the existing ring-fencing obligations that apply to incumbent Transmission Network Service Providers (**TNSP**). Robust ring-fencing arrangements are necessary to protect competition in the transmission industry.

In summary, AEO considers that:

- the current distribution ring-fencing guideline is an appropriate starting point for updating the transmission ring-fencing guideline
- stronger ring-fencing provisions should be imposed to promote competition for transmission connections
- care should be taken to ensure that ring-fencing does not stifle innovation for new and emerging contestable electricity services

Alignment with distribution ring-fencing guidelines

We support the alignment of the transmission ring-fencing guideline with the current distribution ring-fencing guideline. The distribution ring-fencing guideline contains stronger restrictions on the behaviour of the regulated entity in relation to cross-subsidies, information flows and non-discrimination, as well as requiring that contestable services are provided by a legally separate entity.

While the distribution ring-fencing guidelines are an appropriate starting point for the transmission ring-fencing guidelines, we note that COGATI and other reforms affecting transmission will need to be considered in developing the updated guideline.

The transmission ring-fencing guidelines should not be less rigorous than the distribution guidelines. Contrary to AER assertion, discrimination in the provision of information and cost allocation remain issues that cannot be overcome by the level of resourcing available to customers and potential competitors to the incumbent TNSP.¹

Promoting competition for connection services

In Victoria, competition for transmission connection services has resulted in accelerated innovation, product and service differentiation and lower prices for generators and ultimately consumers. The regulatory framework must continue to promote competition for these services, to the benefit of electricity consumers.

Contrary to AER assertion, the transmission and planning arrangements rule change (**TCAPA**) is not a panacea for all risks of harm to consumers in transmission connections. These arrangements are inadequate, and have not been successful in providing an environment for a third party to effectively compete and win a new connection in any state other than Victoria (where the TCAPA does not apply).

The TCAPA allows for full contestability of the management of 'dedicated connection assets' and only partial contestability of the management of 'identified user shared assets' – namely contestability in detailed design, construction and ownership of the asset, while high-level design and operation and maintenance (**O&M**) of the asset remain the responsibility of the incumbent TNSP. Therefore the TCAPA:

- does not allow contestable TNSPs to manage their assets' performance, and without full accountability it is unlikely to be viable for a competitive TNSP to invest
- increases incumbent TNSPs' risk exposure if they are fully accountable for the performance of the assets but have not managed design and construction, leading to higher costs.

The failure of the TCAPA arrangements to promote contestability in transmission connection services is evident by the fact that since the TCAPA came in to effect 18 months ago, there have been no new TNSP registrations with AEMO.

Ring-fencing is a mechanism that can be used to promote competition for connections. In particular, ring-fencing can reduce the risk of an incumbent TNSP providing preferential treatment to an affiliate, through:

- price, where there is cross-subsidisation
- non-price terms and conditions, such as timeframes for delivery, quality of service (including technical requirements) and variations.

¹ Australian Energy Regulator, Electricity Transmission Ring-fencing – a review of current arrangements, p. 27

For example, an incumbent TNSP could impose advantages to an affiliate in terms of the timing and cost of the “cut-in” to the shared network, or through the price, terms and conditions associated with the O&M for the identified user shared asset.

Ring-fencing could further support competition for competitive connection services by requiring that bids involving both regulated (prescribed and negotiated) and unregulated works be separated, to remove the risk of cross-subsidisation by the incumbent TNSP to lower the costs associated with the unregulated works. It could also require that the incumbent TNSP to provide proforma connection contracts for regulated works, to remove the risk of discrimination in non-price terms and conditions.

Care needs to be taken to avoid stifling innovation

We consider that ring-fencing controls should apply to TNSPs who are involved in the provision of new and emerging contestable electricity services. However, care needs to be taken to avoid stifling innovation and development of efficiencies in the provision of such contestable services. The guideline should not prevent or impose barriers for the incumbent TNSP to provide access to regulated resources by third parties including affiliates, but costs must be appropriately allocated. This will allow benefits for the regulated customers through the sharing of fixed costs plus the potential for the most efficient provision of the contestable service, as a TNSP could be in a position to do so more efficiently than other providers (for example, in the supply of frequency control ancillary services). The guidelines should include flexibility to allow ongoing change to the industry.

If you have any queries, please contact me on 03 9683 2096.

Kind regards



Eric Lindner
Chief Executive Officer