

**CitiPower and Powercor
Ring Fencing Waiver
Application
May 2017**

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1 Overview

1.1 Background

On 30 November 2016, the Australian Energy Regulator (**AER**) released its final Ring Fencing Guideline (**guideline**). The guideline seeks to prevent distributors from providing their affiliates operating in unregulated markets from having an unfair advantage.

In recognition of potential unintended consequences and the costs from immediately adopting all ring fencing obligations, the guideline allows distributors to apply for waivers from the following ring fencing obligations:

- legal separation—distributors may only provide distribution services;
- offices, staff branding and promotions—
 - staff involved in the provision or marketing of distribution services may not be involved with, or co-located with staff that provide, non-direct control services (unless an exclusion applies);
 - distributors must not use the same branding for direct control services as non-direct control services; and
 - distributors may not advertise or cross promote non-direct control services together with direct control services;
- conduct of service providers—distributors must ensure new or varied agreements with service providers require the service providers to meet ring fencing obligations.

Waivers are not available for cost allocation (cross subsidy), non-discrimination and information disclosure provisions.

1.2 Overview and purpose

On 17 February 2017, the AER requested CitiPower and Powercor (**us** and **we**) to submit a compliance strategy, waiver applications and No Action Letter requests by the end of July 2017. This application outlines our waiver and No Action Letter requests. In brief, we are seeking waivers in respect to:

- restrictions around the provision of negotiated and unclassified services;
- use of the Powercor Network Services brand (which includes the term 'Powercor') when undertaking unregulated services for large commercial and industrial customers;
- use of the CitiPower and Powercor brand in the provision of unregulated field services for large commercial and industrial customers; and
- a No Action Letter for adopting a single business operating model for CitiPower and Powercor.

2 Waiver applications and No Action Letter requests

2.1 Waiver approach

We have sought to balance adopting all ring fencing obligations immediately with the cost of doing so. To this end, we are only seeking waivers where the cost of complying with the guideline would be material and likely to outweigh the benefits, and in turn, only when waivers are in the long term interests of consumers.¹

We view waivers as temporary but necessary. Without the waivers we will incur material costs to comply with the guideline, which would be reflected in consumer prices. Over time, we will adopt all ring fencing obligations by taking advantage of natural changes to our business and the regulatory framework. We believe this is a pragmatic approach to comply with ring fencing and is consistent with the AER's intent.

The guideline specifies the information that waiver applications must contain and the factors to which the AER will have regard when assessing them.² Below we have outlined the relevant information and we will provide the AER with additional information as requested.

2.2 Negotiated and unclassified services waiver

The guideline places restrictions on the provision of negotiated and unclassified distribution services. We are seeking a waiver from these restrictions because current service classifications were not made with ring fencing in mind and as a result, ring fencing provisions do not fit well with existing classifications.

2.2.1 Waiver details

Service description

We are seeking a waiver for seven negotiated and unclassified services.³ The service descriptions outlined below include consideration of whether the service is contestable and the frequency with which we provide the service. We believe there is a strong case for waivers where a service is not contestable or has non-contestable elements, or where we offer the service in limited circumstances only. This is discussed more in section 2.2.2.

1. Alteration and relocation of distributor public lighting assets (Negotiated)

This service relates to public lights already connected to (and forming part of) the distribution system that are altered or relocated at a customer's request.

In the Framework and Approach Paper for the 2006-2010 regulatory control period (**Framework and Approach paper**), the AER concluded there remains monopoly element in the provision of services for existing public lights because distributors own and operate supporting infrastructure, the safety aspects of working in close proximity to overhead powerlines and the safety issues associated with the different lighting connection design standards that have traditionally applied.⁴ As a result, the alteration and relocation of public lights can only be undertaken by the distributor and there is no effective competition for this service.

2. New public lights - that is, new lighting types not subject to a regulated charge and new public lighting at greenfield sites (Negotiated)

¹ AER, Ring-Fencing Guideline; Electricity Distribution, November 2016, clause 5.3.2

² AER, Ring-Fencing Guideline; Electricity Distribution, November 2016, section 5

³ Services are outlined in the AER, Final Decision; Powercor distribution determination 2016 to 2020, Attachment 13 – Classification of services, May 2016. The non-standard connection service for which we are seeking a waiver is additional to those in the AER's Final Decision.

⁴ AER, Final Framework and approach for the Victorian Electricity Distributors, Regulatory control period commencing, 1 January 2016

Public lights in greenfield sites are contestable services. We neither participate in competitive tenders nor actively advertise that we can provide this service. Rather, we only provide the service when developers directly approach us, which typically occurs when:

- they were satisfied with our service on a previous occasion and do not want to incur the costs / time of searching for an alternative supplier; and
- there is an absence of other service providers in the area (that is, the service is not always contestable).

In the Framework and Approach paper, the AER considered distributors to have a role in providing this service due to challenges with implementing new lighting technologies, such as the need to satisfy safety, quality and energy usage requirements. It therefore classified the service as negotiated.

3. Reserve feeder construction (Negotiated)

A reserve feeder is a second connection from a distributor to a customer.⁵ The AER considered this a contestable service because customers can secure their energy supply in a number of ways, and therefore classified the service as negotiated.

Where a customer seeks a reserve feeder as their preferred way to secure energy supply, parts of the service are contestable under our Tender Policy for Extension Work.⁶ In practice, most customers select their distributor to provide the service and under the tender policy there are still elements of the service that are not contestable including the tie-in, premise connection assets and any necessary augmentation.

4. Collection of meter data, processing and storage of meter data, and provision of access to meter data for type 1-4 metering installations (excluding smart meters) (Unclassified)

It is a requirement of the National Electricity Rules (**NER**) that distributors have access to type 1-4 meter data. The data is provided to us by Meter Data Providers for billing purposes. This service is one which distributors must provide and is not contestable.

5. Emergency recoverable works (Unclassified)

When third parties cause damage to our network we may recover the cost under common law and in accordance with this emergency recoverable works service. This service is not contestable and can only be provided by distributors.

6. Installation, repair, and maintenance of watchman lights (Unclassified)

We provide watchman lights to local councils to assist with public safety in unlit areas such as parks. While this service is theoretically contestable, in practice the majority of the work is to connect watchman lights to the network, which is not contestable as per the alteration and replacement of public lighting. We do not advertise our provision of this service and it is rarely provided.

7. Non-standard connections (Unclassified)

⁵ AER, Final Framework and approach for the Victorian Electricity Distributors, Regulatory control period commencing, 1 January 2016

⁶ See <<https://www.powercor.com.au/our-services/electricity-connections/upgrade-or-extend-electricity-supply/tender-policy-for-extension-works/>>

This is a service for connections that are delivered to a higher standard than the least cost technically acceptable standard at a customer's request. The service only applies to works forming part of the distribution network or when a customer has waived its right to conduct a tender for contestable parts of the connection service. As such, the service is not contestable. This service is rarely provided.

Waiver obligations and duration

For the abovementioned services, we are seeking a waiver in accordance with clause 4.2.5 for obligations in clause 4.2.1—Physical separation/co-location, 4.2.2—Staff sharing and 4.2.3—Branding and cross promotion.

We are seeking this waiver for the duration of the current regulatory control period, being to 31 December 2020.

2.2.2 Reasons for seeking a waiver

The harm from not adopting ring fencing provisions

Market harm may arise from restricting competition in a market. We are not restricting competition in the markets for the alteration and relocation of public lights, emergency recoverable works, the collection of type 1-4 meter data services, watchman light and non-standard connection services because they are services that only we may provide.

We do not actively promote our provision of the contestable negotiated and unclassified services—being new public lights and reserve feeder construction. Given we rarely provide the services and when we do, it is often because we are the only provider in the area, our provision of the services is unlikely to affect competition or result in market harms.

The cost from adopting ring fencing provisions

To accord with ring fencing obligations for negotiated and unclassified services we would need to change our business processes for delivering these services. For example:

- negotiated and unclassified services cannot be provided with our brand in accordance with 4.2.3 of the guideline. Therefore we would need to establish a new brand, branding material (uniforms, fleet branding etc) and website; and
- we would potentially need to split the roles and relocate staff in the public lighting team. These staff may have access to electricity information (e.g. from knowing that a new connection request could result in public lighting work) which in theory could provide them with an advantage in offering lighting services.⁷ As discussed in the next section, this does not occur in practice, although the staff sharing and co-locating restrictions are triggered by the potential for it to occur.

Under the regulatory framework, the majority of these costs would be borne by consumers. Given there is little harm from providing the service as discussed, we believe these cost are unwarranted.

Further, the AER has flagged a number of changes to its service classification approach including developing a classification guideline and the removal of the negotiated classification.⁸ In the Preliminary Framework and

⁷ Splitting roles and re-locating staff that provide non-competitive negotiated and unclassified services is unlikely to be required as they do not have the opportunity to discriminate—as no other competitors exist (meaning they would receive an exemption under clauses 4.2.1(b)(i)(b) and 4.2.2(b)(i)(b)). It similarly may not be required for staff involved with reserve feeder construction given the Tender Policy ensures equal opportunity for all suppliers.

⁸ AER, Submission on contestability of energy services, 1 March 2017.

Approach Paper for NSW distributors, the AER has demonstrated it will consider ring fencing obligations when re-classifying services in the future. For example, the AER proposes to classify the emergency recoverable works service as standard control (rather than retaining the existing unclassified classification) to avoid ring fencing restrictions.⁹ Any changes to business practices we make now to comply with the guideline may either be unnecessary or not suitable after services are re-classified in 2021 with ring fencing in mind.

The potential for cross-subsidisation and discrimination

In deciding whether to grant a waiver, the AER must have regard to the potential for cross subsidisation and discrimination.¹⁰

Our cost allocation method (**CAM**) ensures no cross subsidisation between distribution services. Our accounts will also be auditable under the ring fencing guideline. Further, given we do not actively compete against other providers for the provision of these services, we do not have any incentive to cross subsidise them.

As discussed in section 2.2.2—*The cost from adopting ring fencing provisions*, in theory the public lighting team could use electricity information for discriminatory purposes. While the *opportunity* to discriminate is the trigger for the staff sharing and co-location restrictions, in practice our public lighting team does not use electricity information for discriminatory purposes. This is because we do not actively seek new public lighting projects, meaning we do not use electricity information to discriminate. Therefore a waiver from staff sharing and co-location restrictions will not lead to discriminatory practices.

Discrimination concerns do not arise for the other negotiated and unclassified services because they are either not competitive (meaning discrimination is not possible), or in the case of reserve feeder construction, are subject to a tender policy.

2.3 Powercor Network Services branding waiver

The guideline places an obligation on Powercor to have independent and separate branding to its related electricity service providers. We are seeking a waiver for using the Powercor brand, which is included in Powercor Network Services' name and branding material.

2.3.1 Waiver details

Powercor Network Services provides design and field services to us, affiliates and third parties. The Powercor Network Services entity and brand was established in 2006 and appears on:

- uniforms;
- fleet;
- advertising material; and
- contracts (to perform unregulated work or procure services).

More recently the use of the brand has been phased out—no new material is created with the Powercor Network Services brand and there are few instances of it still appearing. Energy Solutions Pty Ltd, trading as beon Energy Solutions (**contestable service provider**), has been created with distinct and separate branding as the

⁹ AER, Preliminary framework and approach Ausgrid, Endeavour Energy and Essential Energy Regulatory control period commencing 1 July 2019, March 2017, p. 20.

¹⁰ AER, Ring-Fencing Guideline; Electricity Distribution, November 2016, clause 5.3.2(a)(ii).

vehicle for the provision of unregulated services. Nevertheless, the guideline places an absolute obligation that Powercor must use branding that is independent from related electricity service providers.

Service description

We are seeking a waiver for the use of the Powercor name, which is included in Powercor Network Services' name, and branding material. We propose to narrow the scope of this waiver in the following ways:

- the waiver would allow the Powercor brand if Powercor Network Services only uses its brand when undertaking works for us (i.e. distribution services) or works for large commercial and industrial customers (i.e. distribution and non-distribution services). That is, Powercor Network Services' brand will not be used in connection with non-distribution services to residential and business customers; and
- when tendering for large commercial and industrial projects, the contestable service provider will be the tendering party; however field crews may have uniforms and equipment with Powercor Network Services branding.

Waiver obligations and duration

In accordance with clause 4.2.5, we are seeking a waiver from clause 4.2.3(a)(i)—that we must use branding for direct control services that is independent and separate from the branding used by a related service provider.

We are seeking this waiver for the duration of the current regulatory control period, being to 31 December 2020.

2.3.2 Reasons for seeking a waiver

The cost from adopting ring fencing provisions

Guideline compliance may be met by either rebranding Powercor or Powercor Network Services. Prior to 31 December 2020, we will rebrand Powercor Network Services and ensure associated legacy branding is removed.¹¹ We are nevertheless seeking a waiver from having to immediately adopt this guideline obligation because:

- we would otherwise need to identify and remove all instances of the Powercor Network Services brand. Immediately removing the brand will increase the cost of complying with the guideline, for example by prematurely retiring uniforms; and
- it will take time to rebrand Powercor Network Services, the process for which includes developing, internally consulting on, and receiving board approval for a new brand.

The harm from not adopting ring fencing provisions

There is little harm from granting this waiver because:

- during the development of the ring fencing guideline, the AER was concerned customers may be confused into thinking unregulated services provided by a distributor come with regulatory protections. In accordance with our service description, residential and small businesses will only associate the 'Powercor' name with regulated work to avoid confusion. Small scale solar PV, for example, will not be undertaken with any 'Powercor' branding;
- in accordance with our service description, the Powercor Network Services brand may be associated with unregulated work for large business and industrial customers. This should not create confusion because

¹¹ While the obligation to rebrand is on Powercor, rather than rebranding Powercor we will seek Powercor Network Services to rebrand.

these customers understand the distinction between regulated and unregulated work. Such customers consist of wind and solar farm developers and AusNet Services (for whom we provide transmission maintenance services);

- by not allowing the Powercor Network Services brand to be present on tender documentation, at the time a supplier is awarded a contract, we will not have provided an impression that CitiPower and Powercor have involvement in the unregulated work. Tenders for contestable non-distribution services will only be submitted under the contestable service providers' brand; and
- there are few instances of the brand name still being present in public as new uniforms and fleet are branded CitiPower and Powercor, and contracts for unregulated works are now made in the contestable service provider's name.

We believe that ensuring Powercor Network Services is only present in the abovementioned circumstances is a pragmatic approach that will not lead to the consumer harms that the guideline is targeted towards.

The potential for cross-subsidisation and discrimination

In deciding whether to grant a waiver, the AER must have regard to the potential for cross subsidisation and discrimination.¹²

This waiver only relates to branding issues meaning cross subsidisation concerns are not relevant.

The potential for providing an unfair discriminatory advantage to the contestable service provider (by being able to utilise field crew with the Powercor Network Services brand) have been addressed by ensuring the contestable service provider, which has no reference to Powercor in its brand, will be the tendering party.

2.4 CitiPower and Powercor branding

The guideline does not allow the use of the CitiPower and Powercor brand in connection with non-direct control services.

2.4.1 Waiver details

Service description

We are seeking a waiver from the prohibition on CitiPower's and Powercor's brand from being present when performing field work for third parties and affiliates (i.e. non-direct control services), where the works are solely for large commercial and industrial customers. Such circumstances would include:

- assisting AusNet Services with transmission maintenance services;
- wind and solar farms seeking reticulation work within their site; and
- real estate developers seeking reticulation within their development.

The effect of this waiver is to allow the contestable service provider and third parties to engage Powercor Network Services' staff with uniforms and equipment that bears the CitiPower and Powercor brand.

We propose to narrow the scope of this waiver in the following ways:

- the waiver does not allow staff branded CitiPower and Powercor promoting the services of the contestable service provider. Measures outlined in our compliance strategy ensure this will not occur;

¹² AER, Ring-Fencing Guideline; Electricity Distribution, November 2016.3.2(a)(ii)

- for large commercial and industrial customers, the CitiPower and Powercor brands would not be present at the time of tendering for work; it may only be present once a tender is completed; and
- the waiver is not being sought for residential customers or small business customers seeking non-distribution services.

Waiver obligations and duration

In accordance with clause 4.2.5, we are seeking a waiver for clause 4.2.3(a)—Branding and cross-promotion.

We are seeking this waiver for the duration of the current regulatory control period, being to 31 December 2020.

2.4.2 Reasons for seeking a waiver

The harm from not adopting ring fencing provisions

We have limited the scope of this waiver so that it does not result in consumer harms. In particular:

- it only applies to large commercial and industrial customers—these customers are well aware of which works are regulated and unregulated, and in turn which works come with the protections of the regulatory framework. For example windfarms and developers almost always tender the reticulation work within their site as they know this is unregulated work. AusNet Services uses the contestable service provider to assist with its transmission maintenance work and it understands this work is undertaken on a contractual basis that is not subject to the regulatory framework; and
- by not allowing the CitiPower and Powercor brands to be present on tender documentation, we will further avoid giving the impression that CitiPower and Powercor have involvement in the unregulated work at the time the supplier is awarded. Tenders for contestable non-distribution services will only be submitted under the contestable service provider brand (although the field crew that undertake the work may bear the CitiPower and Powercor brands).

The only advantage from the waiver is that CitiPower and Powercor receive some brand awareness when driving branded vehicles to the contestable worksite. However, we consider any advantage is irrelevant to ring fencing concerns because:

- we do not receive unfair market advantage from brand awareness because we do not provide non-distribution services in competitive markets. Rather, this situation is most likely to represent a disadvantage to the contestable service provider that does not have its brand advertised; and
- the amount of work undertaken for the contestable service provider and third parties with the CitiPower and Powercor brands present, is less than 2 per cent of time.

As such, allowing this waiver would not create consumer harm.

The potential for cross-subsidisation and discrimination

In deciding whether to grant a waiver, the AER must have regard to the potential for cross subsidisation and discrimination.¹³

This waiver only relates to branding issues meaning cross subsidisation concerns are not relevant.

¹³ AER, Ring-Fencing Guideline; Electricity Distribution, November 2016, 5.3.2(a)(ii)

The potential for providing an unfair discriminatory advantage to the contestable service provider (by being able to utilise field crew with the CitiPower and Powercor brands) have been addressed by ensuring the contestable service provider, which has no reference to CitiPower or Powercor in its brand, will be the tendering party.

2.5 Seeking No Action Letter

CitiPower and Powercor hold separate licenses but essentially operate as a single business with shared management, employees and systems. This may give rise to potential areas of strict non-compliance with the guideline. For example:

- CitiPower and Powercor have a single website, which could be seen as cross promoting services in contravention of clause 4.2.3(a)(iii); and
- employees share confidential electricity information (i.e. within CitiPower and Powercor, and not with the contestable service provider) for regulatory purposes in contravention of clause 4.3.

We believe it is not the guideline's intent to place ring fencing obligations between CitiPower and Powercor as this arrangement promotes efficiencies and does not lead to consumer or market harms. We therefore propose that in respect to areas of non-compliance arising from single business models and where there is no impact on other affiliated entities, the AER either:

- amend the guideline; or
- issue a general No Action Letter.

We believe these options are more appropriate than a waiver because it will be difficult to individually identify all the activities needing to be included in the waiver, waivers may not be available for all activities, and given the waiver's potential to not be renewed, it provides insufficient certainty to our business and shareholders.