

Ref: fC117935

15 August 2017

Mr Chris Pattas
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Dear Mr Pattas

Essential Energy Submission on the Draft Amended Ring-Fencing Guideline

Essential Energy appreciates the opportunity to comment on the Draft Amended Ring-Fencing Guideline (amended Guideline).

The items in the amended Guideline with which we are providing comment on are:

- > The Regional office exemption in Clause 5.6; and
- > Suppliers in Clause 4.4.1(a).

Each of these items is discussed in more detail below.

Changing the Definition of Regional Office

Energex indicated in their Ring Fencing Compliance Strategy that they would be proposing an amendment to the definition of 'regional office' in their response to the AER's draft amended Ring Fencing Guideline. Their proposed amended definition (according to their compliance plan) is:

'An office that has less than 25,000 connection points within a 100 kilometre radius of that office or where there is no locally located alternative service provider.'

Essential Energy supports Energex's proposed amendment and proposes an additional amendment as indicated below:

'An office that has less than 25,000 connection points within a 100 kilometre radius of that office or where there is no locally located alternative service provider or where services can't be provided by an alternative service provider within a reasonable timeframe given the nature of the services.'

As previously indicated in our letter accompanying our compliance plan submission to the AER in July Essential Energy has made a strategic decision not to provide contestable services across our footprint in order to achieve compliance with the Ring Fencing Guideline. However, we are concerned about the possibility of reduced services to those communities in regional locations where there is limited or no existing competition. Our concern for regional communities where there may be a lack of competition can be categorised into two main areas:

- Lack of access to affordable services – where only a single competitive provider exists and abuses their market power or where service providers may be located a significant distance away and mobilisation becomes a significant cost; and
- Lack of access to timely services – where providers advise customers that they are unable to perform the works requested in a timely manner and there is a lack of alternative suppliers.

In many of the areas in Essential Energy's footprint that don't qualify as a regional office there are either no service providers or a limited number of service providers. Our proposed amendment to the regional office definition, adding to the proposed amendment from Energex, allows us to both achieve compliance with the Guideline and ensure regional customers don't lose access to services.

Narrowing the scope of the revised Suppliers clause 4.4.1(a)

The amended Guideline at clause 4.4.1(a) includes new wording '*...that enable or assist the DNSP to supply direct control services*' in an attempt to resolve DNSP concerns with the broad wording in the original Ring-Fencing Guideline that unintentionally captured a range of contracts not targeted by the policy intent of this clause.

Essential Energy continues to have the same concerns with the amended clause. The interpretation of the AER's proposed addition of the words '*...that enable or assist the DNSP to supply direct control services*' to the clause is unclear. The phrase '*enable or assist*' could be read broadly to apply to a wider range of agreements than necessary. For example, security or cleaning services (which the AER has stated that the amendments are intended to exclude) could be interpreted as services that '*assist*' the AER to supply direct control services.

As a result, Essential Energy proposes to inclusion of the following amended clause 4.4.1(a):

A DNSP:

*(a) must ensure that any new or varied agreement between the **DNSP** and a **service provider** who provides services to both the **DNSP** and a **related electricity service provider** of the **DNSP**, which provides for the **service provider** to perform any of the **DNSP's** functions in respect of **direct control services**, for the provision of services to the **DNSP** that enable or assist the **DNSP** to supply **direct control services**, requires **the service provider** to comply, in providing those services, with:*

- i. clauses 4.1, 4.2.1, 4.2.2 and 4.3.2 of this **Guideline**; and*
- ii. clause 4.2.3 of this **Guideline** in relation to the brands of the **DNSP**;*

*as if the **service provider** was the **DNSP**.*

This drafting ensures that the clause only captures agreements for services with a close relationship to the provision of direct control services and, therefore, better excludes agreements for general services, such as security or cleaning services, as well as excluding the providers of inputs into Essential Energy direct control services such as traffic control, civil works contractors on major projects, and under-boring contractors.

The drafting operates to confine the operation of clause 4.4.1(a) to agreements with a service provider under which the provider performs some of the functions of the DNSP (e.g. an operating agreement). This is consistent with ring-fencing guidelines that have previously been in place in the electricity industry. For example, the Essential Services Commission of Victoria's Electricity Ring-Fencing Guideline (October 2004) included a clause entitled 'Outsourcing' that provided '*If a distributor or a retailer arranges for another entity to perform any of its business functions it must ensure that the entity complies with this guideline as if it were the distributor or the retailer*'.

In addition, the revised clause restricts the obligations of clause 4.4.1(a) to those contracts where the supplier supply's services to both the DNSP and a related electricity service provider (RESP). Essential Energy believes that this is where the greatest risk lies in supplier contracts, and that clause 4.4.1(b) operates to reduce the risk of discrimination in other contracts.

Essential Energy is concerned that requiring all contracts that provide for the performance of any of the DNSP's functions to incorporate the obligations outlined in clause 4.4.1(a) would unnecessarily increase the costs of these contracts and therefore the costs of delivering standard control services for little benefit in terms of reduced compliance risk. For example, Essential Energy has a number of contracts in place for the supply of vegetation management services. These contracts were established following a competitive tender process and were awarded to a number of suppliers completely unrelated to Essential Energy. Requiring them to 'ring fence' their employees and offices for their work related to Essential Energy from their other work would impose increased costs on Essential Energy which could only be recovered from customers. It may even result in the perverse outcome of increasing the costs of supply above the costs that Essential Energy would be able to

deliver the service for itself and thereby possibly undermine the competitive markets the Guideline is looking to protect.

We thank you for the opportunity to comment on the amended Guideline. Should you have any questions on this submission, please don't hesitate to contact Natalie Lindsay on (02) 6589 8419.

Yours sincerely

A handwritten signature in black ink, appearing to be 'G. Humphreys', written in a cursive style.

Gary Humphreys
Executive General Manager Regulation and Innovation