

Legal and Functional Separation Guideline – *Electricity* *Infrastructure Investment Act* Draft

August 2023

© Commonwealth of Australia 2023

This work is copyright. In addition to any use permitted under the *Copyright Act 1968* all material contained within this work is provided under a Creative Commons Attributions 3.0 Australia licence with the exception of:

- the Commonwealth Coat of Arms
- the ACCC and AER logos
- any illustration diagram, photograph or graphic over which the Australian Competition and Consumer Commission does not hold copyright but which may be part of or contained within this publication.

The details of the relevant licence conditions are available on the Creative Commons website as is the full legal code for the CC BY 3.0 AU licence.

Inquiries about this publication should be addressed to:

Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601
Tel: 1300 585 165

AER reference: XXXXX

Amendment record

Version	Date	Pages
1	3 August 2023	17

Contents

1	Introduction	2
1.1	Objectives of this Guideline	2
1.2	Process for revisions	3
1.3	Scope of Guideline	3
1.4	Relationship with other instruments	3
2	Legal and Functional Separation	4
2.1	Legal Separation.....	4
2.2	Staff Separation.....	4
2.3	Obligation not to discriminate.....	4
3	Establishment and maintenance of separate accounts.....	6
3.1	Separate Accounts – internal activities	6
3.2	Separate Accounts – related entities.....	6
4	Limitations on flow of information	7
4.1	Protection of EII Regulated Activity information	7
4.2	Disclosure of information	7
4.3	Sharing of information.....	7
4.4	Information Register	8
5	Waivers	9
5.1	Application for a waiver.....	9
5.2	AER’s consideration of a waiver request.....	9
5.3	Class waivers	10
5.4	Publication of reasons	10
5.5	Reviewing a waiver.....	11
5.6	Waiver register	11
6	Compliance and reporting	12
6.1	Maintaining Compliance.....	12
6.2	Annual Compliance Reporting	12
6.3	Compliance Breaches.....	13
6.4	Complaints and investigations	13
	Glossary.....	14

Invitation to make submissions

We invite interested parties to make written submissions in response to this draft Guideline, and the other draft supporting guidelines for the Electricity Infrastructure Investment Act released by the AER, by close of business 23 August 2023.

Please contact us if you would like to meet with AER staff during this consultation period. Submissions should be sent electronically to REZ@aer.gov.au with the title 'Submission – Draft Guidelines EII Act' We ask that all submissions sent in an electronic format are in Microsoft Word or another text-readable document form.

Alternatively, submissions may be sent to:

Kami Kaur
Acting General Manager,
NSW REZ Branch
Australian Energy Regulator
GPO Box 3131 Canberra ACT 2601

Enquiries about this paper, or about lodging submissions, should be directed to REZ@aer.gov.au.

Confidentiality

The AER prefers that all submissions be publicly available to facilitate informed and transparent consultation. Submissions will be treated as public documents unless otherwise requested.

Parties wishing to submit confidential information are requested to:

- clearly identify the information that is the subject of the confidentiality claim, and
- provide a non-confidential version of the submission in a form suitable for publication.

All non-confidential submissions will be placed on the [AER's website](#). For further information regarding the AER's use and disclosure of information provided to it, please see the [ACCC/AER Information Policy](#) available on our website.

Public forum

The AER will host an online public forum to allow stakeholders the opportunity to ask questions about our draft Guidelines before submissions close.

The public forum will be held from 10 am to 11 am (AEST) on 14 August 2023. To register your interest in the public forum, please email REZ@aer.gov.au by close of business on 11 August 2023.

Next steps

We will consider submissions received and feedback from the public forum before we publish a final Guideline in early September 2023.

1 Introduction

The Australian Energy Regulator (AER) is the regulator of electricity networks in all jurisdictions except Western Australia. We are empowered to regulate electricity networks by the National Electricity Law (NEL) and the National Electricity Rules (NER). We are also a regulator appointed under the *Electricity Infrastructure Investment Act 2020 (NSW)* (EII Act).

The EII Act requires us to perform several functions, including those prescribed by the *Electricity Infrastructure Investment Regulation 2021 (NSW)* (EII Regulation).¹ One of our functions under the EII Regulation is to issue a guideline (this Guideline) for Network Operators about:²

- The legal separation of an entity through which a Network Operator conducts regulated activities from any other entity through which it conducts business,³
- The establishment and maintenance of consolidated and separate accounts for regulated activities and other activities conducted by the Network Operator,⁴ and
- The limitations on the flow of information within a Network Operator, if there is the potential for a competitive advantage or disadvantage to arise.⁵

We are also required to set standards about the legal and functional separation of regulated activities from other activities of a Network Operator and monitor the compliance of network operators with these standards.⁶

1.1 Objectives of this Guideline

This Guideline aims to promote competition in the provision of electricity services by addressing the risk that Network Operators could use their position as monopoly providers to distort outcomes in contestable markets.

This Guideline imposes obligations on Network Operators to prevent these outcomes by addressing the risks of cross-subsidisation and discrimination.

- **Cross-subsidisation** occurs when a Network Operator uses revenue it earns in providing regulated activities to subsidise its activities in other, contestable markets (i.e., offering a lower-than-cost price in contestable markets). Cross-subsidisation can undermine or damage competition and innovation in contestable markets. In addition, it can result in consumers paying more than they should for regulated activities.
- **Discrimination** occurs when a Network Operator uses its monopoly position in regulated markets, or information obtained through the provision of those regulated activities, to favour itself (or an affiliated entity) or to discriminate against a competitor in contestable markets. This harms consumers by distorting outcomes in

¹ EII Act, s. 64(4)(b).

² EII Regulation, cl. 42(1).

³ EII Regulation, cl. 42(1)(a)(i).

⁴ EII Regulation, cl. 42(1)(a)(ii).

⁵ EII Regulation, cl. 42(1)(a)(iii).

⁶ EII Regulation, cl. 42(1)(b) & (c).

competitive markets by reducing competition which increases prices and reduces innovation.

Regulated activities of a Network Operator refers to activities for which the Network Operator is paid under a revenue determination under the EII Act.⁷

1.2 Process for revisions

We may amend this Guideline from time to time. Should we amend this Guideline, we will publish the proposed amendment on our website for a period of at least 20 business days and consider submissions received within that period.⁸ We may not consult on amendments we consider to be minor or administrative.⁹

1.3 Scope of Guideline

This Guideline applies to all Network Operators subject to an authorisation or direction under the EII Act, to carry out a Network Infrastructure Project or a Priority Transmission Infrastructure project.

Network Operators are required to comply with this Guideline, as described in their contractual arrangements.

1.4 Relationship with other instruments

This Guideline should be read in conjunction with:

- The AER – Cost Allocation Guideline – Electricity Infrastructure Investment Act Draft,
- The Network Operators’ approved Cost Allocation Methodology,
- Any regulatory information instrument served on a Network Operator, and
- Any relevant NER guidelines (such as the NER Cost Allocation Guideline and the relevant NER Ring-Fencing Guideline).

References to legal and function separation requirements, or ring-fencing, are made in other EII guidelines published by the AER:

- [Revenue determination guideline for NSW contestable network projects.](#)
- [Transmission Efficiency Test and Revenue Determination Guideline for Non-contestable network infrastructure projects.](#)

In the event of any inconsistency between this Guideline and the guidelines mentioned above, this Guideline will be used.

⁷ EII Regulation, cl. 42(2).

⁸ EII Regulation, s. 47C(1).

⁹ EII Regulation, s. 47C(2)(b).

2 Legal and Functional Separation

2.1 Legal Separation

Subject to the obligations in this Guideline, a Network Operator conducting regulated activities under the EII Act may:

- Conduct other regulated activities under the EII Act,
- Deliver other regulated or non-contestable electricity services,
- Deliver other contestable electricity services, and
- Deliver other services.

This Guideline does not affect the operation of the NER Ring-Fencing Guidelines or any other regulatory instrument the Network Operator is required to comply with.

2.2 Staff Separation

A Network Operator must ensure that:

- a) staff involved in the provision of regulated activities under the EII Act or in the provision of other regulated or non-contestable electricity services, are also not marketing staff involved in the provision of contestable electricity services by a related electricity services provider; and
- b) marketing staff involved in the provision of regulated activities under the EII Act or in the provision of other regulated or non-contestable electricity services, are also not staff involved in the provision of contestable electricity services by a related electricity service provider, and
- c) staff involved in planning for network activities in consultation with the Infrastructure Planner (EnergyCo), are also not staff involved in preparing responses or submissions to contestable procurement processes for that network activity, and
- d) staff involved in planning for network activities in consultation with the Infrastructure Planner (EnergyCo), are physically separate from staff involved in preparing responses or submissions to contestable procurement processes for that network activity, for the duration of the procurement process.

A Network Operator may apply for a waiver of the obligations set out in this clause 2.2.

2.3 Obligation not to discriminate

A Network Operator must not discriminate (either directly or indirectly) between a related electricity service provider and a competitor (or potential competitor) of a related electricity service provider in connection with the provision of regulated activities under the EII Act or other regulated or non-contestable electricity services.

- A related electricity service provider (in relation to a Network Operator) includes any affiliated entity of the Network Operator, or part of the Network Operator that provides contestable electricity services but excludes the part of an affiliated entity that provides EII regulated activities, prescribed transmission services, negotiated transmission services, or direct control services. This includes a customer, or potential customer, of the related electricity service provider of the Network Operator.

- A competitor (or potential competitor) of a related electricity service provider includes a customer, or potential customer, of the competitor (or potential competitor) of the related electricity service provider.
- Dealing or offering to deal includes dealing or offering to deal in relation to the provision of goods or services, or the granting of rights by the Network Operator, or to the Network Operator.

A Network Operator must deal or offer to deal with related electricity service providers, in the same manner as if they were not a related electricity service provider, including if they are a competitor (or potential competitor).

For clarification, this means the Network Operator must, in like circumstances:

- Deal or offer to deal with all electricity service providers on substantially the same terms and conditions,
- Provide substantially the same quality, reliability, and timeliness of service to all electricity service providers, and
- Not disclose information obtained through dealings with one electricity service provider, to another electricity service provider, where the disclosure would or would be likely to provide an advantage to an electricity service provider,

regardless of whether the electricity service provider is a related electricity service provider of the Network Operator or a competitor (or potential competitor).

A Network Operator cannot apply for a waiver of the obligations set out in this clause 2.3.

3 Establishment and maintenance of separate accounts

3.1 Separate Accounts – Internal Activities

A Network Operator must establish and maintain both consolidated and separate accounts for each type of activity conducted by the Network Operator.¹⁰ Activity types are:

- EII regulated activities,
- Other regulated activities or services, and
- Other activities or services.

The Network Operator must allocate or attribute costs (including costs allocated or attributed to the Network Operator by a parent entity) to its' activities or services in a manner consistent with:

- the EII Cost Allocation Guideline,
- its' approved cost allocation methodology,
- and any existing obligations arising from relevant NER guidelines (such as the Cost Allocation Guideline and the appropriate Ring-Fencing Guideline).

3.2 Separate Accounts – Related Entities

A Network Operator must establish and maintain appropriate internal accounting procedures to ensure that it can demonstrate the extent and nature of transactions between the Network Operator and its related entities.

A Network Operator must establish, maintain, and keep records that demonstrate how it meets the obligations in this section 3 (3.1 and 3.2).

A Network Operator cannot apply for a waiver of the obligations section out in this section 3 (3.1 and 3.2).

¹⁰ EII Regulation, cl. 42(1)(a)(ii).

4 Limitations on flow of information

EII Regulated Activity information refers to *electricity information* acquired or generated by a Network Operator in connection with its regulated activities under the EII Act or other regulated activities, that is not already publicly available. This includes *electricity information*:

- That the Network Operator derives from that information, or
- Information provided to the Network Operator by or in relation to a customer or prospective customer of regulated services under the EII Act, or other regulated services.

Electricity information means information about electricity networks, electricity customers or electricity services, other than aggregated financial information or other service performance information that does not relate to an identifiable customer or class of customer.

4.1 Protection of EII Regulated Activity information

A Network Operator must keep *EII Regulated Activity information* confidential and only use this information for the purpose for which it was acquired or generated.

4.2 Disclosure of information

A Network Operator must not disclose *EII Regulated Activity information* to any person, including a related electricity service provider unless:

- a) The Network Operator has first obtained the explicit informed consent of the person from whom the information was obtained,
- b) The disclosure is required by, or for the purpose of complying with, any law,
- c) The disclosure is necessary to enable the Network Operator to provide services (including by acquiring services from other legal entities),
- d) The information has been requested by or on behalf of a customer, or potential customer, of another legal entity, and the disclosure is necessary to enable the legal entity to provide services to the customer or potential customer,
- e) The disclosure is solely for the purpose of providing assistance to the extent necessary to respond to an event (such as an emergency) that is beyond the Network Operator's reasonable control,
- f) The disclosure is solely for the purposes of research by a legal entity other than a related electricity service provider of the Network Operator,
- g) A related electricity service provider of the Network Operator has requested the disclosure and the Network Operator complies with section 4.3 in relation to that information, or
- h) Another legal entity, other than a related electricity service provider of the Network Operator, has requested the disclosure.

4.3 Sharing of information

Subject to clause 2.3 and this section 4, a Network Operator must provide access to *EII Regulated Activity information* to other legal entities on an equal basis:

- a) Where a Network Operator shares *EII Regulated Activity information* with a related electricity service provider, or

- b) Where a Network Operator shares *EII Regulated Activity information* with another legal entity under clause 4.2(f) or (h), which is then disclosed to a related electricity service provider.

A Network Operator is only required by clause 4.3 to provide information to a legal entity where:

- The legal entity has requested that it be included on the information register in respect of information of that kind, and
- The legal entity is competing, or is seeking to compete, with a related electricity service provider, in relation to the provision of contestable electricity services.

A Network Operator is not required by clause 4.3 to provide information to a legal entity where the Network Operator has disclosed the information in the circumstances set out in clauses 4.2(a) to (e).

A Network Operator must establish an information sharing protocol that sets how and when it will make the information referred to in clause 4.3 available to legal entities and must make that protocol publicly available on its website.

Where a Network Operator discloses information referred to in clause 4.3 to any other legal entity under this clause 4.3, it must do so on terms and conditions that require the other legal entity to comply with clause 4.1 and 4.2(a) to (d) in relation to that information as if the other legal entity were the Network Operator.

4.4 Information Register

A Network Operator must establish, maintain, and keep a register of all:

- Related electricity service providers, and
- Other legal entities who provide contestable electricity services but who are not affiliated entities of the Network Operator

who request access to EII Regulated Activity information identified in clause 4.3 and must make the register publicly available on its website.

For each entity that has requested that the Network Operator provide access to this information, the register must:

1. Identify the kind of information requested, and
2. Describe the kind of information requested in sufficient detail to enable other legal entities to make an informed decision about whether to request the same information from the Network Operator.

A legal entity may request that the Network Operator include it on the information register in relation to some or all of the kinds of information that the Network Operator is required to provide under clause 4.3, and the Network Operator must comply with that request.

A Network Operator cannot apply for a waiver of the obligations set out in this section 4 (4.1 to 4.4).

5 Waivers

The AER will not grant a waiver of an obligation under this Guideline other than in accordance with this section.

5.1 Application for a waiver

A Network Operator may apply for a waiver of its obligation/s under sections of this Guideline, either on its own behalf or on behalf of itself and one or more other Network Operators. An application for a waiver must contain:

1. The obligation the Network Operator is requesting to waive (including a reference to the clause in this Guideline),
2. The reasons why the Network Operator is requesting the waiver,
3. Details of the service or services in relation to which the Network Operator is requesting the waiver,
4. The proposed start and end dates of the waiver (if any), including reasons for the dates,
5. Details of the costs associated with complying with the obligation if the request for a waiver were to be refused,
6. The regulatory control period (or periods) to which the waiver would apply,
7. Any additional measures the Network Operator proposed to undertake if the waiver were granted, and
8. The reasons the Network Operator considers the waiver should be granted, with reference to the matters described in clause 5.2 – including the benefits, or likely benefits, of the grant of the waiver to electricity consumers.

5.2 AER's consideration of a waiver request

The AER must consider an application for a waiver, and may:

- Grant the waiver subject to any conditions the AER considers appropriate; or
- Grant the waiver as an interim waiver subject to any conditions the AER considers appropriate; or
- Refuse to grant the waiver.

In assessing a waiver request and deciding whether to grant or refuse a waiver, the AER will have regard to:

- The potential for cross-subsidisation and discrimination if the waiver is granted or refused,
- Whether the benefit, or likely benefit, to consumers associated with the Network Operator complying with the obligation (including any benefit, or likely benefit, from increased competition) would be outweighed by the cost to the Network Operator of complying with the obligation.

Also in assessing a waiver request and deciding whether to grant or refuse a waiver, the AER may:

- Have regard to any other matter it considers relevant,

- Request further information from the Network Operator the AER considers appropriate,
- Invite public submissions on the applications, and
- Otherwise conduct such consultation as it considers appropriate with any person.

5.2.1 Interim Waivers

The AER may, in its absolute discretion, grant an interim waiver, without having regard to any of the matters specified in clause 5.2.

An interim waiver ceases to have effect:

- When the AER makes a further decision to grant or refuse to grant the waiver, or
- On the expiry date (if any) specified by the AER when granting the interim waiver,

whichever occurs first.

5.2.2 Form of waiver

The AER may grant a waiver or interim waiver that applies:

- To one or more of the Network Operators that are the subject of the waiver application,
- For a term that coincides with part of or all the Network Operator's current regulatory control period, next regulatory control period, or both periods,
- For a different term or terms, and
- Subject to such conditions as the AER considers appropriate.

The AER may, in its absolute discretion, refuse to grant an application for a waiver or interim waiver, without having regard to any of the matters specified in clause 5.2, if it determines that the application was made on trivial or vexatious grounds.

5.3 Class waivers

The AER may, on its own initiative, in its absolute discretion and at any time, grant, vary or revoke a class waiver of an obligations under this Guideline:

- For a term the AER consider appropriate, and
- Subject to any conditions the AER considers appropriate,

provided that, in the case of a variation or revocation, it has given at least 40 days' notice that it is considering doing so.

5.3.1 Class waiver assessment

In deciding whether to grant, vary or revoke a class waiver, the AER:

- Will have regard to the matters set out in clause 5.2 of this Guideline,
- May have regard to any other matter it considers relevant,
- May request information from one or more Network operators, and
- May take the steps set out in this Guideline.

5.4 Publication of reasons

The AER may publish its reasons for granting or refusing to grant a waiver or interim waiver.

5.5 Reviewing a waiver

The AER may, in its absolute discretion and at any time, vary or revoke a waiver (including the terms and/or conditions of a waiver) as long as it has given the Network Operator at least 40 days' notice that it is considering doing so.

In deciding whether to revoke or vary a waiver, the AER will have regard to matters specified in clause 5.2, and any other matters it considers relevant.

5.6 Waiver register

A Network Operator must establish, maintain, and keep a register of all waivers (including any variation of a waiver) granted to the Network Operator by the AER under this Guideline, and must make the register publicly available on its website.

The register must include a description of the obligation to which the waiver or interim waiver applies, and the terms and conditions of the waiver or interim waiver. These must match the AER's written decision, provided by the AER to the Network Operator.

6 Compliance and reporting

6.1 Maintaining Compliance

A Network Operator must establish and maintain appropriate internal procedures to ensure it complies with its' obligations under this Guideline and any other relevant Guideline.

The AER may require the Network Operator to demonstrate the adequacy of these procedures upon reasonable notice. However, any statement made or assurance given by the AER about the adequacy of the Network Operator's compliance procedures does not affect the Network Operator's obligations.

6.2 Annual Compliance Reporting

A Network Operator must prepare an annual compliance report each calendar year in accordance with this Guideline and submit it to the AER.

- If the Network Operator already submits an annual compliance report to the AER due to obligations under NER ring-fencing guidelines, that compliance report may be adjusted to accommodate any additional obligations under this Guideline.

The annual compliance report must identify and describe, in respect of the calendar year to which the report relates:

1. The measures the Network Operator has taken to ensure compliance its obligations under this Guideline,
2. Any breaches of this Guideline by the Network Operator, or which otherwise relate to the Network Operator,
3. All services provided by the Network Operator, and
4. The purpose of all transactions between the Network Operator and an affiliated entity.

The annual compliance report must be accompanied by an assessment of compliance with each provision of this Guideline by a suitably independent authority.

A Network Operator's annual compliance report may be based on information provided to the AER under a regulatory information instrument for the Network Operator's most recent regulatory year. If so, that annual compliance report must cover the entirety of that regulatory year.

6.2.1 Timing of annual compliance reporting

A Network Operator must submit its annual compliance report to the AER within four months of the end of the calendar year to which the compliance report relates.

6.2.2 Reporting by the AER

The AER may publish annual compliance reports or publish reports about the Network Operator's compliance with this Guideline on the basis of the information provided to it in this section 6.

6.3 Compliance Breaches

A Network Operator must notify the AER in writing within 15 business days of becoming aware of a breach of its obligations under this Guideline, including any breach of clause 6.2.2 or this section (6.3) of this Guideline.

6.4 Complaints and investigations

Network Operators must provide a written response to a complaint or concern raised by the AER about the Network Operator's compliance with this Guideline, including where the AER has previously required the Network Operator to provide one or more written responses to the relevant complaint or concern.

Glossary

Term	Definition
EII Act	Electricity Infrastructure Investment Act 2020 (NSW).
EII Regulation	Electricity Infrastructure Investment Regulation 2021 (NSW) made under the EII Act.
Related electricity service provider	In relation to a Network Operator, includes; <ul style="list-style-type: none"> - Any affiliated entity of the Network Operator, and - The part of the Network Operator that provides contestable electricity services, but excludes the part of the related entity that provides regulated electricity services.
Contestable electricity services	Means services for the supply of electricity or that are necessary or incidental to the supply of electricity, which are permitted to be provided by more than one electricity service provider or network operator, as a contestable service or on a competitive basis.
Legal entity	A natural person, a body corporate (including a statutory corporation or public authority), a partnership, or a trustee of a trust, but excludes staff in their capacity as such.
EII Regulated Activities	Activities of a Network Operator, for which the Network Operator is paid under a revenue determination made under the EII framework (the EII Act and EII Regulation).
Other regulated Activities or services	Activities of a Network Operator, for which the Network Operator is paid under a revenue determination made under the NER. These are prescribed transmission or direct control services.
Other activities of services	Activities or services of a Network Operator, where the revenues earned by a Network Operator do not fall under a revenue determination under the EII framework or the NER.
EII Regulated Activities information	Electricity information, acquired or generated by a Network Operator in connection with its provision of EII Regulated Activities, that is not publicly available and includes electricity information; <ul style="list-style-type: none"> - That the Network Operator derives from that information, or - Provided to the Network Operator by or in relation to a customer or prospective customer of EII Regulated Services.
Electricity information	Information about electricity networks, electricity customers or electricity services, other than: <ul style="list-style-type: none"> - Aggregated financial information, or - Other service performance information That does not relate to an identifiable customer or class of customer.
Staff	Means: <ul style="list-style-type: none"> - Employees of an entity, - Direct or indirect contractors to the entity, and - Individuals (including secondees) otherwise made available to the entity by another entity.
Marketing Staff	Means staff directly involved in sales, sale provision or advertising (whether or not they are involved in other functions) but does not include: <ul style="list-style-type: none"> - Staff only involved in technical, administrative, accounting or service functions, or - An officer of both the Network Operator and a related electricity provider.