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Mr Chris Pattas
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Australian Energy Regulator

sent by email: ringfencingguideline2016@aer.gov.au

Dear Mr Pattas

RING FENCING DRAFT GUIDELINE – SUBMISSION BY POWER AND WATER CORPORATION

Thank you for the opportunity to provide a submission on the Australian Energy Regulator's (AER) draft ring fencing guideline (the guideline).

Power and Water Corporation (Power and Water) agrees with the intent of ring fencing, however considers the approach outlined in the draft guideline in relation to physical and legal separation, to be heavy-handed and delivers inefficient outcomes to customers.

Power and Water is currently structured as a multi-utility, thereby providing synergies within the business and economies of scale to our customers. To fully implement the proposed guideline would be cost prohibitive. With such a small customer base to recover costs from, it is unlikely that the benefits to Territorians would outweigh the costs.

The requirement to seek a waiver presents unnecessary risk to network service providers as the waiver may not be granted. Applying for a waiver prior to the commencement of each regulatory control period is also unnecessarily burdensome. Mechanisms other than physical and legal separation should be considered to remove cross-subsidies between regulated and contestable services.

In addition, as Power and Water makes the transition to the National Electricity Rules (NER) adoption, there are a number of practical limitations which pragmatically will require bespoke arrangements for Power and Water, including the application of this guideline.

For instance, as you would be aware, the National Electricity (Northern Territory) (National Uniform Legislation) (Modification) Regulations amend certain aspects of the NER, including chapter 6 so that it only applies in this jurisdiction for the

purpose of allowing both Power and Water and the AER to prepare for the transition to the NER by 1 July 2019.

As such, two of the key pre-requisites for the operation of the draft guideline will not be in place in time for Power and Water to comply by 1 December 2016, including:

- an approved cost allocation methodology (CAM) which is unlikely to be approved until January 2017, although the exact timing is a matter for the AER; and
- an approved services classification, noting that Power and Water's current services are classified under the local definitions, not the NER definitions and while there is some overlap in service classification, it would be inappropriate to apply the national ring fencing obligations to the current local service definitions.

As such, the earliest Power and Water could reasonably be expected to comply with the guidelines would be 1 July 2019.

Furthermore, the Northern Territory Government has yet to finalise whether metering contestability will be adopted in this jurisdiction. Consequently, it is questioned whether the drivers are equally applicable in the Northern Territory for these reforms, as they are in other jurisdictions. It may be reasonable to align the introduction date for the guideline with the Northern Territory adoption date of Chapter 7.

Power and Water has sought approval from the Northern Territory Government to defer the adoption of the Ring Fencing Guideline under the Northern Territory implementation legislation. This will provide Power and Water with the time to adapt to the regulatory regime of the NER and align the implementation of the guideline with Chapter 7 in the Northern Territory.

Power and Water has also attached to this letter a number of issues which it would suggest require clarification by the AER in its deliberations on the final guideline.

If you would like to discuss this matter further please don't hesitate to contact Jodi Triggs – A/Senior Executive Manager Compliance, Economics and Market Services on (08) 8985 8456 or by email: jodi.triggs@powerwater.com.au.

Yours sincerely



Michael Thomson
Chief Executive

28 September 2016

ISSUES FOR CLARIFICATION AS THEY RELATE TO THE DRAFT RING FENCING GUIDELINE

1. Possible inconsistencies and therefore unintended consequences in the definition of a distribution network service provider (DNSP) and the legal separation requirements of the draft guidelines

Given that the definition of a DNSP under the NER is *A person who engages in the activity of owning, controlling, or operating a distribution system*, it could be argued under a strict interpretation that both Power and Water and its sole shareholder, the Northern Territory Government, are both owners and controllers of the regulated network.

Therefore under clause 3.1 of the draft guideline which requires legal separation of a related body corporate as a ring-fencing measure, the Government may not retain control of Power Networks or comply with the requirement to only provide network services, regardless of the extent to which it uses other entities to provide non-network services, given its ownership of Territory Generation and Jacana Energy.

It is assumed that this is not the intention of the draft guidelines, but rather an unintended consequence that will could be clarified during the finalisation of the guideline.

2. Application of non-discrimination provisions to pricing for other government owned corporations

Further to the interpretation above that other government owned corporations are a related body corporate captured under the requirement for legal separation, clause 4.1(b)(ii) of the draft guideline could therefore preclude Power and Water developing specific distribution services tariffs for other government owned corporations.

Clarification is therefore sought as to whether the draft guideline intends to drive pricing policy outcomes or whether this is an unintended consequence arising out of the definition of DNSP under the NER, as outlined above.

3. Application of the waiver process

Where the AER departs from its proposed classification of a service in the Framework and Approach Paper at the time of its final revenue determination the DNSP would not have sufficient time to make the necessary organisational changes necessary to comply with the draft guideline and needs to be given the opportunity to seek a waiver. Further, if that waiver is rejected the DNSP would require an appropriate transitional period to implement the relevant ring fencing obligations.

Further clarification of the practical application of the waiver process in this regard would be of assistance through the final guideline.

4. Definitions in the draft guideline that require clarification

The draft guideline states that words presented in bold have the meaning in the NER but a number of terms are not currently defined in the NER, most importantly "non-network services" and "energy related services".

a. Non-network services

Defining the term “non-network services” in the final guidelines will confirm whether or not the term is intended to capture any service which is not captured by the definition of network services.

There is further potential confusion of this term through the draft guidelines explanatory statement, which on page 47 states that the draft Guideline “excludes from ring-fencing obligations a range of non-network services”, but it is not immediately clear where the draft guidelines provide such exclusions as the range of non-network services is not defined.

b. Non-regulated distribution services

The draft guideline recognises two types of unregulated services – unregulated distribution services and unregulated non-distribution services. Clarification is therefore sought as to how the AER will define an unregulated distribution service as opposed to an unregulated non-distribution service.

Furthermore, the National Electricity Law defines an “electricity network service” as “a service provided by means of, or in connection with, a transmission system or distribution system” and so clarification is sought as to how the AER will interpret the term “in connection with” as expressed in the definition of distribution services.

c. Energy related services

The term “energy-related service” used in the draft guideline is not defined in either the glossary to the NER or the draft guideline.

The draft guideline assumes that all energy-related services are contestable, which in practical terms is not the case for all of Power and Water’s non-network electricity services, such as the provision of supply to remote communities, which it provides under contract to the Northern Territory Government.

d. Services and shared services

There is some ambiguity throughout the draft guidelines as to what constitutes a “service” and in particular, when does expenditure on an activity become classified as a “service” for the purpose of being considered to be a non-network service? Does it require a customer to enter into a contractual relationship involving the exchange of valuable consideration with a DNSP, for an activity undertaken by the DNSP, to constitute a “service” for the purpose of ring-fencing?

For example, clause 4.2.2(6)(ii) of the draft guideline provides an exception to clause 4.2.2(a) in that it appears to allow a DNSP to provide corporate services to a related body corporate that provides contestable energy-related services.

However, clause 3.1(a) prohibits a DNSP from providing any services other than network services. Such services could include corporate services provided to related entities that may provide energy-related and non-energy related services. This apparent contradiction would benefit from further clarification in the final guidelines.

Furthermore, does clause 3.1(a) mean that a DNSP which is a separate legal entity within a group of related entities, is required to procure corporate services from another group entity, as it would be unable to act as a provider to corporate services to related entities?

e. Connection services

Some types of DNSPs services, for example connection services partly funded by the connecting party may not comply with the definition of network services but would be considered distribution services.

While Power and Water's classification of connection services will be considered by the AER through the upcoming Framework and Approach paper, the final guideline would benefit by clarifying the treatment of all connection services including capital contributions.

5. Use of the cost allocation methodology for non-distribution services

Clause 3.2.2 of the draft Guideline states that:

A DNSP must allocate or attribute costs to distribution services in a manner that is consistent with the cost allocation principles and its approved CAM, as if those cost allocation principles and CAM otherwise applied to the allocation and attribution of costs between distribution services and non-distribution services.

Firstly, since the draft guidelines preclude a DNSP providing non-distribution services, the intent of this clause is unclear and on face value, is redundant.

However more importantly, it is unclear whether the NER provides scope to the AER to use the CAM for the allocation of shared costs allocation outside of the DNSP, to the DNSP.

6. Scope of non-discrimination provisions between a DNSP and related body regarding the provision of distribution services

The scope of non-discrimination requirements under clause 4.1 of the draft guidelines covers how a DNSP must deal with related bodies in relation to both distribution services and non-distribution services whereas the NER, clause 6.17.2 relates to ring-fencing of direct control services from the provision of other services.

Clarification is therefore sought as to how the NER provides scope to the AER to use the ring-fencing clauses to impose obligations on how a DNSP must interact with any related body in regard to the provision of direct control services.

7. Treatment of negotiated services and unregulated distribution services

Clarification is sought as to whether negotiated services and unregulated services are captured by the obligation to operate independent and separate offices between provision of direct control services and energy related services.

Is it not clear why these service types are exempt from the staff sharing restriction under clause 4.2.2 of the draft guideline and from legal separation, but not the locational aspect of functional separation.

8. Treatment of contractors

The final guideline would benefit from clarifying the treatment of contractors and consultants with respect to obligations for functional separation and staff sharing under clause 4.2.2 of the draft guideline.

9. Inconsistency with current Rules on metering data

Clause 4.3.2 of the draft guideline appears inconsistent with clause 7.7(a) of the NER and limits access to certain information to certain parties including the DNSP and the customer's retailer, but not other retailers. This apparent inconsistency should be clarified as part of the final guidelines.

10. Disclosure of Information

Clause 4.3.3 of the draft Guideline requires a DNSP to obtain explicit informed consent of relevant customers or prospective customers to whom the information relates, before disclosing information acquired in providing direct control services or disclosing information derived from that information. The AER needs to provide guidance on how in practical terms, this is to be implemented where the information may relate to a body or cohort of many customers (such as the customer base as a whole) or where individual customers are not identified.