SP AusNet Submission
AER re Approach to compliance
Final consultation

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SP AusNet
A member of Singapore Power Group

About SP AusNet

SP AusNet is a major energy network business that owns and operates key regulated electricity transmission and electricity and gas distribution assets located in Victoria, Australia. These assets include:

- A 6,574 kilometre electricity transmission network indirectly servicing all electricity consumers across Victoria;
- An electricity distribution network delivering electricity to approximately 575,000 customer connection points in an area of more than 80,000 square kilometres of eastern Victoria; and
- A gas distribution network delivering gas to approximately 504,000 customer supply points in an area of more than 60,000 square kilometres in central and western Victoria.

SP AusNet's purpose is to provide our customers with superior network and energy solutions. The SP AusNet corporate values are :

- Safety: is our way of life. Protect and respect our people and our community.
- Passion: to bring energy and excitement to what we do. Be innovative by continually applying creative solutions to problems.
- Teamwork: to support, respect and trust each other. Continually learn and share ideas and knowledge.
- Integrity: to act with honesty and to practise the highest ethical standards.
- Excellence: to take pride and ownership in what we do. Deliver results and continually strive for the highest quality.

For more information visit: www.sp-ausnet.com.au

Contact

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SP AusNet is pleased that the AER has accepted a number of the changes to the compliance framework as suggested by the industry, including by SP AusNet.

However as detailed below we still have some concerns with respect to some elements of the AER approach as defined in the two documents as drafted.

Statement of approach

1. Co-regulatory framework and compliance

The AER in the Notice of draft instrument (the Notice) has given consideration to the concerns raised by industry with respect to the significant level of uncertainty regarding the specific detail of the NECF implementation in each Jurisdiction given the potentially major impact that could be made by the Jurisdictionally specific transitional arrangements.

The AER's statement in the Notice is a very optimistic one which:

- relies on major industry commitments to implementation of the NECF, and
- assumes that the transitional arrangements will be in place in a timely manner and that these will provide a seamless regime with the NECF

However, neither the joint Jurisdiction implementation group (JIG) nor the Victorian government have provided:

- a clear scope as transitional arrangements are still unclear; nor
- a clear program for having these in place; nor
- a clear industry cost recovery mechanism.

Without these in place business' full commitment is an issue.

Further some aspects of the NECF require development of market and industry processes, drafting of procedures and change consultation, followed by industry and potentially AEMO builds and testing. Even if the NECF instruments provided a clear framework for this work, achieving a July 2012 effective data would be a challenge. With lack of certainty caused by potential Jurisdictional transitional impacts, and also by a number of the aspects of the NECF as drafted being short of sufficient detail to support industry process development without further SCO interpretation, the ability to meet the full NECF requirements by mid 2012 is unlikely.

Hence whilst it is understandable that the AER in the Notice has taken an optimistic view of the outcomes which is aligned with the MCE stated intent, for example declaring that "processes for implementation in each jurisdiction …..will allow regulated entities to refine their systems in time for commencement", we consider that based on the above statement of the current position, this is unlikely.

Unless further SCO/JIG program considerations and/or transitional arrangements change the situation, then it is likely that despite industry efforts a significant level of non compliance with the NECF will potentially exist from July 2012.

Whilst we are hopeful that the JIG and the Victorian government will recognise these issues and adjust the scope and/or timing, it is of concern if the AER continue to insist that 100% compliance to the full NECF is achievable in this situation.

2. Market intelligence and information (Section 4.2.1)

SP AusNet are pleased that the AER has recognised that market information can lead to spurious identification of issues if industry parties involved are not consulted regarding the specifics of the breach before the matter is escalated to a review or audit.

We are concerned however that the AER has committed to only "endeavour to engage" the relevant industry party in this situation. It is difficult to conceive of circumstances where a check with the "accused industry party" is not possible and appropriate, and we would like the Statement of Approach to have a firm AER commitment, or at least define the circumstance where such a check is not appropriate.

3. Targeted compliance reviews (Section 4.2.3)

SP AusNet support the concept of utilising a more informal review process, rather than moving immediately to an audit to deal with compliance concerns. However this concept strongly suggests that in the circumstance where a party has no breaches, or the AER has no compliance issues with the party, a review would not be held. We are concerned regarding the statement in the Notice that "each regulated party can expect to be subject to at least one review each year".

It is our view that AER requests for reviews of an entity (or entities) should be on a case-by-case basis, and the concept of frequency is not a driver. A review would be requested by the AER if there was an issue or suspected issue. If there was no suggestion that an entity was not compliant, then no reviews would be held; if there were a number of compliance concerns then there would be more reviews. We consider that this provides to best incentive for industry bodies to strive for full compliance and hence avoid the impact of a review.

Further even informal reviews can be resource intensive and hence the expectation would be that the AER would limit their use. For example we would not expect a compliance issue with an individual entity to "automatically" become a review of every entity in the wider group of similar entities.

We consider that these concepts should be specifically captured in the AER's compliance framework.

Further our submission on the first draft of the Approach made the following statement:

> As stated by the AER in the Draft Decision, reviews "provide a combination of evaluative and educative benefits to the market". This benefit may be realised in a review outcome which identifies that an aspect(s) of the NECF is uncertain, ineffective, and/or inefficient, or may identify that some other element of the regulatory regime is misaligned; for example the NECF and a Jurisdictional regulatory regime. Although we accept the statements in the Draft Decision (Section 7.1 p32) that compliance must be enforced against the NECF as drafted, we would like the Statement of Approach to clearly recognise that where NECF issues are revealed by a review (or by an audit), the AER will commit to follow through to recommend to the AEMC potential NECF changes to overcome the issue.

We still consider that this commitment by the AER would contribute to the perception of this framework being a co-operative one with benefits for all parties.

4. Non compliance Reporting (Section 4.2.4)

SP AusNet are still concerned that the AER has not recognised the misalignment between insisting on reporting of single or very low numbers of non compliances for mass market tasks, and the cost/risk basis of price determinations used as the basis of funding for these type of tasks. The measure of individual customer impact as stated in the Notice does not lead to outcomes which are consistent with the service provision and cost model which is

used by the AER in determining within a distributor's price determination what is a fair and reasonable approach to that service provision. The impact on a individual customer of a re-energisation not being done can be sever, however the distributor is not funded to achieve 100% compliance in this mass market task, for example by having double or triple checks within such processes, but rather to achieve a balance between costs and service. The reporting requirements should reflect this approach and thresholds established for reporting of mass market tasks.

5. Inquiries and investigations (Section 5)

The AER has provided some valuable insights in the Notice with respect to how they intend to involve the party(s) being investigated in the report finalisation. However it is unclear why these desirable features and commitments have not been articulated in the Statement of Approach.

Compliance Procedure and Guideline issues

1. Processes for revisions (Section 1.4)

In SP AusNet's submission on the first draft we stated that the *retail consultation procedure* should be applicable to proposed AER changes to the whole AER Compliance Procedures and Guidelines including the content of Appendices B1, B2, B3 which identify those requirements of the NECF with reporting requirements. This was because the AER's choice of these can have a significant affect on the reporting effort required and hence industry input is required to ensure that the regulatory risk and reporting costs have an appropriate balance.

AER did not comment on this aspect and we still consider that the choice of reporting items should be subject to consultation.

2. Concept of "possible breaches" (Section 3.1.6)

Despite the AER's recognition of the issues with the concept of "possible breaches" and the change of the definition to be "…any possible breach that the regulated entity believes is highly likely to occur", and in the Notice "a highly likely future breach", SP AusNet still have concerns. This concept must be very clear as a Participant failing to report a possible breach would we understand be subject to the punitive enforcement mechanisms under the NECF.

SP AusNet consider that in the interests of certainty the concept should be removed, but if AER still considers it of value, then some scenarios should be provided in the Statement of Approach which clearly identify how the AER expect the concept to apply in typical situations.

Further whatever the situation expected to be covered by the concept, it would appear that the concept of a likely future breach makes no sense with respect to Type 2 and Type 3 breaches and should be removed. There should presumably be no circumstances where, at the time of the submission of the Type 2 or Type 3 report two months after the reporting period (eg Type 2 submitted in February for the 6 months to 31 December), a "highly likely breach" should not already have occurred. We note also that the Type 2/3 Pro-forma in Appendix A.2 does not refer to possible breaches.

3. Compliance audits – scope (Section 4.3)

SP AusNet are pleased that the AER has recognised in the Compliance Procedure and Guidelines the need for a specific consultation period regarding an audit scope. However the AER has also provided some additional detail in the Notice with respect to how they intend to manage this consultation process. It is unclear why these desirable features and commitments have not been articulated in the Statement of Approach.

4. Compliance audits – cost (Section 4.4)

SP AusNet stated in our initial submission that the costs of compliance audits should be seen as an expected expense of fulfilling the roles expected of regulated entities, and hence the cost, whether for external or internally sourced auditors, should be recognised as a legitimate expense in the entity's price determination. It could also be added that this imposes a discipline on the AER to ensure that audits are only instigated where a risk concern is real and has real customer impacts.

The Notice recognised this to an extent with the AER stating that "costs associated with meeting regulatory obligations …are appropriately considered by the AER under those [decision] frameworks in accordance with the relevant determination process".

However, SP AusNet consider that the AER position should be included in the Statement of Approach and that the AER should be prepared to commit to the concept that the reasonable costs of audits would be recognised as a legitimate cost of compliance in price determinations. The AER current words appear to be specifically drafted to avoid this desirable commitment, without any explanation of why this is not being given.

5. Compliance Audits Reports (Section 4.6)

Whilst SP AusNet are pleased that the AER has recognised the advantages of the relevant regulated entity being provided with a copy of the final audit report for review before it is made publically available, it is unclear why that this has not been drafted as a firm commitment by the AER rather than being qualified with "will endeavour to provide" a copy. Similarly in the Notice the AER does not commit to provide a copy but rather uses the phrase "may provide" a copy.

Again the AER current words appear to be specifically drafted to avoid this desirable commitment, without any explanation of why this is not being given.

6. Reportable obligations – Details of obligations (Appendix B)

The AER has not interpreted SP AusNet's and the industry's request for a level of AER co-operative guidance in the way it was intended. We recognise the matters raised by the AER in the Notice. We recognise that our compliance approach must cover all obligations, and we are not requesting the AER to provide an interpretation of all these obligations[1]

Rather the AER has selected their major items of concern for specific reporting and hence greater clarity with respect to the AER's view of these obligations and the compliance requirements would provide for a more effective and efficient regulatory regime. The primary aim of the regime is surely to ensure compliance with the intent of the NECF, NOT specifically to punish those that are non compliant, particularly where their primary error is in a misalignment with the AER's view of the intent of the obligation.

[1] Although in the interests of the co-operative approach espoused by the AER, a willingness to put forward a view of what would constitute compliance with specific obligations in response to individual or joint industry request might be helpful.