

31/01/2020

Ms Sarah Proudfoot
General Manager, Consumers and Markets
Australian Energy Regulator

Lodged by email: Ringfencing@aer.gov.au

Dear Ms Proudfoot

Discussion paper – Electricity Transmission Ring-fencing—a review of current arrangements

TransGrid welcomes the opportunity to provide comments on the discussion paper released by the Australian Energy Regulator (**AER**) in November 2019 on its review of existing transmission ring-fencing arrangements. We support the AER's review of the current transmission ring-fencing arrangements given the significant changes in the provision of transmission services since the current guidelines were put in place in 2002.

This submission is structured in two parts. The first part provides our views on the objectives of ring-fencing arrangements. The second part provides our views on four specific ring-fencing issues identified in the AER's discussion paper.

Part 1 – TransGrid's views on ring-fencing objectives

Consumers are at the centre of our business and the energy system. Consistent with our commitment under the Energy Charter to deliver energy in line with community expectations¹, we support ring-fencing arrangements that ensure:

- the charges electricity consumers pay for prescribed transmission services do not subsidise the provision of negotiated transmission services or the unregulated activities of Transmission Network Service Providers (**TNSPs**)
- TNSPs' and their related businesses do not gain any competitive or commercial advantage in contestable markets due to the TNSP regulated business (e.g. by lessening competition in other markets where consumers buy or sell other goods and services)
- TNSPs are able to innovate and provide prescribed transmission services to electricity consumers in the most efficient way possible, including through the use of new and emerging technologies
- TNSPs are open and transparent in demonstrating compliance with ring-fencing requirements.

We consider any changes to the existing ring-fencing guidelines that achieve these legitimate goals would be in the long-term interests of consumers.

In reviewing the ring-fencing arrangements to apply to TNSPs, we also encourage the AER to consider:

¹ The Energy Charter 2019: https://www.theenergycharter.com.au/wp-content/uploads/2019/04/TheCharter_20190328.pdf

- the costs of compliance with the ring-fencing arrangements having regard to the potential consumer harm that may flow if the ring-fencing arrangements are not in place, and
- the differences between transmission and distribution businesses including the nature and scope of the services they provide and the customers they directly serve.

Part 2 – TransGrid views on specific ring-fencing issues identified in AER discussion paper

The AER's discussion paper identified key ring-fencing issues that it considers require consideration as part of the review of the transmission ring-fencing arrangements. Set out below are our high-level perspectives on four of those issues, which require careful consideration as part of the AER's review:

1. New and emerging services
2. Electricity generation and retail services
3. Non-electricity services
4. Negotiated transmission services.

1. New and emerging services

We support the AER assessment that new and emerging technologies have the potential to provide significant benefits to consumers through enabling TNSPs to increase their efficiency in providing prescribed transmission services.

New and emerging technologies such as storage technology offer new ways to maintain system security and reliability. The ability for storage technology to provide a number of services allows TNSPs to maintain system reliability and security more efficiently and at lower cost to consumers than alternative technologies that only provide network services (such as synchronous condensers). This is because storage technology can provide multiple value streams including network services, generation and retail services, allowing the costs of the technologies to be efficiently shared between TNSPs and wholesale market participants. As synchronous generators retire or reduce output there will be an increased need for power system security services such as inertia and system strength services. Because of these changes in the market, new and emerging technologies such as energy storage will play an integral role in maintaining the security and stability of the National Electricity Market in the future.

If customers are to fully realise the benefits from the use of emerging technologies then it is critical that TNSPs have flexibility to access these technologies to provide prescribed transmission services. This could be either through investing in the relevant assets themselves or purchasing network services from third parties who invest in those assets, whichever is most efficient and results in lower costs to consumers.

2. Electricity generation and retail services

The AER has expressed concern that TNSPs may be in a position to provide discriminatory advantage to affiliated generators trading on the wholesale market through the physical access to the market. The AER's discussion paper refers specifically to our securityholders in this context.

We take our legal obligations seriously and recognise the importance of dealing with affiliates and competitors on an arms-length basis to deliver the best outcomes for consumers. We also maintain strict communications protocols with all our securityholders, including but not limited to restricting access to board papers where there may be a perception of a conflict of interest. All enquiries or communications to or from any securityholder are made through a secure online portal administered and maintained by the Company Secretariat team. Our securityholders also have confidentiality obligations in relation to TransGrid information under the contractual arrangements between them. All directors are required to comply with their duties under the Corporations Act and at common law. Our directors and staff must also comply with internal codes of conduct and governance policies, which regulate what information is made available and to whom and how potential conflicts of interest are managed.

In considering functional separation requirements under transmission ring-fencing arrangements that relate to information sharing, we expect the AER will appropriately recognise the requirement for TNSP's to share information with their Boards where that information is provided to enable informed decision-making.

3. Non-electricity services

We agree with the AER that there is limited scope for TNSPs to provide discriminatory advantages in competing to provide non-electricity services. Cross-subsidisation concerns are addressed through rigorous cost allocation practices in accordance with TransGrid's approved cost allocation methodology and compliance with the shared asset guidelines.

We offer a range of non-electricity services. These services include leasing of passive real estate assets not involved in the provision of prescribed transmission services. These assets are leased to third parties on commercial market terms, and telecommunication services. These services make up a comparatively small section of the business on a revenue basis, are market based, and there is strong competition in the relevant markets in which we compete.

The provision of non-electricity services by TNSPs should be encouraged given they provide benefits to electricity customers. Consumers benefit where TNSPs use assets that are predominately required to provide prescribed services to also provide non-electricity services, such as TransGrid's telecommunications services, by reducing prescribed transmission prices in accordance with the shared asset guidelines. In addition, TNSP's provision of non-electricity services increases the level of competition in the markets in which they operate. This increases choice and competition (including from very large competitor service providers) for consumers of those services.

If TNSPs are required to fully functionally separate their non-electricity businesses from their regulated business then there is a high likelihood that:

- customer outcomes will be compromised; and
- competition in non-electricity markets will be reduced.

In some cases, TNSPs will cease to provide some or all of those services because:

- the services cannot be provided by a *fully* functionally separated business such as in cases where the services rely on the use of shared assets that are required to provide prescribed transmission services, or
- the services are relatively infrequent, bespoke, and are unlikely to generate enough revenue to justify the costs associated with a separate business being established on a completely standalone basis.

4. Negotiated transmission services

We agree with the AER that as negotiated transmission services are provided exclusively by the licenced TNSP under the Rules (unlike some negotiated distribution services that are not provided on an exclusive basis), the provision of negotiated transmission services by TNSPs does not create the same risks to consumers as the provision of non-regulated services. This is because there is no competitive market for negotiated transmission services that could be harmed by TNSP's providing these services. Any cross-subsidisation concerns are addressed through cost allocation practices in accordance with our approved cost allocation methodology.

If the AER requires the functional separation of TNSP's prescribed and negotiated transmission services' businesses:

- this may require changes to the transmission connections and planning rules under which the TNSP licensed entity is required to provide negotiated transmission services, and
- this would add significant cost to the provision of negotiated transmission services without providing any compensating benefits to consumers. Any additional costs would be borne by TNSPs' connection customers, and ultimately consumers.

We look forward to working with the AER on this review and how proposed changes to the Guidelines should be implemented. We would welcome further engagement with the AER prior to publication of the draft Guideline in May 2020. If you would like to discuss this submission, please contact Catriona Webster, Head of Public Policy on 02 9284 3147 or Zainab Dirani, Senior Analyst, on 02 9284 3534.

Yours faithfully

Stephanie McDougall

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