Transmission Ring-fencing Guideline

Response to AER Draft Guideline

December 2022

Energy Networks Australia

Contents

Key messages

- Energy Networks Australia (**ENA**) supports the intent of the ring-fencing arrangements, which is to prevent Transmission Network Service Providers (**TNSP**) from potentially causing harm to the market by using their monopoly position to distort outcomes in contestable markets through cross-subsidy, discrimination and any misuse of confidential information. Given the National Electricity Rules (**NER**) contain substantial protections against these potential harms arising through actions of TNSPs, the Transmission Ring-fencing Guideline (**TRFG**) need not replicate the protections included in the distribution Ring-Fencing Guideline and should be substantially simpler as a result.
- ENA broadly supports the Australian Energy Regulator's (**AER**) draft Transmission Ring-fencing Guideline (**DTRFG**) on the basis that in most cases it has struck the appropriate balance between protecting competitive markets while also ensuring TNSPs can provide transmission services in a way that promotes the long-term interests of consumers.
- ENA endorses the AER's views not to impose functional separation between prescribed transmission services and other services. Importantly, however, these justifications remain equally valid when extended to whether functional separation should exist between negotiated transmission services and contestable connection services. A comprehensive framework already exists in the NER that imposes obligations on the provision of negotiated transmission services to protect customers undertaking contestable connection. Additional ring-fencing measures (such as additional functional separation requirements) have the potential to be materially detrimental to customers. As such, even if it had the power to do so, there is no need for functional separation obligations to be extended by the AER to negotiated transmission services. An independent expert report from Incenta Economic Consulting that accompanies this submission provides detailed advice demonstrating that the current framework adequately addresses potential harms to contestability.
- While the ENA welcomes the AER's clarification that there is no restriction on TNSPs employing batteries to provide prescribed transmission services, the approach to require a waiver to lease battery capacity to third parties needs to provide more certainty and be streamlined. The level of regulatory oversight sought by the AER with respect to leasing battery capacity is not justified and imposes substantial regulatory risk for investors. ENA recommends it be replaced with a 'report and comply' approach based on specific obligations in the guideline that deliver the same intent whilst allowing TNSPs to minimise investment risk by eliminating regulatory uncertainty associated with the waiver process. If the AER decides to retain a waiver approach, at a minimum, we encourage the AER to include criteria in the guideline as to what the AER would require in order to provide a waiver.
- The proposed waiver framework lacks procedural safeguards that are necessary to minimise regulatory risk. Specifically, the AER needs to include obligations to publish a decision with reasons, and for that decision to be made within a prescribed timeframe. ENA also considers it is unnecessary to limit the matters that a waiver can apply to. This only reduces flexibility in the regime without a corresponding benefit.
- ENA supports the intent behind non-discrimination provisions. However, the current drafting is complex, does not appear to meet the intent, and appears in one respect to prevent competition. One of the provisions also appears to extend beyond the AER's stated powers. ENA recommends the AER provide a discussion of the intention behind the drafting of all of the clauses in this section, including a detailed description of the types of actions that would or

would not constitute discrimination, and refine the drafting to deliver on its intent and avoid any unintended consequences.

- The drafting of the obligation to functionally separate marketing staff has the consequence that the marketing staff who provide contestable connection services would need to be staff of a separate legal entity and functionally separate from the TNSP. This outcome appears to be unintentional given the AER's stated intent to retain the existing approach which relates only to non-transmission activities.
- ENA considers that there is no justification for legal separation to be extended to non-electricity services and distribution services, with the likelihood that the costs of legal separation are expected to outweigh the benefits. In each case cost allocation provisions are sufficient to protect against cross-subsidy.
- ENA requests that the AER clarify its intent with respect to breach and compliance reporting during the transitional period, given that most of the guideline will not apply during this time, in order to provide an orderly transition to the new arrangements.

Introduction

Energy Networks Australia (**ENA**) is pleased to make this submission to the Australian Energy Regulator (**AER**) on behalf of its transmission members in response to the Draft Transmission Ring-Fencing Guideline (**DTRFG**). ENA is the national industry body representing Australia's electricity transmission and distribution and gas distribution networks. Our members provide more than 16 million electricity and gas connections to almost every home and business across Australia.

As articulated in previous submissions to this process, ENA supports the intent behind the ring-fencing arrangements. ENA advocates for outcomes that promote the National Electricity Objective (**NEO**) and therefore appreciates the need to prevent the potential harms of cross-subsidy, discrimination, and any misuse of confidential information that permits TNSPs to misuse their monopoly position in contestable markets.

In transmission, the National Electricity Rules (**Rules, NER**) do significantly more to protect contestable outcomes than is the case in distribution. This is particularly the case given the extensive protections that the Australian Energy Market Commission (**AEMC**) introduced for contestable transmission connection services. This comprehensive Rules framework, supported by the ring-fencing guideline, gives appropriate recognition to the fundamentally different nature of markets associated with transmission compared to distribution. The main consequence for the AER's current review is that the ring-fencing guideline has substantially fewer issues to manage in transmission as compared to distribution.

ENA welcomes the constructive engagement with the AER to date and looks forward to continued engagement to ensure that the final guideline is clear and practical to implement. ENA is considering the implications of the drafting and would also welcome the opportunity to engage on this further as the DTRGF is settled to ensure it delivers on its stated intent and avoids any unintended consequences.

ENA broadly supports the AER's draft guideline

In most cases the AER has struck an appropriate balance between protecting competitive markets while also ensuring that TNSPs are able to provide transmission services in a way that promotes the long-term interests of both small and large consumers. In key areas, the AER has acknowledged that material differences exist between transmission and distribution, which would mean that excessive costs may be

imposed by onerous ring-fencing measures compared to the limited benefits that might accrue from those measures.

ENA supports the following aspects of the AER's approach in the DTRFG:

- TNSPs are permitted to continue to provide all transmission services within the same legal entity.
- No additional functional separation between the TNSP's regulated activities and contestable connection activities. Nevertheless, we note that the AER expressed some support for additional functional separation but found itself legally constrained from doing so. The need for any functional separation for contestable connection services is not well-founded given the nature of the market and the extensive provisions governing connections in the rules. We expand upon this below.
- That the strengthening of obligations relating to the prevention of cross-subsidy and discrimination can provide additional confidence to market participants that TNSPs are not harming competitive outcomes. We observe that the proposed arrangements for accounting separation are consistent with how TNSPs currently operate.
- Ensuring robust arrangements to protect confidential information. The proposed arrangements, combined with the comprehensive provisions in the Rules, mean that no additional functional separation obligations are needed.
- That agreements with 3rd party service providers mirror those imposed on TNSPs.
- The requirement for reasonable reporting requirements to provide confidence to market participants that TNSPs are complying with the arrangements. Nevertheless, the AER needs to be mindful that the burden of compliance obligations does not outweigh the benefits. This means making sure that the detail expected in reporting is commensurate with the nature of customers and services offered in transmission.
- That an appropriate timeframe has been provided for the transition to the new arrangements.

While ENA supports the broad approach taken by the AER, there are aspects of the draft guideline where changes are required in order for the framework to promote the NEO. The remainder of this submission focuses on those areas where ENA considers the DTRFG needs to be improved to deliver on its intent.

The combination of rules and guideline obligations will protect outcomes for contestable connection services

ENA endorses the observations the AER made when considering whether to impose functional separation between prescribed transmission services and other services. These observations included the following:[1]

[1] AER, 'Electricity transmission Ring-fencing Guideline, Explanatory Statement – Version 4, Draft, November 2022, p. 34.

- Physically separating offices and staff is likely to be more costly for TNSPs than DNSPs. This is because TNSPs have smaller and more highly specialised teams. The implication being that the cost of duplicating these positions for TNSPs is high.
- Increased functional separation arrangements may be excessive for some TNSPs that operate on a smaller scale, and it is preferrable that the approach to functional separation be appropriate for the majority of TNSPs.
- The potential harms that might emerge can be addressed through both the general obligation not to discriminate and the information access and disclosure requirements already in the NER.

While, necessarily, the AER has framed its discussion with respect to prescribed transmission services, these justifications remain equally valid when extended to the question of whether further separation arrangements should exist between negotiated transmission services and contestable transmission connection services. As we have commented previously, there is a comprehensive framework in the Rules that imposes specific obligations that are targeted to negotiated transmission services and protecting contestable connection outcomes. Therefore, there is no need for the AER to impose any additional obligations even if it could extend ring-fencing obligations to negotiated transmission services, which would only risk reducing competition.

Imposing additional ring-fencing measures to contestable connections on top of those that already exist in the Rules, especially requiring functional separation, would be inconsistent with the intended design of the framework. The AEMC has recently undertaken two comprehensive Rule change investigations into the framework for transmission connections. Each time it made a deliberate decision that the NEO is promoted by providing the flexibility for the TNSPs to provide both regulated and contestable connection services – without functional separation – if this is what the connection proponent wants, but also provides these large and sophisticated connection proponents with the option of initiating a competitive process for the contestable elements if this is what they want. Moreover, a robust process is included to protect the competitive process if this decision is made.

Imposing additional functional separation on top of the comprehensive framework that already exists would be in conflict with the AEMC's views of the framework that best promotes the NEO, and creates the very real potential that outcomes for customers would worsen. There is the potential that the expected volume of work for a TNSP from contestable connection projects may not be sufficient to make it commercial to sustain a separate team for the contestable aspects of connection projects, and they would be forced to withdraw from providing these services. This reduces, rather than promotes, competition at a time when timely and efficient generator connection is more important than ever.

ENA is also concerned about the AER's lack of critical analysis of stakeholder claims on this topic. Stakeholder submissions related to connection services lacked evidence and ignored the framework that already exists in the Rules. Relying on these views to justify a change in approach would be misguided. ENA engaged Incenta Economic Consulting (Incenta) to analyse if there are material gaps in the framework that suggest the DTRFG needs to provide additional protections to competition. This analysis was done in the context of claims made by stakeholders to the AER. In summary, Incenta found that the current framework adequately addresses potential harms to contestability and that the claims made by stakeholders about the framework are unsubstantiated. Further, Incenta noted, given the framework that

exists in the Rules, that any gaps that are subsequently identified should be addressed as part of a Rule change process. Specifically, Incenta stated the following:[2]

> *However, in our view, the regulatory framework that the AEMC introduced as part of the rule changes discussed above, combined with the measures already in place,[3] provides a comprehensive framework to address the potential actions that a TNSP could take to reduce competition (referred to below as "harms" to competition). We do not think that there are any material gaps in this framework that may warrant more onerous measures being imposed. Indeed, more onerous measures, such as permanent functional segregation of staff between monopoly and contestable activities, would be more likely to reduce competition and act against the interests of customers.*

The approach to batteries needs to provide certainty and be streamlined

ENA welcomes the AER's clarification that there is no restriction to TNSPs employing battery and other storage technologies to provide prescribed transmission services. ENA also accepts that potential ring-fencing issues arise when a regulated asset has the potential to provide contestable energy market services. However, as set out in earlier submissions, where a battery or another storage technology is required for prescribed transmission services, there are substantial benefits to providing TNSPs with the ability to determine if the least-cost option is to purchase the services from a third party or to own the assets themselves. In turn, in the cases where the energy storage device is to be owned by the TNSP, there then may be substantial benefits to customers from the capacity from that device also being used to provide contestable services, thereby unlocking greater value from the asset and defraying the cost required to be recovered from customers.

It is important, therefore, that the ring-fencing requirements do not create unnecessary barriers to TNSPs owning energy storage devices to provide prescribed transmission services, but rather seek to minimise the cost to customers (including through the use of the energy storage device to provide contestable services). Creating unnecessary barriers to the use of energy storage devices for contestable services has the potential to distort decisions away from the provision of these contestable services, to the ultimate detriment of customers.

The degree of regulatory oversight sought by the AER with respect to leasing capacity from energy storage devices is not proportionate and creates unnecessary regulatory risk for investors. The proposed waiver framework is not justified for the following reasons:

- There is no evidence that the current arrangements are leading to harms to competitive market outcomes for grid scale storage. It is clear that there are no barriers to the contestable provision of energy storage devices and that TNSPs are not crowding-out third party provision or harming

[2] Incenta, 'Competition issues for contestable connection projects' December 2022, p.3.

[3] We note that the regulatory regime already included a highly codified process governing new connections (comprising a connection enquiry, response to the enquiry, preparation for the making of a connection offer, connection offer, and acceptance of the connection offer), that includes detailed specification of requirements on all parties at each step, including the information required to be provided and the timelines.

competition in these markets given there are currently around 160 energy storage projects that are currently anticipated, committed or in-service in the NEM and 97 per cent of these are owned by someone other than a TNSP and approximately 92 per cent of either in service or committed scheduled capacity from batteries is supplied through facilities owned by participants other than TNSPs.

  - Further, TNSPs have demonstrated a capability to implement models that robustly address competition concerns associated with energy storage that provide network services. These models have been implemented without the need for an upfront waiver requirement in the DTRFG. This demonstrates that TNSPs are operating in good faith and that there is no justification for onerous oversight on the actions taken by TNSPs in this regard.

- It does not align with the practical realities of negotiating and investing in an energy storage device that leases some capacity to a third party. Making an investment in a storage facility, and particularly where that might involve the leasing of capacity for use in the contestable energy market, is a highly iterative process involving ongoing negotiation with multiple parties. Commercial terms are often time-sensitive given the pace of change in expected market outcomes. We understand that a waiver process may take months to decide by the AER. The proposed waiver framework, especially with this timeframe, is incompatible with this investment process. Third parties will be reluctant to undergo an extensive negotiation process only for it to be disallowed by the AER at the final hurdle. This will hold back innovation in the provision of network services, making it more difficult for energy storage to be used in the place of traditional network assets to meet a network need.
- It is inconsistent with the intended operation of incentive regulation in the NEM. A robust framework to promote efficient investment by TNSPs already exists in the NEM. This framework includes: financial incentives for capital and operating expenditure as well as service performance, annual planning and reporting obligations, and an economic test in the form of the Regulatory Investment Test for Transmission (**RIT-T**) to demonstrate proposed investments deliver a net benefit. Conversely, the AER's waiver framework effectively gives it the power to block an investment decision that has been found as efficient by the TNSP in consultation with stakeholders and competitive tenderers under this framework. ENA contends that this conflicts with the principles of good regulatory practice, introduces a material new regulatory risk for TNSPs, and so does not promote the NEO.

ENA recommends that a more proportionate and balanced approach that achieves the required objectives for grid scale storage would be for the AER to instead adopt a 'report and comply' framework that contains all of the relevant requirements to be met. This approach will achieve the same outcomes sought by the waiver framework, but in a way that substantially enhances certainty and predictability in the framework for TNSPs and investors alike for both new and amended energy storage agreements, and allows the AER to set out clear expectations up front.

Regulatory certainty

A 'report and comply' framework provides the certainty and predictability needed for efficient investment while also delivering the protections that are sought under the waiver model. ENA recommends that this framework be based on the successful deployment of energy storage facilities that have already occurred in transmission networks in line with the AER's expectations.

However, should the AER decide to retain its 'prohibit and waiver' approach for transmission connected energy storage, at a minimum, it needs to include criteria in the guideline as to what the AER would require in order to provide a waiver. This would provide the necessary clarity about what conditions need to be met in order for the AER to approve the waiver. While it is very much a second best outcome, this type of guidance in a waiver framework significantly reduces the chances of an unanticipated decision being made by the AER. A waiver also needs to be for the life of the asset in order to provide the relevant regulatory certainty at the time investments are being made.

Under a 'prohibit and waiver' approach, unintended consequences for established services should also be avoided. The waiver process could potentially limit the flexibility for TNSPs and third parties to simply update or extend agreements in response to changing circumstances once an agreement has been approved. This is because a new waiver would be required for any variation to the agreement between a TNSP and a third party under the current drafting of the DTRFG. We understand the intent is for only material changes in leasing arrangements to be captured by this provision. We therefore recommend the AER clarify the drafting of this provision in line with this intent to ensure that a new waiver is required only for material changes to agreements.

Transitional arrangements

ENA appreciates the AER's decision to not apply the new waiver process in relation to the TNSP-owned storage facilities that have leases in place for output from the storage device (and which were developed in consultation with the AER). However, as noted above, the guideline would require a waiver in relation to an existing project if there was a variation to any pre-existing agreements in place, no matter how trivial. As above, we understand that the AER intends a waiver only to be required where the agreements are varied in a substantial way and recommend the drafting reflect this intent to avoid unintended consequences for pre-existing agreements.

A more robust framework is needed to support waiver decision making

The AER has adopted for transmission the model for general waivers that applies in distribution. ENA considers, however, that there are some material flaws with the proposed waiver model as it would apply to the transmission framework that need to be rectified. These mostly go to administrative and procedural matters. Specifically:

- There is no obligation for the AER to publish a waiver decision with reasons or timeframes for making a decision.
- The restriction on the matters that the AER can apply a waiver to is unnecessarily limited.
- There is no provision for the AER to create an evergreen waiver despite it indicating this is something it intends to permit for transmission.

Procedural arrangements

Effective procedural arrangements work to reduce the level of inherent regulatory risk in a regime. The proposed framework in the DTRFG lacks the minimum safeguards needed to limit regulatory risk. ENA considers it is essential that the AER amend the guideline to include the necessary procedural safeguards.

The current framework does not oblige the AER to decide on a waiver application, or where it does make a decision, to provide reasons for that decision. Instead, while it must consider an application, it *may* decide to grant or refuse to grant a waiver, and *may* publish reasons for doing so. ENA contends it is essential for the AER to be required to publish a decision with respect to a waiver application and for this to include reasons for that decision as part of good regulatory governance. Publishing a decision with reasons is a minimum requirement for delivering accountability and transparency in a regulatory regime. This would help set clear expectations across TNSPs and, over time, reduce regulatory risk. If timeframes are not codified in the guideline it would permit the AER to hold-up, inadvertently or otherwise, investment and operational decisions of TNSPs.

The Explanatory statement notes that the AER will endeavour to make a decision on an application within 90 days. The reasonable endeavours timeframe for the AER to make a decision should be reflected in the Guideline. ENA suggests that a timeframe similar to the decisions on cost pass throughs could be adopted (i.e. 40 business days) with a stop the clock provision if further information were needed with the expectation that all decisions are made within 90 days.[4]

The power to unilaterally vary or revoke a waiver must also be clearly delineated, transparent and limited. While we recognise that the circumstances that gave rise to a waiver may change, the AER's proposed approach creates significant uncertainty and risk (cost) which could jeopardise projects or, if those projects do proceed, they proceed more slowly and/or at greater cost. Therefore, it is appropriate that the guideline stipulate the limited circumstances in which the AER can vary or revoke a waiver.

We also note the disproportionately short period that the AER considers is appropriate to enable a TNSP to implement the changes to commercial and operational arrangements to comply with the guideline if a waiver is varied or revoked. Such changes, which the proposed guideline does not presently require the AER to consult with the affected TNSP about, could have significant unintended repercussions for a business. This aspect of the Draft Decision should be reconsidered and clarified. The AER should be required to consult with the impacted TNSP and make clear why the AER is considering changing the waiver. Failure to provide sufficient certainty will undermine the stability of the regulatory regime and could see a fall in investment/lack of market development, all of which will have adverse consequences for customers.

As noted above, should the AER seek to vary or revoke the class waivers, the TNSPs impacted should be consulted and the AER should make clear the reasons why they are varying or revoking the class waiver.

Restriction on waivers

ENA considers that there is no benefit from the guideline restricting the provisions that can be subject to a waiver. Doing so only serves to reduce the flexibility for the AER and TNSPs to respond to unforeseen events or changes in a timely manner.

Permitting waiver applications for all aspects of the guideline will not materially increase administrative costs or regulatory uncertainty. This is because the AER retains the capability to quickly dismiss any

[4] Clause 6A.7.3(e) of the NER.

vexatious waiver applications. This capability means that the AER should expect to only ever see an application for a waiver of the currently restricted provisions where there is a genuine need.

One set of obligations for which the AER proposes not to provide the flexibility to grant a waiver are the non-discrimination obligations. However, even for these obligations there may be compelling reasons to provide a waiver (which may be tightly constrained and/or subject to conditions). In our earlier submission, we explained that decisions the TNSPs make about matters like access to essential plant that may have a legitimate basis (including for reasons of national security) could be interpreted as discriminatory.[5] In the absence of protections built into the provisions themselves (as our previous submission advocated) a waiver process could be used to cater for such matters should they arise.

Evergreen waiver option

In the draft Explanatory Statement the AER suggests that there would be an evergreen waiver applied to existing arrangements and it would retain the option to implement an evergreen waiver on a case-by-case basis.[6] Indeed, the DTRFG implies in clause 5.2(d) that TNSPs can request an evergreen waiver, however, the AER is required to limit the term of a waiver to either or both of a TNSP's current or next regulatory control period.[7] This is also inconsistent with the understanding that a waiver in relation to an energy storage agreement would be expected to be for the life of the asset or agreement involved.

We note that one area where an evergreen waiver (or waiver with an extended term) may be necessary is in relation to the "separate legal entity" obligations. It is conceivable that the obligation may require a TNSP to seek to change the counter-party to an existing contract – which must be agreed to by the counter-party – and for various reasons may not be possible (or at least not without incurring a disproportionate cost). The implication being that an evergreen waiver might be required so that the contract can remain with the TNSP.

Non-discrimination provisions are unclear and may lead to unintended consequences

ENA supports the intention of provisions associated with non-discrimination. However, the drafting of the arrangements for transmission, while drawn from the distribution arrangements, are complex provisions that clearly have a number of assumptions and intentions underpinning them. This makes it difficult for TNSPs to gain a concrete practical understanding of the full range of behaviours that would cause a breach of the guideline.

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[5] The Explanatory Statement appeared to accept this concern as an issue, However, the AER's example focused on individual events and so falls well short of what might be required by a TNSP with respect to national security. Given this, additional measures are still required that would protect TNSPs where they undertake legitimate discrimination. See: AER, 'Electricity transmission Ring-fencing Guideline, Explanatory Statement – Version 4, Draft, November 2022, p.30.

[6] AER, 'Electricity transmission Ring-fencing Guideline, Explanatory Statement – Version 4, Draft, November 2022, p.46.

[7] Clause 5.3.4(b) of the DTRFG.

ENA has particular concerns with clause 4.1.(b)(ii). This clause, on its face, appears to extend non-discrimination provisions beyond what is appropriate and beyond what is permitted under the Rules. ENA recommends that this clause be removed, or at a minimum re-drafted, to improve clarity. This clause implies that the TNSP cannot discriminate between its related electricity service provider and any other party in relation to contestable services provided by any party. However, as well as providing prescribed transmission services, the TNSP also provides negotiated transmission services and contestable transmission services. Thus, this clause appears to impose non-discrimination provisions on the provision of negotiated transmission services. However, the AER has stated that it does not have the power to impose ring-fencing obligations on negotiated transmission services given the requirements of clause 6A.21.2(a) of the NER.

More generally, however, as indicated above, ENA observes that the drafting of the non-discrimination provisions is complex. A lack of clarity of the TNSPs' obligations could lead to inadvertent compliance issues, the consequences of which may be significant if civil penalties are attached to non-compliance. Therefore, at a minimum, ENA requests that the AER provide a discussion of the intention behind the drafting of all of the clauses in this section, including a detailed description of the types of actions that would constitute discrimination, and which would not. Moreover, this discussion should be self-contained within the Explanatory Statement for the transmission ring-fencing guideline and so not rely on cross-references to – or an assumed knowledge of – discussions that may have been had in the development of the distribution ring-fencing guideline.

ENA queries the application of a number of provisions:

- Compliance with clause 4.2.3 (a) may in some cases be impractical. For example, how is a TNSP to know if ring-fenced information that a TNSP has disclosed is "then disclosed by *any person*" to a related electricity service provider. If the TNSP and its related electricity service provider are ring-fenced this may not always be apparent to the TNSP.
- The exceptions in clause 4.2.2 appear to be too narrow, particularly when you come to apply 4.2.3. There is no express ability to disclose to lawyers, insurers, auditors or financiers or AEMO. This becomes particularly important with 4.2.3(e) which only permits the other legal entity to disclose information as permitted by 4.2.2(a) to (d). To provide an example, if the other legal entity is seeking to get finance for a project, how do they make any disclosure to their prospective financiers or any independent engineer engaged by the financiers?
- Clause 4.2.4(b) does not seem to contemplate that some of the information on the register may be confidential – i.e. the register is publicly available and there is no ability to claim confidentiality. This may not just be an issue for the TNSP, it may be an issue for the other legal entity. For example if another legal entity is asking for information because it is seeking to develop a currently confidential project, it may not want this fact publicised.
- Clause 4.4.1(a) seems very broad and ENA queries why a service provider has to be subject to the same restrictions as are in clauses 4.1 and 4.3. ENA queries what it means to deem a service provider a TNSP when they are not a TNSP. Is it intended that an Australia-wide engineering company that is helping a TNSP repair a powerline providing prescribed services can't discriminate in favour of its own affiliates who are providing services (even though the engineering company operates in the competitive space). This hypothetical engineering company may have multiple subsidiaries and if staff of one subsidiary help provide prescribed transmission services (e.g. repairing a pole) does this now mean that those staff are restricted from marketing for another subsidiary of the engineering firm that principally provides unregulated network services? S

ENA would be happy to engage further in the detailed drafting of this clause to ensure that the stated intent is delivered and unintended consequences are avoided.

The separation of marketing staff requirements are inconsistent with the AER statements and other parts of the DTRFG

The AER indicates in the draft Explanatory Statement that it has retained the existing approach to functional separation other than to update the language of the drafting.[8] Currently, the provision relating to marketing staff only requires a separation of marketing staff between prescribed transmission services and generation and retail services. However, as the provision has been drafted, a much broader obligation would be created, which we assume to be an unintended consequence. Specifically:

- the obligation as drafted says that the TNSP must ensure that its staff are not also marketing staff of a "related electricity service provider", however
- the TNSP is allowed to perform all transmission activities, including contestable connections (a subset of "related electricity services"), and so
- this clause will require contestable connections (and any other contestable transmission services) to be undertaken via a separate legal entity (i.e., so that marketing staff were not also staff of the TNSP).

This has the consequence of imposing both legal and functional separation between prescribed transmission services and contestable connection activities, both of which appear to be unintended.

This would be a substantial shift from current practice as no TNSPs are currently providing generation or retail services under the current Guideline and therefore are not impacted by the current restriction in the use of marketing staff. However, as all TNSPs provide contestable connection services all would be materially impacted by this expanded clause under the DTRFG.

In addition, the proposed marketing staff clause is stricter than the Distribution Ring-fencing Guideline. This is because the transmission provision refers to who can employ the marketing staff, while the distribution provision instead refers only to the tasks that may be performed by staff of the distributor.

We recommend that the drafting of this provision be amended so that it retains the approach in the existing guideline to functional separation, and so does not extend to contestable transmission connection services. It should also focus only on the tasks performed by staff rather than which entity employs them.

[8] AER, 'Electricity transmission Ring-fencing Guideline, Explanatory Statement – Version 4, Draft, November 2022, pp.33-34.

There is no compelling reason to preclude the TNSP legal entity from providing non-electricity services and distribution services

ENA understands that the obligation for legal separation is not intended to prevent the sharing of resources between the TNSP and related (separate legal) entities. For example, we understand that this will not preclude the TNSP providing a financial guarantee to the related entity, staff employed by the TNSP being deployed to a related entity (provided this is not inconsistent with the functional requirements), and for finance to be raised at a group level (i.e., collectively for the TNSP and other related entities). We would welcome an explicit clarification that this is consistent with the AER's intentions.

Notwithstanding, as has been stated in previous submissions, ENA considers that there is limited basis for legal separation of TNSPs given it imposes additional costs but does not achieve much beyond what can be achieved through cost allocation and the requirement to produce separate accounts. In this context, ENA considers that legal separation has been implemented in two areas where there is almost no benefit. These are with respect to non-electricity services and distribution services. Therefore, ENA recommends that legal separation be removed with respect to these services.

Non-electricity services

Non-electricity services, such as telecommunications or property services, are services that have a purpose other than the delivery of electricity. Therefore, in the first instance, there is no role for the DTRFG with respect to competitive market outcomes for non-electricity services. In the second instance, there is no ability for TNSPs to discriminate in the provision of services in these unrelated markets. Given this, and recognising there is limited additional benefit obtained by legal separation compared to existing cost allocation provisions, the proposed legal separation obligations are overly onerous in this instance. We therefore recommend the requirement for legal separation be removed for non-electricity services.

Distribution services

There is no reason that the transmission arrangements are not aligned with the distribution arrangements when it comes to the provision of distribution services by TNSPs. Distributors are a regulated monopoly in the same way that TNSPs are. Therefore, there is no justification for distributors to be able to provide all transmission services via the DNSP legal entity but for TNSPs to be restricted from providing some distribution services. This has the effect of reducing competition.

The AER cites an absence of regulatory oversight and cost allocation methodology with respect to contestable distribution services as its reason for the differential treatment. However, regulatory oversight does not apply to contestable distribution services because they are not monopoly services, in the same way that contestable transmission services are unregulated because there is no justification for regulation.

To the extent TNSPs provide contestable distribution services, then the obligations in the new transmission ring-fencing guideline will require costs to be properly allocated in accordance with a TNSP's cost allocation methodology. This cost allocation ensures that there is no cross-subsidy between

regulated and unregulated services. Moreover, the cost allocation methodologies do not require legal separation in order to be robust and effective. We therefore recommend the requirement for legal separation be removed for distribution services.

Transitional arrangements and compliance/breach reporting

The AER has included a 12-month transitional period for the majority of the provisions in the DTRFG. However, it requires compliance reporting and breach reporting to commence immediately, together with the obligations relating to energy storage and service agreements. It is not clear, therefore, what compliance and breach reporting that the AER is requesting during the transition period. For instance, it would not seem appropriate to require TNSPs to report breaches for provisions that have yet to take effect within the transition period. Equally, it is not clear there is any value in an initial annual compliance report that covers only the limited matters in effect above. We therefore recommend that the breach reporting and compliance reporting requirements during the transition period be reconsidered.

Alternatively, if the AER's intention is for breach reporting and the first annual compliance report to address compliance with the existing guideline, then ENA would question the merit of devoting substantial resources to this exercise given that much of this exercise would be a one-off (i.e., subsequent compliance reports would address the materially different obligations in the new guideline). Furthermore, as the new guideline represents a substantial rewrite of the existing guideline and appears intended to fully replace the existing guideline once it takes effect in March 2023, there again appears to be no specific need or scope for breach or compliance reporting against a guideline that will be fully superseded. Therefore, ENA requests that the AER clarify its intent in this respect.