



16th November 2016

Mr Chris Pattas  
General Manager, Networks  
Australian Energy Regulator  
GPO Box 520  
Melbourne VIC 3001

By email to: [Ringfencingguideline2016@aer.gov.au](mailto:Ringfencingguideline2016@aer.gov.au)

Dear Mr Pattas

### **RE: AER Exposure Draft Electricity Ring-fencing Guideline**

ERM Power Limited (ERM Power) welcomes the opportunity to respond to the Australian Energy Regulator's (AER) Exposure Draft of the Ring-Fencing Guideline for Electricity Distribution (the Exposure Draft).

#### **About ERM Power Limited**

ERM Power is an Australian energy company operating electricity sales, generation and energy solutions businesses. The Company has grown to become the second largest electricity provider to commercial businesses and industrials in Australia with operations in every state and the Australian Capital Territory. A growing range of energy solutions products and services are being delivered, including lighting and energy efficiency software and data analytics, to the Company's existing and new customer base. ERM Power also sells electricity in several markets in the United States. The Company operates 497 megawatts of low emission, gas-fired peaking power stations in Western Australia and Queensland. [www.ermpower.com.au](http://www.ermpower.com.au)

ERM Power Limited also has subsidiary businesses in metering services, energy efficiency, behind the meter technologies and data analysis – businesses that we consider may compete with networks or their affiliates.

#### **General Comments**

ERM Power is very concerned with the recent changes to the Ring-Fencing Guideline presented in the Exposure Draft. We strongly believe that the Exposure Draft has eroded protections which were put in place to ensure emerging markets develop appropriately, allowing multiple players to have equal access to provide customers with efficient low-cost technology products. Further we are concerned that the Exposure Draft has been published with a 6-day consultation period and where there has been no decision statement provided to guide participants in the reasoning behind the material changes. We are therefore left to speculate on the AER's reasoning.

The following submission focusses on those areas of greatest concern, where we see a substantial threat to the effectiveness of the guideline in protecting and promoting competitive markets, and which is likely to result in detriment to consumers.

### **Issues with the Exposure Draft**

#### **1. Waivers to Legal Separation**

The AER's Draft Decision attempted to suppress the ability of the DNSP to cross-subsidise contestable activities with regulated income through legal separation, separate cost allocation and accounting. Legal separation has been seen as critical for protecting against cross subsidisation. The Draft Guideline gave appropriate weight to this issue by placing a prohibition on legal separation exemption, as "waivers could undermine certainty and therefore confidence in the market for non-network services, and customers' confidence in efficient prices for regulated services"<sup>1</sup>.

We agree that waivers will undermine the market and suspect that DNSPs will exploit this now weakened obligation around legal separation in the Exposure Draft and apply for waivers unreservedly. Of most concern, the Exposure Draft does not limit legal separation waivers to extraordinary circumstances, such as where DNSPs have a conflicting legal obligation, but can be sought for any reason.

#### **Recommendation**

- If exemptions to legal separation are required to overcome incompatible legal requirements or obscure regulatory scenarios, explicitly detail the narrow situations whereby legal separation waivers can be sought.
- Ensure any waiver application is subject to full public consultation to determine any impacts to competitive markets (which will only be revealed through a consultation process).
- interim waivers should not apply to legal separation at all.

#### **2. Interim waiver provisions**

ERM Power strongly believes that an interim waiver facility undermines the due process and diligence of testing the legitimacy of the DNSP's right to an exemption. The drafting suggests that an interim waiver may be applied as a default position, which may be used by the AER if it cannot make a decision to refuse a waiver under 5.3.1. Rather, we believe that the ring-fencing obligations should apply as a default position, and a waiver only be granted in extraordinary circumstances after legitimacy of the reason is validated and thorough testing of the impacts of the exemption has been undertaken.

We are concerned that interim waivers:

- are not subject to any test of the national electricity objective (NEO), cross subsidisation or discrimination, or costs to consumers (including the impacts to competition). This provides the

---

<sup>1</sup> AER DRAFT Ring-fencing Guideline Explanatory Statement August 2016, page 25

DNSP with an unrestrained entry to markets, oblivious to harm, while the AER works to progress decision making (in an unspecified timeframe);

- are likely to be used by DNSPs to justify exemption to the ring-fencing requirements by persuading the AER to focus on short-term analysis and an impact assessment over the interim waiver period. This may prejudice full waiver decisions to ignore the longer term impacts to customers who will be disadvantaged by dampened or distorted competitive markets.
- may be issued without an expiry date. This is very concerning as the waiver may continue in perpetuity with no testing of harm to customers or the market. The drafting suggests that an expiry date is at AER's choosing and is not mandatory; and
- could apply to legal separation before any testing of impact to competition is undertaken.

**Recommendation:**

- Interim waivers are removed. We believe the Exposure Draft has generously provided DNSPs with adequate time from the date of the Final Decision to arrange and provide evidence of the need for an exemption to ring-fencing requirements. If this time is insufficient, we would question whether the waiver process is no longer being applied to extraordinary and exceptional circumstances but rather occurring on a widespread and frequent manner, undermining the ring-fencing guidelines.

3. Lack of consultation around waivers:

We note that the AER 'may' consult around the application of waivers. We remain concerned at the lack of transparency surrounding the waiver process. In our view, consultation becomes even more imperative if waivers start applying to legal separation. We argue that any discrimination implications for potential or current market competitors are more likely to be revealed through a consultation process. In particular, information relating to the potential for cross subsidisation, discrimination and consumer impact, should emanate from a consultation process rather than the AER relying on information provided by the DNSP or its own assumptions.

**Recommendations:**

- Clause 5.4 should be worded as the AER "must" publish reasons for granting or refusing waivers, and terms and conditions of waivers for transparency and confidence in the process; and
- all waivers should be subject to consultation to ensure that the AER is informed to come to an opinion around 5.3.2 (a) iii - the likelihood of impact to competition will only be exposed through a consultation process.

4. Compliance

We recommend that waiver conditions be tested and monitored as part of information submitted in the DNSPs' annual compliance reports. This will inform the AER in deliberations under clause 5.5 and necessity to trigger 5.5(b).



Where DNSPs are active in the competitive space, ERM Power sees ring-fencing as essential to protecting emerging competitive markets and allowing consumers to benefit from effective competition. The AER should not underestimate the harm to competitive markets with the inability of participants to compete against DNSPs that seek to exploit the Guideline's waiver provisions, even those granted on an interim basis.

Please contact me if you would like to discuss this submission further.

Yours sincerely,

[signed]

Libby Hawker  
Manager Regulatory Affairs  
03 9214 9324 - [lhawker@ermpower.com.au](mailto:lhawker@ermpower.com.au)