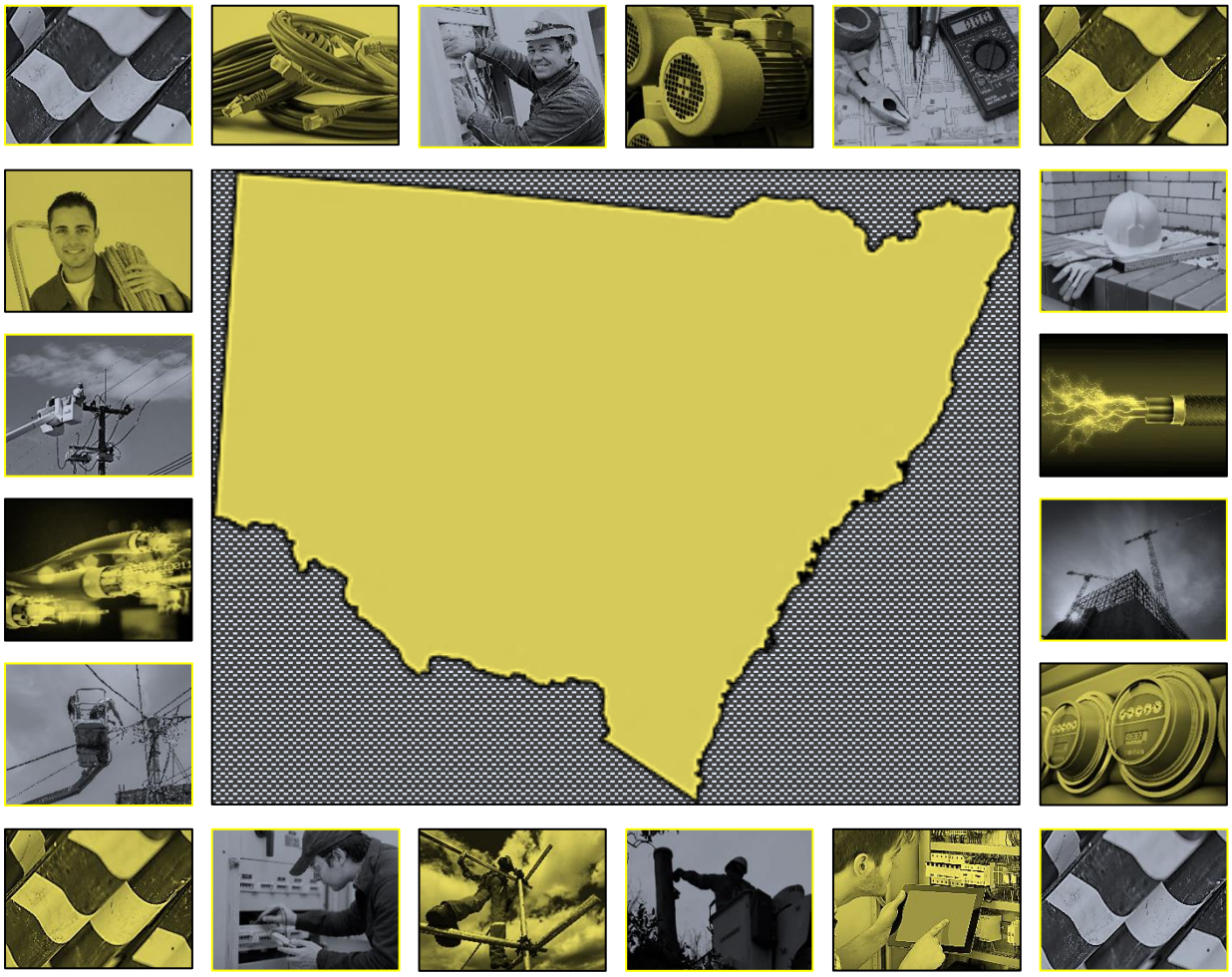
NECA submission on the AER's

Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline



November 2017

About NECA

The National Electrical and Communications Association (NECA) is the peak industry body for Australia's electrical and communications contracting industry, which employs more than 145,000 workers and delivers an annual turnover in excess of $23 billion. We represent approximately 5,000 electrical contracting businesses across Australia.

NECA represents the electrical and communications contracting industry across all states and territories. As a result of NECAs bi-annual industry survey, we are aware that NSW is the chosen headquartered state for many of the larger electrical contractors, making NSW issues critical for our members and the industry at large.

NECA aims to help our members and the wider industry to operate and manage their business more effectively and efficiently. To this end, NECA NSW owns and operates a Group Training Organisation, Registered Training Organisation, and its own Law Firm which all provide valued and industry focussed services to our members.

NECA represents members' interests to Federal and State Governments, regulators and principal industry bodies such as the Australian Chamber of Commerce and Industry (ACCI) and Standards Australia.

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Foreword

We thank the Australian Electricity Regulator (AER) for the opportunity to provide feedback on its *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline.*

NECA is supportive of the overarching approach taken by the AER in the *Ring-Fencing Guideline*, which we consider will enhance the rigour and transparency of the ring-fencing of electricity distributors and their related service providers.

However, NECA has concerns with some of the waivers the AER proposes to grant.

The most significant of these relate to:

- The six-month waiver with respect to legal / functional separation may cause harm to ASP (accredited service provider) businesses in NSW;
- The contestability of asset relocations should be enhanced going forward, not reduced; and
- Sale of inventory may provide DNSPs with an unfair advantage in the contestable works market.

The contestable works market in NSW is unique, with ASP business and market conditions distinct from the rest of Australia.

In our view, the AER should give further consideration to these differences in finalising the *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline*.

For example, it may in fact be appropriate for the AER to consider waivers requested by DNSPs operating in NSW separately, as opposed to grouping them together with other similar waivers requested by DNSPs operating in other states and territories.

These issues have the potential to not only impact NECA's member businesses but also reduce competition to the detriment of consumers.

The remainder of this submission spells out these and our other concerns in greater detail.

I would be happy to discuss further and can be contacted on telephone: 02 9439 8523 or email: suresh.manickam@neca.asn.au

Yours faithfully

Suresh Manickam
Chief Executive Officer
National Electrical and Communications Association (NECA)

Definitions

For clarity, the following terms are used in the remainder of this document:

- *DNSP Monopoly Business* to describe that part of the DNSP business which owns the assets and provides regulated, monopoly services;
- *DNSP Commercial Business* to describe that part of the DNSP business that competes openly in the marketplace; which can include contestable works as an ASP or other private works; and
- *ASP* to describe a private Accredited Service Provider but can extend to any third party company that is competing against the DNSP Commercial Business in the marketplace.

Legal / functional separation – 6 month transitional waiver applications

The issue of waivers with respect to legal / functional separation is addressed on page 35 of the AER's *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline*.

NECA has serious concerns with the AER's proposed granting of six-month waivers to Ausgrid, Endeavour Energy, Ergon Energy, Energex and TasNetworks in transitioning their 'Other Services' to affiliated entities.

If implemented, this waiver may allow Ausgrid and Endeavour Energy, who are currently preparing to re-enter the contestable works market in NSW, to compete against ASPs while Ausgrid and Endeavour Energy are non-compliant with the *Ring Fencing Guideline*.

In our view, this may thus provide these DNSPs with the opportunity to unfairly entrench themselves in the contestable works market in NSW, as they will have six months to undercut the competition (ASPs) and drive them out of the contestable works market.

The contestable works market in NSW is unique. ASP business currently already operate in the contestable works market, resulting in market conditions distinct from the rest of Australia.

In our view, the *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline* does not demonstrate that the AER has considered these differences adequately.

For example, it may in fact be appropriate for the AER to consider waivers requested by DNSPs operating in NSW separately, as opposed to grouping them together with other similar waivers requested by DNSPs operating in other states and territories.

Furthermore, this would undoubtedly reduce competition to the detriment of consumers.

We appreciate that Ausgrid for example has issues caused by the negotiation of its enterprise bargaining agreements (EBA).

However, there is no reason for our ASP members to be penalised due to a DNSP's own internal issues.

Our ASP members do not see why DNSPs should be given favourable treatment, when they themselves receive none themselves respect to the regulatory regime they face and have far fewer resources available to dedicate to compliance.

NECA's strong preference is therefore for the DNSPs to delay their re-entry into the contestable works market until such time as they can demonstrate full compliance with the *Ring-Fencing Guideline*.

Failing this, we believe that the onus is on the DNSPs and by extension the AER to demonstrate why our concerns are unfounded and / or how the risks for the contestable works market we have outlined will be mitigated.

While we understand that the AER is taking a longer term view towards securing compliance in relation to ring-fencing, this must be set against the short-term harm that could occur to ASPs, most of whom are small-to-medium sized enterprises.

Public lighting and nightwatchman lights – reclassification of services

Asset relocation projects involve the relocation or undergrounding of electrical assets; this often includes the upgrading and improvement of public lighting and nightwatchman lights.

Reasons why asset relocation projects are undertaken include:

- To accommodate road construction works;
- To improve the visual amenity of an area. The need for such projects is typically driven by local councils or other government authorities; and
- To remove obstructing assets from within or around a site.

NECA has consistently advocated that clarification be provided that asset relocation projects in NSW are contestable and are therefore subject to ring-fencing.

ASPs have been carrying out this work in NSW for some years, however currently the DNSPs have some discretion with regards to which asset relocation projects should be treated as contestable, i.e. whether ASPs can offer to undertake this work.

As a result, there is inconsistency in each DNSP's approach to the contestability of planned recoverable work and this has led to DNSPs exercising this discretion in different ways.

This means that the recoverable work that is contestable is different across the networks in NSW, leading to confusion and complexity for customers and ASPs. It also means that there may be some recoverable work that ought to be contestable that customers cannot ask an ASP to undertake on a particular network. Where this is the case, it results in a lessening of competition, resulting in increased costs to consumers.

Section 5.3 Recoverable Work of the NSW government document *Review of contestable services on the New South Wales electricity network – Final Report* of July 2010 describes the need to make more work contestable thus:

> *"Recoverable work is contestable at a DNSP's discretion. During consultation, DNSPs said that where a customer pays for work it should be contestable, except if there is a risk to the network. The review supports this view as it ensures the maximum*

level of competition on the network, leading to lower costs for consumers and efficiency on the network, as well as making sure that the safety and reliability of the network is maintained. The review recognises that emergency recoverable work (for example, work to reinstate a power line after it has been damaged in a car accident) should remain a monopoly service provided by DNSPs.

Currently, there is inconsistency in each DNSP's approach to the contestability of planned recoverable work and this has led to DNSPs exercising discretion in different ways. This means that the recoverable work that is contestable is different across the networks, leading to confusion and complexity for customers and ASPs. It also means that there may be some recoverable work that ought to be contestable that customers cannot ask an ASP to undertake on a particular network.

Options for resolving this problem include mandating contestability of planned recoverable work, prescribing contestability for certain types of work, or requiring transparent justification by DNSPs if they determine that recoverable work is a monopoly service.

Mandating contestability could risk safety and reliability of the network as it would limit a DNSP's control of their network. Prescribing the types of recoverable work that are contestable would require rigid definitions that would not be adaptable to changes in the marketplace or in work or work practices.

Requiring DNSPs to justify a decision that planned recoverable work is a monopoly service is a preferable approach as it would place pressure on DNSPs to classify recoverable work as contestable while preserving a DNSP's ability to do high risk work. It would redress some of the imbalance in the relationship between DNSPs who have all the relevant information and have the power to make a decision based on that information, and ASPs.

The Government should require that all planned user funded work on the network be contestable unless a DNSP justifies a decision that the work be a monopoly service provided by the DNSP. This approach recognises there may be times when safety and reliability considerations preclude the work being undertaken by a third party. It also introduces transparency and means that an ASP has access to information about a DNSP's decision where recoverable work is not considered contestable. This, in turn, reduces the likelihood that a DNSP applies its discretion inappropriately.

The review considered whether it was appropriate to include an appeal mechanism to allow customers to challenge a DNSP's decision that particular work was a monopoly service. However, as the asset owner, the DNSP should have ultimate control over what is built on the network and how that work is undertaken. An appeal mechanism would pass network decisions to another body, which would undermine the DNSP's role as owner and manager of the asset. Increasing transparency around DNSP decision making is a more effective way to ensure decisions are reasonable while protecting network safety and integrity."

If asset relocations were made non-contestable at the discretion of a DNSP, for e.g. through a waiver:

- The DNSPs would have an unregulated, monopolised source of revenue that could be exploited to the detriment of the NSW government, private developers, home owners and the community; and
- Many developments require the relocation of assets along with sub-division work and the connection of street lighting. Part of the work would be non-contestable (asset relocation) whilst other parts are contestable (sub-division work and street lighting). It is often impractical to split the design and construction works between non-contestable and contestable, hence the DNSPs have the natural advantage in undertaking this work; even where asset relocation works is as low as 10 per cent of the total project cost. Further, because non-contestable asset relocations are often associated with a larger project, it allows the DNSP to understand the entire project, build relationships with the client and structure their pricing to ensure they win all project stages on the back of them undertaking the non-contestable asset relocation stage.

NECA therefore advocates that all connection services and planned recoverable works should be contestable. If a DNSP considers work that a customer pays for is non-contestable, it should be required to justify this decision on request, including any determination of cost.

This would have the effect of enhancing the predictability and promoting confidence in the market for asset relocations, which aligns with the *COAG Best Practice Regulation Guide* cited on page three of the Guideline's explanatory statement.

The AER should give consideration to how this might be achieved.

NECA has also been advised that there are many local governments in NSW who feel disadvantaged and disempowered with the current system of service delivery by Essential Energy with respect to public lighting and nightwatchman lights. Much of the liability regarding street lighting provision resides with the respective local governments, yet they are powerless to manage their street lighting system.

In this context, continuance of the system being managed by Essential Energy (via a waiver) is likely to further degrade the relationship between local governments and Essential Energy.

Going forward, NECA will also be advocating that consideration should be given that the following works be made contestable:

- Tiger tails;
- Asset access;
- Transmission spotting;
- Transmission inspections (Distributors can subsequently audit ASPs' inspections);
- Network cable jointing; and
- Street lighting.

As such, we therefore request that the AER consider the classification of these services and relevant proposed waiver in this light.

Emergency recoverable works

NECA advocates with respect to the AER's proposed granting of a waiver for emergency recoverable works that the AER should ensure that DNSPs do not exploit the waiver by classifying repairs to their networks as being emergencies (for example caused by third parties) and thus not subject to ring-fencing, when in fact they were caused by the DNSPs themselves and were foreseeable.

However, NECA does not object to recoverable work that can genuinely be characterised as emergency in nature, (for example, work to reinstate a power line after it has been damaged in a car accident) remaining a monopoly service provided by DNSPs.

NECA's advocacy is consistent with the approach outlined in Section 5.3 "Recoverable Work" of the NSW government document *Review of contestable services on the New South Wales electricity network – Final Report* of July 2010:

> *"The Government should require that all planned user funded work on the network be contestable unless a DNSP justifies a decision that the work be a monopoly service provided by the DNSP. This approach recognises there may be times when safety and reliability considerations preclude the work being undertaken by a third party. It also introduces transparency and means that an ASP has access to information about a DNSP's decision where recoverable work is not considered contestable. This, in turn, reduces the likelihood that a DNSP applies its discretion inappropriately."*

Non-standard connections and customer-requested supply enhancements

These distribution services refer to situations where a customer requests a connection or an enhancement to an existing connection at a higher standard than the least cost technically acceptable standard. This service also includes customer or third-party requested asset relocations.

NECA has consistently advocated that asset relocations should be contestable. The AER should re-consider the waivers requested and classification of these distribution services in this light.

Asset relocation projects involve the relocation or undergrounding of electrical assets; this often includes the upgrading and improvement of public lighting.

Reasons why asset relocation projects are undertaken include:

- To accommodate road construction works;
- To improve the visual amenity of an area. The need for such projects is typically driven by local councils or other government authorities; and
- To remove obstructing assets from within or around a site.

Currently in NSW, DNSPs have some discretion in relation to the contestability of asset relocations, i.e. whether ASPs can offer to undertake this work.

As a result, there is inconsistency in each DNSP's approach to the contestability of planned recoverable work and this has led to DNSPs exercising this discretion in different ways.

This means that the recoverable work that is contestable is different across the networks in NSW, leading to confusion and complexity for customers and ASPs. It also means that there may be some recoverable work that ought to be contestable that customers cannot ask an ASP to undertake on a particular network. Where this is the case, it results in a lessening of competition, resulting in increased costs to consumers.

Section 5.3 “Recoverable Work” of the NSW Government document *Review of contestable services on the New South Wales electricity network – Final Report* of July 2010 describes the need to make more work contestable thus:

> *“Recoverable work is contestable at a DNSP’s discretion. During consultation, DNSPs said that where a customer pays for work it should be contestable, except if there is a risk to the network. The review supports this view as it ensures the maximum level of competition on the network, leading to lower costs for consumers and efficiency on the network, as well as making sure that the safety and reliability of the network is maintained. The review recognises that emergency recoverable work (for example, work to reinstate a power line after it has been damaged in a car accident) should remain a monopoly service provided by DNSPs.*
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> *Currently, there is inconsistency in each DNSP’s approach to the contestability of planned recoverable work and this has led to DNSPs exercising discretion in different ways. This means that the recoverable work that is contestable is different across the networks, leading to confusion and complexity for customers and ASPs. It also means that there may be some recoverable work that ought to be contestable that customers cannot ask an ASP to undertake on a particular network.*
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> *Options for resolving this problem include mandating contestability of planned recoverable work, prescribing contestability for certain types of work, or requiring transparent justification by DNSPs if they determine that recoverable work is a monopoly service.*
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> *Mandating contestability could risk safety and reliability of the network as it would limit a DNSP’s control of their network. Prescribing the types of recoverable work that are contestable would require rigid definitions that would not be adaptable to changes in the marketplace or in work or work practices.*
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> *Requiring DNSPs to justify a decision that planned recoverable work is a monopoly service is a preferable approach as it would place pressure on DNSPs to classify*

recoverable work as contestable while preserving a DNSP's ability to do high risk work. It would redress some of the imbalance in the relationship between DNSPs who have all the relevant information and have the power to make a decision based on that information, and ASPs.

The Government should require that all planned user funded work on the network be contestable unless a DNSP justifies a decision that the work be a monopoly service provided by the DNSP. This approach recognises there may be times when safety and reliability considerations preclude the work being undertaken by a third party. It also introduces transparency and means that an ASP has access to information about a DNSP's decision where recoverable work is not considered contestable. This, in turn, reduces the likelihood that a DNSP applies its discretion inappropriately.

The review considered whether it was appropriate to include an appeal mechanism to allow customers to challenge a DNSP's decision that particular work was a monopoly service. However, as the asset owner, the DNSP should have ultimate control over what is built on the network and how that work is undertaken. An appeal mechanism would pass network decisions to another body, which would undermine the DNSP's role as owner and manager of the asset. Increasing transparency around DNSP decision making is a more effective way to ensure decisions are reasonable while protecting network safety and integrity."

If asset relocations were made non-contestable at the discretion of a DNSP, for example, through a waiver:

- The DNSPs would have an unregulated, monopolised source of revenue that could be exploited to the detriment of the NSW government, private developers, home owners and the community; and
- Many developments require the relocation of assets along with sub-division work and the connection of street lighting. Part of the work would be non-contestable (asset relocation) whilst other parts are contestable (sub-division work and street lighting). It is often impractical to split the design and construction works between non-contestable and contestable, hence the DNSPs have the natural advantage in undertaking this work; even where asset relocation works is as low as 10 per cent of the total project

cost. Further, because non-contestable asset relocations are often associated with a larger project, it allows the DNSP to understand the entire project, build relationships with the client and structure their pricing to ensure they win all project stages on the back of them undertaking the non-contestable asset relocation stage.

NECA therefore advocates that all connection services and planned recoverable works should be contestable. If a DNSP considers work that a customer pays for is non-contestable, it should be required to justify this decision on request, including any determination of cost.

This would have the effect of enhancing the predictability and promoting confidence in the market for asset relocations, which aligns with the COAG Best Practice Regulation guide cited on page three of the *Ring-fencing Guideline*'s explanatory statement.

Sale of inventory

On page 24 of the *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline* the AER states its intention to grant Energex, Essential Energy and Ergon Energy a waiver with respect to "sale of inventory".

NECA advocates that AER should re-consider its proposed granting of this waiver.

We believe that the default position should be that sale of inventory should be ring-fenced.

At the point of sale (or even at point of purchase from the manufacturer) it is impossible to determine whether the materials will:

- Be used back on the DNSP's own network; and / or
- End up on another DNSP's network; and / or
- End up on a private network.

The lack of ring-fencing in regards to sales of inventory provides the opportunity for DNSPs to exploit a significant unfair competitive advantage in the market place.

The DNSP Monopoly Business has long, well established procurement departments that support its monopoly activities of capital, maintenance and breakdown works. As a result of significant volume and the low risk of such a contract, the DNSP Monopoly Business obtains very competitive pricing. Such pricing would provide an unfair advantage to the DNSP Commercial Business if it is allowed to purchase materials (and other services) off the back of these procurement contracts.

The DNSP Monopoly Business controls the approval process of materials and typically link product approval to success in the tendering process. In some cases, only one supplier is approved and previous suppliers are disapproved. This creates a monopoly which restricts an ASP's ability to choose alternate manufacturers and can disrupt an ASP's existing supply chain. Such actions provide an unfair advantage to the DNSP Commercial Business and can be exploited to the detriment of ASPs.

The successful supplier favours the DNSP in order to maintain approvals and its preferred supplier status; and the supplier does not discriminate between the DNSP Monopoly Business

and the DNS Commercial Business. Examples of favouritism include providing priority for manufacturing or material delivery to a DNSP at the expense of or delay to an ASP.

Where the DNSP Monopoly Business changes standards or removes the approval of an item, the DNSP is still able to use existing stock or have commercial arrangements in place to be reimbursed by the supplier for non-conforming stock. An ASP is not able to run down its stock but must treat such stock as obsolete, thus incurring financial penalty.

Further, as many DNSP approvals create a monopoly of supply, ASPs are in weakened bargaining position and are unable to negotiate as favourable commercial arrangements with suppliers. This provides an unfair advantage to the DNSP Commercial Business.

NECA advocates that in our experience, DNSPs stockpile inventory such as cables. DNSPs hold significant stock to support their monopoly activities of capital, maintenance and breakdown works. The DNSP Commercial Business can take advantage of this "availability of stock" compared to an ASP who may have to wait up to 12 weeks for delivery of certain items. This immediate availability provides the DNSP Commercial Business with an unfair advantage.

Further to this should the DNSPs in NSW, who are re-entering the contestable works market, follow the same business model as adopted in South Australia by SA Power Networks with Enerven , i.e. material on-selling and contracting in the same business entity, they will have an distinct unfair advantage.

The AER should therefore re-consider its proposed waiver regarding sale of inventory in this light.

Networks safety services

The classification of network safety services is addressed by the AER on page 24 of the *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline*.

These services include a range of activities that DNSPs undertake to ensure the safety of the network.

NECA wishes to inform the AER that we may seek in future to have tiger tails made contestable in NSW, in other words accredited service providers (ASP) would be able to tender with respect to these services as part of the contestable works market.

Going forward, NECA will also be advocating that consideration should be given that the following works be made contestable in NSW:

- Tiger tails;
- Asset access;
- Transmission spotting;
- Transmission inspections (Distributors can subsequently audit ASPs' inspections);
- Network cable jointing; and
- Street lighting.

As such, we therefore request that the AER consider the classification of these services and relevant proposed waiver in this light.

Customer-initiated asset relocations

As per our comments with respect to “Non-standard connections and customer-requested supply enhancements”, NECA has concerns that this waiver might lead to DNSPs exercising discretion in relation to the contestability of asset relocations, thus circumventing the *Ring-fencing Guideline*.

The DNSPs may be able to classify relocation of assets as having a potential impact on the safety or security of their networks, and thus rule them as non-contestable, when this is not in fact the case.

NECA has consistently advocated for some time that the default position should be that asset relocations should be contestable, i.e. open to ASPs.

The AER should therefore ensure that the waiver is not used to this end.

Regional service delivery "provider of last resort"

Essential Energy sought a waiver that would allow it to offer unregulated contestable services where alternative service providers are unwilling or unable to offer service on a timely and affordable basis to customers.

This regional service delivery as "provider of last resort" is addressed by the AER on page 62 of the *Draft decision: DNSP applications for waivers from the Electricity Distribution Ring-fencing Guideline*.

NECA echoes the concerns of the AER that the waiver as requested would grant Essential Energy too much discretion to decide whether or not customers had access to services from third parties at a reasonable price and on reasonable terms. Further, there is a risk is that if the waiver was granted, Essential Energy's presence in the market could drive away competition. This assessment by competitors could be based on the perception (real or otherwise) that Essential Energy is willing to provide services even where it is not commercially viable to do so.

Additionally, NECA advocates that in its final decision the AER mandates that Essential Energy should be required to use a full cost recovery model with respect to their charging of customers as a "provider of last resort", i.e. consumers should not be billed on an incremental cost basis.

NECA is also happy to provide the AER with feedback going forward as to whether there are ASPs who would be willing to provide services in the relevant regional areas.

Our information is that there are in fact many regionally located ASPs willing to provide all of these services.

Essential Energy – technical training courses

The issue of the provision of technical training courses by Essential in regional areas is addressed on page 65 of the Draft Decision.

NECA has no objection to the waiver that the AER proposes to grant Essential with respect to its provision of technical training courses in certain regional areas.

NECA Training (NECA's RTO) will be offering these courses in Canberra in the near future.

While we do not consider that the waiver will negatively impact NECA's ability to deliver training in the ACT and surrounding regions, NECA advocates that this waiver should definitely be reviewed as flagged on 30 June 2024, in order to ascertain the situation at that time.