



National Framework for Distribution Regulation

Response to Retail Policy Working Group Consultation Paper

18 July 2007

1. Overview

Key messages

- Significant policy choices are still outstanding and early consideration of these issues from jurisdictional governments would assist in their resolution
- Experience from the first tranche of economic regulatory law and rule changes highlights the importance of providing sufficient stakeholder input into both the policy development and drafting processes
- It is critical that more formal and transparent processes are developed to better provide for the interaction of the first and second tranches of regulatory reforms, with sequencing of the elements of reform one way to achieve this

The Energy Networks Association (ENA) welcomes the opportunity to comment on the Allens Arthur Robinson Composite Consultation Paper *National Framework for Non-Economic Distribution and Retail Regulation* (Composite Paper) released by the MCE Retail Policy Working Group in June.

Energy network businesses have responded in detail to the previous Working Papers developed by Allens Arthur Robinson for the Retail Policy Working Group. The comments made in this submission summarise distribution industry comments and some core areas of concern, including the policy development process from here. A lack of clear overarching policy guidance, and the status of the Composite Paper as not representing the views of any MCE body or individual government has, however, constrained the capacity of industry to fully assess the proposed options.

A key lesson from progress on the first tranche of changes to energy laws and rules has been the importance of enabling structural opportunities for industry to contribute to both the policy development process, and assessing draft rules and laws. Industry considers that the limited steps in this regard will be proven to have been critical to improving the practicality and quality of proposed National Electricity Law amendments and National Gas Law. Whilst the Retail Policy Working Group has achieved much in this area of engagement over the past year, it is imperative the substantive consultation surrounds the next, more complex, stages of developing agreed policy options and translating these into draft rules and energy law amendments.

A further result of the development of two separate regulatory packages is the need for adequate mechanisms to ensure the rules developed by each MCE work stream 'fit together' in a cohesive and commercially practical way. A more sequenced process potentially extending implementation of the 'second tranche' of reforms in the Composite Paper until the end of 2008 is one practical way to maximise the chances of a stable, cohesive, and internally consistent set of reforms.

2. Background

This submission responds to the Allens Arthur Robinson Composite Consultation Paper *National Framework for Non-Economic Distribution and Retail Regulation* released on 19 June.

This submission responds at a high level to a series of proposals and recommendations made across areas of relevance to energy distribution networks. Further details of ENA member views on the detailed aspects the Composite Paper are contained in submissions to the preceding Allens Arthur Robinson Working Papers.

The Energy Networks Association is the national representative body for gas and electricity distribution network businesses. Energy network businesses deliver electricity and gas to over 12 million homes and businesses across Australia through approximately 800 000 kilometres of electricity lines and 75 000 kilometres of gas distribution pipelines. These distribution networks are valued at more than \$35 billion, and each year energy network businesses undertake capital investment of more than \$5 billion in network reinforcement, expansions and extensions.

3. High level views on distribution framework development

The energy distribution sector considers that the work of the Retail Policy Working Group is one of the most important areas for achieving the MCE objective of streamlining energy regulation.

3.1 Status of conclusions and recommendations

A key next step in the Retail Policy Working Group process should be the development of an initial **policy position** from jurisdictions on:

- core *objectives* of the national distribution framework
- preferred approaches to some *threshold framework design issues*
- further consultation and development of the detail behind the framework design issues

The reason for the importance of this next step is a lack of clarity regarding the precise status of the Allens Arthur Robinson report. As the paper notes the recommendations do not reflect the views of MCE, SCO or the Retail Policy Working Group itself.

Given these caveats and the early stages of this policy development process it is unclear to what extent industry or stakeholder endorsement of particular options or recommendations would be meaningful. Industry experience with other elements of the MCE's policy development process has demonstrated that significant policy departures from earlier agreed options are a common occurrence. This potential is heightened where the objectives and evaluation criteria as set out in the Composite paper remain high-level and contain a range of unresolved competing objectives.

The distribution sector notes that it originally provided a comprehensive set of responses on issues around a national distribution framework in 2004 in the context of a previous NERA-Gilbert and Tobin led project.

Recommendation

ENA recommends that RPWG:

- *Consider clarifying and refining the objectives and evaluation criteria for the national distribution framework (Section 1.4)*
- *Develop in consultation with stakeholders a set of initial guiding policy options which are potentially capable of agreed implementation by all jurisdictions*

3.2 Timetable and consultation process

Energy network businesses welcome the consultation that has occurred to date under the Retail Policy Working Group process. As the policy development process moves forward, however, there will be a need for more intensive consultative mechanisms around detailed policy options set out by RPWG or SCO, and the draft rules and energy law amendments which will give effect to the new arrangements.

The recent rules and law development process on the access and pricing components of the national distribution regulatory regime highlights the strong need for effective early engagement of stakeholders on both the policy framework and detailed implementation of significant regulatory reforms. To this end, ENA recommends an extension of the current timetable for implementation of the non-economic regulatory package from the current 1 July 2008 deadline. This extension would also allow better opportunity for all stakeholders to consider and refine the important interactions between the first (access and pricing) and second (non-economic tranches of rule and law amendments). Any extension may give rise to the need for further transitional arrangements.

Recommendation

ENA recommends that RPWG seek SCO MCE approval for a six month extension of the current formal timetable for entry into effect of the national distribution and retail framework from its current 1 July 2008

4. Response to selected issues in the Consultation Paper

4.1 Contractual models

The contractual relationships between distributors, retailers and customers are a critical commercial issue for energy network business. As well as being central to their daily commercial operations, these arrangements shape their corporate, legal and financial risk profiles.

The model of contractual relationships set out in the original working paper has been clarified further in the Composite Paper.

ENA welcomes this development and the explanation of the differing scope of use of system agreements in electricity and interface contracts in gas. The removal of the ambiguous regulatory concept of a 'local distribution network provider' is also helpful.

The core concern of industry is to maintain appropriate arrangements which:

- reflect current commercial arrangements
- minimise costly regulatory step changes justified only on the basis of consistency
- avoid forcing either gas or electricity network businesses to adopt systems and processes not required by actual identified customer needs

In principle, electricity distribution businesses are broadly comfortable with the 'modified linear' approach set out in the Composite Paper.

It is also important that there is careful integration of the economic and non-economic regulatory reform. To date these packages have been developed as separate work streams. This is understandable in the context of the enormous work load currently being progressed through the MCE processes. However, it is clear that the point has been reached where these process must be properly integrated so that each package can be understood by stakeholders as part of the larger NEM reform process. Whilst it may appear to be a small point, the fact that the Composite proposed a definition of 'distribution services' for non-economic regulatory purposes without discussion or any references to the existing and quite different definition used in the National Electricity rules for the general NEM indicates a dangerous disconnect between these processes.

ENA remains concerned, however, that this is not an appropriate default arrangement for introduction into the gas distribution sector, as the model duplicates major elements of the current 'linear' model supported by terms and conditions spelt out in individual access arrangements.

4.2 Business authorisations

ENA supports the development of a simple national framework for distribution and retail business authorisation consistent with ENA's previous submission responding to the Retail Policy Working Group Working Paper 3. Energy network businesses continue to support a high level business licence that identifies relevant market players and which does not have the effect of directly imposing substantive regulatory obligations.

The RPWG Composite Report provides eight recommendations addressing the legislative and regulatory treatment of business authorisation for distribution and retail businesses. Broadly, ENA agrees with the outlined recommendations. In particular, ENA agrees with the recommendations which require a retailer, distributor or other person (which satisfy the relevant description) to obtain an energy business authorisation and comply with the outlined criteria respectively.

ENA does have some concerns with some aspects of the report's recommendations. Recommendation 44 states that the Law should authorise the AER to exempt a person from the prohibition in accordance with the Law, the Rules and any guidelines issued by

the AER. ENA considers that in relation to the power of the AER to provide an exemption, it is essential that the decision-making process surrounding this be public and transparent and includes a consultation process.

Recommendation 46 of the Composite Paper states that the Law should authorise the AER to revoke a business authorisation or exemption if the AER determines that the holder ceases to satisfy the entry requirements. ENA reinforces its previous position that the threat of revocation should not be used for regulatory breaches. The threat of revocation, however improbable, affects the assessment of the risk profile of a regulated business.

ENA supports the development of a single licence at a national and state and territory level. It is noted that the proposed approach does not address the issue of dual licensing/authorisation regimes between national and state government or the appropriate party to be licensed. It is critical that state and territory economic licences transition to the national authorisation without the requirement for re-application and that associated licence fees are removed.

Recommendation

ENA recommends that for the AER to provide an exemption to authorisation, it is essential that the decision-making process be public and transparent and should include a public consultation process.

4.3 Ring fencing

ENA considers the next stage of work from the composite paper would benefit from a clear re-examination of the objectives or ring-fencing and the principles which should underpin ring fencing obligations.

Despite this, taking into account the proposal to mirror existing ring-fencing provisions in the draft National Gas Law, ENA members broadly support the approach adopted in the relevant Working Paper and the Composite Paper.

4.4 Retailer of last resort

ENA supports the proposed approach to retailer failure arrangement of developing a national best practice system. ENA considers it important that retailer failure arrangements are referred to the AEMC to develop and progress the establishment of a national retailer failure regime through a comprehensive consultation process.

ENA does consider it inappropriate to include details of the regulatory scheme for retailer of last resort schemes in the legislation. Recommendation 55 states that the Law should set out the matters to be addressed in the Rules by way of general description, an outline of the type of matters that will be provided within the Law have been provided. It is essential that any general descriptions do not result in impeding future development in the regime as experience in the regime develops. Additionally, the general description in the Law should not assume a particular outcome from the AEMC rule change process.

ENA has concerns with the proposal that an expert review could be used to develop and consult on a retailer of last resort scheme with the outcome being implemented by Rule changes made by Ministerial order where the MCE considers that timing and resource issues are such that the task should be undertaken by the AEMC. ENA considers this to be an inappropriate and insufficient solution to a potential AEMC resource issue. If timing and resources are an issue, then this should be directly addressed to allow the AEMC to conduct the Rule change process.

Recommendation

ENA recommends that:

- *Any legal heads of power for a national retailer of last resort scheme should not prescribe the final operational form of any scheme*
- *Any identified AEMC resourcing issues following from future recommendations of the RPWG on a national retailer of last resort scheme should be addressed directly by decisions of the MCE, and not result in the development of ad hoc policy or rule development mechanisms outside of the AEMA governance framework*

4.5 Enforcement

Energy network businesses consider it essential that the regulatory compliance and enforcement regime is predictable, effective, unambiguous and comprehensive. ENA outlined its main concerns in its response to the Supplementary Working Paper by the Retail Policy Working Group the importance for distribution businesses to have confidence that an orderly process will be followed by the AER in regard to any enforcement action.

The Composite Report does not address this issue, and it appears that the AER will have full discretion in determining which enforcement mechanism or combination of mechanisms to use in any given case. ENA concludes that such an approach will result in increased risks and therefore costs faced by distribution businesses.

As a minimum requirement in this area energy distribution businesses consider that the AER should be under an *obligation* set out in the Law or Rules to develop and set out its proposed approach to exercising its wide discretion on enforcement issues. This guidance should enable market participants to make decisions based on a stable and predictable enforcement regime administered by the AER.

Recommendation

ENA recommends that

- *future policy options on enforcement should make clear that withdrawal of a business authorisation is not intended to be an option under enforcement activities by the AER*
- *future national distribution law and rules should provide an obligation on the AER to develop a guideline on its regulatory enforcement approaches*

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