

# Transmission Ring-Fencing Guideline

Response to AER Discussion Paper

31 January 2020

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## Key messages

### *General comments*

- » Transmission Network Service Providers (TNSPs) support the intent behind ring-fencing arrangements.
- » The current TNSP arrangements are working well and do not require material change.
- » Any material changes to the ring-fencing arrangements must be driven by evidence that the current arrangements, including the broader competition law protections, are inadequate to meet the relevant policy objectives.
- » Energy Networks Australia supports the Australian Energy Regulator's (AER)'s assessment that there is no need for ring-fencing between negotiated transmission services and prescribed transmission services, and for contestable connection services the range of protections already in place are appropriate.

### *Cross subsidy provisions*

- » If the benefits of network support technologies such as batteries, synchronous condensers or generation are to be fully realised it is essential that TNSPs maintain the 'build or buy' option with respect to their provision and are able to operate them for network services within the TNSP main entity. Energy Networks Australia supports the AER's recognition of existing commercial arrangements with respect to non-traditional network devices that ensure that TNSPs have a full suite of technology solutions available to meet a network need while also ensuring that customers benefit from any market facing services such devices can offer.
- » The current 5 per cent threshold that allows the TNSP main-entity to have a small interest in other activities that provide incidental market facing services should be maintained.
- » Consistent with the distribution arrangements, the conduct of transmission and distribution activities should be permitted to be undertaken by the same legal entity. Further, those TNSPs that also have a distribution entity must be able to operate in the same way as a stand-alone TNSP.<sup>1</sup>
- » If legal separation in any specific area is demonstrated to be clearly in customers' interest, this should be applied on a prospective basis only given it can impose material costs (such as tax implications) and may interact with existing licences/registrations.

### *Non-discrimination*

- » It is unclear that any additional non-discrimination requirements are warranted given the robust competition law requirements that exist under section 46 of the *Competition and Consumer Act 2010*, including substantial penalties for breaches and the potential for private actions. Should broader provisions be clearly shown to be in customers' interest, these should come with appropriate

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<sup>1</sup> Additionally, arrangements for joint TNSP and DNSP entities should not hinder the way that stand-alone TNSPs are able to operate.

protections/waivers for circumstances where third-party access to transmission infrastructure may raise legitimate transmission reliability issues or potentially even national security concerns. This would be akin to the approach the Australian Energy Market Commission (AEMC) has taken for network connections where TNSPs maintain responsibility for certain services and operation of assets.

***Functional separation***

- » It is unlikely that the sharing of resources with potential contestable electricity services provided by a TNSP would generate a material harm to competition – whereas without resource sharing, continued provision by TNSPs may be unviable – and so substantial functional separation arrangements would be counter-productive for customers.

***Other measures***

- » For TNSPs, the costs of auditing and compliance reporting obligations are expected to outweigh the benefits and are not needed in a fit for purpose model.
- » The AER’s proposed compliance timeframe of 1 July 2021 may need to be revised depending on the extent of new compliance obligations.

## Overview

Energy Networks Australia is pleased to make this submission to the AER on behalf of its transmission members in response to the Discussion Paper for the review of transmission ring-fencing arrangements.

Energy Networks Australia 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.

Energy Networks Australia supports the intent behind ring-fencing arrangements. When properly applied, ring-fencing can provide benefits to customers by ensuring the proper allocation of costs and the protection of competition where this is feasible. The current ring-fencing arrangements, in conjunction with the extensive provisions in the Rules and competition law protections, are working well and are largely fit-for-purpose for transmission businesses. As such, material change to current arrangements is not required. To the extent changes are made these should be focused on refinements, including to update the terminology and modernise how obligations are specified.

In undertaking this review it is important for the AER to have regard to the significant future demands and challenges facing transmission networks. A rapid transformation is underway in the energy sector. This transformation is creating a bow wave of investment needs to address connections from new sources of generation, a desire for stronger national flow paths, and also a need to strengthen the resilience of the system to protect against major outages. These future challenges mean that TNSPs need to have the full toolkit available to them to respond efficiently. As such, the ring-fencing arrangements should not impose barriers that unnecessarily limit the

capability for TNSPs to respond to the needs of customers in an innovative, flexible and timely way.

In summary, Energy Networks Australia has the following substantive views in response to the AER Discussion Paper:

- » If not properly focussed, ring-fencing measures can impose greater costs than those caused by the harms they are seeking to address. For instance, by imposing unnecessary changes to business operations and / or duplicating existing arrangements. Any material changes to the ring-fencing arrangements need to be justified against evidence that the current arrangements, including broader competition law protections, are inadequate and will lead to harm for relevant contestable markets and customers. Further, any changes need to be the lowest cost means of addressing the perceived harm.
- » The AER has appropriately recognised that there are material differences between transmission and distribution and this requires a different approach to the application of ring-fencing. A fit-for-purpose ring-fencing arrangement means taking into account the unique characteristics of transmission compared to distribution, which includes its investment and operational characteristics, the nature of its customer base, as well as differences in the regulatory framework that applies.
- » Energy Networks Australia supports the AER's assessment of the arrangements for negotiated transmission services and contestable connection services. In the case of negotiated transmission services, these are monopoly services provided to large and sophisticated entities such that there is no need for further ring-fencing provisions. For contestable connection services the extensive Rules framework and regulatory obligations already address any competition harms that may emerge. Having TNSPs able to offer contestable connection services without explicit requirements over the functional separation of staff will ensure a deeper market for the services and lower costs, to the benefit of customers. To the extent the AER identifies any gaps in this framework these should be addressed through a Rule change in order to maintain the integrity of the regime established by the AEMC.
- » The AER has given significant attention to the use of battery technology by TNSPs. This technology, along with other network support devices, can deliver significant benefits to customers when TNSPs are able to deploy it for the benefits of the transmission network. Further, arrangements that allow for the use of such devices to provide other services can also bring additional benefit customers by reducing prescribed transmission charges through the application of cost allocation and shared asset provisions. It is essential for these benefits to be delivered that TNSPs maintain the 'build or buy' option with respect to the provision of batteries or other non-traditional network solutions, including being able to operate them within the main TNSP entity. To the extent contestable electricity services also can be provided by network support technologies, then it is accepted that this should be done by (at least) a ring-fenced entity. Energy Networks Australia requests that the AER confirm that the arrangements imposed

by ElectraNet for its battery assets at the Dalrymple substation demonstrate an appropriate way to efficiently deliver network services while addressing possible harms from competitive market facing activities.<sup>2</sup>

- » The AER has sought views on what arrangements are needed for any other potential contestable electricity services offered by TNSPs. These services include consulting services, microgrids and testing services. It is difficult to foresee material harms from sharing resources in relation to these types of services, and so functional separation arrangements are unlikely to provide a competitive benefit. Either the TNSP holds no material advantage or there are no barriers to third parties providing the services in the same way as the TNSP (e.g. information can be provided to third parties upon request). Ring-fencing these services would be particularly onerous relative to the value of the services such that it would mean that for some TNSPs it would be uneconomic to continue to provide these services. This would mean customers would no longer have access to a well-resourced and expert service provider and reduce overall the supply options available to customers.
- » As identified by the AER, TNSPs have limited capacity to provide a discriminatory advantage with respect to contestable non-electricity services, such as telecommunications. Therefore, other than for cost allocation, there is no role for the ring-fencing guideline with respect to these services. Indeed, the provision of contestable services<sup>3</sup> by TNSPs should be encouraged given they enable benefits to be delivered to regulated customers through the application of cost allocation and shared asset provisions.

The remainder of this submission provides some further commentary on key matters emerging from the AER's Discussion Paper, it then responds directly to the specific list of questions put forward by the AER.

## The current arrangements are working well

The current ring-fencing arrangements for transmission have proven to be successful in protecting against potential harms to competition while also ensuring that TNSPs can maintain efficient service delivery. A significant contribution to this success is that the arrangements work in concert with requirements in the Rules as well as broader competition laws that also aim to protect competition where it is feasible. Moreover, in

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<sup>2</sup> In this case ElectraNet built and owns the battery assets for the purposes of providing a network function. It has leased the market facing operation of the plant to an independent third party to be used to provide contestable energy and frequency control services. The RAB value for the assets was reduced commensurate with the value of the lease.

<sup>3</sup> In this submission contestable services are those services that are neither prescribed transmission service or negotiated transmission services.

the one area where participants had raised concerns – namely, in relation to connection services – a comprehensive regime for competition, including robust safeguards, was introduced as part of the 2017 Transmission Connection and Planning Arrangements (TCAPA) rule. Energy Networks Australia welcomes the AER’s views that the safeguards that were introduced are appropriate. This means that there is no need to make material changes to existing arrangements. Doing so would only serve to duplicate existing arrangements and increase costs without a corresponding benefit to customers. To the extent changes are made to the ring-fencing arrangements, these should be focused on updating the terminology and modernising how obligations are specified.

### **Competition law already provides adequate protection against discrimination**

The section 46 arrangements of the *Competition and Consumer Act 2010* (CCA) have recently been upgraded and strengthened such that they are very robust to concerns that ring-fencing may also seek to address, in particular, discrimination by a TNSP in the conduct of its monopoly activities against potential competitors to the TNSP’s (or the TNSP’s affiliates) contestable business.

Given the nature of the contestable services that TNSPs might provide (i.e. large and high value, infrequent, largely transparent) and that they are provided for large and sophisticated customers, there is an increased likelihood breaches of section 46 are raised with the ACCC, or the aggrieved party itself takes action, relative to what might be the case for distribution. Energy Networks Australia notes a recent lawsuit by Cube Holdings for misuse of market power against the Port of Newcastle is evidence of such private actions being a realistic prospect.

Accordingly, broadening non-discrimination provisions in the ring-fencing guideline beyond those that already exist would most likely serve only to unnecessarily duplicate these competition law requirements, and so raising compliance costs without a competitive benefit.

Should the AER establish the need to broaden non-discrimination provisions in the TNSP guideline it is essential that these contain protections and / or waivers against non-discrimination requirements in circumstances where third party access may impact on the security and reliability of the network or system, or even national security more broadly. This would be akin to the approach the AEMC has taken for network connections where TNSPs maintain responsibility for certain services and operation of assets. These protections would not be intended to preclude third parties from providing the same contestable services that a TNSP might, it simply means that they may need to be provided in a different way (e.g. beyond the fence) or in collaboration with the TNSP.

Energy Networks Australia considers it is particularly important for the AER to be cognisant of the potential, less obvious, indirect costs that may be imposed by inappropriate ring-fencing arrangements. The direct costs of ring-fencing are obvious and include the implementation and administration costs of changing and maintaining different operational models. Indirect costs include lost efficiency where economies of scale and scope cannot be realised, or a loss of expertise available to provide the service. Additionally, it may simply become uneconomic for TNSPs to continue to

provide the service such that the depth and effectiveness of competition in the market is severely compromised. These are not outcomes that are in the best long-term interests of consumers.

An implication of the potential for material indirect costs from onerous ring-fencing obligations is that in conducting this review the AER should be predisposed towards retaining existing arrangements unless there is compelling evidence to do otherwise. The presence of these costs mean that the burden of proof needs to be that there is a clear harm that exists that is not being addressed by the current guideline, Rules or competition law, and the benefits of addressing this harm are clearly outweighed by the costs of the measures imposed to remedy it.

An additional matter that the AER needs to take into account during the review is the interaction between transmission and distribution. Consistent with the distribution arrangements, the conduct of transmission and distribution activities should be permitted to be undertaken by the same legal entity. Further, however, the AER needs to ensure that those TNSPs that also have a distribution entity are able to operate in the same way as a stand-alone TNSP. This means that distribution arrangements should not restrict how the TNSP is able to operate for the purpose of providing transmission services. The corollary of this is that arrangements for joint TNSP and DNSP entities should also not hinder the way that stand-alone TNSPs are able to operate.

## A different approach is needed for transmission

It is necessary that the unique characteristics of transmission are taken into account in the AER's review of the ring-fencing arrangements. To that end, Energy Networks Australia supports the recognition that important differences exist between transmission and distribution that mean a different approach is needed for ring-fencing. Characteristics of transmission networks that Energy Networks Australia believes the AER needs to take into account for its approach to ring-fencing include:

- » Service outcomes for transmission networks can have material and wide-ranging impacts, in particular, with respect to impacts on the wholesale market, broader network security and interconnection across regions. For this reason, well defined service standards and a single point of accountability has been seen as critical for the delivery of transmission services. This is also the justification for there being a comprehensive framework in the Rules on how the contestable connections framework is to operate. This includes how service outcomes are maintained while also ensuring contestability can operate effectively.
- » Transmission projects tend to be large, lumpy, and infrequent, and in the case of connections, bespoke to the individual needs of the connecting party.
- » Unlike for distribution services, negotiated transmission services are monopoly services in transmission and are only regulated in a negotiate / arbitrate framework (rather than as prescribed transmission services) because they are bespoke services that are directly attributable to a large and sophisticated commercial entity.

- » Customers directly connected to transmission networks tend to be very large and sophisticated commercial entities and the services they request also tend to be large and of high value, meaning:
  - competition law provisions related to conduct can be expected to be brought to bear and so are 'front-of-mind' for TNSPs in the way they operate
  - branding would not be expected to affect competition as they have the capacity to "see through" brands
  - customers are likely to ensure all potential providers of contestable services are well informed in advance of works being needed such that it is unlikely that a Primary TNSP would obtain any competitive advantage in this respect, and
  - there is a much greater capacity for the reasonableness of offers to be tested, which reduces the benefit that may be generated by additional ring-fencing measures.

## **An effective framework exists to protect against harms to contestable connection services**

The AER has given appropriate recognition to the comprehensive framework that has been imposed by the AEMC to facilitate the extension of contestability for network connection services. This is a framework that has been carefully designed to protect competition while also enabling the efficiency benefits and expertise of TNSPs to be harnessed for the benefit of customers. It does this by including comprehensive protections to competition while also avoiding the need to functionally separate the TNSP's provision of prescribed services from contestable connection services. It is notable that the framework was designed by the AEMC in full knowledge of the existing transmission ring-fencing arrangements, as well as those implemented for distribution. Additional ring-fencing requirements would only serve to undermine the efficiency benefits sought by the AEMC in designing its regime and so would not promote the long-term interests of consumers.

The arrangements that exist to protect competition for contestable connection services, including some that were already present in the Rules, go beyond what can be achieved in a ring-fencing guideline and include:

- » extensive information transparency to reduce the information asymmetry between customers and alternative providers and the TNSP, including the general ex-ante publication of information to inform potential connecting parties and specific information provided as part of the connection process when direct enquiries are made
- » a requirement for a functional specification for a connection with the aim of setting a level playing field and to limit the scope for preferential access
- » negotiating principles / framework to limit the ability for a TNSP to deliver preferential treatment to its own contestable customers with respect to the

monopoly services it provides, including a requirement for TNSPs to identify the reasonable costs of providing the service and, upon request, demonstrate that charges reflect costs

- » recourse is available to an independent engineer to the extent that there are concerns that the functional specification for the project may discriminate against a rival provider of the service, and
- » recourse is available to a commercial arbitrator to assist in preventing TNSPs imposing inefficiently higher costs on customers of other contestable providers.

If experience with the practical application of the scheme suggests there are shortcomings in the framework and refinements are needed, these refinements should be progressed through the Rules. This approach ensures that the framework envisaged by the AEMC can be maintained and also maintains the continuity of the regulatory approach to contestable connection services.

## The full suite of build versus buy solutions need to be available to TNSPs

Currently TNSPs are motivated to actively seek to identify the most efficient solution to meet a network need. Increasingly, this is not always traditional network infrastructure with storage, demand-side services and generation now better able to meet the needs of the network at an efficient cost than may have been the case in the past. It is essential that ring-fencing arrangements do not compromise innovative solutions being sought and so the use of alternatives to traditional network infrastructure for the efficient delivery of network services.

The long-term interests of consumers are promoted through TNSPs continuing to be able to consider the full suite of build or buy solutions for meeting a network need. Whilst in some circumstances there may be an existing deep market for the provision of non-traditional network services, or where a tender for such services will be highly competitive, this will not always be the case, and especially where the service is required in an area that is remote or the service required is of a small scale. Procuring these services from another party in such a situation may come at a much higher cost than if the TNSP owns the assets in question. Preserving the “build or buy” option requires that the legal entity that provides prescribed transmission services continues to also be able to own and operate any assets that may be used to provide transmission services, even if these include non-traditional network assets such as batteries, generators or synchronous condensers. Importantly, TNSP provision of these assets does not preclude third party provision where this is more efficient.

### A proven model exists for addressing potential harms from TNSP ownership of storage or generation

Assets that provide storage (such as batteries) and generation used for network support often are also able to provide services in addition to network support at times

when the asset is not required for the network.<sup>4</sup> Customers are better off if these assets can be utilised for these other functions rather than limited only to network support. This is because revenue earned from unregulated activities can be used to reduce regulated charges.<sup>5</sup> Further, costs can be allocated between regulated and unregulated services as appropriate.

Energy Networks Australia recognises that competition concerns emerge with respect to assets that may participate in the sale of energy in wholesale markets or directly to customers. Therefore, it is apparent that some form of ring-fencing is needed to provide an assurance that ownership of the network and provision of transmission services using non-traditional assets does not lead to harms being imposed in these competitive markets. Importantly, TNSPs have already developed successful models under the current framework that address these concerns.

A specific example is ElectraNet's treatment of the Dalrymple battery project. This project is a large-scale battery that is connected to the grid to provide regulated network services that is also providing competitive market services. It is connected to ElectraNet's Dalrymple substation. The network service provided by the battery is improved reliability for the southern Yorke Peninsula when transmission supply is lost, and also a fast frequency response to reduce Heywood interconnector constraints and improve power system security by quickly injecting power into the grid. So that capacity or capability not required for prescribed transmission services is not wasted, the TNSP in this case has leased the market facing operation of the plant to an independent third party. This third party (AGL), can then sell this storage in the energy and FCAS markets. This model ensures that TNSPs can efficiently implement network services, allows customers to benefit from the revenue stream from the leasing arrangement, while protecting the integrity of competitive markets. Energy Networks Australia requests that the AER confirm that this approach adequately addresses potential harms to competition.

## Other contestable electricity services

The AER has sought views on what arrangements are needed for any other potential contestable electricity services offered by TNSPs. The AER referred to services such as consulting services, microgrids and testing services that are currently offered by TNSPs.

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<sup>4</sup> Or, alternatively, it may be more efficient to construct an asset that provides the network need and also has capacity to provide competitive electricity services. In addition, the network need may be projected to increase over time, in which case there may be a need for spare capacity for a period that is able to be used to provide competitive electricity services.

<sup>5</sup> Or, if the asset is intentionally built with spare capacity, customers may be better off as a consequence of the larger asset being installed and the cost allocation / shared asset arrangements being applied.

Contestable services offered by TNSPs arise infrequently, are bespoke, tend to be closely related to core network services in function, and are provided for large and sophisticated customers. These factors mean that incumbent TNSPs tend to be an important supplier of services to customers in the market, although the value of the services is comparatively low. In this context, the existing competition law provisions along with cost allocation measures are sufficient to address any concerns about the proper operation of these markets. Ring-fencing these services further would be particularly onerous relative to the value of the services such that it would mean that for some TNSPs it would be uneconomic to continue to provide these services. This means customers would no longer have access to a well-resourced and expert service provider, it would also reduce the overall number of supply options available to customers.

The table below considers the other electricity services identified by the AER in its Discussion Paper. It sets out the key features of the service, potential harms, and how the existing arrangements already protect against those potential harms. The implication being that additional ring-fencing provisions are unnecessary and likely to be harmful to the interests of customers overall.

**Table 1: Mitigants against competitive harms for other contestable electricity services**

Service	Potential Harm	Mitigant
<p><b>Consulting services</b></p> <ul style="list-style-type: none"> <li>» Advice on network information that can facilitate connection applications</li> <li>» Infrequent and low value services</li> <li>» Adjacent to other prescribed network services but provided on an 'at request' basis</li> <li>» Not a service for the supply of electricity</li> </ul>	<ul style="list-style-type: none"> <li>» Access to information before the 'market'</li> <li>» Access to confidential information</li> <li>» Cross-subsidy from regulated services</li> </ul>	<ul style="list-style-type: none"> <li>» Confidentiality provisions in existing framework</li> <li>» Non-confidential information already published or available to any party upon request</li> <li>» Current robust cost allocation framework in the Rules</li> <li>» Competition law</li> </ul>

<p><b>Micro-grid</b></p> <ul style="list-style-type: none"> <li>» A 'behind the meter' service where supply is offered independent of the main grid</li> <li>» Potential to remain connected to broader grid and sell generation to the wholesale market</li> </ul>	<ul style="list-style-type: none"> <li>» Access to information before the 'market' to assist in optimising the investment in the microgrid</li> <li>» Real-time information on network congestion</li> </ul>	<ul style="list-style-type: none"> <li>» Real-time information is already public or available from AEMO</li> <li>» Confidentiality provisions in existing framework</li> <li>» Non-confidential information already published or available to any party upon request</li> </ul>
<p><b>Testing services</b></p> <ul style="list-style-type: none"> <li>» Technical advice and support (eg insulation testing)</li> <li>» Condition monitoring</li> <li>» Not a service for the supply of electricity</li> </ul>	<ul style="list-style-type: none"> <li>» Cross-subsidy of competitive activities through regulated services</li> </ul>	<ul style="list-style-type: none"> <li>» Current robust cost allocation framework in the Rules</li> </ul>

## Negotiated transmission services are monopoly services and no ring-fencing is required

Energy Networks Australia supports the AER's view that negotiated transmission services should be treated in the same way as prescribed transmission services. Unlike for distribution, TNSPs remain the monopoly provider of negotiated transmission services. The classification of these services reflects the sophisticated nature of the customers served and the fact that the costs associated with the services can be directly attributed to specific customers.

Given negotiated transmission services remain monopoly services there is no justification for the ring-fencing of resources from other monopoly services, namely, prescribed transmission services. As such, any limits on the ability for TNSPs to share resources would serve only to increase the cost to customers of providing services with no additional benefit.

## Non-electricity services

TNSPs may provide services other than electricity services including telecommunications services or property services not related to the delivery of electricity services. These are services that are not for the supply of electricity, or that are necessary or incidental to the supply of electricity and are not transmission services or distribution services. Further, they also have industry specific legislation

that applies to the operation of the respective markets, for instance, the *Telecommunications Act 1996*, and oversight by sector specific regulators where needed. As indicated by the AER, there is limited scope for TNSPs to provide a discriminatory advantage with respect to these services. Therefore, other than for cost allocation, there is no role for the ring-fencing guideline with respect to these services.

The provision of contestable services by TNSPs should be encouraged given they enable benefits to be delivered to regulated customers. This is because they may allow some costs to be allocated outside of regulated services or for the shared asset arrangements to work to reduce customer bills.

# Response to AER Questions

This section responds to the specific questions that were raised by the AER in its Discussion Paper.

Table 2: Response to specific questions raised by the AER

AER Question	Energy Networks Australia Response
<b>Q1: Are the objectives and aims in the Electricity Distribution Ring-fencing Guideline relevant to transmission ring-fencing</b>	The aims and objectives the AER specified for the DNSP ring-fencing guideline are appropriate for TNSPs. Importantly, however, adopting consistent aims between transmission and distribution does not mean that ring-fencing measures should be applied in the same way. To that end, Energy Networks Australia supports the AER for seeking to only achieve consistency between distribution and transmission when it is needed and economically efficient. In practice, this means not simply adopting distribution arrangements without proper regard to the real differences between each of the networks and a demonstrated evidence-based need.

**Q2: What issues should we consider in our review with respect to non-regulated electricity services provided by TNSPs?**

The AER needs to ensure its analysis is focused on the specifics of TNSPs, how they operate, the broader market and the associated regulatory framework. It is important to be clear about the specific harms that could emerge for the provision of electricity services due to the TNSPs also providing prescribed transmission services. In doing so, it is necessary to recognise that a TNSP having an advantage due to its scale or experience is not something where ring-fencing is required, this merely reflects its characteristics as a competitor. As identified above, a key task is to identify what existing arrangements exist to protect against harms, noting these may include Rule obligations or competition law provisions. It is only where gaps exist that further consideration of ringfencing options is necessary.

In addition, it is important that the analysis also consider the indirect costs that can arise through onerous ring-fencing arrangements being imposed for contestable electricity services. This is particularly relevant in transmission where contestable services are frequently adjacent to monopoly services and may arise infrequently. In this case onerous ring-fencing measures may make the provision of such services subscale, and possibly encourage the local TNSP to withdraw from provision (and so reduce competition). The consequence would be higher prices for customers.

**Q3: With respect to non-electricity services provided by TNSPs, what issues should we consider in our review of transmission ring-fencing?**

As stated by the AER, there is limited scope for TNSPs to provide a discriminatory advantage in competing to provide non-electricity services. The current cost allocation arrangements, as applied by the businesses, and shared asset rules have proven adequate to address the issues associated with the provision of non-electricity services and there is no need for any additional ring-fencing measures.

The AER needs to ensure that any actions taken do not limit the use of existing resources to provide non-electricity services noting that the use of these resources delivers benefits to customers, namely through the application of the shared asset guideline and cost allocation arrangements.

**Q4: To prevent harm from cross-subsidies, can we rely on the TNSPs' application of cost allocation methods and audits of annual financial reports to the AER?**

The current TNSP arrangements, as implemented by the businesses, are adequate and have proven successful in addressing potential harms from cross-subsidy. The cost allocation methods currently applied by the TNSPs adopt the same cost allocation principles and methodology across all activities (i.e. this includes transmission and non-transmission activities) undertaken by the licenced transmission business. Therefore, the AER needs to demonstrate a failure with the existing arrangements before making a change given any change will impose additional costs onto TNSPs and consumers.

**Question 5: Should we align measures to prevent cross subsidies in transmission with the Electricity Distribution Ring-fencing Guideline?**

Refer to the response to Question 4 in terms of cost-allocation measures. In terms of legal separation more generally, changing the current legal status of entities currently within the TNSP legal entity has the potential to impose costs that outweigh the benefits. There is the possibility that material tax effects emerge from any requirements imposed to move existing activities out of the TNSP legal entity and into a separate legal entity. Further, it may trigger costly compliance costs through the need to have new entities establish new commercial agreements, licences and other regulatory obligations. In the first instance, Energy Networks Australia recommends the current legal separation arrangements, including the 5% threshold be retained. Further, this threshold should be broadened to include any devices that may provide incidental market facing services.

Where the AER identifies there is a case for separation of legal entities Energy Networks Australia believes there is a good case for transitional arrangements to apply, particularly given the cost, staffing, legal issues and potential tax implications. For instance, requirements for separate legal entities should be done on a prospective basis only.

**Q6: The NER allows the AER to ring-fence prescribed services from any other service provided by the TNSP. For ring-fencing purposes, should negotiated services be treated as if they were prescribed services?**

Yes, negotiated transmission services are monopoly services and there is no justification for them to be ring-fenced from prescribed transmission services.

**Q7: In what ways could a TNSP discriminate in favour of part of the business or an affiliate providing non-regulated transmission services? To what extent does TCAPA address these harms?**

Energy Networks Australia strongly support the AER's preliminary view that the TCAPA address any potential harms with respect to contestable connection services, recognising that these are the main contestable transmission service provided by TNSPs. To impose additional arrangements would put at significant risk the expected efficiency outcomes sought by the AEMC in designing the regime.

To the extent that any gaps are identified by the AER or stakeholders these should be addressed through a rule change rather than through the ring-fencing guidelines in order to ensure the Rules provide a comprehensive and consistent framework.

In terms of any other contestable transmission service that might be offered by a TNSP, Energy Networks Australia supports the AER's view that such services are very limited and with limited scope for competition. Ring-fencing that precluded the sharing of resources to provide these services would not be in the interests of customers as it would mean valuable expertise is lost to the market and potentially see TNSPs withdraw entirely from providing the service given their relatively low value.

**Q8. Should staff, office or branding restrictions be applied where a TNSP affiliated entity provides generation and retail services?**

Energy Networks Australia requests that the AER confirms what is believed to be a shared understanding that ownership of generation and storage for the purpose of network support is a prescribed transmission service and can be undertaken by the TNSP legal entity without any functional separation. As identified in the main body of this submission, Energy Networks Australia considers that ElectraNet's treatment of the Dalrymple substation battery project is one example of a good case study for how the framework is intended to operate.

**Q9: The current Guideline permits a TNSP to carry on a 'related business' if it earns revenue of less than or equal to 5 per cent of the TNSP's total annual revenue. Should this be retained in a new transmission Guideline?**

See response to Question 5. Energy Networks Australia believes that, in the absence of evidence that any investments TNSPs have undertaken within this threshold have caused harm, the current threshold should be retained, noting that robust cost-allocation arrangements exist to address any cross-subsidy concerns. Further, it is reasonable also for the threshold to be extended or to be made more flexible so that it includes any devices a TNSP may use that can also provide incidental market facing services. A requirement for separation would impose material compliance costs due to the need to have new entities registered and licenced in the NEM and with State based authorities. This is an unnecessary cost burden and so not in the long-term interests of consumers.

**Q10: What ring-fencing controls (if any) should apply to TNSPs participation in new and emerging contestable electricity services? Can you provide some examples of TNSPs delivering these kinds of services, and any associated harms (or benefits)?**

As identified in the main body of this submission, there are limited other contestable electricity services offered by TNSPs beyond connection services. For those services that are provided the potential harms are immaterial. If the services leverage off the transmission network competition law protections are expected to provide meaningful protection against anti-competitive behaviour.

With respect to the two examples cited by the AER, battery leasing and a microgrid, any potential harms that are relevant to ring-fencing are expected to be addressed either through current ring-fencing arrangements, current Rules arrangements and / or competition law requirements. Further, with respect to microgrids it is not clear that this would be defined as electricity services if defined in the same way as in distribution, and so would fall outside the scope for concern of the ring-fencing guidelines. To the extent other issues remain these should be addressed directly in the Rules in the same way as contestable connection services.

Importantly, the AER should not seek to create ‘catch-all’ provisions in the ring-fencing guidelines for potential, but unknown, contestable activities as this would risk overly onerous arrangements being created that only increase costs for customers.

If and when a substantial new contestable activity emerges in the future that brings with it competition concerns, this is best addressed in the same manner as the connection arrangements, namely through changes to the National Electricity Rules (NER).

**Q11: Are there particular aspects of the COGATI reforms and other reforms affecting transmission we should take into consideration in developing a new transmission ring-fencing guideline?**

The Coordination of Generation and Transmission Investment (COGATI) framework, as well as the expected actionable ISP arrangements, have the potential to require TNSPs to provide new services, undertake new functions or preclude TNSPs from providing services in particular ways. The TCAPA demonstrated an appropriate way of managing such changes for transmission. The AER should not attempt to second guess the outcomes of these processes, or what it may end up implying for how services are provided. Instead, the Rules should first be used to ensure the stable management of the power system through the significant transformation being experienced and the efficient delivery of the services. To the extent that there are perceived gaps remaining, these should be addressed through rule changes rather than ring-fencing guidelines to ensure a consistent approach is taken in the transmission framework.

<p><b>Q12: Is regular compliance reporting and independent assessment of compliance with transmission ring-fencing required?</b></p>	<p>Consistent with the views in this submission, Energy Networks Australia contends that the transmission ring-fencing arrangements should be consistent with current arrangements and so not overly complex to administer. Therefore, the reporting and compliance arrangements need to be fit-for-purpose. Imposing onerous compliance and reporting arrangements onto TNSPs would likely introduce substantial new costs without a corresponding benefit. Relevantly, under the existing arrangements the AER retains the capacity to require compliance reporting at any time and this requirement can be invoked when necessary.</p>
<p><b>Q13: Should we adopt a similar approach to waivers for transmission?</b></p>	<p>Implicit in the current guideline is an evergreen waiver option. This is appropriate given transmission services are clearly defined and so stable over time. If a change was made such that waivers could be revoked at any time, or were time limited, this would impact on staff resourcing, services and costs, which will ultimately impact on customers. Therefore, Energy Networks Australia advocates that the current waiver requirements for transmission be retained.</p>
<p><b>Q14: What factors should the AER consider in determining a reasonable transition period?</b></p>	<p>The duration of the transitional period depends on the extent of changes that TNSPs are required to make to their operations. If the changes are limited to refining the transmission guidelines to update the terminology and modernise how obligations are specified a shorter transition period is reasonable.</p> <p>However, as noted by the AER in its Discussion Paper, the profile of a TNSP's workforce tends to be smaller and more specialised than for distribution. This means that significant ring-fencing changes can have material effects on the operations of TNSPs. In particular, it may require new staff to be hired and new teams formed where a ring-fence is placed in the middle of the functions of certain staff. Further, it may prompt consideration of whether some services continue to be provided by the TNSP at all. These are not actions that can occur quickly. In this case a longer transition period would be justified.</p> <p>Energy Networks Australia supports waivers to extend the transition period in specific situations should the AER choose to impose a short transition period.</p>