

REVIEW INTO EXTENDING THE REGULATORY FRAMEWORKS TO HYDROGEN AND RENEWABLE GASES

RING FENCING AND ASSOCIATE CONTRACT WORKSHOP

AEMC
28 JUNE 2022

AEMC

Acknowledgement of Country

*In the spirit of reconciliation
we acknowledge the Traditional
Custodians of country throughout
Australia and their connections to land,
sea and community. We pay our respect
to their Elders past and present and
extend that respect to all Aboriginal and
Torres Strait Islander peoples today.*

Before we start, an important notice: Compliance with Competition Law

- The attendees must not discuss, or reach or give effect to any agreement or understanding which relates to:
 - Pricing
 - Targeting markets or customers
 - Tendering processes
 - Boycotting other parties
 - Sharing competitively sensitive information
 - Breaching confidentiality obligations

Each entity must make an independent and unilateral decision about their commercial positions.

Workshop arrangements

- Today's workshop is not being recorded
- The workshop will be a mix of open room discussion and breakout rooms
 - For those sessions with breakout rooms, please save your questions for the breakout rooms
- Presentation from today will be posted on our website after the workshop
- Please engage respectfully

Agenda

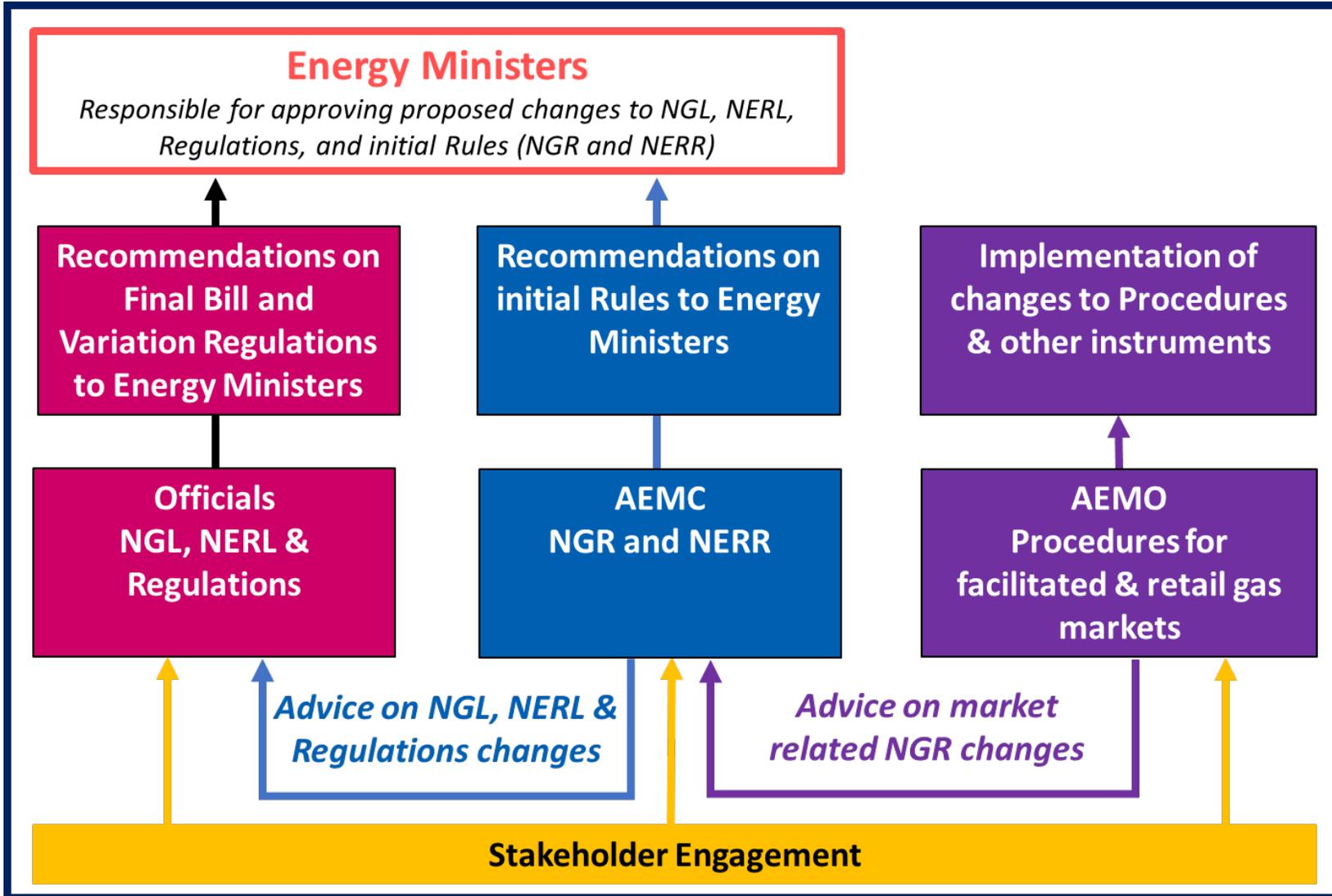
	Time (AEDT)	Item	Time
1.	1:00 PM	Introduction, context and background	10 minutes
2.	1:10 PM	Associate contract arrangements	20 minutes
3.	1:30 PM	Breakout session 1	25 minutes
4.	1:55 PM	Ring fencing arrangements	20 minutes
5.	2:15 PM	Breakout session 2	25 minutes
6.	2:40 PM	Ring fencing orders and consultation process for variations/revocations	15 minutes
8.	2:55 PM	Wrap up and next steps	5 minutes

CONTEXT AND BACKGROUND



Overview of current work

National gas and retail regulatory frameworks



Jurisdictional legislation

All jurisdictions

Responsible for amending their own legislative instruments to ensure that:

- they can accommodate hydrogen and renewable gas blends
- they can accommodate the changes to be made to the national framework.

Vic, NT, Tas & WA

Responsible for amending jurisdictional consumer protection legislation.

What advice did the AER provide on the associate contract and ring fencing provisions?

AER advice		Responsibility	
Associate contract arrangements	Associate contract approval process	Require service providers to obtain <i>ex ante</i> approval of associate contracts of a certain class or kind	AEMC
		Place the onus on service providers to demonstrate an associate contract will not have an anti-competitive effect or breach the competitive parity rule	AEMC
		Extend the timeframe within which regulator must make its decision and/or introduce a stop-the-clock provision if regulator requests further information	AEMC
	Competitive parity rule	Provide more guidance on the competitive parity rule	AEMC
Ring fencing arrangements	Exemptions from the minimum ring-fencing requirements	Provide for greater regulatory discretion for exemptions from minimum ring fencing requirements through changes to the minimum ring fencing exemption criteria	AEMC
		Provide for class exemptions from the minimum ring fencing requirements	AEMC
		Allow the regulator to impose conditions on minimum ring fencing exemptions	Officials/AEMC
	Additional ring-fencing requirements	Allow the regulator to issue a class ring fencing order for additional ring fencing requirements	Officials/AEMC
	Consultation process	Provide the regulator with greater discretion to determine level of consultation for varying or revoking additional ring fencing requirements or exemptions	AEMC

Current ring fencing framework

The NGL and NGR currently include tools to address the risks posed by vertically integrated pipelines, including:

- **Ring fencing provisions:**

- Service providers are subject to the following **minimum ring fencing requirements**, unless they obtain an **exemption** from the regulator under the NGR:
 - service providers are prohibited from carrying on a related business of producing, purchasing or selling natural gas or processable gas unless necessary for the safe and reliable operation of the pipeline, or for balancing.
 - service providers must ensure marketing staff are not shared with an associate that takes part in a related business.
 - service providers are required to prepare, maintain and keep separate accounts.
- Individually named service providers and associates can also be subject to additional ring fencing requirements if the regulator makes a ring fencing determination.

- **Associate contracts provisions:**

- Service providers are subject to the associate contract provisions, which prohibit service providers from entering into or giving effect to contracts with an associate in relation to pipeline services that:
 - have an anti-competitive effect unless approved by the regulator under the NGR; or
 - are inconsistent with the competitive parity rule (i.e. the service provider must treat an associate as if it were a 'separate unrelated party'), unless approved by the regulator under the NGR.

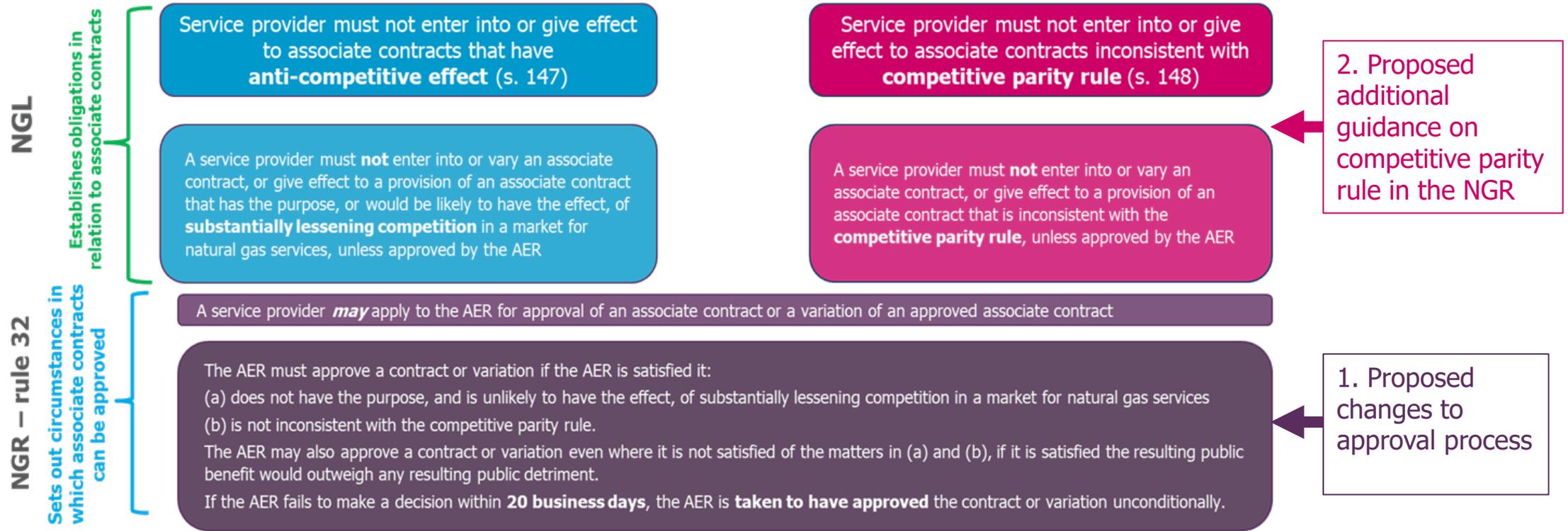
- **Confidential information:**

- Service providers of scheme pipelines are prohibited from disclosing confidential information provided by users, and from using it for a purpose other than for which it is given.

ASSOCIATE CONTRACT ARRANGEMENTS



What changes did the AER propose to the associate contract arrangements?



* An associate contract is defined in the NGL as

(a) a contract, arrangement or understanding between a service provider and an associate of the service provider in connection with the provision of an associate pipeline service; or

(b) a contract, arrangement or understanding between a service provider and any person in connection with the provision of an associate pipeline service—

(i) that provides a direct or indirect benefit to an associate; and

(ii) that is not at arm's length.

An associate pipeline service is defined as a pipeline service provided by means of a pipeline other than a pipeline to which a greenfields incentive determination applies.

The competitive parity rule is the rule that a pipeline service provider must ensure that any pipeline services that the pipeline service provider provides to an associate of the pipeline service provider are provided to that associate as if that associate were a separate unrelated entity

1. Associate contract approval process: Contracts to be approved

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested that associate contracts of a certain class or kind be submitted to the regulator for approval before the contract is entered into.</p> <p>The intention of such a power would not be to require all associate contracts to be pre-approved, but rather it would focus on those contracts that pose a high risk of contravening the NGL.</p>	<p>Stakeholders were divided on this proposal.</p> <p>Retailers stated that ex ante approval should be required for contracts presenting the greatest risk, which they stated were contracts with associates operating in contestable (or potentially contestable) parts of the market.</p> <p>In contrast, pipeline service providers believe the current framework is fit for purpose and the proposed change would give rise to additional costs.</p>	<p>Our preliminary position is to:</p> <ul style="list-style-type: none"> • require ex-ante approval for contracts with associates operating in contestable parts of the market • specify an initial list of types of contracts to be subject to ex ante approval in the NGR and to allow this list to be added to by the regulator through a guideline, with the initial list including contracts with associates involved in: <ul style="list-style-type: none"> • the production, purchase or sale of covered and/or processable gases • the provision of blend processing services by means of a blend processing facility • for associate contracts not requiring ex ante approval, service providers should include a description of why the contract does not breach the associate contract provisions in the NGL when providing the contract to the regulator. <p>Reasons for the preliminary decision: We consider that the current rules do not effectively deal with the risks associated with service providers contracting with their associates.</p>

Questions

1. Do you agree with the preliminary position, or have alternative suggestions?
2. Do you agree with the specification of the initial list of contracts to be included in the NGR?

1. Associate contract approval process: Change in onus

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested amending rule 32(2) to change the onus of demonstrating that an associate contract complies with the NGL and allowing the regulator to request further information when assessing these contracts.</p>	<p>Retailers supported the change and noted regulators can face significant information asymmetries in this type of assessment.</p> <p>AGIG and APA claimed that the onus already sits with the service provider.</p> <p>AusNet think the onus should remain with the regulator.</p>	<p>Our preliminary position is to amend rule 32(2) as suggested by the AER to:</p> <ul style="list-style-type: none">• place the onus on service providers to demonstrate an associate contract will not breach the anti-competitive effects or competitive parity rule in the NGL• only require the regulator to approve an associate contract if the service provider has demonstrated to the regulator’s reasonable satisfaction that it will not breach the NGL• allow the regulator to request further information from the service provider if required. <p>Reasons for the preliminary position: The service provider is better placed than the regulator to demonstrate compliance with the NGL, given the significant information asymmetries the regulator can face in this regard.</p>

Questions

Do you agree with the preliminary position, or have alternative suggestions?

1. Associate contract approval process: Decision timeframe

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested that:</p> <ul style="list-style-type: none"> the time for making an associate contract decision be extended; and/or a stop-the-clock provision be included to allow the decision-making time to be extended if the regulator requests further information. 	<ul style="list-style-type: none"> Retailers and a number of pipeline service providers supported providing the regulator more time to make an associate contract decision, with some suggesting it be extended by 20 days. A number of these stakeholders also supported the implementation of a stop-the-clock provision. However, some service providers claimed this could 'impede investment decisions' if it resulted in a protracted decision-making process. Only two service providers were opposed to the change, one of whom stated the rules do not 'force' a decision in 20 days. 	<p>Our preliminary policy position is to:</p> <ul style="list-style-type: none"> replace 20 business days with 40 business days include a stop-the-clock provision that can be triggered if a regulator requests information <p>Reasons for the preliminary position:</p> <p>We consider that 20 business days is an insufficient amount of time to determine whether or not an associate contract is likely to breach the competitive parity rule and/or anti competitive effects provisions in the NGL</p> <p>In our view, the concerns raised about the risk of a stop-the-clock provision could be mitigated if service providers provide the regulator all the information it requires to make an informed decision upfront. This could be facilitated by the regulator publishing a guide on the information to be provided and the process to be followed.</p>

Questions

- Do you agree with the preliminary position, or have alternative suggestions?
- Do you think the rules should require the regulator to publish a guide that sets out the information to be provided and the process to be followed for associate contract decisions?

2. Competitive parity rule

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested greater guidance on the application of the competitive parity rule be provided for in the NGR.</p> <p>It has suggested this be done by including a new rule that requires service providers, in dealing with associates, to:</p> <p>A. Treat the associate on an arm’s length basis B. In like circumstances: <ul style="list-style-type: none"> ▪ deal or offer to deal with an associate and its competitors on substantially the same terms ▪ provide substantially the same quality, reliability and timeliness of service to an associate and its competitors C. not disclose information from dealings with a competitor.</p>	<p>Retailers stated there would be benefit in providing greater guidance on the matters the regulator should consider when assessing whether the competitive parity rule has been complied with.</p> <p>Pipeline service providers did not see the need for any additional guidance. Some service providers also stated that the matters identified by the AER did not provide any additional clarity relative to what is already provided for in the NGL.</p>	<p>Our preliminary position is to:</p> <ul style="list-style-type: none"> • not provide more guidance on the competitive parity rule in the NGR • extend rule 137, which requires scheme pipelines to maintain confidentiality, to non-scheme pipelines. <p>Reasons for the preliminary position:</p> <p>Competitive parity rule: There is a risk that providing more guidance in the NGR on the competitive parity rule could inadvertently narrow its intended operation.</p> <ul style="list-style-type: none"> • Rule 137: Prohibiting service providers from disclosing confidential information is a key element of the ring fencing framework that currently only applies to scheme pipelines, but should also apply to non-scheme pipelines.

- Questions**
1. Do you agree with the preliminary position on the competitive parity rule, or have alternative suggestions?
 2. If you think the NGR should provide more guidance on the competitive parity rule, what do you think the benefits would be of doing so?
 3. Do you agree with the proposed extension of rule 137 to non-scheme pipelines?

Associate contract arrangements: Breakout room questions

Associate contract approval process: Contracts to be approved

1. Do you agree with the preliminary position to:
 - require ex-ante approval for contracts with associates operating in contestable parts of the market?
 - specify an initial list of types of contracts to be subject to ex ante approval in the NGR and to allow this list to be added to by the regulator through a guideline, with the initial list including contracts with associates involved in:
 - (a) the production, purchase or sale of covered and/or processable gases
 - (b) the provision of blend processing services by means of a blend processing facility?
 - for associate contracts not requiring ex ante approval, service providers should include a description of why the contract does not breach the associate contract provisions in the NGL when providing it to the regulator?
2. Do you agree with the specification of the initial list of contracts to be included in the NGR?

Associate contract approval process: Change in onus

1. Do you agree with the preliminary position to amend rule 32(2) as suggested by the AER to:
 - a. place the onus on those service providers that are required to submit their contracts for review (or that voluntarily decide to do so) to demonstrate an associate contract will not breach the anti-competitive effects or competitive parity rule in the NGL?
 - b. only require the regulator to approve an associate contract if the service provider has demonstrated to the regulator's reasonable satisfaction that it will not breach the NGL?
 - c. allow the regulator to request further information from the service provider if required?

Associate contract arrangements: Breakout room questions

Associate contract approval process: Decision making time frames

3. Do you agree with the proposal to allow the regulator 40 business days to make a decision on associate contracts and to include a stop-the-clock provision?
4. Do you think the rules should require the regulator to publish a guide that sets out the information to be provided and the process to be followed for associate contract decisions?

Competitive parity rule

5. Do you agree with the preliminary position on the competitive parity rule, or have alternative suggestions?
6. If you think the NGR should provide more guidance on the competitive parity rule, what do you think the benefits would be of doing so?
7. Do you agree with the proposed extension of rule 137 to non-scheme pipelines? This rule states that:

(1) *A scheme pipeline service provider must not:*

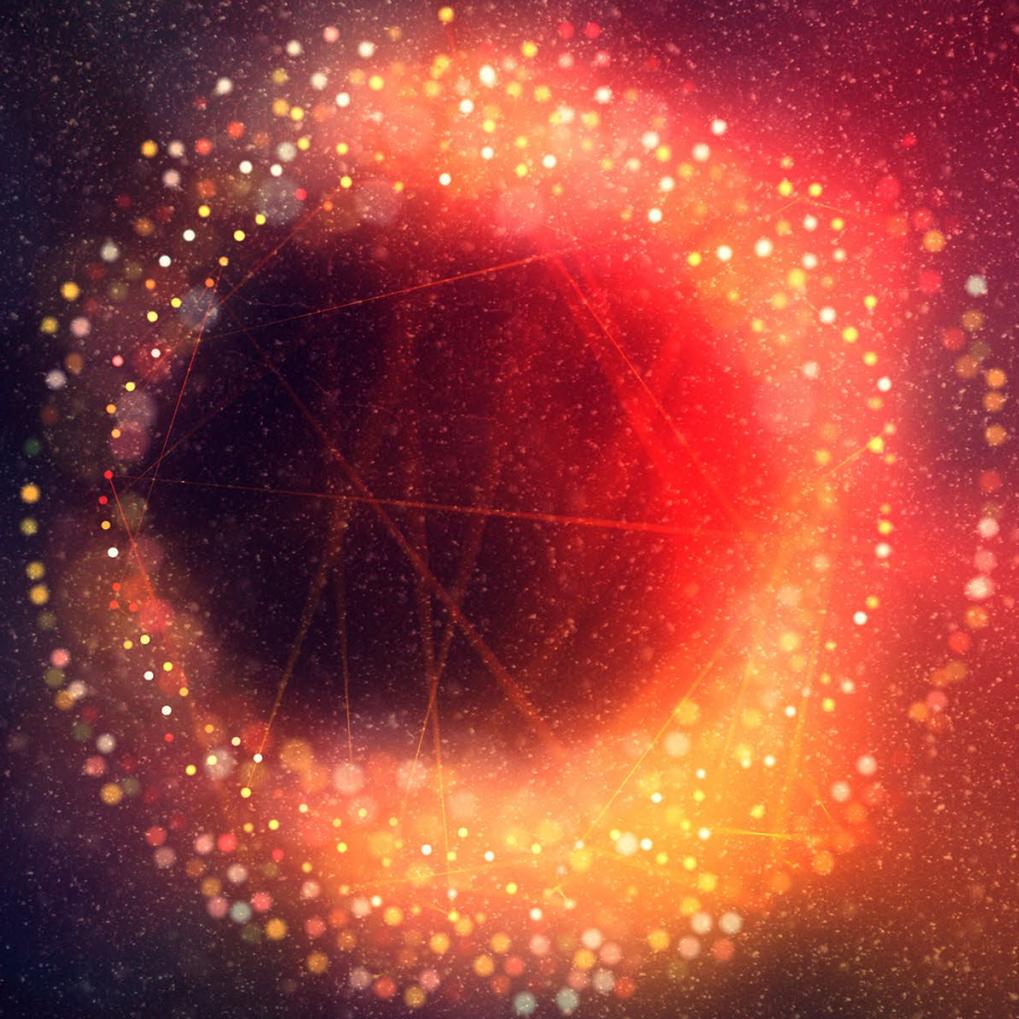
(a) disclose relevant confidential information; or

(b) use relevant confidential information for a purpose other than the purpose for which the information was given to the service provider.

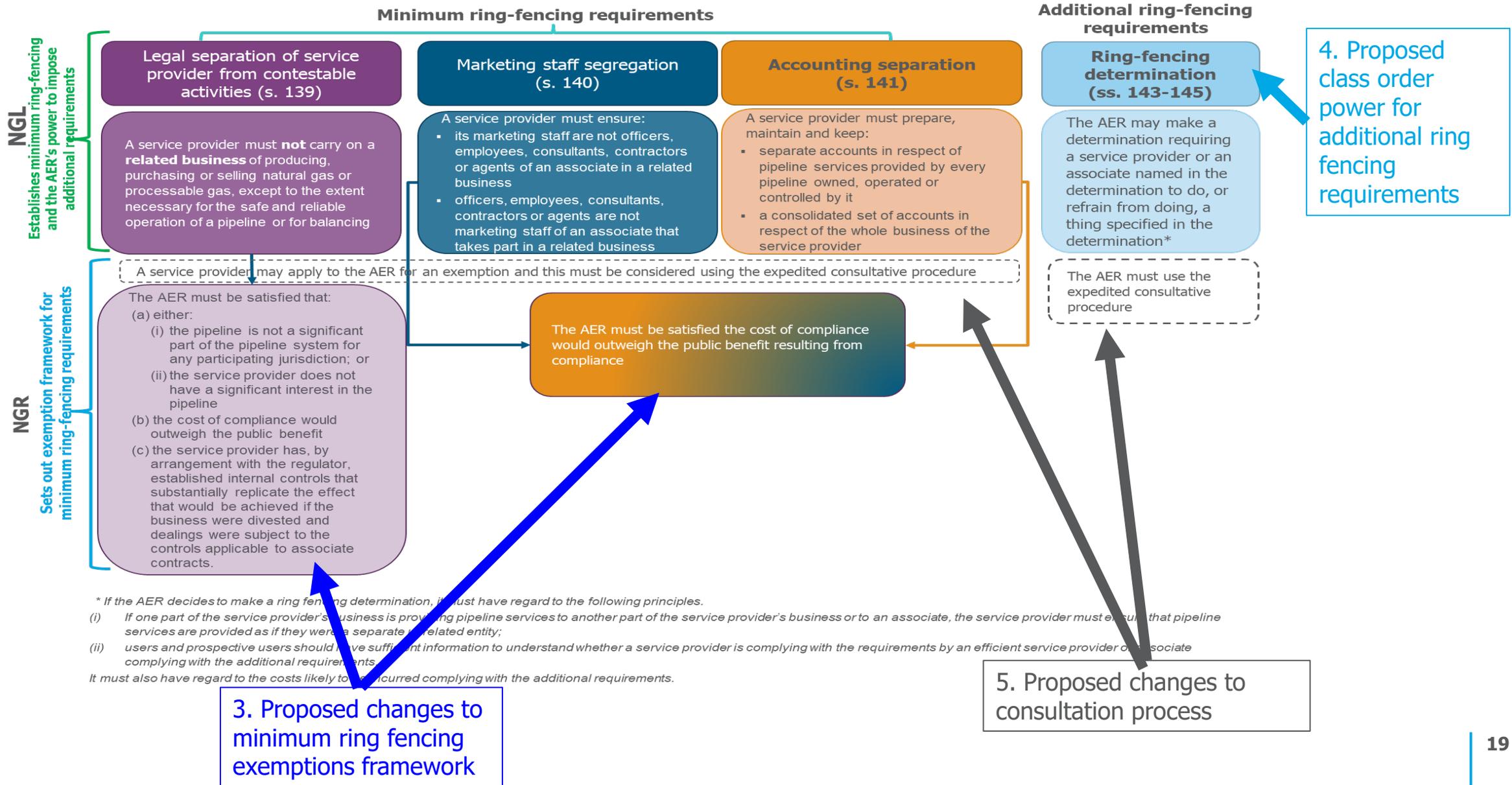
(2) *A scheme pipeline service provider must take all practicable steps to protect relevant confidential information in the service provider's possession against improper disclosure or use.*

It also sets out a number of exceptions to these requirements (e.g. where information is already in the public domain, or where disclosure is required or authorised under the NGL or NERL)

RING FENCING



What changes did the AER propose to the ring fencing arrangements?



3a. Minimum ring fencing exemption framework: Exemption criteria

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested greater discretion for the regulator to grant exemptions from the minimum ring fencing requirements.</p> <p>It suggested this be achieved by replacing the current criteria with similar criteria to what apply in electricity distribution, with the regulator to consider:</p> <ul style="list-style-type: none"> • whether an exemption would better achieve the NGO • the potential for cross-subsidisation or discrimination • the costs to service providers and the benefits to consumers • the effect on competition • other matters the regulator considers relevant. 	<p>Pipeline service providers supported the change because they believe it will provide greater flexibility to deal with market changes. A number also noted it would bring the exemption framework into line with electricity.</p> <p>Retailers and other stakeholders were opposed to the change, stating the case had not been made for such a material change and that:</p> <ul style="list-style-type: none"> • effective ring fencing was required to promote the development of competition in contestable parts of the market, which is in the long-term interests of consumers • greater discretion could result in divergence of regulatory outcomes and make it harder for market development. <p>Alinta noted that if the current criteria are maintained, rule 31(3)(c) should be amended because it appears to require full ring fencing</p>	<p>Our preliminary position is:</p> <ul style="list-style-type: none"> • Not to provide for greater discretion in this area, but if it becomes clear in the future that it would be in consumers’ interests to provide for this, it could be considered through a rule change process. • Amend rule 31(3)(c) to clarify that its intent is not to require full ring fencing. Rather, its intent is to require a service provider that obtains an exemption and is itself using the pipeline, to put in place arrangements that give effect to the associate contract requirements. <p>Reasons for preliminary position:</p> <ul style="list-style-type: none"> • We are concerned that greater discretion could result in a relaxation of the minimum ring fencing requirements, which could adversely affect competition and consumers. • Although analogies have been drawn with the ring fencing that applies to electricity distribution, the starting point for ring fencing in electricity is very different and there are also stronger safeguards against cross-subsidisation in electricity.

Questions

1. Do you agree with the preliminary position, or have alternative suggestions?
2. If you think greater discretion should be provided for, in what circumstances do you think it would be appropriate for the regulator to exercise this discretion?

3b. Minimum ring fencing exemption framework: Class exemptions

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested the regulator have the power to grant class exemptions from the minimum ring fencing requirements.</p>	<p>Most stakeholders, including a number of pipelines, opposed the AER’s suggestion because:</p> <ul style="list-style-type: none"> • they are concerned about the risk of regulatory error (i.e. the risk an exemption is granted when it shouldn’t be resulting in competition in and consumers being adversely affected) • they do not think there is a demonstrated need for class exemptions at this time. <p>In contrast, there were a small number of pipelines who thought class exemptions would provide for greater flexibility and efficiency in the framework.</p>	<p>Our preliminary position is not to provide for class exemptions now, but if it becomes clear in the future that there is a need for them, it could be considered through a rule change process.</p> <p>Reasons for preliminary position:</p> <ul style="list-style-type: none"> • We are concerned about the risk of regulatory error, which cannot easily be mitigated. • The circumstances in which this power would be used are unclear. For example, it is unclear in what circumstances it would be appropriate to allow a class of service providers to: <ul style="list-style-type: none"> • produce, process or purchase gas • not comply with the accounting separation and/or marketing staff segregation requirements.

Questions

1. Do you agree with the preliminary position, or have alternative suggestions?
2. If you think class exemptions should be allowed, in what circumstances do you think this power should be used?

3c. Minimum ring fencing exemption framework: Conditions on exemptions

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested that the NGR be amended so that it can impose the following types of conditions on exemptions, where appropriate:</p> <ul style="list-style-type: none"> • a time limit, a scope limit and/or a volumetric limit • a requirement that service providers divest assets at the expiration of the exemption • a requirement that trial findings be published. 	<p>There was broad support for this suggestion. The majority of stakeholders also supported our draft report suggestions that the NGR:</p> <ul style="list-style-type: none"> • require service providers to immediately notify the AER if conditions change, such that it no longer qualifies for an exemption • clarify the power the regulator has to revoke an exemption and to vary conditions • require a register of exemptions and additional ring fencing requirements to be maintained. <p>There was also some support for the proposal to require exemptions to include a review or expiration date, although some pipelines noted an expiry date may not always be appropriate.</p>	<p>Our preliminary position is to amend the ring fencing exemption framework in the NGR to:</p> <ol style="list-style-type: none"> allow the regulator to impose conditions on minimum ring fencing requirements require service providers to notify the regulator if they no longer qualify for an exemption specify a review date (but not an expiration date) for exemption decisions clarify the right the regulator has to revoke an exemption and to vary conditions require the regulator to maintain a register of exemptions and additional requirements and for this to also be on the pipeline register. <p>Reasons for preliminary position: The proposed changes will provide more clarity on the operation of any ring fencing exemptions that are granted. They will also bring the exemption framework into line with other exemption frameworks in the rules.</p>

- Questions**
1. Do you agree with the preliminary position, or have alternative suggestions?
 2. Are there any other matters that you think should be clarified in relation to conditions or the matters in (b)-(e)?

Breakout room questions for minimum ring fencing exemption framework

1. Exemption criteria:

- a. Do you agree with the preliminary position not to provide for greater discretion in the exemption criteria?
- b. If you think greater discretion should be provided for, when do you think it would be appropriate to exercise this discretion?
- c. Do you agree with the proposal to amend rule 31(3)(c) to clarify that the intent is not to require full ring fencing. Rather, the intent is to require a service provider that obtains an exemption and is itself using the pipeline, to put in place arrangements that give effect to the associate contract requirements?

This rule currently states the following:

"the service provider has, by arrangement with the AER, established internal controls within the service provider's business that substantially replicate, in the AER's opinion, the effect that would be achieved if the related business were divested to a separate entity and dealings between the service provider and the entity were subject to the controls applicable to associate contracts".

2. Class exemptions:

- a. Do you agree with the preliminary position not to provide to provide for class exemptions?
- b. If you think class exemptions should be provided for, when you think it would be appropriate for the regulator to use this power?

3. Conditions on exemptions:

- a. Do you agree with the preliminary position to allow for conditions and to:
 - i. allow the regulator to impose conditions on minimum ring fencing requirements?
 - ii. require service providers to notify the regulator if they no longer qualify for an exemption?
 - iii. specify a review date (but **not** an expiration date) for exemption decisions?
 - iv. clarify the right the regulator has to revoke an exemption and to vary conditions?
 - v. require the regulator to maintain a register of exemptions/additional requirements and to include this on the pipeline register?
- b. Are there any other matters that you think need to be clarified in the NGR?

4. Class orders for additional ring fencing requirements

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has suggested that the NGL be amended to allow the regulator to issue a ring fencing order, so that additional ring fencing requirements can apply to a class of service providers and/or associates.</p> <p>The AER noted:</p> <ul style="list-style-type: none"> • while it could achieve the same outcome under the current framework by naming all service providers and/or associates, there is a risk that some may be missed. • a class power would enable it to address market-wide concerns more efficiently. 	<p>Most stakeholders were opposed to the suggestion to allow the regulator to make a class ring fencing order, with a number noting it could inadvertently capture service providers and associates that should not be subject to the requirements.</p>	<p>Our preliminary position is that if jurisdictional officials decide to amend the NGL to provide for ring fencing orders, then the NGR should be amended to:</p> <ul style="list-style-type: none"> • require the regulator to use the standard consultation process when making an order and the expedited consultation process when deciding whether to grant an exemption from an order. • recognise the ability of service providers to apply to the regulator for an exemption from the order • set out the criteria to be used for any individual exemptions from the order, which could be based on the exemption criteria for accounting and marketing staff separation, i.e.: <i>the cost of compliance would outweigh the public benefit resulting from compliance.</i> <p>Reasons for preliminary position: If the power to make a ring fencing order is provided for, it will be important for:</p> <ul style="list-style-type: none"> • the order to be subject to fulsome consultation before it is made • the rights service providers will have to apply for exemptions and the matters to be considered by the regulator to be made clear.

Questions

1. Do you agree with the preliminary position, or have alternative suggestions?
2. Do you agree with the exemption criteria for individual exemptions, or have alternative suggestions?

5. Consultation process for variations/revocations of exemptions from the minimum or additional ring fencing requirements

AER PROPOSAL	STAKEHOLDER FEEDBACK	PRELIMINARY POSITION
<p>The AER has proposed that the regulator have the discretion to determine the appropriate level of consultation to employ when varying or revoking an exemption from the minimum or additional ring fencing requirements.</p> <p>In doing so, the AER noted that it may not be appropriate to employ the expedited consultation procedure (as it is currently required to do) when making minor or uncontroversial variations to exemptions, or when revoking these instruments.</p>	<p>While some pipeline service providers and retailers supported the proposal, others were opposed to the change because, in their view, these types of decisions should be subject to stakeholder consultation and transparent.</p>	<p>Our preliminary position is that the concerns raised by both the AER and stakeholders could be addressed by:</p> <ol style="list-style-type: none"> 1. Allowing the regulator to employ a simpler consultation process where an amendment is required to address a clerical mistake, or omission or defect in form. <p>In such cases the regulator would be required to consult with the service provider and any other persons with whom it considers consultation would be appropriate.</p> <ol style="list-style-type: none"> 2. For other types of variations/revocations, the regulator would be required to employ the same consultation process it used to make the original decision: the expedited consultation process. <p>Reasons for preliminary position: There should be flexibility in the arrangements to deal with minor amendments (which is akin to what applies elsewhere in the rules), but for more substantive changes there should be appropriate consultation and transparency of decision-making.</p>

Questions

Do you agree with the preliminary position, or have alternative suggestions?

AEMC contact details

Review into extending the regulatory frameworks to hydrogen and renewable gases

Meredith Mayes

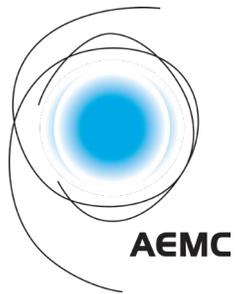
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Link to project page ([here](#))

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