



Level 2, 35 Spring St  
Melbourne 3000, Australia  
Telephone +61 3 9651 0222  
+61 1300 664 969  
Facsimile +61 3 9651 3688

## COMPLIANCE POLICY STATEMENT

FOR VICTORIAN ENERGY  
BUSINESSES

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## 1.1 Purpose

This *Compliance Policy Statement for Victorian Energy Businesses* (Compliance Policy Statement) outlines the Essential Services Commission's (the Commission's) approach to monitoring and enforcing compliance with regulatory obligations for regulated energy businesses in the Victorian market.<sup>1</sup>

This Compliance Policy Statement is to be used as a guide only. It is not intended to be legally binding. In carrying out its functions, the Commission will act in accordance with its objectives and functions as set out in the *Essential Services Act 2001* or as otherwise promulgated by Parliament.

## 1.2 Statutory powers of the Commission

The powers, functions and objectives of the Commission are set out under the *Essential Services Commission Act 2001*, *Electricity Industry Act 2000*, and *Gas Industry Act 2001*.

Section 8 of the *Essential Services Commission Act 2001* requires that in performing its functions, the Commission must have as its primary objective the protection of the long term interests of Victorian customers with regard to the price, quality and reliability of essential services; and at the same time have regard to the need:

- a. To facilitate efficiency in regulated industries and the incentive for efficient long-term investment;
- b. To facilitate the financial viability of regulated industries;
- c. To ensure that the misuse of monopoly or non-transitory market power is prevented;
- d. To facilitate effective competition and promote competitive market conduct;
- e. To ensure that regulatory decision making has regard to the relevant health, safety, environmental and social legislation applying to the regulated industry;

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<sup>1</sup> In this Compliance Policy Statement, the term 'regulated energy business' or 'regulated energy businesses' includes any holder of a retail or distribution licence issued under the *Electricity Industry Act 2000* or the *Gas Industry Act 2001*.

- f. To ensure that users and consumers (including low-income or vulnerable customers) benefit from the gains from competition and efficiency; and
- g. To promote consistency in regulation between States and on a national basis.

Sections 10 to 10B of the *Essential Service Act 2001* set out the functions of the Commission. These functions include:

- a. To perform such functions as are conferred by the *Essential Services Act 2001* and the relevant legislation under which a regulated industry operates;
- b. When requested by the Minister to do so, to conduct an inquiry into any systemic reliability of supply issues related to a regulated industry or other essential service specified by the Minister in the request;
- c. To conduct inquiries and report on matters relating to regulated industries;
- d. To make recommendations to the Minister as to whether an industry which provides an essential service should become a regulated industry or whether a regulated industry should continue to be a regulated industry;
- e. To advise the Minister in relation to any other matter referred to the Commission by the Minister; and
- f. To administer the *Essential Services Commission Act 2001*.

Section 11 of the *Essential Services Commission Act 2001* gives the Commission the power to do all things necessary or convenient to be done for or in connection with the performance of its functions and to enable it to achieve its objectives under this Act and under relevant legislation.

Subject only to the Act or as specified in other legislation, the Commission is not subject to the direction or control of the Minister in respect of any determination, report or enquiry.

### **1.3 Relationships with other organisations**

The Commission seeks to coordinate formally with other regulators to avoid duplication and to achieve more integrated decisions and outcomes.

The Commission has relationships with a number of organisations that have a role in the energy retail and/or distribution industries relevant to regulated energy businesses' compliance. These organisations include:

- Energy and Water Ombudsman (Victoria) Limited (“EWOV”)
- Consumer Affairs Victoria
- Department of Human Services
- Australian Energy Market Operator
- Australian Competition and Consumer Commission
- Australian Energy Regulator, Australian Energy Market Commission
- Office of the Minister for Energy, and
- EnergySafe Victoria

The Commission takes a coordinated approach to monitoring and enforcing regulated energy businesses' compliance. Compliance issues may be discussed with other regulatory agencies, and a lead agency may be assigned to the issue to avoid inefficiencies resulting from duplicated efforts or inconsistent approaches.

The Commission has Memoranda of Understanding with other organisations to articulate the relationships between the Commission and these organisations.<sup>2</sup>

## **1.4 Transition to national energy regulation**

The Ministerial Council on Energy (MCE) announced in 2006 that a framework for the transfer of economic regulation of distribution networks and enabling legislation to transfer national distribution and retail regulatory functions to the Australian Energy Market Commission (AEMC) and the Australian Energy Regulator (AER) was expected to be passed by 1 July 2007. Implementation of the national distribution and retail Rules was scheduled for 1 January 2008.<sup>3</sup> The Commission understands that the transfer of Victorian energy retail regulatory functions to the AER is scheduled to occur on 1 July 2012.

To facilitate the transition to the AER, therefore, the Commission has purposely developed a Compliance Policy Statement that is consistent with best practice and approaches in other jurisdictions. Against this background, it has considered the practices in comparable jurisdictions - New South Wales and South Australia - and has adopted to the extent possible the approaches in those jurisdictions.

In particular, this Compliance Policy Statement is consistent in the following key aspects:

- publication of a Compliance Policy Statement by the regulator
- provision of information on regulatory obligations by the regulator to businesses
- differentiated compliance reporting by businesses to the regulator
- acknowledgement of compliance by regulated businesses' management, and
- public reporting of compliance performance by the regulator.

## **1.5 Structure of this statement**

This Compliance Policy Statement outlines:

- the statutory powers of the Commission
- the Commission's compliance activities
- the categorisation of regulatory obligations, and reporting requirements associated with those obligations
- the range of enforcement actions available to the Commission in the event of non-compliance and how and when they should be applied

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<sup>2</sup> See Memoranda of Understanding published at <http://www.esc.vic.gov.au/public/About+ESC/Memoranda+of+Understanding/>

<sup>3</sup> See Energy Market Reform Bulletin No. 69 at [www.mce.gov.au](http://www.mce.gov.au)

- the criteria against which enforcement decisions may be made, and
- the public reporting of compliance activities and performance by the Commission.

## **1.6 Compliance Policy Statement implementation**

In accordance with its Charter of Consultation, the Commission will consult with all relevant stakeholders to categorise the regulatory obligations in accordance with this Compliance Policy Statement (see section 3.3) and to define the standards of compliance required. These obligations are contained in the legislative and regulatory instruments listed in section 6 of this Compliance Policy Statement and the final categorisation will be published in the *Energy Businesses' Compliance Reporting Manual* by 31 March 2007.

During this consultation process, the Commission may also take the opportunity to rationalise the regulatory instruments as appropriate, for example, by integrating the separate electricity and gas retail guidelines into energy guidelines.

The requirement for compliance reporting by the regulated energy businesses is scheduled to commence on 1 July 2007. Consistent with NSW and South Australia, reporting will be on a financial year basis and within two calendar months of the end of the reporting period.

The Commission will formally notify each regulated business of its reporting obligations by 30 April of each preceding year.

## 2 | COMMISSION'S APPROACH TO COMPLIANCE AND ENFORCEMENT

The Commission has been guided in developing its Compliance Policy Statement by the OECD's framework<sup>4</sup> that outlines three conditions for effective compliance. For a regulated business to comply with regulation, the three conditions that must be satisfied are:

- Condition 1 — it must *know* and *understand* its obligations;
- Condition 2 — it must be *able* to comply — that is, regulatory design must take account of the technological possibility of compliance, and ongoing compliance must be possible in light of the full range of legal and regulatory obligations imposed on the regulated body; and
- Condition 3 — it must be *willing* to comply.

The overall approach by the Commission is to encourage a culture of compliance by the regulated businesses. To this end, it supports the voluntary adoption by businesses of the *Australian Standard AS3806-2006 Compliance Programs*, which provides principles and guidance for implementing a flexible and effective compliance program within a business.

The Commission also is committed to adopting a co-operative and persuasive enforcement approach because when this approach is successful it works better than punitive sanctions in accomplishing long-term compliance. However, compliance cannot be based solely on encouraging voluntary compliance, because some businesses may not comply. Sanctions are necessary for those who do not comply voluntarily.

The Commission has identified eight key elements of good compliance practice required to facilitate satisfaction of the three conditions for compliance. The elements are:

- **Good regulatory design** — regulation needs to be simple, clear, meet its stated objectives, have benefits that outweigh costs and minimise compliance costs
- **Integration of compliance and other regulatory activities** — compliance issues should inform the regulation design stage and the compliance strategy should adjust as the nature of regulation changes
- **High quality engagement with regulated businesses** — regulated businesses need to be consulted both during the development of regulation and once it is in

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<sup>4</sup> Organisation for Economic Co-operation and Development 2000, *Reducing the Risk of Policy Failure: Challenges for Regulatory Compliance*, OECD, Paris, [www.oecd.org](http://www.oecd.org), pp. 14–23.

- place; communication needs to be straightforward, occur regularly, and be 'culturally' appropriate
- **Provision of information** — regulated businesses need to understand the purpose and objectives of the regulation, know what their obligations are and be informed of the consequences of non-compliance
  - **Practical obligations** — requirements must be suitable for the particular regulated businesses and be able to be complied with in the time available and to the required standard
  - **Monitoring of compliance** — compliance is unlikely unless the regulator monitors whether it occurs
  - **Procedural fairness** — processes and decisions need to be consistent, impartial and ethical to build trust with the regulated businesses and encourage voluntary compliance, and
  - **Escalating levels of interference and sanctions in response to non-compliance** — responses to non-compliance generally begin with co-operative approaches to maximise voluntary compliance, with action escalating as far as is needed to achieve compliance; sanctions must be credible threats.

This Compliance Policy Statement and the Commission's strategy to implement it reflect the eight key elements of good compliance practice.

## 3 | ENSURING COMPLIANCE

### 3.1 Facilitating compliance by businesses

The Commission will maintain a comprehensive document, *Energy Businesses' Compliance Reporting Manual*, setting out licence obligations and reporting requirements for each obligation or type of obligation for regulated businesses.

This manual will assist regulated businesses to understand their compliance reporting obligations. As detailed below, however, the Commission has a range of mechanisms for detecting non-compliance by the businesses and will take the necessary enforcement action in accordance with the approach outlined in section 4 of this policy statement.

The Commission will incorporate the compliance requirements implied by any proposed new or changed regulatory obligation into its current open and transparent processes considering proposed changes to regulatory obligations, and developing guidelines and codes. New compliance requirements finalised in this way would be consistent with this Compliance Policy Statement.

In addition, specific support may be provided to those needing assistance with regulatory obligations, such as preparation of compliance reports, interpretation of regulatory obligations and advice relating to regulatory documents.

### 3.2 Monitoring compliance

The Commission's activities to ensure compliance with energy retail and distribution obligations follow the six key work streams set out below.<sup>5</sup>

In deciding the degree to which regulatory compliance oversight is required, the Commission may consider whether the regulated business has:

- Established a robust regulatory compliance system — that the internal systems and processes are sufficient to accurately and reliably identify incidences of non-compliance (the Commission will consider adoption of Australian Standard 3806 as an indicator of an effective internal system)
- Maintained good compliance practice — that it has consistently complied with its regulatory obligations (and that the internal systems consistently provide reliable information on compliance levels)
- Rectified known non-compliant behaviour in a timely manner

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<sup>5</sup> This Compliance Policy Statement applies only to energy distribution and retail businesses at this time. However, it is the Commission's intention going forward to also implement its compliance strategy consistently across the regulated industries, as appropriate.

- Been transparent in its compliance management processes and advised the Commission on non-compliance issues in a timely manner.

### **3.2.1 Regulatory compliance audits**

Each regulated energy business is required under its licence to appoint an independent auditor to conduct audits of:

- its compliance with obligations under its licence, including obligations to comply with codes and guidelines; and
- the reliability and quality of information reported by the regulated business to the Commission, and the consistency of that information with the Commission's specifications.

Audits are performed on a regular basis, or as required by the Commission. The Commission specifies the audit scope and the auditor must enter into a standard tripartite deed with the Commission and the regulated business. The Commission approves the auditor, audit team and the final audit scope, and briefs the auditor in the presence of the retailer or distributor. The Commission publishes a summary of compliance audit results.

The Commission may vary an energy businesses' required frequency or scope of regulatory audits in response to past compliance levels and compliance reports by that business (see section 3.2.6). This will particularly apply to the energy distribution businesses' audits.

An inter-jurisdictional approach to retail audits, where the jurisdictions co-ordinate energy retail audit activities, and take into account the businesses' compliance history, has been adopted from 2005-06.<sup>6</sup>

The Commission will also audit each retailer's compliance with its wrongful disconnection compensation obligations generally and the information submitted as part of the retailer reporting obligations, as part of the normal regulatory audit program.

### **3.2.2 Audits of regulatory accounts**

The Commission requires regulated businesses to have regulatory accounts audited to verify the reliability and quality of the financial information provided to the Commission as the basis for price setting and approval.

### **3.2.3 Monitoring determinations**

The Commission monitors compliance of regulated energy businesses with the terms of determinations made by the Commission. For example, the Commission's 2006 Price Determination requires electricity distributors to submit to the Commission a 5-Year Tariff Strategy Report. The Commission may also make determinations on non-price matters. Conditions for certain electricity distribution

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<sup>6</sup> See the agreement between the Commission, the Essential Services Commission of South Australia, the Independent Competition and Regulatory Commission of the Australian Capital Territory and the Independent Pricing and Regulatory Tribunal of New South Wales at <http://www.esc.vic.gov.au/public/Energy/Regulation+and+Compliance/>

excluded services such as repair, maintenance and replacement of street lighting, are an example. These requirements are contained in distribution licences.

### **3.2.4 Response to complaints and other data**

The Commission receives complaints from energy customers directly and through the Energy and Water Ombudsman of Victoria (EWOV), Consumer Affairs Victoria (CAV), in correspondence from or via the office of a Minister or Member of Parliament and in the media. The Commission has monthly meetings with EWOV on complaints received and potential non-compliance by regulated energy businesses and is also in regular contact with CAV.<sup>7</sup>

As a matter of practice, the Commission will refer any enquiries or complaints received from a customer directly to the retailer concerned or, if the retailer has dealt with the complaint to EWOV<sup>8</sup>. Significant market conduct complaints will be referred to CAV. However, if the complaint reflects a significant or systemic non-compliance with the regulatory obligations, the Commission may conduct an initial investigation.<sup>9</sup>

Consistent with clause 6.4 of the EWOV Charter, EWOV should seek guidance from the Commission on any questions of interpretation of the Energy Retail Code or retailers' terms and conditions of supply.

A retailer may also seek guidance from the Commission on any questions of interpretation of the Energy Retail Code. The Commission will send a copy to EWOV and each retailer, and will publish details of all guidance provided in its annual compliance report.

The Commission also monitors, and may investigate, media reports indicating non-compliance. Information gathered for performance monitoring is another source available to the Commission to indicate potential non-compliance with obligations, based on trends identified through the performance indicators. However, performance reports are not compliance documents. The primary purpose of performance monitoring is to encourage competition by comparing the performance of businesses and providing information to customers and stakeholders. The reliability of processes to collect the data, and its accuracy, are assessed in regulatory compliance audits.

### **3.2.5 Response to notifications by regulated businesses**

If a regulated energy business becomes aware of a material breach of a licence condition, code, standard, rule, guideline or customer-related standard or procedure, they must, under a licence condition, notify the Commission in accordance with any guidelines issued by the Commission or, in the absence of

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<sup>7</sup> The Commission has memoranda of understanding with each of EWOV and CAV regarding communication and coordination of regulatory activities.

<sup>8</sup> The Commission expects that EWOV will handle enquiries and complaints about alleged wrongful disconnection in accordance with EWOV's usual procedures. Retailers should have regard to EWOV's Complaint Handling and Disconnection Policies.

<sup>9</sup> The Commission will keep a record of brief particulars of each complaint received and to whom it has been referred.

such guidelines, as soon as practicable. Any breach of a Type 1 regulatory obligation constitutes a material breach (see section 3.3.3). The Commission may respond to notifications of material non-compliance from regulated energy businesses with an initial investigation.<sup>10</sup>

### **3.2.6 Response to regulated energy businesses' compliance reports**

Regulated energy businesses are required (from 1 July 2007) to report on their compliance of regulatory obligations as described in this Compliance Policy Statement and *Energy Businesses' Compliance Reporting Manual*. The Commission may consider these reports, seek clarification on report contents and the systems on which they are based from regulated energy businesses where necessary. The required frequency and scope of regulatory audits may be varied in response to these compliance reports and other information received by the Commission.

## **3.3 Nature of regulatory obligations and reporting requirements**

The Commission has adopted a multi-tiered approach to compliance reporting by classifying all licence obligations as Type 1, 2 or 3 based on the Commission's assessment of the potential impact of the non-compliance on its primary objective.

In addition, retailers and EWOV have reporting obligations in relation to wrongful disconnections which are outlined in section 3.4.6.

### **3.3.1 Categorisation of regulatory obligations**

The Commission's *Energy Businesses' Compliance Reporting Manual* lists and categorises all regulatory obligations as Type 1, 2 or 3.

The Commission has categorised all energy regulatory obligations based on its assessment of the potential impact of the non-compliance to its primary objective of protecting the long term interests of Victorian customers with regard to the price, quality and reliability of essential services. The relevant factors for determining the classification of the obligation include:

- the actual or potential impact of the breach on customers, with specific regard to the financial impact on customers, the impact on vulnerable customers and customers with low income, any loss, a reduction or a denial of an essential service and the number of customers affected; and
- the actual or potential impact on other stakeholders, insofar as this has a consequent impact on customers, including actual or potential impact on safety and risk to the public, the impact on the interests of other market participants, the social and environmental impact of a breach and the impact on the capacity for the Commission to achieve its objectives.

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<sup>10</sup> Regulated businesses are required to notify the Commission of material non-compliance with regulatory instruments as part of electricity distribution licence condition 23.2, gas distribution licence condition 4(d), electricity retail licence condition 14.3 and gas retail licence condition 15.3.

### 3.3.2 Frequency of compliance reporting

The classification allocated initially determines the frequency with which regulated energy businesses must report non-compliance.

- Type 1 – Immediate Notification
- Type 2 – Six-monthly, and
- Type 3 – Annual.

The Commission will categorise every new and amended regulatory obligation according to this classification.

All regulated energy businesses will be required to report Type 1 breaches immediately.

Regulated energy businesses that are new to the market or have poor compliance records, as assessed by the Commission from time to time, may be required to submit a six-monthly statement that the regulated energy business has complied with all obligations classified as Type 1 and Type 2 (other than those where non-compliance is reported), and the annual statement on Type 3 obligations.

For these regulated businesses, the Commission may reward the development of good compliance practice by reducing the required frequency of reporting of Type 2 obligation compliance.

Alternatively, for those regulated energy businesses that have participated in the market for some time and have good compliance records, as assessed by the Commission, it may be that only immediate reporting of breaches of Type 1 regulatory obligations and annual reporting of compliance with all regulatory obligations will be required.

Notwithstanding the above, the decision as to the reporting frequency may be differentiated between distribution and retail regulated businesses and will take account of all the compliance requirements on a regulated business, including audit requirements.

Reporting will be on a financial year basis and the Commission will formally notify each regulated energy business of its reporting obligations by 30 April of each preceding year.

### 3.3.3 Type 1 regulatory obligations

Type 1 regulatory obligations are considered to be those regulatory obligations where non-compliance would have a critical impact on the Commission's primary objectives and where the impact of that non-compliance increases over time if it is not rectified quickly.

For all regulated energy businesses, immediate notification of non-compliance with Type 1 obligations is required. This takes the form of a telephone call to a Commission Compliance Manager and follow-up written confirmation to the Commission's Chief Executive Officer from the Chief Executive Officer (or equivalent) of the regulated energy business concerned within 5 business days. Notification must occur as soon as the event occurs, or as soon as a regulated energy business becomes aware that the event has occurred or is likely to occur.

Any notification of non-compliance must include:

- extent and nature of the non-compliance (including whether and how many customers and/or other regulated energy businesses have been affected)
- reasons for non-compliance
- actions taken to rectify the non-compliance and to prevent it reoccurring, and
- actual/anticipated date of full compliance.

This information may be taken into account by the Commission in deciding the enforcement action to be taken (see section 4.3)

For completeness, Type 1 non-compliance should also be briefly summarised in six-monthly (if required) and annual compliance reports. These reports should include an update of any further actions taken by the regulated energy business in respect of the original Type 1 non-compliance.

Retailers are required to notify the Commission of material breaches with regulatory obligations as part of electricity distribution licence condition 23.2, gas distribution licence condition 4(d), electricity retail licence condition 14.3 and gas retail licence condition 15.3. Non-compliance with Type 1 regulatory obligations will be considered a material breach of which regulated energy businesses must notify the Commission as a licence condition.

### **3.3.4 Type 2 regulatory obligations**

Type 2 regulatory obligations are those where:

- non-compliance would seriously impact on the Commission's objectives; and/or
- the obligation is 'new' or has not been complied with in previous years; and/or
- there is a need to raise regulated energy businesses' awareness of the obligation; and/or
- the impact of that non-compliance increases over time.

Regulated energy businesses should report Type 2 non-compliances that were identified during the six-monthly reporting period. Notification of non-compliance must include:

- extent and nature of the non-compliance (including whether and how many customers and/or other regulated energy businesses have been affected)
- reasons for non-compliance
- actions taken to rectify the non-compliance and to prevent it reoccurring, and
- actual/anticipated date of full compliance.

This information may be taken into account by the Commission in deciding the enforcement action to be taken (see section 4.3).

For completeness, non-compliance reported in the six-monthly compliance reports should be summarised in the annual compliance report, including an update of any further action taken by the regulated energy business with respect to the original Type 2 non-compliance. The updated report should include information on the status of the non-compliance and the date of full compliance for each relevant

obligation, which should be consistent with the information provided in the six-monthly report.

### **3.3.5 Type 3 regulatory obligations**

Type 3 regulatory obligations are all other obligations not listed in the above categories.

All regulated energy businesses are required to submit an annual statement reporting compliance against Type 3 regulatory obligations (as well as compliance against Type 1 and Type 2 obligations). The annual compliance report must be signed by:

- the Chief Executive Officer (or equivalent), and
- the Chairman of the Board or a duly authorised Board member other than the CEO.

### **3.3.6 Wrongful disconnection reporting**

Retailers must report to the Commission within 20 business days of the end of each calendar quarter:

- All instances where wrongful disconnections have been detected and compensation has been paid, together with the reasons for the wrongful disconnection.
- Enquiries, including those referred by EWOV and the Commission to be identified separately, and complaints received directly about disconnections and the decisions made, identifying:
  - The numbers of wrongful disconnections that have occurred, including the reasons for the wrongful disconnections and the amount of compensation paid;
  - The numbers where wrongful disconnections did not occur.

EWOV will report to the Commission within 10 business days of the end of each month:

- The total number of actual disconnection cases received;
- The number of actual disconnection cases received as enquiries and referred to a Higher Level Contact;
- The number of actual disconnection cases received as Level 1 complaints for investigation;
- The number per retailer;
- The number of each case type per retailer (“Enquiry RHL” or “Received as Level 1 complaints”);
- The number of actual disconnection cases where wrongful disconnection compensation was paid by the retailer (before a decision was made by the Commission); and
- If requested by the Commission, the EWOV case reference number.

### **3.3.7 Maintaining the categorisation of regulatory obligations**

The Commission will maintain a fully categorised listing of regulatory obligations, which arise from the legislative and regulatory instruments relevant to the regulated energy businesses (detailed in section 6 of this Compliance Policy Statement).

These will be documented in the *Energy Businesses' Compliance Reporting Manual* accessible on the Commission's website.

## 4 | RESPONDING TO NON-COMPLIANCE

### 4.1 Range of responses

The previous section outlined how the Commission will monitor and detect potential non-compliance by the regulated businesses, including categorising the regulatory obligations for reporting purposes. The Commission will determine the enforcement approach to take in instances of non-compliance, including in response to non-compliance with Type 1, Type 2 or Type 3 obligations reported by the regulated businesses, taking into account all the circumstances of the matter.

The enforcement measures available to the Commission range from less formal and less punitive options to progressively more substantive statutory-based responses.

The Commission may proceed with more serious enforcement actions in appropriate circumstances and when other measures have not had the desired effect. This approach is consistent with the pyramid of enforcement model, which has been adapted to illustrate the enforcement activities which may be adopted by the Commission.<sup>11</sup>

Notwithstanding the above, If the Commission considers the matter sufficiently serious, the Commission may use its statutory enforcement powers in the first instance to ensure regulated energy businesses comply with their obligations.

### 4.2 Assessing compliance

This section is intended to provide guidance to assist retailers and other stakeholders to understand what factors the Commission may have regard to when determining compliance with regulatory obligations.

#### 4.2.1 Fair and Reasonable

The definition of “fair and reasonable having regard to related costs incurred by the retailer” may include matters such as:

- The charging methodology (for instance, does the retailer charge a flat rate or the actual cost of energy)
- Billing period (monthly or quarterly)

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<sup>11</sup> I. Ayres and J. Braithwaite 1992, *Responsive Regulation, Transcending the Deregulation Debate*, Oxford University Press, New York, quoted in Organisation for Economic Co-operation and Development 2000, *Reducing the Risk of Policy Failure: Challenges for Regulatory Compliance*, OECD, Paris, [www.oecd.org](http://www.oecd.org), p. 44

- Related costs incurred by the retailer (both connection costs and disconnection costs)
- The cost of managing any default by the business
- Whether the retailer has taken sufficient steps to manage the risk of additional costs being accrued.

### **4.3 Enforcement action**

#### *Communication and consultation*

Commission staff may become aware of potential non-compliance of regulatory obligations through compliance monitoring (as well as through compliance reporting as detailed in section 3.3). The Commission may make initial contact with the regulated energy business concerned to obtain preliminary information and to determine the appropriate next steps. On-going cooperative communication facilitates an understanding of the issues and the appropriate actions to take.

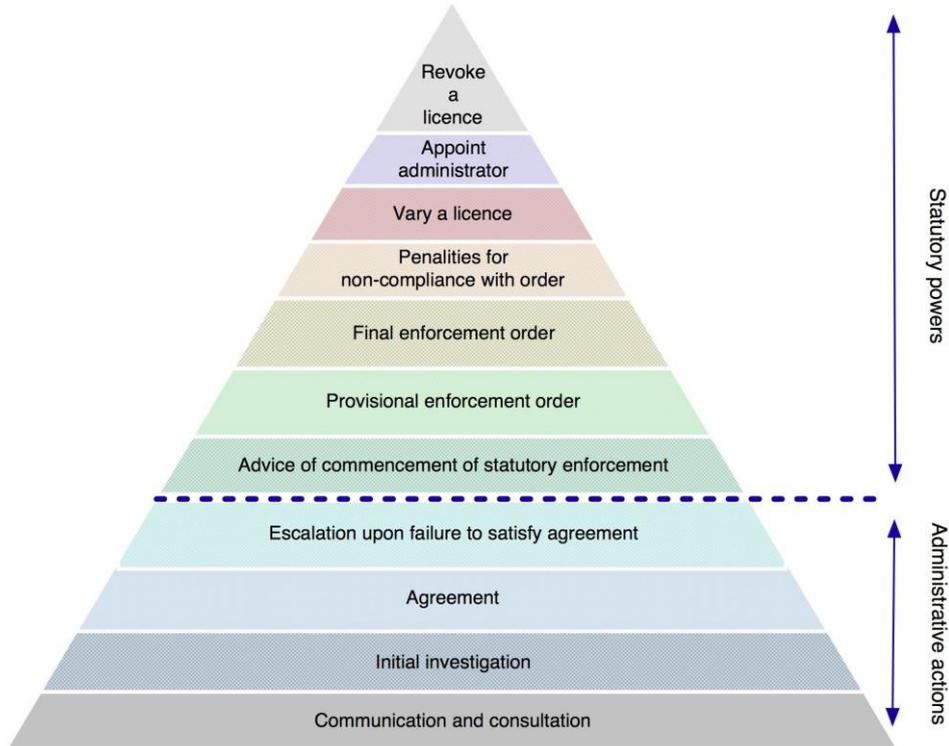
#### *Initial investigation*

If the Commission considers that there may be significant or systemic non-compliance with regulatory obligations, it may conduct an initial investigation. That is, Commission staff may seek information from the regulated energy business on:

- the nature of the potential breach;
- the actual and potential impact of the potential breach; and
- the proposed response to the potential breach, including how the regulated energy business intends to remedy the impact of the potential breach, and how it intends to prevent similar events in the future.

Figure 1

### An enforcement pyramid for regulation of Victorian energy businesses



#### 4.3.1 Administrative actions

If, following initial investigation, staff considers the issue systemic or material, the Commission may seek agreement from the regulated energy business on an action plan to resolve the issue by an agreed date. This agreement, which is usually directed to the Regulatory Manager in the business, may be decided taking into account information provided from the regulated energy business (which may have been provided in accordance with the reporting obligations in section 3.3) and the source of the complaint through the initial investigation.

The Commission may seek agreement from the regulated energy business that sets out how, and the timeframe in which, compliance is expected to be achieved, whether any remedies are to be provided for customers and the reporting requirements until compliance is achieved.

Should the regulated energy business not wish to enter, or fails to complete, the agreement, the matter may escalate within the regulated energy business to the chief executive. At this stage, the Commission's Chief Executive Officer or Commissioners may become involved.

### 4.3.2 Statutory powers

Following failure to fulfil an administrative agreement by a regulated energy business or if the Commission considers the matter sufficiently serious in the first instance, the Commission may use its statutory enforcement powers to ensure regulated energy businesses comply with their obligations.

#### *Serve a provisional enforcement order*

Where a regulated energy business has contravened, is contravening, or, in the opinion of the Commission, is likely to contravene, a licence condition, the Commission may serve a provisional enforcement order under section 53 of the *Essential Services Commission Act 2001*. A provisional order may require the regulated energy business to comply with a licence condition, or to rectify a contravention. Where a provisional order has been made, the regulated energy business may undertake to comply with the licence condition. Where the regulated energy business has undertaken to comply with the provisional enforcement order, a final order cannot be made. Provisional orders must be published in the Government Gazette.

#### *Serve a final enforcement order*

The Commission may serve a final enforcement order under section 53 of the *Essential Services Commission Act 2001* following 28 days notice to the regulated energy business of the intention to serve the order, and following an opportunity to make a submission in respect of the order and the Commission's consideration of any submission or other objection to the order it receives. Final orders must be published in the Government Gazette.

#### *Penalties for non-compliance with order*

If regulated energy businesses do not comply with a provisional or final order, an offence under section 53(8) of the *Essential Services Commission Act 2001*, the Commission may apply to the Courts for the levy of a penalty. Under section 53(9) the penalty is up to 5000 penalty units and in addition, there may be a further penalty not exceeding 500 penalty units for each day after service of the order that contravention continues.<sup>12</sup>

#### *Vary a licence*

Under section 38(3) of the *Gas Industry Act 2001* and section 29(3) of the *Electricity Industry Act 2000*, the Commission may vary a licence where the regulated energy business does not comply with an enforcement order or the Commission is satisfied that the variation of the licence is necessary having regard to the Commission's objectives and the nature of the material breach.

#### *Appoint an administrator*

Under section 34 of the *Electricity Industry Act 2000* or section 41 of the *Gas Industry Act 2001* the Commission may appoint an administrator to the business of

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<sup>12</sup> Under the Victorian Monetary Units Act 2004, the value of a penalty unit as at December 2011 is \$122.14. Therefore, during 2011-12 the penalty under s.53(9) is up to \$610, 700 plus up to \$61,070 for each day after service of the order that contravention continues.

a licensee. Such an appointment may be made where there has been a contravention of licence conditions, which threatens the security of the electricity and gas supply, and any other remedies to enforce compliance are not adequate. The timeframe for appointment is 28 days but may be renewed for further periods.

#### *Revoke a licence*

Under section 38(3) of the *Gas Industry Act 2001* and section 29(3) of the *Electricity Industry Act 2000*, the Commission may revoke a licence where the regulated energy business does not comply with an enforcement order, or the Commission is satisfied that the revocation of the licence is necessary having regard to the Commission's objectives and the nature of the material breach.

## **4.4 Deciding the enforcement response**

In deciding what enforcement response is appropriate, the Commission may consider:

- (a) The history of the regulated energy business' compliance with regulatory obligations
- (b) In relation to the intent and knowledge of the regulated energy business:
  - i. Whether the regulated energy business knowingly failed to comply with its licence or other relevant regulatory instrument
  - ii. Whether the regulated energy business' senior management were involved in the non-compliance
  - iii. Whether the regulated energy business voluntarily reported the non-compliance or attempted to conceal it from the Commission or other monitoring organizations, and
  - iv. Whether the regulated energy business has taken appropriate action to remedy the non-compliance.
- (c) In relation to the impact of the non-compliance on the regulated energy business
  - i. Whether the regulated energy business derived a benefit (financial or otherwise) from the non-compliance;
  - ii. Whether enforcement action is likely to create an incentive to improve compliance and deter future non-compliance; and
  - iii. Whether the regulated energy business has taken steps to secure compliance either specifically or by maintaining a robust compliance system.

## **4.5 Monitoring implementation and continuing compliance by regulated energy businesses**

The Commission may monitor the implementation of breach remedies and continuing compliance by regulated energy businesses with regulatory obligations.

## **4.6 Continuing non-compliance**

The Commission may vary the reporting requirements for the relevant regulated energy business in response to past non-compliance, regardless of the classification of the obligation. The Commission will formally notify each regulated energy business of its reporting obligations by 30 April of each preceding year.

## 5 PUBLIC REPORTING ON COMPLIANCE

### 5.1 Reporting by the Commission

In order to ensure regulated energy businesses and their customers understand the Commission's compliance and enforcement practice, the Commission may publish a report of its compliance activities and the compliance performance of regulated energy businesses each year. This annual report would be in addition to the reporting required of the Commission under legislation.

### 5.2 Annual report

As part of its compliance monitoring and reporting role, the Commission may publish an annual report of compliance activity and enforcement action in order to inform:

- the public of the Commission's response to non-compliance with regulatory obligations by regulated energy businesses, and
- industry of the compliance standards expected and the consequences of failing to meet these standards.

The Commission may document the following information in the annual report:

- the number of instances and types of non-compliance by individual regulated energy business and summary details of agreements and compliance action taken
- number of initial investigations, provisional and final enforcement orders served, penalties levied, administrators appointed and licences varied or revoked,
- administrative agreements and enforcement orders aggregated by industry and classification of the regulatory obligation
- timeliness of data received for regulatory accounts and in response to other information requests made by the Commission; and
- details of any guidance provided to EWOV as part of any referred wrongful disconnection complaints or interpretation of any other regulatory instrument.

The Commission does not publish the details of ongoing investigations. The Commission's approach to compliance is to encourage a cooperative environment so that in the first instance regulated energy businesses are given the opportunity to agree to put in place certain actions to remedy potential or actual non-compliance. To ensure the fairness of the investigation process, the Commission advises only those parties directly involved in any ongoing investigation. However, the Commission may seek stakeholder views on the extent and impact of potential non-compliance, including what may be considered appropriate remedial actions for the businesses to put in place.

### **5.3 Enforcement orders**

The Commission is required by section 53 of the *Essential Services Commission Act 2001* to publish a copy of an enforcement order in the Government Gazette as soon as possible after the order has been served.

### **5.4 Regulatory audit reports**

The Commission may publish regulatory audit reports (or extracts or summaries thereof) of regulated energy businesses. The summaries may be published on the Commission's website.

## 6 SUMMARY OF LEGISLATIVE AND REGULATORY OBLIGATIONS

Document type	Energy Retail	Electricity Distribution	Gas Distribution
Legislation	<ul style="list-style-type: none"> <li>▪ Essential Services Commission Act</li> <li>▪ Gas Industry Act</li> <li>▪ Electricity Industry Act</li> </ul>	<ul style="list-style-type: none"> <li>▪ Essential Services Commission Act</li> <li>▪ Electricity Industry Act</li> </ul>	<ul style="list-style-type: none"> <li>▪ Essential Services Commission Act</li> <li>▪ Gas Industry Act</li> </ul>
Licences	<ul style="list-style-type: none"> <li>▪ Electricity Retail Licence</li> <li>▪ Gas Retail Licence</li> </ul>	<ul style="list-style-type: none"> <li>▪ Electricity Distribution Licence</li> <li>▪ Electricity System Code</li> </ul>	<ul style="list-style-type: none"> <li>▪ Gas Distribution Licence</li> <li>▪ Gas Distribution System Code</li> </ul>
Codes	<ul style="list-style-type: none"> <li>▪ Energy Retail Code</li> <li>▪ Code of Conduct for Marketing Retail Energy</li> </ul>	<ul style="list-style-type: none"> <li>▪ Electricity Distribution Code</li> <li>▪ Electricity Metering Code</li> </ul>	
Guidelines	<ul style="list-style-type: none"> <li>▪ Gas Industry Guideline No 8: Operational &amp; Compliance Audits (Retail Businesses)</li> <li>▪ Gas Full Retail Contestability Guideline No 9: Development of Retail Gas Market Rules</li> </ul>	<ul style="list-style-type: none"> <li>▪ Public Lighting Code</li> <li>▪ Guideline No 3: Regulatory Information Requirements</li> <li>▪ Guideline No 5: Connection &amp; Use of System Agreements</li> <li>▪ Guideline No 11: Voltage Variation Compensation</li> </ul>	<ul style="list-style-type: none"> <li>▪ Guideline No 7: Gas Distribution Pipeline Access Disputes</li> <li>▪ Guideline No 16: Regulatory Audits of Distribution Businesses</li> <li>▪ Guideline No 17: Regulatory Accounting Information Requirements</li> </ul>

Document type	Energy Retail	Electricity Distribution	Gas Distribution
	<ul style="list-style-type: none"> <li>▪ Electricity Industry Guideline No 9: Regulatory Audits of Retail Businesses</li> <li>▪ Electricity Industry Guideline No 13: Greenhouse Gas Disclosure on Electricity Customers' Bills</li> <li>▪ Electricity Industry Guideline No 17: Electricity Ring-Fencing</li> <li>▪ Energy Industry Guideline No 19: Energy Product Disclosure</li> </ul>	<ul style="list-style-type: none"> <li>▪ Guideline No 14: Provision of Services by Electricity Distributors</li> <li>▪ Guideline No 15: Connection of Embedded Generation</li> <li>▪ Guideline No 16: Regulatory Audits of Distribution Businesses</li> <li>▪ Guideline No 17: Electricity Ring-Fencing</li> <li>▪ Guideline No 18: Augmentation &amp; Land Access</li> </ul>	
Rules & Other Requirements	Gas Retail Market Rules Operating Procedure: Wrongful Disconnection Compensation	Electricity Distribution Price Review 2006-10, Final Decision Volume 2	Gas Access Arrangements 2003-2007
Information Specifications	Information Specification (Service Performance) for Victorian Energy Retailers	Information Specification (Service Performance) for Victorian Electricity Distributors	Performance Indicators Information Specification