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Mr Lew Owens
Chairperson
ESCOSA
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Email: escosa@escosa.sa.gov.au

Dear Mr Owens

COMPLIANCE AUDIT FRAMEWORK FOR THE ELECTRICITY SECTOR – DISCUSSION PAPER

NRG Flinders offers the following comments on the proposals contained in the above discussion paper, released for comment by ESCOSA in April 2004.

At a broad level, NRG Flinders acknowledges ESCOSA's efforts in seeking to bring greater certainty and clarity to the compliance audit process. The arrangements proposed appear to offer a more robust framework, and scope to increase certainty and transparency for licensees.

In terms of the specific arrangements proposed, it is understood that the approach described is confined purely to the compliance audits initiated by ESCOSA on a periodic and regular basis. NRG Flinders understands that the proposals are not expected to impact on the annual compliance reporting and auditing process undertaken by licensees pursuant to Guideline 4. To avoid any potential uncertainty, it is suggested that ESCOSA's final decision on this issue should confirm this intent.

In considering audit frameworks established by other regulatory bodies, it would appear that compliance auditing undertaken elsewhere generally focuses on the regulatory obligations of distribution entities and retailers. Auditing of compliance by generation licensees does not appear to be a specific area of focus. In this regard, in order to ensure that competitive neutrality is not compromised and that some degree of consistency in regulatory application is applied across jurisdictions, it is suggested that ESCOSA satisfy itself that the compliance reporting and auditing obligations imposed on SA licensees are not more onerous than those applied interstate.

In defining the scope of compliance audits, ESCOSA has proposed that such audits should be reserved for matters of significant regulatory importance, such as obligations involving a significant degree of customer impact or evidence of material non-compliance. NRG Flinders agrees that audits should be confined to issues of such magnitude in view of the regulatory costs involved.

In appointing an auditor to perform a compliance audit, ESCOSA has suggested that it would not be appropriate for such audits to be conducted through an outsourced internal audit function of the licensee.

NRG Flinders would assume that the use of auditors in this capacity would remain acceptable for the purpose of annual compliance reporting and auditing. As noted above, it is assumed that the audit framework does not impinge on the existing compliance reporting framework. NRG Flinders is not aware of any concerns over the independence or quality of the audits undertaken in this capacity to date, and would note that this approach is consistent with financial audits of company accounts undertaken annually and reported to ASIC as the relevant regulator.

Having said this, it is not immediately apparent that the use of an outsourced internal auditor for specific compliance audits initiated by ESCOSA would necessarily be inappropriate from the perspective of independence and diligence in the conduct of the audit. This option would also appear to provide for more economical use of auditing resources.

On a separate note, NRG Flinders would concur with ESCOSA's preference for a simpler approach than the use of a formal tripartite agreement between auditor, licensee and ESCOSA, given the obligations already in place.

ESCOSA has highlighted a range of areas that could potentially be subject to assessment under the specific compliance audit framework, based on issues of emerging importance from a compliance perspective and the experience of regulators elsewhere. NRG Flinders would note that these issues appear to be concerned primarily with the obligations of regulated segments of the industry. This is consistent with the general intent of the 'regulatory bargain', whereby entities earning a regulated return on the one hand are held to account for the quality of their services on the other. A significant case would need to be mounted to extend the scope of specific audits beyond issues of this nature.

Compliance with FRC regulatory obligations is one area of focus identified by ESCOSA. In this regard, NRG Flinders would support ESCOSA's view that there is no case for widespread compliance auditing of FRC regulatory obligations at the present time, and that compliance auditing in the area should therefore be carefully targeted at critical obligations where compliance issues have arisen.

In conclusion, NRG Flinders supports the thrust of ESCOSA's proposals to establish a framework for compliance auditing for electricity licensees, on the basis that this approach is restricted to key obligations determined through a formal assessment process, clearly distinct from the established compliance reporting and auditing process observed by licensees under Guideline 4.

Should you have any queries in relation to this submission, please feel free to contact Simon Appleby (Ph 8372 8706) in the first instance.

Yours sincerely



Reza Evans
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Regulation and Market Development