21 December 2020

General Manager, Consumers and Markets Branch
Australian Energy Regulator
GPO Box 520 Melbourne VIC 3001

Submitted via email to AERringfencing@aer.gov.au

Dear Sir or Madam,

**Re: Issues paper: Updating the Ring-fencing Guideline for Stand Alone Power Systems (SAPS) and Energy Storage Devices**

The Australian Energy Council (AEC) welcomes the consultation opportunity in the Australian Energy Regulator's Issues paper on Updating the Electricity Distribution Ring Fencing Guideline (Distribution Guideline) for Stand Alone Power Systems and Energy Storage Devices.

The AEC is the industry body representing 22 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

The AER has identified that the development of new technologies that are perceived to operate on the boundaries of regulated and unregulated electricity markets, creating challenges for the AER. The question as to whether the current Distribution Guideline is fit for purpose in this new technology environment is considered. In the AEC's view the current regulatory regime is still adequate and change is not required.

The AEC does not support the introduction of a further exemption framework for Distribution Network Service Provider (DNSP) led Stand Alone Power Systems (SAPS). We understand that it would enable DNSPs to make SAPS investment decisions without existing requirements of regulatory review, and that some circumstances, such as bushfire supply restorations and recovery, are arguably benefitted by an exemption framework. However, these discrete circumstances can be readily addressed under the existing waiver arrangements, and general exemptions which would make it easier for DNSPs to own generation for stand-alone power systems is not in the long term interests of all customers. Policy approaches should foster the development of competitive third-party providers and competitive platforms, and not provide a mechanism to undermine that policy objective.

The Distribution Guideline is in our estimate by no means perfect in its ambition to promote effective competition for services and minimise the harm that follows from DNSPs cross subsidising their competitive services and discriminating in favour of affiliates. However, if we are to accept the premise that competition and non-discriminatory access are the best mechanisms for providing services to customers at an efficient cost, then the inclusion of an exemption framework that would reduce the threshold applied under the current waiver framework in the Guideline creates further harm by threatening both competition and efficiency. Competition in this market is at an early stage, and the exemption framework, by giving DNSPs direct ownership rights for Stand Alone Power System generation, will crowd out new entrants. The AER is already able to grant a DNSP a waiver under the Distribution Guideline for it to provide contestable services through storage devices where a net benefit can be demonstrated. The market for energy storage is also in its early stages of development meaning an incorrect decision on access by the AER could have serious consequences on long term competition. The AEC believes that the review and decision

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threshold under the current waiver framework gives the best scope to test and adjust in the early stages of this nascent market.

Greater net economic benefits will always be achieved by having the contestable markets solving the economics of energy storage services (batteries) rather than DNSPs directly investing because of the DNSPs potential to cross subsidise their contestable activities where an energy storage service (ESS) is used to provide multiple services across the supply chain. The AEC notes that this cross subsidy can theoretically be resolved through the Cost Allocation Methodology (CAM). Whilst this allocation and attribution in the DNSP's CAM must be consistent with the cost allocation principles in NER clause 6.15.2, the AEC is concerned that the cost allocation principles outlined in the Rules are broad, and offer little guidance beyond high level, generic principles. The AER's compulsory information gathering powers do not extend to other services that are offered by DNSPs. As a result, there is no way to verify if the cost allocations that have been used by the DNSP between its regulated and unregulated businesses were fair and reasonable. The practical effect is DNSPs shifting commercial risks to customers of their regulated business to give themselves a competitive advantage. This has the potential to crowd out potentially more efficient service providers from ESS market in the short-term, which diminishes productive efficiency, and would have a chilling effect on competition and technological development in the ESS market in the long-term, which diminishes dynamic efficiency. Because of this, and the nature of joint costs themselves, there is a range of outcomes that might be deemed to be "economically efficient" that in fact are not.

The AEC has previously raised concerns at the rise of distributor centric models that displace competition between third party providers at the centre of Distributed Energy Resource (DER) frameworks. Our position is that competition and non-discriminatory access are the best mechanisms for providing services to customers at an efficient cost, and that all policy approaches should foster the development of competitive third-party providers and competitive platforms for each of DER and SAPS. When considered against the potential small number of SAPS in the next decade, the disproportionate nature of the proposed distributor centric exemption framework increases our concerns.

Any questions about this letter should be addressed to David Markham by email to david.markham@energycouncil.com.au or by telephone on (03) 9205 3107.

Yours sincerely,

**David Markham**
Networks and Distributed Energy Resources Policy Manager
Australian Energy Council