28 November 2015

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Mr Warwick Anderson
General Manager-Network Finance and Reporting
Australian Energy Regulator
via email: AERInquiry@aer.gov.au

Submission on Ergon Energy's Ring Fencing Waiver, commencement date 29 Oct 2015

Dear Mr Anderson:

Thank you for the opportunity to comment on Ergon's proposal for a Ring-fencing Waiver regarding its plan to install 'GUSS' on some of its SWER lines ('The Proposal'). I am writing because I am concerned about repercussions of granting such a waiver, and I question some logic employed in the application. I make this submission as an individual concerned about network strategies which ultimately work against the long-term interest of the public. Here is a summary of my concerns. I would be happy to expand on any of these topics at your request.

1) **Granting this waiver would unfairly provide Ergon with a competitive advantage over businesses offering energy-efficiency solutions now and in the future.** The project places Ergon in competition with other battery storage businesses as well as many other forms of Demand Management. It may also put Ergon in competition with community energy solutions, and therefore places it against entire communities. This, in combination with the next item, is likely to create incentives which work against the National Electricity Objective.
2) **Ergon has substantial leverage to set prices and policies for network customers and storage solutions**. This is not compatible with its being a competitor in the Demand Management market. Ergon should not be allowed to profit from crippling off-grid efficient competition through onerous policy requirements or pricing. This conflict of interest would ultimately hold back the efficient uptake of technology by consumers and communities.
3) **Granting this waiver may inadvertently imply that this project provides no profit to Ergon**, **thus avoiding all requirements to share the benefit with customers.** There may also be implications about how the project is regulated. Ergon provides a reason for granting the waiver on Page 6 of The Proposal,

   "*…the ongoing operation of these assets does not constitute a 'business'. In particular, their (ownership and) operation does not represent a commercial activity and there is no attempt to make profits from ownership or operation of the assets.*"

   This statement is false. There is a clear attempt to make profits from ownership and operation of these assets. Profit from ownership comes from growing the Regulatory Asset Base for the next period, rather than, for example, facilitating the orderly decommissioning of SWER lines and the responsible uptake of community-owned microgrids. Profit from operation comes from any reduction in total costs (vs the redacted 'traditional' upgrade path, the path on which costs are currently based) which is not passed through to the customer. Additionally, there is a potential reduction to the overall network peak demand (or the opposite, should the network prefer such an outcome).

4) **The timing of this proposal is suspicious.** There are two concerns about the timing:
    a. **This proposal comes just after 'efficient' network costs were estimated in Ergon's Regulatory Proposal.** Any savings found by networks after the AER determines their allowance is kept as profit, as if to say that the network performed better than an efficient network could. The only way this could occur, of course, is through gaming the system (or a radical new technology, but this would not qualify as such). This project has been around for many years, and could lower the cost of network service permanently. If Ergon's claims of efficiency and savings are accepted, the timing may allow Ergon and the other DNSPs to reap the benefits of inflated cost forecasts made because they were not frank and forthcoming about their true less-costly plans. It would be a violation of the NEO to allow Ergon to proceed with its project and make profit through it. Ergon's insincere comparison of value vs the cost of 'traditional upgrades', without considering other Demand Management solutions, shows that it would rather not talk about what it already considers 'competing' solutions. I note that the technology lifespan forecasts seem rather large compared to similar commercial products. Will customers bear the expense and uncertainty of these forecasts if they don't pan out? There could be significant protection to the public in requiring that risk to be taken by a separate company.
    b. **The proposal comes just at a time when community-owned power grids are becoming viable.** Since we must assume that profit is the motivation for all proposals, we must ask whether availability of technology has really been the driver of this project's timing. The timing appears to be based instead on strategic profit-maximisation. Tyalgum NSW recently announced plans to be the first Australian community to go off-grid. If Tyalgum succeeds, other communities will follow. This is not a 'death spiral' situation, but rather could be an efficient outcome which reduces the need for costly SWER lines serving few customers. Ergon's plan could be seen as a response to competitive pressure from these communities. Was this technology available previously, but Ergon profited from not using it? Is this technology not actually ready, but Ergon is able to extract maximum profit from implementing it now?
5) **The purported savings are likely to vanish as customers take up cost-reflective tariffs.** Cost-reflective pricing is the network's main tool for offering efficient service. Customers should have incentives to conserve (and sell back) energy during actual or likely network peaks, and to draw/store energy at other times. It is clear from studies by DNSPs such as SMUD (Sacramento, California, USA)[1] that a strong price signal can strongly influence customer behaviour, to a much greater extent than Australian DNSPs may care to admit. While it *could* be efficient to have storage on the network, it would make little sense to have both grid-scale batteries and individual customer batteries, a result which would be stimulated by

[1] http://www.greentechmedia.com/articles/read/How-Solar-Batteries-and-Time-of-Use-Pricing-can-Add-Up-to-Value accessed 28 11 2015

proposed 'cost-reflective' tariffs for small customers. If the network has effectively fixed its peak problem all by itself, and is charging customers for the solution, then peak pricing is no longer cost-reflective.

6) **Does the cost of having a commercial business own and operate the technology outweigh the benefit only because of the extremely small scale of projects proposed at this time?** If this is indeed an efficient solution, it is likely to be used for more SWER lines and by other DNSPs. To begin offering waivers now would risk allowing major scale increases later which would be difficult to regulate under DNSP Rules and Regulations.
7) **Would the public approve of Ergon having full control over the operation of this system?** Even if there were no actual conflict of interest, there is certainly the perception that one would exist. Ergon would use its control over this system to pursue profit, with potential for the network to manipulate key data which is used, for example, in forecasting network demand. The network does not have a clear price signal to lower overall peak demand, and may even be stimulated to increase it as much as possible, due to regulatory problems. I would not trust any DNSP to use this technology optimally without transparency. On the other hand, businesses operating the same equipment would be incentivised by a transparent set of tariffs which would at least keep the price signal pointed in the correct direction.

To be clear, I do not claim to know that any particular configuration of technology is better than any other, and Ergon's proposed solution may be optimal in some sense of the term. My concern lies entirely with the lack of transparency and the reasonable chance of this project working against the NEO due to a conflict of interest. The Ring-Fencing Guidelines exist in order to prevent precisely these kinds of conflicts of interest from arising or appearing to exist.

My conclusion on this topic is that **Ergon's profit is not clearly aligned with the National Electricity Objective in this instance, thus the AER must be very cautious about approving any related proposals, and especially about handing out policy waivers like the one being considered here. Given the many issues with this proposal, I ask that the AER refuse to grant this Ring-Fencing waiver at this time.**

Thank you again for the opportunity to comment on this proposal. I hope that the AER will continue to make careful regulatory decisions which are in the long-term best interest of consumers.

Best regards,

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