

Our ref: 13483791
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21 January 2016

Mr Chris Pattas
General Manager – Networks
Australian Energy Regulator
GPO Box 520
Melbourne VIC 3001

Dear Mr Pattas,

ERGON ENERGY RING-FENCING WAIVER APPLICATION – AER DRAFT DECISION

Western Power appreciates the opportunity to comment on the AER's draft decision to waive ring-fencing requirements in support of Ergon's Grid Utility Storage System (GUSS) program.

Western Power acknowledges that the focus of the draft determination is limited to the ring-fencing arrangements currently in place in Queensland, and the subsequent focus on conducting a "related business".¹ In this context, Western Power supports the waiver granted to Ergon, and the notion that prescribing onerous ring-fencing requirements might undermine the ability to select the most efficient option for network investment, as intended by the regulatory framework.

In addition, in making their draft determination, the AER touches on a number of issues for network businesses pertinent to this consultation process.

Ring-fencing requirements

In the draft determination, the AER notes that its national ring fencing guidelines due for release in December 2016 will "necessarily have regard to battery storage technologies and how related services may best be provided". When considering ring-fencing in light of the current complementary regulatory mechanisms of cost allocation requirements, shared asset guideline approaches, and the regulatory investment test process, it does not appear to be clearly established that ring-fencing is a necessary intervention in an emerging market, and any onerous requirements may in fact have a detrimental impact to market development.

For example, the Council of Australian Governments Energy Council's *Strategic Assessment of Network Regulation* has recently observed that for a range of potential future market scenarios, the presence of overly restrictive ring-fencing provisions may limit network innovation and business model development in a manner that is not consistent with the long-term interests of consumers.²

It is reasonable to expect that the approach to a market-led deployment of storage include additional regulation such as ring-fencing only where the costs and benefits are adequately assessed, and consistent with best practice regulatory design. The potential for market failure that necessitates ring-fencing arrangements does not appear to have been established, and a full, evidenced based review is required prior to regulatory intervention.

Flexibility for Network businesses

Western Power supports Ergon's proposal to own and maintain the GUSS units and include the capital expenditure within its Regulated Asset Base. Ownership decisions are typically embedded

¹ defined as producing, purchasing or selling electricity

² COAG Energy Council, Policy Advice - Electricity network economic regulation: scenario analysis, June 2015

within standard investment decision making processes, where the cost and risks associated with any investment model are evaluated against, and guided by, the relevant regulatory framework.

The AER notes in its Draft Determination that it “may be appropriate for DNSPs to source network storage services from third parties”.

The principles of a market-led deployment of storage offerings are consistent with delivering long term benefits to customers, where ownership of energy storage solutions by network businesses should be encouraged within a competitive market. For example, battery storage has a variety of efficient uses for network businesses, particularly where network topology and constraints are diverse (for example summer and winter peaking locations on the same network).

The characteristics of storage such as functional flexibility, transportability and scalability offer the potential to realise efficiencies in network service provision across an array of applications and locations. These characteristics naturally lend themselves to ownership situations, and these efficiency opportunities may ultimately be lost, to the detriment of consumers, if an ownership prohibition is put in place. Where network ownership models are appropriate, Network businesses are likely to be sourcing products from the competitive market, and as such taking the ownership risk associated whilst stimulating market development.

The treatment of storage within the regulatory framework should not result in incentives for inefficient technology choices for any party, with any direct intervention to regulate the entry of specific technologies into the market avoided to the greatest extent possible.

Western Power again acknowledges the opportunity to comment on the ring-fencing waiver submitted by Ergon to the AER. In the context of the ring-fencing waiver application, Western Power recognises the current ring-fencing requirements in Queensland and the necessity for Ergon to seek a waiver in this instance.

Yours sincerely,



Noel Ryan
Economic Regulation Manager
Western Power