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Ms Gillian Gout
Director, Strategic Energy Policy and Energy Systems Innovation
Australian Energy Regulatory (AER)
GPO Box 3131
Canberra, ACT, 2601

Sent via email: AERringfencing@aer.gov.au

Dear Ms Gout,

AER Initiation notice: Distribution ring-fencing class waiver

Endeavour Energy welcomes the opportunity to provide this response to the AER's Initiation notice for a distribution ring-fencing class waiver for projects funded under the Commonwealth Government's Community Batteries for Household Solar Program (the **program**). The program aims to deliver 400 community batteries across Australia to support lower electricity bills and emissions, support storage of excess solar energy and reduce pressure on the grid.

DNSPs are well placed to help achieve the objectives of the program and we strongly support the AER granting a class waiver with respect to clauses 3.1, 4.2.1 and 4.2.2 of the Distribution Ring-fencing Guideline. Specifically, DNSP knowledge and understanding of their networks make them well positioned to deliver on the stated objective to provide a net benefit to the electricity network, having regard to matters such as network constraints[1]. DNSP participation would increase the pool of eligible proponents and the competitiveness of the grant selection process ensuring all viable proposals can be considered for funding.

We understand that DNSP participation in the program is implicit and would be encouraged if the restriction on DNSPs leasing spare battery capacity to third parties was waived. Notably, the constraint on DNSPs providing market services from batteries would be preserved. DNSP involvement would therefore require joint-collaboration with third parties to optimise the full use and value of batteries which would promote competition for the services among prospective providers.

Class waivers would facilitate collaboration and efficient proposals

A ring-fencing waiver would be necessary to allow DNSPs to contract with third-parties to maximise all possible value streams and the total consumer benefits of the battery deployment. Specifically, a class waiver would provide upfront certainty over the ability of DNSPs to participate in the program and facilitate DNSP negotiations with market providers ahead of submitting an application. This certainty is imperative in the context of the program's requirement for all joint applications to[2]:

- include details of each project partner and a description how they will work with the lead organisation to successfully complete the project;

[1] Department of Climate Change, Energy, the Environment and Water, Grant Opportunity Guidelines, Community Batteries for Household Solar Program - Delivery of Election Commitments Stream 1, December 2022, p.5

[2] Ibid, p.11

- include the roles/responsibilities the project partner will undertake, and the resources it will contribute (if any); and
- have a formal arrangement in place with all parties prior to execution of the grant agreement.

Given these requirements, an assessment of individual waiver applications through either the AER's conventional or streamlined battery waiver process would not provide the upfront regulatory and investment certainty needed to negotiate arrangements with third-party providers and submit a robust application within the program's timeframes. Furthermore, we do not consider these alternative waiver processes are pragmatic given the large volume of applications the AER will likely need to assess.

Importantly, a class waiver does not presuppose that DNSPs will seek or be awarded funding in every instance. Funding decisions will follow an independent, merit-based approach with grants to be awarded to applications that best address the program's assessment criteria as outlined in the program's respective guidelines. A class waiver merely allows a DNSP's application to be considered on the same terms as other prospective applicants and does not afford DNSPs an unfair advantage over other parties in the assessment process.

The NER protects against information and data sharing concerns

In deciding whether to grant a ring-fencing waiver, the AER must consider the potential for DNSPs to discriminate between itself (or an affiliated entity) and a competitor (or potential competitor) as well as the potential for cross-subsidisation if the waiver is granted. In relation to former, we understand some stakeholders have raised concerns that DNSPs could be incentivised to not respond appropriately to requests from third parties for technical or commercial information which is required to develop their respective grant application[3].

However, the connections framework requires DNSPs to share network information upon request. For instance, there are provisions in Chapter 5A of the NER which oblige DNSPs to provide a timely response to connection enquiries relating to embedded generation including batteries[4]. This is in addition to obligations on DNSPs to publish information on network constraints in Distribution Annual Planning Reports. The requirement to comply with these provisions and the subsequent risk of enforcement action from the AER from not doing so limits any opportunity DNSPs have to not provide access to data and information relevant to a third-party's grant application in addition to the reputational damage of doing so.

Furthermore, the non-discrimination provisions listed in the Ring-fencing Guideline provide controls which protect against DNSPs favouring their related entity over its competitors. In terms of information disclosure, section 4.3 of the guideline requires DNSPs to provide equal access to ring-fenced information and to publicly report requests received for ring-fenced information in an information sharing register. This requirement provides transparency on how DNSPs have provided fair access to information and discourages conduct that could disrupt a potentially competing application particularly where a DNSP's related entity is involved.

It is noteworthy that ring-fencing breaches are punishable by tier 1 civil penalties[5] which have provided significant deterrent against discriminatory DNSP behaviour. We also agree that DNSPs undertaking a competitive process to select a third-party leasing partner would help to address potential discrimination risks, although we believe it should be open to each DNSP to develop its own processes on engaging with and selecting potential partners.

RAB allocation should be guided by the benefits received by network customers

The initiation notice proposes that a class waiver would apply where a successful DNSP has not allocated the battery asset to their respective RAB (Class A) or alternatively where they have, the DNSP has applied the requisite RAB allocation approach (Class B). In regard to the latter, the AER has proposed that the RAB allocation should be the share of the residual asset cost (i.e. battery cost minus program grant funding) that reflects the portion of total quantified benefits (i.e. regulated plus unregulated benefits) that relates to the provision of direct control services forecast at the time of the investment decision.

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[3] This includes the Stream 1 requirement for non-DNSPs to provide written evidence of an agreement with the relevant DNSP that a suitable network connection point can be identified or provided in the chosen location.

[4] Refer to NER clauses 5.3A6 - 5.3A.8

[5] For a body corporate, the maximum tier 1 penalty is the greater of: (1) $10,000,000; (2) three times the value of the benefit received; or (3) 10% of annual turnover in preceding 12 months. For an individual, the maximum penalty is $500,000.

We have concerns regarding the requirement to forecast unregulated benefits (including leasing revenues) that the DNSP receives over the economic life of the battery to inform the RAB allocation. With few mature practical applications of shared use batteries for DNSPs to draw from and uncertainty over how factors and trends in the wholesale market will impact these benefits, providing accurate forecasts would be challenging and it would be possible that actuals could vary significantly from these forecasts. The main risk is that network customers would end up funding proportionately more(less) than the benefits they receive from the battery if unregulated revenues are greater(less) than initially expected.

We believe customers should pay no more for the cost of the battery than the benefits they receive from them and consider a forecast of these benefits would better inform the RAB cost allocation. We therefore support the ENA's alternative customer benefits approach whereby the RAB allocation would equal the regulated consumer benefits, quantified in accordance with the AER's DER Integration Expenditure Guidance Note, capped at the residual asset cost.

The appeal of this approach is that the RAB allocation is not sensitive to highly uncertain forecasts of unregulated benefits with the sharing of revenue received by the DNSP for leasing the battery can be based on actuals and done post-RAB allocation. DNSPs would be responsible for developing a proposal for sharing any unregulated revenue with its customers, weighted by the portion of the battery allocated to the RAB and representative of the portion of the asset funded by customers. For instance, returning actual unregulated revenues to its customers each year through a control mechanism adjustment would be simple for both the DNSP to implement and for the AER to assess compliance against.

A proposal to share no less than 10 per cent of the benefits the DNSP accrues unconstrained by a materiality threshold would guarantee the terms for sharing any benefits with customers are at least equal to those outlined in the AER's Shared Assets Guideline. We would support this requirement as a 'floor' for all DNSP sharing arrangements noting the competitive application process would incentivise DNSPs to share a greater portion to demonstrate adherence with the community benefit condition of the program's assessment criteria.

The RAB allocation should not be subject to the risk of a 'true-up'

To protect against cross-subsidisation concerns, the AER has also included conditions for projects which fall within Class B which requires the DNSP to:

- attribute asset costs between regulated and unregulated services in a manner that complies with the Cost Allocation Principles;
- provide an annual audit report covering the quantified benefits relating to direct control services and other distribution services from the deployment of the battery and a comparison of the use of the battery to provide these services relative to the initial proposed allocation; and
- provide information as to the terms and conditions of the contracts entered into with third parties for the leasing of battery capacity[6].

We note the proposed requirements generally reflect the conditions imposed by the AER in waivers recently granted to several DNSPs to provide third-party access as part of their respective DNSP-led battery projects (separate to the Commonwealth Government's program). These conditions are generally consistent across the waivers irrespective of whether the DNSP has proposed to allocate a portion of the battery to the RAB or not.

We therefore consider the criteria to be reasonable and support providing transparency in battery usage but would appreciate the AER confirming the intended use for this information. For instance, we do not consider it appropriate to retrospectively require DNSPs to adjust the RAB where actual battery usage, or the benefits thereof, has diverged from the forecast used to inform the initial allocation.

The prospect of a RAB 'true-up' is not conducive to the investment certainty required by both DNSPs and prospective third-party partners to encourage in their joint-participation in the program. Instead, we contend this information should only be used by the AER for the purpose of monitoring battery use for regulated services and to inform the cost allocation approach taken for future shared batteries.

Also, we believe information provided to the AER on the terms and conditions of the contracts entered into with third parties should be treated as commercial in confidence.

[6] Also applies to Class A projects

Waivers should continue to align with the expected life of the battery

We consider that the term of the waiver should be sufficient to provide certainty over the regulatory treatment of the battery over the course of its expected life. In the case of grid scale batteries, 15 years is the generally accepted expected life. This rationale is reflected in the initiation notice which proposes the 30 June 2038 as the date the class waiver would expire. However, with the program expected to end in 2026, we consider the expiry of the class waiver should accommodate batteries installed in this year. An expiry date of 30 June 2041 would therefore be more appropriate.

To discuss our submission further please contact Joe Romiti, Regulatory Analyst at Endeavour Energy on [redacted] or [redacted].

Yours sincerely,

[redacted]

Colin Crisafulli
Head of Network Regulation