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Submission to the Australian Energy Regulator

Submitted by email to [redacted]

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Review of the Ring-fencing guideline (electricity distribution) and Shared Asset Guideline

Introduction

Enel X welcomes the opportunity to provide feedback on the Australian Energy Regulator's review of the Ring-fencing Guideline (Electricity Distribution) and Shared Asset Guideline.

As the National Electricity Market (NEM) continues to evolve, Enel X supports a regulatory framework that maintains a clear distinction between monopoly network services and contestable energy services. This distinction is a foundational element of the market's design and exists to promote competition, innovation and efficient outcomes for consumers.

The ring-fencing framework was established on the basis that Distribution Network Service Providers (DNSPs) operate natural monopoly infrastructure, while the assets and services capable of being competitively supplied should, wherever possible, be provided through market-based mechanisms. Ring-fencing obligations exist because DNSPs' monopoly infrastructure, services and access to information provide advantages that may not be available to other market participants. This includes the potential for cross-subsidisation of non-regulated services using regulated revenue and resources, sharing network planning information and confidential information regarding network needs and direct relationships with customers. Without appropriate safeguards, those advantages may be leveraged to favour affiliated businesses operating in contestable markets.

In recent years, the AER has granted waivers allowing DNSPs to expand their services and activities beyond the traditional boundaries of regulated network services. Enel X understands that the AER has granted ring-fencing waivers intended to promote innovation and emerging technologies, and ensure service availability in remote locations. This has allowed DNSPs to increasingly provide new technologies and service offerings that extend beyond the traditional poles-and-wires model. In some cases, expansion of assets and service provision is supported, directly or indirectly, by regulated revenues which are funded by customers. As a result, an important question for this review is whether these developments represent genuine network innovation or the gradual expansion of monopoly network businesses into areas more appropriately served by competitive markets.

As the NEM continues to evolve with new technologies and services, Enel X supports the ongoing role of the Rules and associated regulatory instruments in clearly defining regulated and contestable services .

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This distinction is particularly important where costs are recovered from consumers through regulated revenues.
Enel X considers that the energy system is evolving and this increases uncertainty between the boundary between regulated and contestable services. While some of this uncertainty is a natural consequence of technological change, there is a risk that regulatory decisions intended to support innovation or facilitate emerging technologies may unintentionally blur these distinctions. Enel X appreciates that the AEMC is undertaking a broader review to consider the services DNSPs should provide as some AER waiver decisions appear to create precedents that are inconsistent with the current market design. It is important that regulatory decisions made prior to this review being completed should remain consistent with the current market design and continue to be assessed against the long-term interests of consumers.

The key issue for this review is not whether any individual waiver decision was justified when assessed on its own merits. Rather, it is whether section 5 of the ring-fencing guideline needs to be clarified to ensure waiver decisions remain consistent with the market design and original policy intent of ring-fencing.

The fundamental question underpinning the role of DNSPs within the market was, in Enel X's view, largely settled when the market framework established which services should be provided through monopoly regulation and which services should be provided through competition. Enel X considers that this distinction remains a fundamental principle of market design and should continue to inform consideration of any exceptions to that framework. Where DNSPs are permitted to undertake both regulated activities and have affiliated electricity service providers, robust protections are required to preserve competition and consumer outcomes. In particular, the framework should ensure that:

- DNSPs do not discriminate between market participants;
- competitive service providers compete on a level playing field; and
- monopoly advantages cannot be leveraged to directly or indirectly cross-subsidise contestable services.

Battery energy storage systems provide a useful example. Ring-fencing waivers have enabled DNSPs to own battery assets that provide network services while making excess capacity available for other uses. This represents a significant evolution from the traditional model in which competitive market participants owned and operated assets and sought to maximise value across multiple revenue streams.

Enel X is particularly concerned by four aspects of this trajectory:

- DNSP ownership and operation of assets that are capable of providing contestable services.
- Increasing reliance on cost-allocation methodologies rather than structural separation.
- Streamlined waiver pathways that may reduce opportunities for stakeholder scrutiny.
- Long-duration waivers that risk becoming enduring market outcomes rather than targeted exceptions.

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The issue is not solely whether a DNSP can demonstrate technical compliance with cost-allocation requirements. Rather, it is whether the framework continues to deliver competitive neutrality. Cost allocation methodologies may address accounting treatment, but they do not necessarily address broader advantages arising from access to regulated capital, lower commercial risk, superior visibility of network needs and information acquired through monopoly planning functions.

Enel X is also concerned that DNSP ownership of contestable assets may transfer commercial risk to consumers. Contestable services are typically provided by competitive market participants who bear the risks associated with investment decisions, including the risk that assets become stranded, obsolete or uneconomic. Where DNSPs are permitted to own and operate those assets, a greater proportion of that risk may ultimately be borne by consumers through regulated arrangements. The AEMC's review should therefore consider not only questions of efficiency, but also whether the resulting allocation of risk remains appropriate.

Enel X continues to believe that efficient outcomes are most likely to be achieved through market-based procurement processes. DNSPs should identify system needs and seek solutions from the market wherever possible. The regulatory framework should incentivise DNSPs to do this. Overall, this approach encourages innovation, competition and efficient investment while ensuring that commercial risks remain with those best placed to manage them.

To support these outcomes, DNSPs should also play an active role in improving market visibility of future network needs. DNSPs possess unique insights regarding network constraints, augmentation requirements and locations where non-network solutions may deliver value. Providing greater transparency of these opportunities would enable a broader range of market participants to develop and invest in competitive solutions, improving the effectiveness of market-based procurement processes and reducing barriers to entry for new participants.

In many cases, improving access to information may be more effective in promoting competition than further expanding ownership rights or service provision arrangements for DNSPs and their affiliates. Enel X encourages the AER to consider whether existing guidelines, including the Shared Asset Guideline and related information disclosure arrangements, could be enhanced to better facilitate third-party participation and investment. In particular, consideration should be given to whether these frameworks can more effectively support competitive providers to access network infrastructure and respond to network needs without requiring DNSPs to own the underlying contestable assets themselves.

Accordingly, Enel X encourages the AER to use this review as an opportunity to revisit first principles, including:

- whether the current waiver framework remains appropriately targeted;
- whether sufficient weight is given to long-term competition outcomes when considering waiver applications;

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- whether structural separation remains preferable to cost-allocation approaches in emerging contestable markets;
- how multi-use assets should be treated;
- how commercial risk should be allocated between investors and consumers; and
- whether the cumulative effect of individual waiver decisions remains consistent with the long-term objectives of ring-fencing and the national electricity objective.

This is particularly important as the market continues to evolve through batteries, distributed energy resources, flexible demand, data centres and other non-network solutions, where decisions made today regarding ownership, risk allocation and market participation will have long-lasting implications for future market structure and consumer outcomes.

Question 1

Have we accurately described the key changes occurring in distribution networks and the broader energy system? Are there any important developments or trends we have not captured?

Yes, Enel X considers that the consultation paper accurately identifies the key developments occurring within distribution networks and the broader energy system.

In particular, the increasing deployment of distributed energy resources, batteries, flexible demand resources and non-network solutions is fundamentally changing the nature of services provided across the electricity sector. These developments are increasingly blurring the distinction between traditional network services and contestable services and make it appropriate to revisit whether the current ring-fencing framework remains fit-for-purpose.

At this stage, Enel X does not propose additional developments or trends that warrant inclusion in the review. We consider that the challenge for this review is less about identifying new technologies and more about ensuring that the regulatory treatment of those technologies remains consistent with the underlying market design principles that have historically separated monopoly network activities from contestable services.

Question 2

Have we accurately reflected the concerns raised by stakeholders regarding the guideline? Are there additional issues that should be considered as part of this review?

Enel X considers that the consultation paper accurately reflects the concerns raised by stakeholders and captures the key areas where questions have emerged regarding the operation of the Guideline.
In particular, Enel X supports further examination of:

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- the role of DNSPs and their affiliates in providing contestable services;
- the operation of the waiver framework;
- the treatment of multi-use assets;
- cost-allocation methodologies; and
- the interaction between emerging technologies and existing ring-fencing obligations.

While we do not propose the inclusion of additional topics, Enel X encourages the AER to consider the cumulative effect of waiver decisions over time. The key question is not whether individual waivers were justified when assessed in isolation, but whether their combined effect is consistent with the original market design and what is in customers' long-term interests.

Question 3

Are there relevant experiences, case studies, examples or evidence that would help illustrate these issues or inform this review?

Enel X acknowledges that practical market experience will be important in informing this review and welcomes continued engagement with the AER throughout the consultation process.

Question 4

Do you consider the scope of this review to be appropriate? Are there additional areas of focus that you believe should be included?

Enel X considers the proposed scope of the review to be appropriate and sufficiently broad to enable a comprehensive assessment of the Guideline.

In particular, Enel X supports the proposed examination of the following areas.

The role of DNSPs in the delivery of negotiated distribution services and unregulated distribution services

Enel X supports further examination of this issue, particularly in light of increasing volumes of large and bespoke customer connection arrangements.

Data centres represent a rapidly emerging example where the distinction between regulated and contestable services may become increasingly important. The review presents an opportunity to ensure these arrangements remain consistent with the principles of ring-fencing and do not inadvertently expand the scope of activities undertaken by monopoly network businesses.

Whether the current decision-making framework for assessing ring-fencing waiver applications allows the AER to adequately consider the benefits and risks of granting or not granting a waiver

Enel X is not convinced that the current framework adequately captures long-term competition impacts.

The current framework necessarily assesses waiver applications on a case-by-case basis. However, competition impacts often emerge cumulatively and may not be apparent when individual applications are considered in isolation.

Opportunities to make the Guideline clearer and more succinct, including supporting compliance and enforcement

Enel X supports efforts to improve the clarity, consistency and practical operation of the Guideline.

However, Enel X considers that compliance and enforcement should form an important part of this review. As the framework has evolved, there has been an increasing reliance on behavioural obligations, cost-allocation methodologies, waiver conditions and ongoing compliance monitoring to manage competition risks that were historically addressed through clearer structural separation between regulated and contestable activities.

This places significant weight on the effectiveness of the compliance and enforcement framework. While the Guideline plays an important role in implementing the ring-fencing framework, it does not provide the same level of certainty or durability as the National Electricity Rules (Rules). As a result, stakeholder confidence in the framework increasingly depends on the AER's ability to monitor compliance, identify breaches and ensure that any resulting costs are not ultimately borne by consumers.

Enel X therefore encourages the AER to consider whether there are aspects of the current framework that have become sufficiently important to competition and consumer outcomes that they would be more appropriately addressed through clearer and more prescriptive obligations, including by elevating certain provisions into the Rules. The review should also consider whether the existing compliance and enforcement arrangements remain proportionate to the increasingly complex activities being undertaken by DNSPs and their affiliates.

Examining what types of services affiliates of DNSPs should be allowed to provide and why

Enel X supports examination of this issue.

The review should maintain a clear focus on the assets that affiliates are permitted to own and the services they are permitted to provide. These arrangements should remain consistent with both the NER and the broader principles underpinning NEM market design. To the extent that this review considers the boundary between regulated and contestable activities, Enel X considers that those questions should

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remain closely aligned with, and informed by, the parallel AEMC processes responsible for determining the treatment of assets and services under the NER. Enel X encourages close coordination between these reviews to ensure transparency and consistency for stakeholders.

The treatment of multi-use assets, including how costs and revenues should be attributed where assets funded through regulated revenues are used to provide other services

Enel X strongly supports the inclusion of multi-use assets within the review scope.

This is one of the most important issues facing the current framework. The review should consider not only how costs and revenues are allocated between regulated and contestable uses, but also whether ownership arrangements themselves remain appropriate.

Enel X encourages the AER to consider whether competitive service providers are better placed to own and operate multi-use assets, with DNSPs procuring services from those assets through transparent market processes. The review should also examine whether existing frameworks, including the Shared Asset Guideline, can provide more effective pathways for third-party participation, asset ownership and access to network infrastructure, while still enabling DNSPs to procure the services they require without owning the assets and transferring associated investment risks to regulated network businesses and ultimately consumers.

The issue is also not simply ownership of assets, but also the informational advantages available to DNSPs through their monopoly planning functions. As DNSPs increasingly participate in areas adjacent to contestable markets, ensuring that information regarding future network needs is made available to the broader market will become increasingly important.

Question 5

Do you have suggestions on ways that we can make it easier for stakeholders to effectively engage with the review process?

Enel X welcomes the AER's commitment to conducting a broad review and encourages ongoing stakeholder engagement throughout the process.

Given the overlapping nature of a number of current reform processes across the energy sector, Enel X believes it would be valuable for the AER to clearly articulate how issues being considered through this review interact with related processes being undertaken by the AEMC and other market bodies.
In particular, stakeholders would benefit from:

- clear identification of areas of overlap between concurrent reviews;
- transparency regarding which body is best placed to address particular issues;

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- opportunities to provide consistent input across related processes; and
- regular communication regarding how findings and decisions from parallel reviews will be taken into account.

Improving visibility of these interactions will assist stakeholders in engaging efficiently and help ensure that outcomes remain coherent across the broader regulatory framework.
Overall, Enel X welcomes the review and considers it an important opportunity to ensure that the Guideline continues to support competition, innovation and consumer outcomes while remaining consistent with the original principles of ring-fencing and the broader design of the National Electricity Market.

Enel X appreciates the opportunity to provide feedback and looks forward to continuing to engage constructively with the AER throughout the review process.

[redacted],

[redacted]

Manager, Market Development and Regulatory Affairs
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