Review of the ring-fencing and shared asset guidelines

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About the Justice and Equity Centre

The Justice and Equity Centre stands for a society that is fair and free from discrimination and disadvantage. Established in 1982 as the Public Interest Advocacy Centre (PIAC), we use the law and policy advocacy to challenge injustice and inequality. We do this through:

- legal advice and representation, specialising in test cases and strategic casework;
- research, analysis and policy development; and
- advocacy for systems change to deliver social justice.

Energy and Water Justice

Our Energy and Water Justice work improves regulation and policy so all people can access the sustainable, dependable and affordable energy and water they need. We ensure consumer protections improve equity and limit disadvantage and support communities to play a meaningful role in decision-making. We help to accelerate a transition away from fossil fuels that also improves outcomes for people. We work collaboratively with community and consumer groups across the country, and our work receives input from a community-based reference group whose members include:

- Affiliated Residential Park Residents Association NSW;
- Anglicare;
- Combined Pensioners and Superannuants Association of NSW;
- Energy and Water Ombudsman NSW;
- Ethnic Communities Council NSW;
- Financial Counsellors Association of NSW;
- NSW Council of Social Service;
- Physical Disability Council of NSW;
- St Vincent de Paul Society of NSW;
- Salvation Army;
- Tenants Union NSW; and
- The Sydney Alliance.

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The Justice and Equity Centre acknowledges and pays respects to the Gadigal as the Traditional Owners of the land on which our office stands.

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1. Introduction

The Justice and Equity Centre welcomes the opportunity to respond to the Australian Energy Regulator' (AER) Review of the ring-fencing and shared asset guidelines call for input.

As the energy system evolves, distribution networks are becoming increasingly involved in activities associated with consumer energy resources, network batteries, electric vehicle charging infrastructure, flexible export services, and other emerging technologies.

These developments raise important questions regarding how we assess the efficient role of regulated networks and how the appropriate boundaries between regulated monopoly activities and services and competitive market services should be set to enable and promote the best outcomes for consumers.

Reframing the problem

In our view, the review should begin from a clear understanding and reiteration of what ring-fencing and shared asset guidelines are intended to achieve.

Ring-fencing is not an objective in itself, nor is competition[1]. Rather, these guidelines and the regulatory frameworks they contribute to, are tools intended to promote the long-term interests of consumers.

The relevant policy question is therefore not whether a service is delivered through competitive or regulated arrangements as a matter of principle—recognising that such a binary does not exist—but how we decide which mix of arrangements is most likely to deliver efficient, equitable, and durable outcomes for consumers.

Reviewing the guidelines in the correct context

From this perspective, decisions regarding ring-fencing, waiver applications, service classifications, and shared asset arrangements should be assessed according to their ability to deliver outcomes consumers value, including:

- affordability of energy services,
- reliability of energy services,
- equity of access and cost recovery for energy services,
- transparency of costs, and
- contribution to an efficient energy transition.

This review presents an opportunity to consider the guidelines in this wider context.

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1 See JEC submission to AEMC Network Regulation Review - Package 1, pp. 1-2.

We support the existing objectives of the ring-fencing guideline and broadly agree with the issues identified in the consultation paper. However, we are concerned that there is a growing gap between the overarching intent of the framework and its implementation in practice.

While this is partly due to technological change and the emergence of new business models, it also reflects an overly narrow and functional focus on promoting competition rather than outcomes for consumers, as well as inconsistencies in the application of waiver processes and uncertainty regarding how emerging services should be assessed.

The review should therefore focus not only on whether changes are required to principles and formal provisions of the guidelines, but also on how assessment, compliance, monitoring, transparency, and enforcement can be strengthened to ensure that the overarching objectives of the framework—to promote good outcomes for consumers—are best met.

2. Decisions should focus on consumer outcomes

The regulatory framework must move away from a focus on assessment of potential impacts on competition, towards actual impacts on consumers.

One of the most important lessons from recent network regulatory debates is that competition should not be treated as inherently beneficial or as the default solution wherever competitive provision appears theoretically possible.

More competitive provision can deliver efficient outcomes under the right circumstances. However, experience demonstrates that this is not always the case. Equally, experiences have shown regulated provision should not be preferred simply because a network business can deliver a service or may theoretically benefit from efficiencies of scale. A more nuanced approach to assessment and decisions is required to determine which arrangements are most likely to produce efficient and equitable outcomes for consumers.

The experience of metering competition is particularly instructive here. Reforms under Power of Choice were intended to improve efficiency and innovation through competitive provision of the metering platform and data services. In practice, implementation has been characterised by years of delays, compounding complexity, increased transaction costs, and continuing regulatory intervention all without any demonstration that assumed benefits are being realised for consumers.

While the broader merits of competitive metering are outside the scope of this review, the experience demonstrates that the introduction of competition does not automatically improve consumer outcomes. This is not to argue against competitive services per se, but to illustrate that a more robust focus on likely outcomes is required in considering questions of regulation and competition.

What this means for ring-fencing arrangements

This lesson is relevant to the future application of ring-fencing arrangements. Whether a distribution network service provider (DNSP) can provide a particular service or whether competition could theoretically emerge is the wrong starting point.

Instead we should ask: what is the role of DNSPs in efficiently delivering the outcomes consumers want and value? And further, what decision-making framework enables us to best assess and determine that role? Consumer outcomes and how best to deliver them must remain the primary consideration in the assessment of both ring-fencing obligations and waiver applications.

The AER can also draw lessons from the evolution of stand-alone power system arrangements (SAPS) here. The SAPS framework reflects a recognition that strict distinctions between traditional network services and other service delivery approaches do not always produce efficient outcomes.

The SAPS experience demonstrates the importance of maintaining consistency between service classification, ring-fencing, and cost allocation frameworks. Better alignment between the ring-fencing and shared asset guidelines would support more efficient utilisation of network assets to improve outcomes for consumers.

As we argue in our submission on this matter[2], competition should not be sought as an end in itself but should be evaluated in terms of the outcomes it is actually likely to deliver for consumers. The question for regulation then is how to best deploy and shape competition to promote the intended consumer outcomes.

3. Strengthening the waiver framework

We support maintaining flexibility within the ring-fencing framework, but this flexibility should be exercised according to consistent principles and a clear focus on promoting the long-term interest of consumers. That is, flexibility must not come at the expense of robustness, clarity, or consistency.

We are concerned that waiver processes increasingly serves as a backdoor by which DNSPs demonstrate that they are capable of participating in an emerging market, establish a precedent, and expand the scope of monopoly service provision, irrespective of whether doing so advances the consumer interest.

Demonstrating the viability of DNSP provision or participation is not, in itself, sufficient justification for an exemption from ring-fencing requirements. A network business may be capable of efficiently delivering a service while still not being the party best placed to deliver that service in a way which improves outcomes for consumers or which best promotes their long-term interests.

The AER should therefore provide clearer guidance regarding:

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[2] See JEC submission to AER Shared Asset Guidelines – Regulated SAPS review.

- the purpose of waiver arrangements;
- the principles which should be applied to waiver arrangements;
- the targeted circumstances in which waivers may be appropriate;
- the evidentiary threshold required to demonstrate actual consumer benefit, including how alternatives must be assessed;
- how innovation claims will be assessed;
- what constitutes a successful trial; and
- the consumer outcome measures that will be used in evaluations.

Waivers should be employed as a flexibility tool, to explore options where it is not necessarily clear what mix of regulated and network service provision best promotes consumers interest.

That is, waivers should be used and granted to test whether alternative arrangements can best deliver improved consumer outcomes, not simply to establish whether a DNSP can technically or commercially undertake an activity. They should also be time-limited and subject to transparent reporting requirements to ensure lessons learned are available to stakeholders and consumers.

4. A beneficiary-pays approach to shared assets

Guidelines and decisions, like the regulatory framework more broadly, should explicitly embed consistent principles of consumer interest—most notably a 'beneficiary-pays' approach.

Changes in network technology are making shared-use assets increasingly common. Network batteries, flexible network assets, stand-alone power systems, EV charging infrastructure, and consumer energy resource integration services can all generate benefits for multiple parties simultaneously. These benefits are not equal, nor are they equally likely, or equally shared.

This growing complexity increases the importance of transparent cost allocation arrangements based on durable principles which can be consistently applied. The question should not be limited to identifying who caused the need for an investment. Rather, regulators should also consider who receives the benefits, the characteristics of those benefits, and how they are distributed.

A stronger beneficiary-pays approach would assist the AER in evaluating both shared asset arrangements and ring-fencing proposals. Such an approach would improve transparency about the expected benefits of investments and improve consistency across service classification, cost allocation, and ring-fencing decisions.

The AER's consideration on these matters should go beyond a narrow binary between individual and social benefits. That is, the guidelines should provide a framework to consider the relative certainty, magnitude, and distribution of benefits and costs. The guidelines should provide a framework that assess questions such as:

- How certain or 'contingent' is each class of benefits (i.e. those accruing to networks vs. users of a service vs. consumers as a whole)? This is critical as there may theoretically be benefits 'on both sides', but those benefits are often not equally direct or likely.

- How significant are those benefits, in aggregate and on a per-customer basis? This is important as benefits may sometimes appear to accrue equally but be materially uneven in quantum.

- How fairly are those benefits distributed? This should also enable a consideration of equity and link to consideration of the impact of costs associated with realising the benefits.

- When are the costs incurred and when are the benefits expected to materialise? This must also consider any imbalance that may result in actual inequity due to costs accruing to some parties immediately, where benefits are only realised over the longer term.

EV charging infrastructure as an example

Consideration of DNSP roles in provision of EVCI is useful in demonstrating the application of the elements set out above. DNSP provision of EVCI as a regulated service is often presented as beneficial to consumers because it can enable more efficient infrastructure coverage, while accruing wider energy consumer benefit through improved network utilisation. In this case, for example:

- the socialised costs of DNSP investment are immediate, material, and inequitably recovered, because they rely on inequitable network tariff recovery frameworks;

- the benefits to EV users are immediate, significant (through wider infrastructure access and subsidised cost); and

- the prospective benefits to energy consumers are contingent, delayed, difficult to quantify, and inequitably distributed. These benefits rely on utilisation improving and then outweighing any cost increases resulting from either inefficient infrastructure deployment and use, or charging which increases peak demand.

Therefore, the regulatory framework—including ring-fencing guidelines—must take a beneficiary pays approach, assess these aspects of benefit and cost, and frame decisions accordingly.

Evaluating shared assets through the lens of beneficiary-pays can help ensure consumers are not exposed to costs associated with commercial activities from which they derive limited or uncertain benefits.

5. Enabling meaningful stakeholder engagement

We encourage the AER to ensure that engagement processes are designed not only to collect stakeholder views, but also to facilitate meaningful deliberation between stakeholders with different perspectives and interests.

Traditional consultation approaches can be effective for identifying issues and gathering evidence. However, where the review is considering complex trade-offs between alternative regulatory arrangements, stakeholder workshops should be structured to allow participants to interrogate assumptions, test competing perspectives, and collectively explore the implications of different options.

Such an approach is more likely to generate useful insights than a process focused primarily on providing stakeholders with opportunities to present pre-existing positions.

A stronger focus on deliberative engagement would help the AER develop a more robust framework for assessing emerging services. As outlined above, the key regulatory question is not whether competition or regulated provision should be preferred as a matter of principle, but which arrangement is most likely to deliver efficient, equitable, and durable outcomes in the long-term interests of consumers.

Engagement processes should therefore focus on helping stakeholders collectively assess how outcomes may differ under alternative arrangements and what evidence should be used to support those assessments.

6. Further engagement

We welcome the opportunity to meet with the AER project team and other stakeholders to discuss these issues in more depth. Please contact [redacted] at [redacted] regarding any further inquiries.