30 September 2022

Sara Stark
Director, DER – Network Regulation
Australian Energy Regulator
Via email: sara.stark@aer.gov.au
cc: AERInquiry@aer.gov.au

Ausgrid

24-28 Campbell St
Sydney NSW 2000
All mail to
GPO Box 4009
Sydney NSW 2001
T +61 2 131 525
ausgrid.com.au

Dear Ms Stark,

Ausgrid submission to the AER's Incentivising and measuring export services performance Consultation Paper

Ausgrid is pleased to provide this submission to the Australian Energy Regulator's (**AER**) Consultation Paper on incentivising and measuring export service performance (**Consultation Paper**). We support Energy Networks Australia's submission to the AER. We outline our complementary submissions at **Attachment A**. Our main points are set out below, specifically that we support the AER:

1. **A. Pursuing opt-in bespoke incentive schemes for distribution network service providers (DNSPs) in relation to export services.** DNSPs are in a state of transition leading to varied distributed energy resources (**DER**) penetration and hosting capacity amongst DNSPs, and insufficient historical data. We do not consider it appropriate right now for the AER to further explore a compulsory, 'one-size-fits-all' incentive arrangement or mechanism for the provision of export services by DNSPs – particularly for financial incentive schemes. We support bespoke incentive schemes which will allow DNSPs to design and trial incentive schemes suitable to their access to necessary data and customer preferences;

   B. Relying on reputational incentives in the short-term. We support reputational incentives as best suited to incentivise networks to efficiently enable customer exports, as we are still in the early stages of the net zero transition. When the time is right for individual DNSPs to implement bespoke incentive schemes, we do not support a non-symmetrical (penalty only) approach, implementing a guaranteed service level (**GSL**) for export service performance, nor the use of the AER's current CECVs for the quantification of incentive payments;

2. **Exploring potential export service performance reporting metrics as part of a paper trial.** The reporting framework should be designed so that it is proportional to the number of customers impacted and should not rely on measures equivalent to existing import measures;

3. **A. Adopting a benchmarking approach that sets baselines for comparability.** We suggest this could include either an approach where the AER re-specifies its econometric benchmarking models to include one or more new output variables to reflect export services being provided by DNSPs, or an approach where incremental (direct and indirect) costs related to export services are excluded from the costs being benchmarked; and

   B. Ensuring that operating environment factors (OEFs) are not used for benchmarking export performance as this would lead to inconsistent baselines across DNSPs, causing comparability challenges. We support inclusion of directly in the benchmarking models or data as the most suitable benchmarking mechanism.

We thank the AER for the opportunity to provide this submission and look forward to continued collaboration on this issue. Should you wish to discuss any of the issues raised in this submission further, please contact Naomi Wynn, Regulatory Policy Manager at [redacted]

Regards,

[redacted]

Alex McPherson
Head of Regulation

Attachment A: Ausgrid's submission to the AER's Consultation Paper on Incentivising and measuring export service performance

1. Incentive review for exports

A. We support the AER pursuing opt-in bespoke incentive schemes for DNSPs in relation to export services

We support the AER exploring opt-in bespoke export service incentive mechanisms with DNSPs. Bespoke mechanisms would provide flexibility for DNSPs and the AER to develop frameworks that reflect customer preferences and provide appropriate incentives for the efficient delivery of export services that are best suited to individual network conditions and leverage the best available information. These mechanisms could evolve with customer preferences, service offerings, network conditions and improvements in DER visibility.

DNSPs could conduct paper trials of bespoke schemes that they tailor to their individual capabilities and what their customers value, before introducing a scheme that may place revenue at risk. This could occur once DER penetration levels and export services stabilise in network areas. This would align with the STPIS paper trial during the 2009-14 period, ahead of AER introducing financial rewards/penalties in the 2014-19 period. Additionally, if made 'penalty-only' then such a scheme could have unintended consequences. For example, it may encourage networks to do the bare minimum and impose lower DER connection limits (e.g. a 7kW limit) to avoid a penalty where there is no incentive to enable higher DER capacities where these may be available.

We do not recommend a compulsory, 'one-size-fits-all' incentive arrangement or mechanism for export services by DNSPs – particularly for financial incentive schemes. We agree with the AER that it is important that we have the necessary historical data to design an effective scheme with a minimum level of baseline data. DNSPs have widely varied geographies, differing levels of DER penetration and hosting capacities[1] and varied access to relevant historical data.

Additionally, many DNSPs have limited visibility over, and access to, data in relation to the provision of export services. This includes the low level of smart metering penetration in Ausgrid's network, when compared to Victorian DNSPs. We require further investment in network visibility to draw firm conclusions on overall curtailment levels in the National Electricity Market (**NEM**) and the influence this should have on the need to enhance incentives for the provision of export services.

As such, we do not think it is not possible to adequately consider the potential impact of incentive schemes given how much is unknown in relation to ultimate DER penetration levels and export services generally at this early stage in the energy transition.

Of note, our 2024-29 regulatory proposal in January 2023 will be the first time Ausgrid requests DER expenditure under the AER's new DER Integration Expenditure guidance note. Without knowing the final form of our 2024-29 investment plan, we cannot accurately make decisions about how an incentive framework or mechanism should work for us, or other DNSPs.

[1] We note that the curtailment volume across our network is relatively low at present and the constraints experienced by exporting customers vary considerably depending on their location and local network conditions. This means that some customers consistently experience curtailment while others will have unconstrained exports. We expect material increases in curtailment with further DER integration over time.

B. The AER should rely on reputational incentives in the short-term

Reputational incentives can be strong for DNSPs in certain circumstances and may be sufficient in the short-term to supply incentives for DNSPs to provide export services. We consider reputational incentives best meet the AER's proposed criteria and are sufficient to address current concerns in the short-term, as for the reasons stated in section 1.A above it is too premature to adopt bespoke incentive mechanisms across all DNSPs.

While bespoke incentive mechanisms in the future may include financial incentives, we do not consider this matter calls for further consultation right now.

C. Additional comments on the proposed financial incentives

In relation to elements of financial incentives proposed in the Consultation Paper we:

- Agree with the AER that there are significant concerns with extending the STPIS to export services, including issues related to downstream data visibility;
- Consider cost-reflective price signals, via Basic Export Levels (**BEL**), are a more efficient way of ensuring customers can receive compensation for exporting their solar generated energy to the network, as opposed to implementing a guaranteed service level (**GSL**) regardless of the local characteristics of the network. A GSL becomes an inefficiency as not all locations in the network have an intrinsic hosting capacity equal to the BEL. For example, Ausgrid's proposed export tariff for 2024-29 includes a reward component between the hours of 3pm and 9pm – incentivising customers to use the network efficiently.
- Note that the AER's CECV (as currently estimated) is materially understated because of the wholesale market assumption it adopts and the exclusion of generation and transmission investment from its opportunity cost calculations. Accordingly, we do not consider the current CECVs provide an appropriate set of values for the quantification of incentive payments at this stage. We are cognisant that the AER's current modelling sets CECVs at zero for many 30-minute dispatch intervals. This could create the implication that there is no reward or penalty at these times and is therefore likely to materially understate the actual value customers place on being able to export energy back to the grid.

2. Export service performance reports

A. We support the AER exploring potential export service performance metrics as part of a paper trial

We agree with the AER that export curtailment is extremely challenging and cost-prohibitive to measure – including for the reasons discussed in Section 4.5.1 of the Consultation Paper. In particular, we note that export service performance cannot easily or efficiently be measured in line with current approaches to measure import service performance (such as interruptions to import services per importing customer due to a network constraint). As such, we disagree with the AER's view that the ideal measurement of export service performance would use equivalent measures to those used to measure import service performance.

Given that DNSP performance for exports and imports cannot be adequately measured in equivalent ways, we would support the AER exploring potential metrics for reporting export service performance as part of a paper trial. Following the approach explored in collaborative research by South Australia Power Networks, Essential Energy and the University of Sydney on export service performance, we recommend the AER explore a combination of different performance measures as part of a paper trial, instead of exploring measures individually, to mitigate perverse incentives or service outcomes and to better reflect the level of export service provided to customers.

In the first instance, we encourage the AER to consider performance reporting that evaluates the ability of DNSPs to meet customer priorities. One example is the amount of time during the year that a customer can export to the grid, or export to the agreed level of service (in the context of dynamic or flexible export limits).

B. We support Option 2 - a two-phase approach to develop the inaugural export performance report

We support the AER's two-phase approach to develop and publish the inaugural export performance report together with existing performance reports because Option 1 overlaps with the submission date for our January 2023 regulatory proposal. We welcome early consultation on the proposed timeframes, which we anticipate being reissued given inter-dependencies with other regulatory processes underway.

3. Benchmarking reports

A. We support adopting a benchmarking approach that sets appropriate baselines for comparability

Comparability between DNSPs is essential for effective benchmarking of export services.

In our view, the benchmarking techniques outlined in Box 3 of the Consultation Paper do not account for export services as an output because none of the measured outputs take into account exported energy flows – a key measure of how much exported energy is being facilitated. We recommend the AER change its benchmarking techniques to adequately take export services into account.

Failing to adequately account for export services as an output when benchmarking would mis-estimate any efficiency scores produced to the extent that expenditure benchmarked using the models includes costs related to the delivery of export services. Consequently, the relative efficiency of distributors supplying export services could be under- or overstated by attributing the inputs used for export service delivery to existing benchmarking output measures.

We recommend the AER consider the following approaches which are based on options proposed in the Consultation Paper to adjust benchmarking techniques so that they account for export services:

<u>Approach 1 – Re-specify the econometric benchmarking models by including one or more new output variables to reflect the export services being provided by DNSPs</u>

While we consider this to be the ideal approach, we note it may not be practical and would require further consultation by the AER on objective measures of export services because the AER's econometric benchmarking models currently utilise input and output data relating to DNSPs in Australia, Ontario and New Zealand.

If the AER continues to use data on overseas DNSPs within its benchmarking analysis, we consider it would not be appropriate to re-specify the way in which Australian DNSPs report certain variables used in the analysis (i.e. to account directly for export services as a relevant DNSP output) without also ensuring that the same variables are reported in a consistent way by New Zealand and Ontarian DNSPs.

Accordingly, the AER may need to consider whether it is appropriate to discontinue the use of New Zealand and Ontarian DNSP data within its econometric opex benchmarking models. This may be appropriate, particularly in the longer term, given inconsistencies in the way data is currently reported by DNSPs in Australia, New Zealand and Ontario, which could introduce distortions into the measurement of the efficiency for Australian DNSPs over time.

Approach 2 – Exclude any incremental (direct and indirect) costs related to export services from the costs being benchmarked'

This approach would ensure that the costs that are benchmarked relate to the existing outputs that are specified as explanatory variables in the AER's benchmarking models. Export services opex incurred by DNSPs could then be benchmarked or efficiency-tested separately (e.g., through Partial Productivity Indicators or other more sophisticated benchmarking analysis). Under this approach, it would not be necessary to change the definition of the output variables or the introduction of an export services output variable (unlike Approach 1).

B. We do not recommend calculating an OEF for export services

We note the Consultation Paper also proposes calculating OEF for export services that reflects different operating environments. While this option is possible, we consider it undesirable because:

- The role of OEF adjustments is to account for exogenous differences between DNSPs that are beyond management control. The delivery of export services is within management control and is therefore not an exogenous factor that should be controlled for using OEF adjustments. Export services should therefore be accounted for directly in the benchmarking models or data;
- Implementation of this option would require the same information (i.e., estimates of the incremental costs related to export services) as would be required to implement Approach 2. If export services-related opex could be estimated and reported, it would seem more robust to be included directly in the benchmarking models rather than being applied as ex-post OEF adjustments; and
- Estimated efficiency scores for each DNSP depend on the estimated relationship between the inputs (i.e., opex) and outputs specified in the model. If the opex that is benchmarked using the models includes costs related to the delivery of export services, but the outputs do not account for the export services being provided by DNSPs, then the efficiency scores produced by the benchmarking models will (in part) reflect differences between DNSPs in the delivery of export services, rather than true efficiency. This could result in some DNSPs being identified as efficient 'reference DNSPs' when in fact they are not, and vice versa. The use of ex-post OEF adjustments would not address this problem because, in the AER's benchmarking process, the OEF adjustments are made (to a DNSP's efficient comparison point) after DNSPs are identified as reference or non-reference DNSPs.

C. The AER's proposed staged approach

It follows from section 3.B above that we do not agree with the AER's proposed approach to considering export services as an OEF as part of Stage 1 in its consultation approach in relation to benchmarking. We are otherwise supportive of the AER's two-staged approach and suggest that:

- As part of Stage 1, the AER should consult with DNSPs on how incremental export services-related costs should be defined and reported, and then, following this consultation, publish clear guidelines on how these incremental costs should be reported by DNSPs to ensure reported costs are comparable.
- Stage 2 could then proceed as described by the AER in the Consultation Paper, including further consultation on model specification options.