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Mr Mark Feather
General Manager
Australian Energy Regulator (AER)
GPO Box 520
Melbourne VIC 3001

Submitted via email: AERringfencing@aer.gov.au.

AER DRAFT DISTRIBUTION RING-FENCING GUIDELINE – VERSION 3

Endeavour Energy appreciates the opportunity to provide this response to the AER's Draft Distribution Ring-fencing Guidelines (the draft guideline). The draft guideline aims to provide clarity on how it will apply to new services provided by distribution network service providers (DNSP) from energy storage devices (ESD) and stand-alone power systems (SAPS) and includes:

1. Providing DNSPs an automatic exemption from the ring-fencing guideline to provide generation services for DNSP-led SAPS up to the applicable generation revenue cap and with quarterly reporting requirements. SAPS generation services beyond this cap will require a ring-fencing waiver. We support these amendments but consider the network categorisation could be improved and/or the threshold increased for the lowest category.
2. Prohibiting DNSPs from providing other (non-distribution) services from a network ESD. DNSPs will have to seek a waiver from the ring-fencing guideline to provide any other services from a network ESD. We accept this approach with the exception of networks providing third parties access to network owned ESD's. A less restrictive approach for this access service would be less burdensome and better facilitate innovative services that are valued by customers.
3. Clarifying and improving relevant obligations to make the guideline clearer and simpler to understand and apply. We support these various amendments.

We acknowledge the limited information and uncertainty the AER must balance in accommodating the emerging and potential markets for SAPS and ESD related services. It is appropriate for regulatory safeguards to be established to ensure the participation of networks in these markets is both transparent and non-discriminatory. However, any regulation must also be proportionate to the risks identified and acknowledge the benefits to customers associated with utilising the resources and knowledge of networks in growing these markets and unlocking the customer benefits associated with SAPS and ESD's.

We support the approach to SAPS exemptions and consider it could be improved further

The proposed SAPS requirements are a positive step and practical improvement on the AEMCs DNSP-led SAPS framework. We support a broad based exemption approach but consider the proposed low generation revenue cap for Category 3 networks may prove impractical. For Endeavour Energy, a network with over 1 million customers and almost 50%[1] of its distribution route lines in rural areas, this threshold equates to 5 SAPS. Where a DNSP is only permitted to deploy a few SAPS under the exemption threshold it may disincentivise investment in identifying and building SAPS opportunities and business capabilities.

Whilst a waiver remains an option, the administrative burden of a waiver process will prove prohibitive relative to the ease and certainty of a traditional network solution. We believe there is significant scope

[1] Source: 2019-20 and 2020 Economic Benchmarking Regulatory Information Notices - Table 3.7.2

to increase the exemption threshold to a level where the cost and benefit of waivers are more closely balanced and can better stimulate the emergence of the competitive market for SAPS services.

Further, given the uncertainty surrounding the estimates upon which the thresholds are based, it would also be appropriate to provide a margin for misspecification error. This could be achieved by considering alternate network categorisation options or adjusting the proposed thresholds (specifically the Category 3 threshold). We consider the risks of doing so to be low. Networks would still engage third party providers to adopt the lowest cost / most efficient option as the regulatory framework incentivises. This is because the SAPS generation revenue is likely to remain trivial for Category 3 networks compared to the potential cost savings, service improvements and specifically bushfire risk reductions that DNSPs could achieve from deploying SAPS.

In order to unlock the full value of ESDs we recommend a less restrictive and more targeted approach is taken for networks providing third party access to ESDs

The draft amendments require an individual waiver to be sought for any other services a network intends to provide with an ESD. Whilst we understand the concern with allowing networks to provide non-distribution services with an ESD, we are surprised this concern extends to networks providing third parties access to a network ESD (for the third party to then provide other services) and that this type of arrangement is not automatically exempt from the ring-fencing guideline or subject to a more targeted set of regulatory controls.

Similar to SAPS, we appreciate this is also an emergent market with a degree of uncertainty surrounding how it will develop. Whilst there is uncertainty around ESD's we do not consider an individual waiver assessment approach is appropriate in instances where there is a low chance of harm, low cost materiality and / or alternative regulatory options available which are less intensive and costly.

We are particularly concerned with the potential harms that have been raised during consultation on the draft guideline. In many cases these harms represent serious allegations of misconduct that are theoretical in nature and are not supported by specific cases or evidence. We would welcome an opportunity to engage with third parties and / or the AER to directly address any such concerns (perceived or otherwise).

We consider a waiver based approach to third party access is disproportionate for a number of reasons:

- **Existing regulatory protections**: many of the harms, such as discrimination, over-investment, cost allocation, etc, are already protected against by existing regulations. In particular, the service classification process, expenditure incentives and planning requirements, cost allocation provisions, ring-fencing obligations (particularly those relating to discrimination) and access requirements (i.e. connection policy and standard connection contracts) all provide significant protection against the noted harms.
- **Immaterial costs**: the network investment in the ESD, i.e. what is included in the RAB and funded by network customers, will be restricted to the network benefit/service that it provides. In many cases this will be a relatively immaterial portion of the ESD cost with third parties funding the majority of the ESD where this represents the primary use of the asset and value stack. In instances where the network investment in the ESD is low it would not be proportionate to subject this to a waiver process.
- **Reputational damage:** there is a high degree of regulatory and public scrutiny associated with ESD's and emerging energy markets. There are significant financial and reputational consequences of non-compliance in conjunction with the AER's extensive oversight and information gathering powers. It is highly unlikely networks would actively discriminate and abuse their market power in full view of the regulator, and in breach of existing obligations, at a time when they are trying to demonstrate the value of their participation in these markets.

- **Waiver based approach is not optimal:** the transparency and confidence the AER wishes to provide market participants may not necessarily be delivered by a waiver process. The waiver process provides the AER with access to information and direct oversight. However, a defined criteria or deemed approval process could better provide investment certainty whilst also requiring for there to be a transparent and open procurement process and information sharing.

Similar to SAPS, it may also be appropriate to provide automatic exemptions to specific uses of ESD's. For instance, the service of sharing an ESD with a third party, or where the network investment in the ESD is below a certain level or the ESD is below a certain size (for instance 1.5MW). All of these options could help reduce the regulatory burden and proportionality of the draft guideline.

In our view, claims that DNSP involvement would distort competition and impede the emergence of competitive markets are not supported by evidence. Similar unsubstantiated views influenced the 'Power of Choice' metering reforms with a broad consensus since emerging that the competitive market has generally failed to deliver the expected service improvements to customers[2].

We are concerned that the draft guideline could stifle the customer benefits that would otherwise be delivered if DNSPs were afforded greater flexibility to facilitate third-party provision of these services. We consider greater regard should be had for the views of networks, customer advocacy groups, local councils and smaller retailers who collectively recognise the value of network involvement in ESD's, particularly in community battery services.

We respectfully maintain that the presumption of harm that underpins the guideline is not shared by these stakeholders. On the contrary, throughout our engagement to date, local Councils have eagerly embraced Endeavour Energy's preliminary discussions regarding community batteries, which have received warm support from the two participating Councils (Blacktown City and Kiama) as well as unsolicited interest from surrounding Councils also wanting Endeavour Energy to deploy ESD in their local government areas. Importantly, key stakeholders and customers at Endeavour Energy's Future Grid workshop on 10 June 2021 were asked to identify and prioritise innovations they believed Endeavour Energy should deliver, and community batteries was the number one innovation nominated by our peak customer and stakeholder reference group.

We therefore consider the interests of customers would be best promoted by a less restrictive regulatory approach; one that better supports networks participation in community battery partnerships in line with stakeholder expectations.

Overall, we share the views detailed in the ENA submission. Our feedback on possible refinements to the draft guideline is provided in the Appendix A along with examples of our recent experiences with non-network market providers. If you have any queries or wish to discuss our submission further, please contact myself on (02) 9853 5195 or Colin Crisafulli, Manager Network Regulation at Endeavour Energy on (02) 9853 6017 or via email at colin.crisafulli@endeavourenergy.com.au.

Yours sincerely

Francoise Merit
Chief Financial Officer

[2] See submissions to the AEMC's Review of the Regulatory Framework for Metering Services: Public Interest Advocacy Centre, Energy Consumers Australia, Energy Networks Australia, Energy & Water Ombudsman NSW, Australian Council of Social Services

Appendix A: Response to the Draft Ring-fencing Guidelines - Version 3

Stand-alone power systems

Generation revenue caps for some Category 3 networks need to be set higher to incentivise efficient SAPS deployments

We agree that there are likely to be many instances where SAPS generation services cannot be procured and the DNSP will be best placed to act as the SAPS Resource Provider (SRP) to allow the SAPS project to proceed. The proposed broad-based exemption framework will assist networks to effectively plan and deploy SAPS in a timely manner in such cases. The proposed tiered exemption framework permitting rural DNSPs to act as the SRP for more SAPS under exemption is also an appropriate distinction to make.

However, there is a high degree of uncertainty surrounding the initial estimates of candidate SAPS sites. These estimates may prove inaccurate as the cost of SAPS change and as networks conduct more detailed reviews of opportunities as the SAPS framework is formally introduced and networks become more familiar with it. In particular, the Category 3 generation revenue cap is prohibitively low for several DNSPs where the distribution area includes significant rural and remote regions and high-risk bushfire areas. Whilst it may align with initial estimates provided by networks it provides no margin for error in these preliminary estimates. For instance, as the table below demonstrates, the draft guideline permits Endeavour Energy to act as the SRP under an exemption for fewer than five 'average sized' SAPS.

Table 1: SAPS permitted under the proposed SAPS generation revenue exemption threshold

Category	Revenue cap as a % of ARR	DNSP	Exempted SAPS
1	0.20%	Ergon	1492.4
		Essential Energy	961.2
2	0.07%	AusNet Services	271.8
3	0.001%	Ausgrid	7.9
		Endeavour Energy	4.9
		Powercor	3.7
		SA Power Networks	4.8
		TasNetworks	2.2
		CitiPower	1.8
		Evoenergy	0.8
		Jemena	1.6
		PWC	1.1
		United Energy	2.5
		Energex	8.6

'Hybrid' networks including Endeavour Energy will typically have more SAPS candidate sites than the urban networks that they are grouped with and will face similar challenges in procuring the suite of SAPS generation services encountered by Category 1 and 2 networks. From our perspective, we consider the spread of our customers in rural, remote and high bushfire risk locations is more closely aligned to AusNet Services than it is to Jemena, CitiPower or United Energy.

We acknowledge that there is limited information upon which to base the exemption thresholds and network categorisations. However, alternate methods are available such as categorising networks by the proportion of rural route line length as detailed in the ENA submission using available RIN data which we propose is more suitable.

Ultimately the thresholds will be arbitrary, but we would recommend the Category 3 threshold (or equivalent under any revised categorisation approach) by materially increased. We would submit that in the absence of categorisation changes, a 0.01% threshold for Category 3 would better balance the need to provide investment certainty and the uncertainty around the competitive market viability for SAPS network solutions.

Accurately estimating the number of SAPS transitions ahead of the formal implementation of the DNSP-led SAPS framework is challenging and problematic

As aforementioned, information provided by DNSPs on their prospective SAPS deployments was used to develop the proposed generation revenue caps and network groupings. In Endeavour Energy's case, we did not envisage this information would be used in a deterministic way and therefore only provided a high-level and unverified estimate of only the most obvious candidate SAPS sites supplied by poles and/or conductors that were at or close to end-of-life. These estimates were derived during consultation on the Australian Energy Market Commission's (AEMC) *Alternatives to grid supplied network services* rule change consultation in 2017. Therefore, it is reasonable to regard our estimate outdated and likely understates our true short-to-medium term SAPS rollout expectations.

Providing an accurate, fit-for-purpose estimate requires us to consider how SAPS will be holistically integrated into our overall network planning framework and reliability strategy. The impact to parts of our network from the 2019-20 Black Summer bushfires also highlighted the importance of embedding network resilience into our network design and planning strategies with SAPS a key tool to delivering strategic network resilience objectives.

However, it is difficult to provide an alternate estimate in responding to this draft guideline for a number of reasons. As the DNSP-led SAPS framework has not been formally implemented we are yet to formally develop a SAPS strategy or plan. This process will not likely commence until there is greater clarity and certainty on how the framework will operate in practice and in conjunction with yet-to-be-determined jurisdictional requirements and standards. It is during this process where we would expect to have a clearer understanding of locations where SAPS could be deployed to deliver a cost saving relative to conventional network asset replacement, improved reliability outcomes for customers and strengthen network resilience against natural hazards.

Our SAPS strategy and plan will not likely be developed prior to NSW opting into the framework. However, once the framework is formalised and implemented, we may require third-party support to review SAPS opportunities across our entire network.

If our initial SAPS deployments are successful, we foresee transitioning from a reactive approach to a more proactive approach where customers are transitioned to a SAPS once it is economically justified and not just considered when lines and poles reach end-of-life. Continued reductions in the cost of SAPS and greater confidence in SAPS supply to meet customer needs will also likely drive deployments well beyond levels first anticipated during the *Alternatives to grid supplied network services* rule change consultation.

DNSPs are not incentivised to compete for SAPS generation revenue

In response to concerns that DNSPs may use their monopoly position to compete for generation revenue and crowd out competition, it should be noted that DNSPs operate under a revenue cap and earning SAPS generation revenue will not add to their overall revenues. We also note the value of SAPS generation revenue to most networks will be immaterial relative to network allowances and the incentive to compete in SAPS markets has been significantly overstated.

The AEMC's package of rule changes underpinning the DNSP-led framework includes an amendment to cl. 6.4.4(c)(3) allowing the AER to deduct revenue earned by a DNSP from the sale of energy from a SAPS from the DNSP's revenue allowance. The AEMC commented[3]:

> *The [Shared Asset] Guideline as currently drafted does not provide for the circumstance where SAPS generation assets would be providing both an input used to provide a standard control service and a non-distribution service (that is, generation to the customer) from the outset. In addition, the current version of the guideline contains a materiality test, such that not all unregulated revenue is deducted from the DNSP's revenue allowance. The Commission*

[3] AEMC, Final Report: Updating the regulatory frameworks for distributor-led stand-alone power systems, 28 May 2020, p.59

considers that, for SAPS generation assets, all payments received from AEMO should be considered material, as the DNSP would have incurred no extra cost to earn them.

These reductions will be given effect via changes to the Shared Asset Guideline the AER is required to make and represents a departure from the typical way in which Shared Asset Guideline allows DNSPs to earn unregulated revenue up to 1% of their annual revenue requirement before deductions are applied. This change removes any opportunity for DNSPs to increase their overall revenue and enables all network customers to share in network tariff reductions unconstrained by a materiality threshold.

Our interest in SAPS is limited to its potential to reduce bushfire risk, improve service performance and lower network costs rather than it as a source of energy-based revenue. We do not value accessing relatively small SAPS generation service revenues. SAPS deployment decisions and business cases for SAPS projects will be based on the relative net benefits between the SAPS and replacement option exclusive of any generation revenue benefit accrued to the DNSP.

A flexible approach is needed to allow DNSPs to procure SAPS services from exempted SRPs

We recently tested the market to ascertain whether third parties could deliver the suite of SAPS generation services to a remote site and the extent to which they could fulfil the requirements of the SRP in accordance to the AEMC's DNSP-led SAPS framework.

Proposals from interested parties focussed on designing a SAPS to meet the demand profile of the site with quotes centred on the provision and installation of SAPS generation assets (e.g. PV arrays, inverters, battery storage, diesel generator).

Some proponents also offered operating and maintenance as a separate, secondary service without committing to specific service levels or KPIs as it was recognised performance requirements and standards vary across networks and within network boundaries and the terms of compliance with these would need to be negotiated with Endeavour Energy at a later stage. Ongoing support was generally offered via remote monitoring capabilities with some proposing to sub-contract fault response and generator refuelling to local providers to reduce response times.

Notably, proponents demonstrated limited understanding of the DNSP-led SAPS framework and its service delivery model. More importantly, there was no reference to the SRP role or the registration requirements and other obligations attached to the role.

Overall, the feedback revealed that third-parties are generally looking to provide the same service offering to DNSPs as private, self-sufficient SAPS owners (i.e. SAPS design, provision and installation only) with limited interest in committing to ongoing obligations with respect to the service provided via the SAPS in order to receive the comparatively low and potentially volatile energy-based revenue. From a commercial perspective, the forecast $1,600 - $1,800 p.a. in generation revenue pales in comparison to the $200,000 - $300,000 sale of an 'average' SAPS with no ongoing commitments or responsibilities outside of Australian Consumer Laws.

With the possible exception of large microgrid conversions, the value of SAPS generation revenue will likely be offset by administrative, registration and other regulatory costs and deter third-party SAPS providers from adapting their service models and registering as the SRP.

Where SAPS providers do not value becoming an SRP, we consider they should be able to apply for an exemption from registering as an SRP. This will require AEMO to update its generator exemption and classification guidelines for SAPS and the AER to provide clarity on a simple process which enables DNSPs to procure services from exempted SRPs. We consider it essential that AEMO provide clarity on an SRP exemption process prior to the framework being implemented.

There will also be situations where DNSPs will need to become an exempt SRP. For instance, when a DNSP is required to step in immediately following an SRP failure or exit, or where the SRP has failed to meet its contractual obligations and KPIs (e.g. below-standard reliability, failure/delay responding to reported faults etc). This way, DNSPs will be able to waive their right to SAPS generation revenue as the exempt SRP in order to manage their compliance to the guideline.

Energy storage devices

Requiring ring-fencing waivers for each ESD project will deter value-adding collaborations between networks and third parties which can maximise benefits to customers

It is appropriate for there to be regulatory oversight, and in some instances restriction, of the participation of networks in certain activities. It is important that the application of regulation is proportionate, evidenced based and in the interests of customers. We therefore accept that networks be subject to a waiver process in providing non-distribution services with ESDs. However, this is with the exception of networks partnering with third parties to unlock the full value stack of an ESD (i.e. networks providing the non-distribution service of third party access).

We do not consider there is a material risk of harm for networks providing third parties the opportunity to make use of network owned ESD to provide other services to customers. In fact, we consider this service will help promote retail contestability and increase growth in the ESD market. There have been successful network ESD projects and trials to date which have involved third parties to optimise value stacking benefits. Endeavour Energy, and presumably other networks, is also engaging positively with third party suppliers on procuring network support from grid-scale ESDs. We are not aware of any evidence from these trials and network support procurement processes of cross-subsidisation or discrimination concerns. Below, we provide further detail of our recent experiences.

Case Study 1: South Penrith network deferral

Endeavour Energy's FY19 Distribution Annual Planning Report (DAPR) included information on an emerging constraint in the South Penrith area. Based on demand forecasts, it was expected that a new Zone Substation would be required by FY23 to address the need, subject to a RIT-D assessment.

During the 'options analysis and case for investment' stage of our investment governance framework, which aligns to the AER's RIT-D we typically identify short-term measures to defer the network investment. Following the exhaustion of these options, the network option becomes credible and a RIT-D process is triggered to solicit longer term non-network solutions.

During this phase Endeavour Energy received an unsolicited offer from a third party based on the information contained in our DAPR in April 2020. The third party proposed a grid connected battery to curtail peak demand and defer a traditional network solution.

To our knowledge this would be the first large-scale independently owned grid-connected battery in Australia. The battery forms part of the Emerging Energy Program, a NSW Government Clean Energy initiative that provides funding to assist in the development of innovative, large-scale electricity and storage projects in NSW. The third party has made a connection application to connect a 20MVA/40MWh unit to the 11kV busbar at Penrith Zone Substation. As an independently owned battery the third party would unlock the full value stack of the battery.

Our understanding is that the main sources of income would be energy arbitrage against the NEM spot market and frequency support to AEMO through the FCAS market. A relatively small portion of the value would be provided by Endeavour Energy in the form of network support payments.

However, in discussions with the third party it was made clear that the RIT-D process, whilst designed to promote non-network solutions, is not well suited to grid-connected battery projects of this nature. The RIT-D adopts a 'just in time' approach where energy demand needs to reach the point in which support is required (and can be economically justified) in order to solicit offers from the market in accordance with prescribed timelines.

This approach makes it difficult for new technologies and/or long lead time solutions to be developed, such that they can be offered as technically and financially acceptable alternate solutions.

Whilst the network support payments would form a relatively smaller component of the value stack, we committed to supporting the third party in its efforts to secure a grant from ARENA for financial assistance and liaising with the AER on RIT-D compliance. In addition, Endeavour Energy committed to providing:

1. Engineering resources to assist with issues affecting control, protection and operation of the Endeavour network at the grid battery location.
2. Provision of data from our Penrith Zone substation, for example power quality data, to assist in understanding any impacts of the battery operation on the network and vice versa.
3. Coordinating the deployment of thousands of customer smart meters to enable removal of the AFIC system for hot water control and enable split bus operation at Penrith.
4. Sharing of the smart meter data with the third party to assist in evaluation of the battery system operation.

We held discussions with the AER in September 2020 and wrote to the AER in February 2021 to confirm our intention to enter into a Network Support Agreement (NSA) with the third party was compliant with the RIT-D (and potentially DMIS) requirements. This included providing assurance that this NSA represented the lowest cost/highest value solution and that a RIT-D process would be unlikely to uncover better options at the expense of precluding this third party from offering support given their financial and technical timeline requirements.

It should be noted that the value of the network deferral has reduced (via the discount rates applied) in line with the application of the 2018 Rate of Return Instrument (RORI) to Endeavour Energy from FY20 in accordance with declining interest rates.

We note that the third party has been appreciative of our information sharing and proactive support in obtaining its ARENA application, overcoming regulatory constraints and supporting the development of a competitive, third party, non-network energy storage service provider market. Overall, we have invested significant time and resources in supporting this third party proposal.

Whilst there will be difficulties associated with incorporating new technologies and solutions in the regulatory framework these difficulties are not reflective of a lack of effort or support from Endeavour Energy. Instead, our efforts serve as compelling evidence that Endeavour Energy has been going above and beyond regulatory requirements to support third party owned energy storage solutions contrary to suggestions of uncooperative and/or discriminatory network behaviour.

Case Study 2: Box Hill RIT-D negotiations

In April 2020 Endeavour Energy released a Non-Network Options Report (NNOR) to solicit non-network options to cater for forecast demand growth in the Box Hill Development Area within the North West Priority Growth Area.

Whilst the Request For Proposal (RFP) closing date was July 2020 we received an unsolicited, non-binding offer for a grid-scale Battery Energy Storage System (BESS) from a battery supplier in November 2020 in a late response to the NNOR. In the absence of other non-network solutions we engaged further with this provider and provided them with a further opportunity to refine their proposal. We then received a revised non-binding offer for a BESS solution from the third party.

Since November 2020 we engaged extensively with this provider with the aim of reaching a binding offer within the RIT-D timeframe. This involved multiple weekly meetings between April and early June 2021 with the provider's regulatory and commercial teams.

During this time, both parties have explored options for improving the competitiveness of the BESS solution. For instance, the third party submitted a request for a full exemption from paying Network Use of System (NUOS) charges. Whilst in May 2021 Endeavour Energy separately engaged with the AER to test the inclusion and valuation of additional market benefits in the RIT-D process.

Despite these deliberations Endeavour Energy had to continue to progress the process in accordance with the RIT-D timeframes and the practical need to address the network constraint in a timely manner. In light of the uncertainties around additional market benefits valuation the value of the network deferral was used to set the contract value ceiling in progressing negotiations.

We note this value has been substantively reduced by the impact of the 2018 RORI and subsequent interest rate reductions on the range of discount rates used to value the non-network option. Further, we did not agree to exempt the BESS from NUOS as we considered this would require a re-opening of our Tariff Structure Statement (TSS). We also do not consider waiving NUOS would be economically justified and consistent with the principles of technology neutrality, consistent with the AER's stated position from the recent Victorian Distribution Determinations where the BESS would be used to also provide non-distribution services.

The third party has since withdrawn their offer in June 2021 noting that the BESS value stack is not commercial at the network deferral value at the level of forecast grid support required. Further, the requirements for third party ownership rather than network ownership of the BESS was also not aligned with their preferred business model. Despite this, Endeavour Energy will continue to engage with the AER on additional market benefits to refine our approach for similar cases which may arise in the future.

It is important to note that Endeavour Energy complied with all obligations during this process and AER precedents (with respect to battery NUOS exemptions). The viability of the project was ultimately due to its lack of competitiveness and in no way did Endeavour Energy act inappropriately. Rather, Endeavour Energy engaged in a collaborative and genuine manner throughout the process in supporting the non-network third party provider.

Case Study 3: Albion Park non-network market solution

Endeavour Energy has an off-peak load control system (the AFIC system) at the Albion Park substation that was at risk of failure due to ageing condition and local load growth. To address this constraint we approached the market for non-network solutions, despite the network option being below the RIT-D threshold.

Following this, Intellihub proposed to install smart meters with load control functionality in the area that would be partly funded by Endeavour Energy. Whilst this was a technically compliant and least cost option there were regulatory constraints. Specifically, the Metering Fault Notification (MFN) prescribed in the Rules prohibits a network from triggering a meter replacement for any reasons other than a metering fault.

Endeavour Energy remained supportive of this solution, not only as it was it the lowest cost option, but also because it would enable customers to benefit from more innovative tariff offerings from their retailers such as dynamically controlled hot water systems that make use of solar generation (referred to by Endeavour Energy as Off Peak Plus).

Therefore, Endeavour Energy engaged with the AER in August 2020 to seek an exemption from this Rule requirement in order to progress the non-network solution and transition 2,850 customers to an in-meter based load control device. In support of the proposal, Endeavour Energy agreed to compliance reporting in order to monitor any customer complaints and opt-out requests. In addition, Endeavour Energy provided a financial incentive to ensure that customers incurred no charge or fee for the installation of the smart meters. Whilst Intellihub engaged with retailers to confirm their support for them acting as the Metering Coordinator at these sites. Intellihub wrote to the AER in June 2020 confirming there was retailer support.

As such, the AER agreed to Endeavour Energy's request and this project has commenced with positive customer feedback to date. This is another example of Endeavour Energy providing support and opportunities to third party providers beyond the requirements of the regulatory framework to support the development of the non-network market, innovative service offerings and positive customer outcomes.

Case Study 4: Distributed Energy Resource Management System provider (DERMS)

Endeavour Energy has commenced a partnership with a third party DERMS provider to develop an independently owned and managed marketplace for DER in conjunction with proposed ARENA funding. The platform will establish trading rules, aggregate bids and operate the market to enable participants to buy, sell and trade capacity and dispatch services at a market generation scale.

This opportunity will be to support the development of an operational market for advanced trading of DER 'flexibilities' and allow Endeavour Energy to acquire DER for network support at the lowest possible cost. The DER platform will also allow a suite of customers to participate in ancillary services markets.

We have been actively supporting this third party through its engagement with ARENA, providing in-kind support in developing the trial and are discussing demand support contracts to procure voltage and network support services to defer network expenditure in selected locations.

Once again these actions demonstrate Endeavour Energy's ongoing commitment to supporting the market for non-network services and systems. Rather than use our scale, expertise and information to frustrate the development of a competitive non-network market we are applying these advantages to support its development.

Our concern is that the sharing of network ESDs will be subject to a waiver process based on issues (perceived or real) with the RIT-D process or theorised harms in the ESD market that do not consider existing regulatory protections or more targeted solutions. As evidenced by the examples above, Endeavour Energy has been proactive and cooperative in supporting third party providers of emerging services. Our concern is that frustrations with aspects of the regulatory framework, such as the timeliness and investment certainty provided by the RIT-D process (or lack thereof) and the application of NUOS to ESDs, are being conflated with the conduct of networks.

If there are problems with the regulatory framework or the behaviour of certain networks we suggest these issues are addressed directly. The unnecessary imposition of costs on networks will inhibit their ability to enter into partnerships and it will reduce the commercial viability and competitiveness of ESD based network solutions. Given the cost of ESDs relative to traditional network solutions it is critical that economies of scale and scope are achieved, and multiple revenue streams accessed.

Restricting networks from contributing to the cost of shared projects also risks creating barriers to entry for ESD service providers who will be forced to rely on the revenue streams from other services to offset the initial and ongoing costs of the ESD to make their investment commercially viable. Similarly, providing access to a third party and having them co-contribute to the costs will in some cases be required for network investment in ESDs to be economically justified.

A waiver process could slow the deployment of ESDs and where they are installed by third-parties and encourage ad-hoc connections of smaller ESDs in locations where their value is not maximised or cannot be easily shared across a range of stakeholders as access would likely be limited to customers of the third-party.

The value of ESDs could be more widely shared through network operated community partnerships where open access arrangements encourage networks to provide more third-party providers (e.g. retailers) fair access to the ESD. This allows more customers the opportunity to benefit from storage services they would otherwise not be able to due to the relatively high cost of private ownership or not being a customer of the retailer owning/operating the ESD.

Shared use of network ESDs also provides an opportunity for smaller retailers and service providers to overcome the cost barriers of participating in storage services and reduce the risks of emerging markets being dominated by larger retailers crowding out participation by smaller competitors. We note that several community groups have also expressed a preference to partner with their DNSP rather than competitive providers.

In these ways, network ESDs can promote customer choice, access and retail contestability in the provision of innovative energy services in way that third-party owned or behind-the-meter ESDs cannot. By working with other parties, DNSPs are well placed to make investments based on accessing a wider range of benefits which will lower supply chain costs and lower network charges for all consumers.

The regulatory framework has substantial and effective safeguards to protect third parties from discriminatory network behaviour. Where additional protections are required targeted control measures should be considered.

In response to concerns that DNSPs will not be impartial to using their own ESD, we note the ring-fencing guideline has several significant protections and safeguards which deter DNSPs from engaging in discriminatory behaviour which to date have been effective in promoting competitive markets. Also, the incentive framework and planning requirements, which have been demonstrably effective in encouraging networks to make efficient investment decisions, will direct networks to the most efficient solution irrespective of which party provides the service or owns the underlying storage asset.

Furthermore, we note Tier 1 civil penalties apply for breaching the guideline and the associated reputational damage which would follow, including the prospect of permanent exclusion from storage services, provide substantial incentives for DNSPs to comply with cross-subsidisation and non-discrimination provisions.

Despite these controls, there remain specific concerns that DNSPs could unfairly discriminate through setting connection conditions and operating envelopes that disadvantage competitive storage providers by limiting their access and use. This view ignores the rules which set clear obligations and principles which guide each DNSPs connection policy to which connection agreements must be consistent with. Importantly, the rules require the AER to review connection policies and model standing offers and only approve them where the AER is satisfied the terms and conditions are fair and comply with applicable requirements of the energy laws. This limits the discretion networks have to set unfair connection charges or conditions for ESD proponents beyond those required to preserve the safety and security of the network.

Regarding concerns on preferential use of network owned or affiliated ESDs, we note that operation and dispatch will be automated and governed by algorithms and control devices that operate in accordance to pre-programmed settings and protocols to meet the needs of the system. There is little scope for DNSPs to interfere with complex and dynamic automated processes based on real-time data to discriminate the use of an ESD based on ownership.

We also consider the draft amendment 4.1(d) appropriately targets and prevents against this scenario. Requiring networks to provide transparency around the dispatch instructions and relevant data (upon AER request) to demonstrate prioritisation has not been unfairly pre-arranged or skewed to favour network ESDs could help alleviate concerns further.

In summary, we believe the ring-fencing guideline protections should apply to services from ESDs on the same terms as they apply to other services with targeted amendments added to the guideline only where there is clear evidence it has failed to deliver (or will) a level playing field for third party providers competing in storage service markets.

An alternative to the ring-fencing waiver process should be considered to better balance competition, transparency and investment certainty concerns

We appreciate the concerns arising from networks being allowed unrestricted access to provide contestable services accept regulation may differ between direct and indirect provision of other services from network owned ESDs. In regard to direct service provision, the waiver process represents a more proportionate and appropriate control measure. In special circumstances a network may be the lowest cost provider or only available provider of ESD services and a waiver process allows for consideration of these unique circumstances as they arise.

In relation to providing services indirectly (i.e. third party access), the proposed waiver process adds cost, burden, delay and investment risk insofar that waivers are administratively complex and are subject to public consultation and AER approval. Whilst the AER's additional guidance on factors it will consider when assessing ESD waiver applications is appreciated, it does not provide the investment certainty and transparency that other regulatory controls offer.

Ultimately, applying for waivers will complicate and deter collaborations between DNSPs and third parties to co-optimise the efficient deployment and utilisation of ESDs for network and other services. Networks are unlikely to engage in the process whatsoever if, as discussed above, weight is given to the views of parties who raise unsubstantiated claims and concerns - without adequate regard to how the regulatory framework mitigates adverse outcomes - to oppose waiver applications as a matter of default.

We consider a new process which allows networks to proceed with joint venture storage projects in tandem with satisfying procurement and information disclosure requirements would better balance the need to provide greater investment certainty for DNSPs and their third-party partners with information transparency to the AER, customers and market participants.

This approach, scaled proportionately to the materiality of the ESD project, would support efficient market development whilst providing the predictability needed to allow mutually beneficial joint venture ESD projects to proceed. It would impose accountability on DNSP's storage investment decision and

avoid the cost, delay and risk that comes from having to pre-test every instance of an ESD partnership with the AER.

The type of information DNSPs might be required to disclose might reflect those expected of a ring-fencing waiver application and include:

- Evidence external stakeholders have been notified of network needs and ESD value staking opportunities and locations.
- Responses/proposals from the market and reasons explaining the network investment decision.
- Cost benefit analysis and the expected benefits to consumers.
- Explanation of cost-allocation arrangements for the life of the project.
- Details on the access and operation protocols of the ESD for network purposes.

This information disclosure allows concerns around network coordinated community battery projects to be raised and addressed whilst the project is being developed. It also reduces the risk of outcomes that conflict with the interest of customers and the cost of remedial actions to correct for these outcomes. Whilst it may be appropriate for large storage projects to be subject to AER consultation and approval, a streamlined exemption process that is contingent upon meeting reporting requirement should be permitted for projects up to a capacity-based (and/or cost) threshold similar to the approach adopted for DNSP-led SAPS services. For instance, a threshold of 1.5MW would provide adequate protection against inefficient oversizing of network ESDs whilst providing third parties with a meaningful ability to utilise the ESD to provide contestable services.

It would also be more proportionate and aligned with existing regulatory precedents. For instance, the Demand Management Incentive Scheme (DMIS) currently recognises that there will be instances where it is most efficient for a network to provide the demand management preferred option (clause 2.2.2(b) of the DMIS). There may be numerous reasons for this being necessary; network management/safety concerns, the absence of a third party provider and non-commercial third party offers or not to scope offers for instance.

Where an in-house option is available to the network, the DMIS requires that competitive testing is carried out and that, should the in-house option be successful, the demand management proposal is approved by a delegate of the CEO of the DNSP. This declaration is to provide assurance that the estimated costs of the in-house proposal are efficient and derived from an approach consistent with an approach a DNSP would typically apply in estimating a project's costs.

A waiver process for sharing an ESD is restrictive and out-of-step with the pragmatism of these DMIS controls for in-house demand management projects. It would be inappropriate for tighter controls to apply to the sharing of an ESD with third parties given this is a more passive involvement in an emerging market than self-supply is in the demand management market.

It is important that the ring-fencing guideline does not classify services

In its draft decision the AER acknowledge ESD's are not currently defined in the NER or NEL and that it is seeking to provide more immediate clarity on the treatment of batteries under the guideline. This may result in future amendments should another definition of battery is introduced elsewhere in the future. We consider this to be an important caveat and one that we support. We assume it extends to clarification of the treatment of batteries not just in the NER or NEL but also via service classification decisions that form part of a distribution determination or review of the AER's service classification guideline.

However, we are concerned that in providing this clarity the ring-fencing guideline may pre-empt matters better suited to the service classification process and considerations prescribed in the NER. In

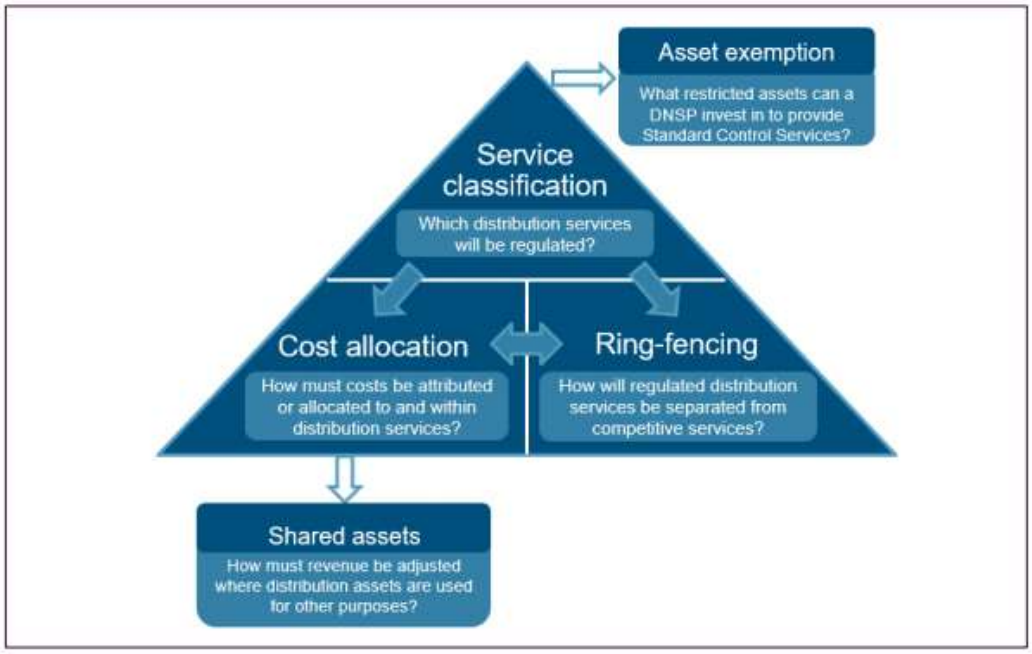
particular, the AER notes DNSPs currently have the ability to share assets under the ring-fencing guideline to[4]:

> *……facilitate the 'shared asset' rules introduced in 2012. This was to facilitate assets (such as poles) that were fully cost allocated for the provision of electricity services to be used for other purposes (such as to support telecommunication cables).*

The AER is correct to note that the shared asset guideline does not apply prospectively to investments. Instead, proper cost allocation is required when accounting for new investments to ensure a fair sharing of costs occur. We are therefore concerned with the addition to 3.1(d)(i) of the guideline that expressly prevents the sharing of ESD's.

This addition gives the impression of an asset based approach to regulation rather than a service based approach. We do not think this approach reconciles with the 'services versus inputs' NER based distinction in service classification that the AER highlights in its service classification guideline[5]. It also appears to not be aligned with the role of the ring-fencing guideline within the regulatory framework[6]:

Figure 1: Interaction between elements of the regulatory framework



Source: AER

Networks should not be precluded from sharing assets where cost allocation has been applied in accordance with the Rules or as may arise in the future under the shared assets Rules. We presume these guideline amendments do not supersede these other elements of the regulatory framework. Whilst it is appropriate to provide clarity on an uncertain regulatory matter, further consideration is required of whether this clarity is aligned with the NER and/or best suited to the ring-fencing guideline or the service classification guideline.

Other amendments to the guidelines

We support changes to the guideline to make obligations clearer and less administrative complex. Our feedback on key drafted amendments is outlined below.

- Staff sharing register enhancement: We agree that better capturing the movements of relevant staff for the previous 12 months in the register would improve transparency for stakeholders.

[4] AER, Draft electricity distribution ring-fencing guideline (version 3) Explanatory Statement, May 2021, pp. 39-40
[5] AER, Electricity Distribution Service Classification Guideline, September 2018, pp.7-8
[6] AER, Draft electricity distribution ring-fencing guideline (version 3) Explanatory Statement, May 2021, p. 2

To ensure this strikes an appropriate balance with the administrative burden on DNSPs, we suggest that 4.2.4(b) be amended to require DNSPs to publish updated registers to the website every six months rather than every three months.

- Timeframe to report breaches: We support increasing the timeframe to report breaches to 15 business days. However, reporting trivial and non-material breaches within this timeframe will create unnecessary burden and add cost for no offsetting benefit as no harm minimalization action will be required.

  We argue that the timeframe to report a ring-fencing breach should be commensurate with harm from the breach. This principle is reflected in the AER's Compliance Procedures and Guidelines which sets specific obligations and timeframes for networks to report identified NECF breaches to the AER. We consider networks, third parties and the AER would benefit if immaterial breaches continue to be reported in the annual Ring-fencing compliance reports.

- Timing of annual compliance reports: We support amending the current guideline so that annual compliance reports are due within four months of the end of the calendar year to which the compliance report relates. This will reduce some of the burden on DNSP regulatory compliance staff during a period where the annual RIN submission is prioritised. We have interpreted the transitional arrangements to mean that our next compliance report is required to be submitted to the AER on 30 April 2022 and cover the period 1 July 2020 to 21 December 2021.

  We also agree that allowing DNSPs to rely on information obtained from their financial year audit undertaken as part of the RIN process in relation to cost allocation obligations under clause 3.2 of the guideline avoids additional audits and is sensible.