Iberdrola Australia
Level 17, 56 Pitt St, Sydney, NSW, 2000
T: +61 2 8031 9900

Mr. Mark Feather
General Manager, Strategic Policy and Energy Systems Innovation
Australian Energy Regulator
GPO Box 520 Melbourne
VIC 3001

By email to: AERringfencing@aer.gov.au

Dear Mr. Feather,

Ring-fencing Guideline Electricity Transmission – Issues Paper

Iberdrola Australia welcomes the opportunity to provide a submission to the AER on the Ring-fencing Guideline Electricity Transmission Issues Paper.

The Iberdrola group has become one of the leaders in the Australian renewable energy market after acquiring Infigen Energy in 2020. The company operates more than 800 MW of solar, wind and storage batteries in Australia and has a significant portfolio of projects, of which 453 MW are under construction and more than 1,000 are in various stages of development.

Iberdrola is also recognised globally by its experience building, operating and maintaining electricity lines, substations, transformation centres and other infrastructures to transfer electrical power from the production centres to the end user across relevant jurisdictions as Spain[1], UK[2], US[3] and Brazil[4]. Iberdrola currently operates one of the world's largest power distribution systems, comprising more than 1.2 million km of distribution lines and more than 4,400 substations, which carry electricity to more than 34 million people around the planet. 40 % of the group's organic investment for the period 2020-2025 (more than €27 billion) will go to the Networks area. Iberdrola Australia is actively looking to fully roll-out these capabilities in country, demonstrating its strong commitment to Australia's energy transition.

While we have provided the submission template as an attachment, we have also provided detailed comments below. In summary, Iberdrola supports stronger ringfencing provisions on Transmission Network Service Providers (TNSPs), that should closely align with the provisions for Distribution Network Service Providers (DNSPs) in the November 2021 Electricity Distribution Ring-Fencing Guideline. We believe that effective ring-fencing guidelines will promote innovation, transparency, and efficiency in the delivery of new transmission.

[1] https://www.i-de.es/home
[2] https://www.spenergynetworks.co.uk/
[3] https://www.avangridnetworks.com/wps/portal/avangridnetworks/home
[4] https://www.neoenergia.com/en-us/about-us/lines-of-business/distribution/Pages/default.aspx

We agree with the AER that the market context in which TNSPs operated in when the original ring-fencing guideline was developed in 2002, are entirely different from today. The transition of the power system is accelerating and over the past 20 years transmission companies have primarily focused on maintaining the large existing electricity grid rather than the current requirement to build the new transmission that is vitally and rapidly needed to decarbonise the National Electricity Market (NEM).

Contestability

Fit-for-purpose ring-fencing guidelines for electricity transmission will be essential to promote competition that will need to underpin the delivery of new transmission in the NEM.

While there is already a degree of contestability applied in the provision of transmission in the NEM for specific connection assets, the current regulatory framework does not broadly support contestability in the delivery of new large-scale transmission projects, as detailed in the Australian Energy Market Operator's Integrated System Plan (ISP).

The current role of the TNSP encompasses planning and design, investment and construction, ownership and operation of transmission networks and the degree of contestability in transmission services is applied differently across the NEM:

State	***TNSP Ownership***	***Contestability***
New South Wales	Private	Yes (some, related to REZ)
Victoria	Private	Yes (all, via AEMO as the planner)
South Australia	Private	No
Queensland	Government	No
Tasmania	Government	No

This mix of contestability arrangements needs to be resolved to create a consistent treatment across the NEM. This will ensure that the unprecedented new transmission build required by the ISP will:

- Attract private finance and potentially alleviating budget constraints in the delivery of transmission.
- Achieve greater efficiency in the construction, operation and maintenance of transmission assets.
- Encourage innovation and idea generation, improving delivery and long-term efficiency.

As the AER stated in their own submission to the AEMC initial consultation paper for the Transmission Planning and Investment Review (EPR0087)[5]:

"*The AER considers that increased contestability in the provision of transmission services has the potential to solve a number of issues identified with both the planning and investment stages. These include driving efficient project delivery, enhancing innovation and value add in the identification and delivery of solutions, reducing information asymmetries by revealing efficient costs and addressing the perceived barriers to the equal assessment of non-network options at the planning stage*."

[5] https://www.aemc.gov.au/sites/default/files/2022-07/Options%20paper%20-%20contestability%20-%20TPIR.pdf, page 7

When developing the revision to the current 2002 ring-fencing guideline for electricity transmission, we would ask that the AER to keep in mind their own statement above on the need for contestability in the provision of transmission services. The AER must ensure that the updated ringfencing guideline accommodates the nascent contestable approaches in NSW and Victoria related to REZ, and any new contestable arrangements that may arise as part of the AEMC's current workstream on contestability, while also ensuring that the established contestable arrangements in Victoria are supported by a robust ring-fencing guideline.

Contestability in the provision of new large transmission is urgently needed to efficiently and cost-effectively deliver the scale and scope of transmission build needed for Australia.

Iberdrola operates internationally in multiple jurisdictions and the variety of contestable approaches and arrangements. The lack of strong regulatory regime, like ring-fencing, to ensure that third parties can compete fairly, in a level playing field, with regulated TNSP monopolies, reduces certainty and erodes confidence for those considering investing in Australia.

Alignment with Distribution Ring-fencing Guideline

The first principle for the ring-fencing guideline electricity transmission should be that it aligns exactly with the recently revised ring-fencing guideline electricity distribution[6]. We have not seen compelling arguments for why a TNSP should have any greater flexibility around ring-fencing than a DNSP.

Preventing Cross-Subsidies

TNSPs should be required to legally and functionally separate the transmission (regulated) business from any non-transmission (unregulated) business. There are no harms to the market or consumers from legally and functionally separating the regulated business from an affiliate unregulated business and this separation will deliver a fairer environment to support contestable provision of services.

Clearly defining the services that are prescribed and that may only be undertaken by the regulated monopoly TNSP, and clearly defining the non-transmission services that can delivered by an unregulated entity, are critical first steps in creating a ring-fencing guideline that will be robust and enforceable.

We agree with the AER that "*as the scope of potential services a TNSP may offer increases and the nature of TNSPs' businesses are changing/growing, it is increasingly important to have transparency between costs that are allocated to transmission services and other services to help prevent cross-subsidisation*[7]".

It is essential that the regulatory frameworks evolve to provide the necessary confidence that will underpin contestable approaches and investment in the cost-effective and timely delivery of new transmission, and so the benefits to consumers far outweigh the incremental cost of introducing more rigorous ring-fencing arrangements.

[6] https://www.aer.gov.au/system/files/AER%20-%20Ring-fencing%20Guideline%20Version%203%20-%20%28electricity%20distribution%29%20%20-%203%20November%202021.pdf
[7] https://www.aer.gov.au/system/files/AER%20-%20Transmission%20Ring-Fencing%20Issues%20Paper%20-%20May%202022.pdf, page 23.

The TNSPs should not be able to provide non-transmission services, such as telecommunications nor should they be able to provide contestable electricity services.

Coordination between TNSPs (and DNSPs) and third parties to deliver batteries at optimal locations will be critical for delivering value to the consumers. This can allow value stacking (delivering multiple benefits and hence revenue streams), improve overall reliability, and unlock higher shares of renewable energy. However, there are material risks to delivering low-cost outcomes if TNSP owned batteries are given preferential treatment.

TNSPs can effectively discriminate against third party battery providers since they can offer preferential connection arrangements (land and infrastructure availability, fees and technical support) to themselves or their unregulated affiliate. Where there are network constraints, the TNSP may preferentially ensure that its battery or that of an affiliate can be utilised for the intended network support service, while excluding other parties and therefore eroding their economic performance. This risk, or perceived risk, could hinder investment in otherwise valuable firming assets.

Furthermore, network connected batteries, at both the distribution and transmission levels, could be delivered more efficiently and cost-effectively by third parties. Such assets should at least be allowed to compete on a level playing field, accessing key information on network infrastructure and system performance. For this purpose, the TNSPs could procure a service from the third-party battery provider. A TNSP ring-fencing guideline that facilitates contestable approaches will be needed to deliver the additional 30 GW of storage that the ISP requires by 2030[8].

We agree with the AER that in an environment where Regulatory Asset Base (RAB) will grow from the current $22 billion[9] by nearly two thirds as a result of the ISP build out of $12.7 billion[4], that the 5% cap on revenue from non-transmission services is no longer appropriate.

It is not clear how a figure of 5% of RAB was determined to be an appropriate cap under which unregulated activities could be undertaken.

In 2002 when the original transmission ring-fencing guideline was developed the RAB was much lower. In 2006 the total TNSP RAB was $9.4 billion[10] and has risen 134% to $22 billion in 2021[5]. Spread over all the TNSP, 5% represents $1.1 billion of unregulated services that regulated monopolies can provide, without the requirement to be ring-fenced. This represents a significant carving out of activities for regulated TNSP that excludes third parties.

Year	Total NEM TNSP RAB	5% Cap across all TNSP
2006	$9.4B	$470M
2021	$22B	$1.1B
2030	$35B	$1.7B

Additionally, the RAB of each TNSP in the NEM is very different, ranging from 1.5 billion (TasNetworks) to $7.2 billion (Powerlink)[5]. This means setting a single cap that would be appropriate for all TNSP will

[8] https://aemo.com.au/-/media/files/major-publications/isp/2022/2022-documents/2022-integrated-system-plan-isp.pdf?la=en
[9] https://www.aer.gov.au/system/files/State%20of%20the%20energy%20market%202021%20-%20Full%20report_1.pdf
[10] https://www.aemc.gov.au/sites/default/files/content/fa459454-333a-4d11-843e-6de9c5dbe125/Draft-Rule.pdf

be challenging, noting that the current DNSP Ring-fencing Guideline has a range of caps to accommodate different DNSP revenues.

Given the cap represents significant opportunities outside TNSP core prescribed services that unavailable to third party providers and the fact that RAB of each TNSP is very different, the cap is no longer fit-for-purpose as a measure of services that a TNSP can provide, and the cap should be retired. It should not be replaced by waivers, since waivers will tend to weaken ring-fencing obligations, providing TNSPs with a route to continue to undermine the delivery of services that should be delivered contestably (and hence deterring competition and alternative business cases).

If a waiver approach is demonstrated by TNSP to be necessary then the process by which a waiver is applied for, assessed, and granted needs to be fully transparent. Any waiver (here and for any other service) must be subject to performance compliance, underpinned by reporting, investigation, and penalties to ensure that waivers are not an opportunity to circumvent ring-fencing obligations.

We support the introduction and strengthening of obligations for TNSPs for information access and disclosure. We agree that no waiver should apply and that these obligations should also apply to third parties providing direct control service to the TNSP. Adequate information sharing will be particularly critical for contestable delivery of new transmission.

Compliance

Compliance and timely reporting are an essential tool to ensure that TNSPs are transparently meeting ring-fencing obligations. This will deliver confidence to the market that TNSPs are behaving appropriately.

Even where compliance reporting has been in place for distribution and where the AER has undertaken a review of compliance, reporting alone has not been enough to prevent ongoing breaches. Even when breaches are self-identified by the DNSPs or identified by the AER, existing enforcement does not seem to be sufficient to prevent repetition[11]:

"*A number of distributors reported multiple breaches of their ring-fencing obligations. While individual breaches may pose minimal harm, repeated breaches of the Guideline by the same distributor may point to a systemic issue with a distributor's compliance processes*"

DNSPs have also not been responsive to rectifying approaches to ensure compliance[12]:

"*…we have been dissatisfied with how distributors have responded to identified breaches and the time taken to rectify these. We are concerned that some of these issues have continued*..."

We understand there has been no reporting on the compliance of TNSPs in the last 20 years and it is essential that not only is the level of compliance transparently shared regularly, but that the ring-fencing guideline offers disincentives to poor compliance, including penalties.

Waivers

[11] https://www.aer.gov.au/system/files/AER%20Annual%20compliance%20and%20enforcement%20report%202020-21%20%20-%20July%202021.pdf, page 12
[12] https://www.aer.gov.au/system/files/Annual%20Report%20Final.pdf, page 2

We agree with the AER that certain clauses should not be subject to waivers. In our view waivers should not be available to TNSPs for:

- The legal and functional separation of the business that delivers prescribed (regulated) service from the unregulated business that unregulated services (noting the existing arrangements for TasNetworks and Ausgrid, which should be grandfathered – these are the only arrangements that should be grandfathered)
- The obligation not to discriminate
- The obligation on information access and disclosure
- The obligation to comply and report on compliance
- As a replacement for any cap under which unregulated services are not subject to ring-fencing.

Waivers should be strictly limited to areas where it can be demonstrated that a TNSP's involvement will deliver benefits to consumers and there should be no presumption that the TNSP (or DNSP) can deliver new and innovative approaches any more efficiently and cost-effectively than a third party.

There are lessons that can be learnt from the application of DNSPs ringfencing waivers. It is not clear that the streamlined waiver process for DNSPs, particularly in relation to batteries, has any benefits for consumers. Even if some smaller trial projects warranted a waiver, once rollouts proceed at scale, third parties should be offered the opportunity to deliver cost savings to consumers.

We encourage the AER to adopt a waiver framework that leverages the issues identified during work on the revision of the distribution ring-fencing guideline. The AER need to ensure that any waiver approach is rigorous and transparent, providing a formal assessment framework for each a waiver that is robust, transparent and easy to follow. The decision criteria against which all waivers will be assessed should be clearly described and all applications, decisions and supporting reasoning must be made public and open to consultation, as this will provide certainty to all stakeholders.

All waivers should have a sunset or review date to account for potential changes in the technological or competitive landscape which mean that a waiver no longer serves the long-term interests of customers.

There should be a minimal transitional period from the 2002 guideline to the compliance dates of the revised TNSP guideline. There is no time to waste in delivering the low carbon transmission system Australia needs and robust ring-fencing arrangements will be the solid foundation on which investment and contestability will build.

Thank you for the opportunity to comment and we look forward to continuing to work with the AER to refine the design of the Ringfencing Guidelines. If you would like to discuss any of the issues raised in this submission, please contact Ricardo Da Silva on Ricardo.dasilva@iberdrola.com.au

Yours Sincerely,

IBERDROLA
AUSTRALIA

Ricardo Da Silva Alvarez

Networks Development Manager

Level 17, 56 Pitt Street, Sydney NSW 2000

M: +61 436 127 180