

Network REZolution Submission

AER Electricity Transmission Ring Fencing Review – Draft Guideline and Explanatory Statement

16 December 2022

General Manager
Strategic Policy and Energy Systems Innovation
Australian Energy Regulator
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Lodged by email: ringfencing@aer.gov.au

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RE: Electricity Transmission Ring Fencing Review – Issues Paper

Dear Mr Feather,

Thank you for the opportunity to comment on the AER's Electricity Transmission Ring Fencing Draft Guideline (Draft Guideline) and Explanatory Statement. We appreciate the AER consulting on these important issues.

The Network REZolution consortium – comprising Pacific Partnerships, UGL, CPB Contractors (members of the CIMIC group) and APA Group – brings a balance of experience in both contestable and regulated electricity infrastructure and is a shortlisted Applicant for the Central-West Orana Renewable Energy Zone (CWO REZ) Network Operator.

Leveraging the consortium's wealth of knowledge and APA's experience as operator of two registered Transmission Network Service Providers (TNSPs) in the National Electricity Market, our submission focuses discussion on the following areas:

- Fostering innovation and competition through ring fencing arrangements
- Challenges associated with the waiver process
- REZ ring fencing arrangements
- Costs and benefits of compliance.

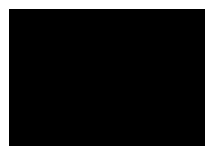
It is important that electricity transmission ring fencing arrangements are fit for purpose. In our view, a balanced and flexible approach to ring fencing will help drive markets towards innovation, timely service delivery and, ultimately, better outcomes for customers.

If you wish to discuss our submission in further detail, please contact John Skinner on [REDACTED] or [REDACTED].

Yours sincerely



Brendan Ng
Network REZolution Project Director
Pacific Partnerships



Darren Rogers
Group Executive Strategy and Commercial
APA Group

1. Submission

Key points

1. It is essential that ring-fencing supports, rather than hinders innovation, as this will ensure that energy can be delivered by the most efficient means possible.
2. Network REZolution broadly supports the AER's revised position on functional separation. Any new or expanded ring-fencing obligations will increase costs for TNSPs, and those costs will ultimately be borne by customers.
3. The proposed waiver process gives rise to some challenges for participants, including investor uncertainty arising from the waiver framework.
4. REZ ring fencing arrangements should be flexible and promote the most competitive bids possible.

1.1 Introduction

Network REZolution (Network REZolution, or the Consortium) – comprising of Pacific Partnerships, UGL, CPB Contractors (members of the CIMIC group) and APA Group – brings together leading infrastructure and energy companies to support the energy transition taking place across NSW.

Network REZolution is a shortlisted Applicant in the CWO REZ tender process. If successful, Network REZolution will contract with EnergyCo in the role of the Network Operator, in which Pacific Partnerships and APA will be equity partners.

The Consortium has extensive experience in delivering, owning and operating both contestable and regulated infrastructure investments across Australia:

- CIMIC, as the largest diversified infrastructure developer in Australia, has been involved in the delivery of over 30 privately financed infrastructure projects (valued at more than \$60 billion) during the past 25 years.
- APA is Australia's largest energy infrastructure business and builds, owns, operates and maintains over \$22 billion of energy infrastructure. APA is the operator of TNSPs registered in the National Electricity Market (NEM) and operates both regulated and unregulated assets across Australia.

We recognise that preventing cross subsidies and discriminatory behaviour is important to facilitate competition. As our participation in the CWO REZ network operator tender process highlights, we fully support competition in energy markets. Strong competition between experienced parties will help drive innovation, timely service delivery and ultimately, better outcomes for customers.

Network REZolution consortium members have a keen interest in the development of the Electricity Transmission Ring Fencing Guideline (the Guideline):

- APA is the registered TNSP of two fully regulated interconnectors in the NEM: Directlink and Murraylink. As registered TNSPs, Directlink and Murraylink will be subject to ring-fencing obligations under the Guideline.
- A new ring-fencing guideline will apply to the CWO REZ network operator. The AER has indicated that the Guideline made under the National Electricity Rules will likely inform development of a similar ring-fencing guideline for NSW REZs.

1.2 Fostering innovation and competition

It is important that ring fencing supports, rather than hinders, innovation. This will ensure that energy can be delivered by the most efficient means possible, and that customers do not pay more than necessary for the investment needed to decarbonise the NEM.

As the recent Integrated System Plan (ISP) has confirmed, the transformation and decarbonisation of the NEM calls for levels of investment in generation, storage, transmission and system services “that

exceed all previous efforts combined”.¹ The 10,000km of new transmission that is required to connect low-cost generation to customers is only part of the story. Investment is also required in storage, system services and other technologies that support the many gigawatts of variable renewable energy (VRE) that will be installed across Australia.

We recognise that ring fencing has an important role to play in preventing cross subsidies and ensuring that regulated businesses do not discriminate in favour of related parties. At the same time, competition, innovation and collaboration between all sectors of the energy supply chain will help ensure that the required investment takes place as efficiently as possible.

1.3 Compared to DNSPs, TNSPs are not homogenous

In contrast to the DNSP industry, which is characterised by a relatively homogenous group of business which, overall, provide a very similar set of distribution services, TNSPs do not have anywhere near the same homogeneity. Some of the characteristics that vary across TNSPs include:

- size and location – some transmission networks are much smaller than the primary TNSPs in each jurisdiction
- operating revenue – the annual operating expenditure of small TNSPs is much lower than the large incumbent TNSPs
- amount of control given to the market operator (e.g., AEMO directly controls operation of some assets)
- planning activities – increasingly, more planning activities are being undertaken by parties other than TNSPs (e.g., jurisdictional bodies)

In our view, ring fencing arrangements will be most effective when circumstances and market characteristics of the industry are recognised.

1.4 Functional separation

In our July 2022 submission, we raised concerns about the unnecessary costs associated with expanded functional separation obligations proposed in the AER’s May 2022 Ring Fencing Guideline Electricity Transmission Issues Paper.²

We therefore support the AER’s revised position to not impose obligations for separate offices, branding and staff. We acknowledge the AER’s position on retaining current obligations for TNSPs to separate marketing staff, so that they do not work for a ‘related electricity service provider’.³

We appreciate the AER considering feedback from stakeholders, including Network REZolution, on this issue. We agree that the benefits of functional separation will not outweigh the costs, given there is less risk of discriminatory behaviour, and associated harm to competition, from TNSP behaviour, compared to that of DNSPs. Some of the reasons for this include:

- The sophistication, size and resourcing of businesses operating in markets where TNSPs operate means there is less risk of discriminatory behaviour, and associated harm to competition, compared to that of DNSPs.
- Some TNSPs – particularly smaller TNSPs such as REZs and interconnectors – are not connected to regional reference nodes and have very limited opportunity to discriminate.⁴

1.5 Challenges arising from the waiver process

In the Explanatory Statement, the AER proposes a waiver framework akin to the distribution ring fencing guideline. Waivers will only be granted in limited circumstances and on a case-by-case basis.⁵

Broadly speaking, a waiver process increases regulatory and investment uncertainty. This is because the service provider must seek regulatory approval prior to commencing a project. This additional step creates risks and reduces certainty for investors. As submitted by other stakeholders including Energy

¹ AEMO, *2022 Integrated System Plan* (June 2022) 3.

² Network REZolution, Submission to AER, *AER Electricity transmission Ring-Fencing Guideline Issues Paper* (22 July 2022) 4-5.

³ AER, *Electricity transmission Ring-Fencing Guideline* (Draft Explanatory Statement v4, November 2022) 33-4.

⁴ Network REZolution, Submission to AER, *AER Electricity transmission Ring-Fencing Guideline Issues Paper* (22 July 2022).

⁵ AER, *Electricity transmission Ring-Fencing Guideline* (Draft Explanatory Statement v4, November 2022) 56.

Networks Australia, AusNet, TasNetworks and Transgrid, challenges are exacerbated when the waiver is not 'evergreen' or does not extend for the life of an asset.

The AER's consultation scope reflects a key focus on the use of batteries at the transmission level. Ring fencing arrangements should not curtail a TNSP's ability to innovate and deliver transmission services via the most efficient means possible. For example, leasing battery capacity to a market participant may enable full utilisation of the battery asset and provide a more efficient option than the traditional network option.

If a waiver process is introduced for batteries, a streamlined approach may be warranted, albeit with clear and strict criteria which ensure that there are clear benefits to electricity consumers from granting the proposed waiver. In our view, the waiver process should also be transparent to enhance accountability and public confidence in the ring fencing framework.

1.6 Ring fencing in Renewable Energy Zones

State governments across Australia are progressing the development of REZs to cluster new wind and solar projects and undertake transmission investment more efficiently, both in terms of time and cost. As the Draft Guideline Explanatory Statement recognises, the role of ring fencing within REZs will likely be determined by individual state governments and depend on the regulatory framework they adopt.⁶

For example, in NSW, the Electricity Infrastructure Investment Regulation 2021 requires the AER to issue a ring-fencing guideline that specifically applies to Network Operators. The CWO REZ is being procured via a contestable process, and the ring-fencing arrangements applicable to this REZ (and future REZs under a similar model) will apply to the CWO REZ Network Operator. For this role, a contestable tender process is being used to select the Network Operator that will build, own and operate the Central West Orana REZ.

REZ ring fencing arrangements should be structured in a way that promotes the most competitive bids possible. They should provide sufficient flexibility to accommodate these frameworks and reflect that the structure and operation of a TNSP within a REZ may differ from a traditional model.

In NSW, for example, EnergyCo's involvement in the planning of the REZ as the Infrastructure Planner and the competitive procurement process for the role of Network Operator means there is less scope for the CWO REZ TNSP to cross subsidise its activities and leverage any market power. This is because the Network Operator's costs will be overseen and approved by a regulator and many of the key planning decisions will be undertaken by the Infrastructure Planner.

REZ ring fencing arrangements should therefore be flexible and allow bidders to take advantage of any efficiencies that can be achieved when developing a greenfields REZ. Given REZ Network Operators are being selected through a competitive process, ring fencing arrangements should ensure that bidders do not need to introduce any structuring arrangements which have the potential to increase costs.

We recognise that the AER's Draft Guideline will inform the development of the NSW Guideline and look forward to participating in that consultation process.

1.7 Assessing the costs and benefits

Any new or expanded ring fencing obligations will increase direct costs for TNSPs, and those costs will ultimately be borne by consumers. Based on the Explanatory Statement, additional costs may be incurred by TNSPs for functions including:

- reporting and compliance
- independent auditing
- staff training
- IT changes relating to information access and disclosure
- regulatory costs associated with waiver applications.

The potential costs associated with expanded ring fencing obligations extend beyond direct costs, as there could be:

- reduced innovation, with network businesses adopting safer and well understood network options

⁶ AER, *Electricity transmission Ring-Fencing Guideline* (Draft Explanatory Statement v4, November 2022) 7.

- regulatory uncertainty, leading to higher hurdle rates, due to regulatory uncertainty associated with the need for subsequent waiver applications.

The AER recognises that it needs to carefully consider whether the benefits of strengthening functional separation outweigh the potential costs. These obligations will significantly increase costs for TNSPs. For small TNSPs, these obligations could be material where aligning the transmission and distribution guidelines in relation to information access and disclosure is unlikely to create any benefits for consumers. This is because issues relating to visibility of connections are unlikely to occur.

2. Responses to feedback questions

Question	Network REZolution response
<p>1. We are seeking evidence from TNSPs regarding any electricity services that are currently provided by TNSPs that do not fit the definition of a transmission service, but which could not practically be provided by any other party. (p 15)</p>	<p>No comment.</p>
<p>2. If current arrangements for preventing discrimination are considered inadequate, we may consider a rule change request that would seek to expand our ring-fencing powers to include the ability to specifically ring-fence negotiated transmission services, in addition to prescribed transmission services. We welcome feedback on this issue. (p 27)</p>	<p>We consider arrangements outlined for preventing discrimination in the Draft Guideline to be adequate.</p> <p>We recognise that deterring cross subsidies and discriminatory behaviour is important to help facilitate competition and better consumer outcomes. However, as raised previously in Network REZolution's submission, the risk of discriminatory behaviour is much lower for TNSPs than it is for DNSPs.</p> <p>When considering expansion of the AER's ring-fencing powers to include oversight over negotiated transmission services, the AER should consider:</p> <ul style="list-style-type: none"> • risks of regulatory burden for both TNSPs and the AER • impact on future market innovation, particularly in light of increased compliance costs • whether ring fencing negotiated services provides a material benefit to industry and consumers. <p>It is important that ring fencing supports, rather than hinders, innovation. This will ensure that energy can be delivered by the most efficient means possible, and that customers do not pay more than necessary for the investment needed to decarbonise the NEM.</p>
<p>3. We welcome further feedback on our approach to functional separation. (p 33)</p>	<p>See section 1.4 of our submission.</p> <p>We support the AER's revised position to not impose obligations for separate offices, branding and staff. As outlined in the Draft Guideline, we acknowledge the AER's position on retaining current obligations for TNSPs to separate marketing staff, so that they do not work for a 'related electricity service provider'.</p>

	<p>We appreciate the AER considering feedback from stakeholders on this issue. We agree that the benefits of functional separation will not outweigh the costs, given there is less risk of discriminatory behaviour, and associated harm to competition, from TNSP behaviour, compared to that of DNSPs.</p>
<p>4. We are seeking feedback from stakeholders on the costs of functional separation where possible. (p 34)</p>	<p>See section 1.7 of our submission.</p> <p>Based on the AER's Explanatory Statement, additional costs may be occurred by TNSPs for functions including:</p> <ul style="list-style-type: none"> • reporting and compliance • independent auditing • staff training • IT changes relating to information access and disclosure • regulatory costs associated with waiver applications. <p>For small TNSPs, these obligations could be material where aligning the transmission and distribution guidelines in relation to information access and disclosure is unlikely to create any benefits for consumers. This is because issues relating to visibility of connections are unlikely to occur.</p>
<p>5. We are specifically seeking feedback from stakeholders on whether a streamlined process is appropriate for battery waivers and what criteria could be used to determine which applications qualify for a streamlined assessment. (p 48)</p>	<p>See section 1.5 of our submission.</p> <p>If a waiver process is introduced for batteries, a streamlined approach may be warranted, albeit with clear and strict criteria which ensure that there are clear benefits to electricity consumers from granting the proposed waiver.</p>
<p>6. We invite stakeholders to advise us if there are additional [existing] services that may require further consideration. (p 53)</p>	<p>No comment.</p>
<p>7. We are seeking stakeholder feedback on whether advocating for civil penalties in relation to guideline enforcement is an appropriate next step to follow the guideline review. (p 54)</p>	<p>No comment.</p>