

09 July 2020

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

Sent via email: AERringfencing@aer.gov.au

Dear Mr Feather

Submission to AER Draft Distribution Ring-Fencing Guideline

SA Power Networks welcomes the opportunity to comment on the AER Draft Ring-Fencing Guideline which seeks to update the Guideline for Stand-Alone Power Systems (SAPS) and Energy Storage Devices.

We have been pleased that the AER has communicated a desire to examine where regulatory flexibility can enable Distribution Network Service Providers (distributors) to provide services using emerging technologies, where this best promotes efficient outcomes in customers' long-term interests.

However, we consider that the specific approaches proposed for the Guideline should reflect a greater focus on achieving practical and efficient outcomes for customers, rather than seeking to predict and pre-empt theoretically potential future market failures, and in the process, introduce barriers to innovation. Our submission, contained in the attachment to this letter, further supports the submission from Energy Networks Australia. Our key views are that:

- we welcome the proposal to apply a broad-based exemption allowing distributor involvement in the provision of SAPS supply as a practical means of recognising that SAPS supply is unlikely to always be most efficiently and prudently provided by a third party, particularly in the short-term;
- we propose that a more objective means of setting a threshold cap for the SAPS exemption would be to base it on the size of each distributor's regional / rural network, as this cap more closely relates to where there is likely to be more opportunities for SAPS deployment, and produces more appropriate outcomes for each distributor;
- we welcome the proposed amendments which allow the AER flexibility in considering waiver applications for higher exemption cap thresholds, and waivers of a longer-term nature; and
- it is disappointing that the AER has applied asset specific regulation, banning certain service delivery models using energy storage devices, to rely instead on a cumbersome and costly waiver process. We consider it unwise for regulators to seek to predict the most efficient service delivery models over time. Industry is best placed to determine this, and there are numerous safeguards to competition in the regulatory framework. If a ban is to be imposed, a pragmatic approach could be to apply a size-based exemption targeting more limited and community-based applications.

If you have any queries or require further information in relation to our submission, please contact Bruno Coelho on 0419 666 389 or bruno.coelho@sapowernetworks.com.au.

Yours sincerely



Mark Vincent
General Manager Strategy and Transformation



1. Stand-Alone Power Systems (SAPS)¹

1.1 SAPS generally

Distributor involvement in SAPS services over the next decade will likely provide the best outcome for customers with respect to the efficiency and performance of these services. As set out in our original submission,² over this period of time there is unlikely to be effective competition for providing SAPS services in South Australia.

We therefore welcome the Draft Ring-Fencing Guideline (Draft Guideline) proposing to include an exemption to provide distributors the option to deliver integrated SAPS solutions to customers. Our view is that an appropriate exemption will:

- avoid unnecessary administrative costs of the cumbersome waiver process, where it is clearly preferable for a distributor to be involved in SAPS supply;
- ensure energy supply to customers is restored as quickly as possible, in cases where SAPS may be provided following an emergency event such as a bushfire;
- provide greater regulatory certainty for distributors to invest, train staff and purchase inventory for SAPS supply, also avoiding delays in SAPS deployment;
- represent a practical way of recognising that cases below the exemption threshold cannot be presumed to always be efficiently and prudently provided by a third party; and
- not present any harm to long-term prospects for competition, noting that exemptions do not provide distributors with exclusivity in SAPS service provision and there are a broad range of existing safeguards for competition as outlined in Breakout Box 1.

Breakout box 1: competition safeguards

Will exemptions allowing distributor involvement in SAPS hurt long-term prospects for competition?

Harm to emerging competition will be avoided:

- Exemptions will not provide distributors with exclusivity in SAPS services over third parties.
- The largest market for SAPS is likely to remain the unregulated market for greenfield applications (third party led).
- Distributors will be guided by incentive regulation to use third parties if efficient.
- Minimising barriers to distributor deployment of SAPS will increase the size of the market.
- Distributor deployment of SAPS can be publicly reported, audited, and reviewed by the AER.
- The AER can review exemption thresholds over time and /or for each jurisdiction so that they reflect the expected state of competition.

We also welcome the Draft Guideline proposing other amendments which can support an exemptions framework, including:

- allowing 'grandfathering' of existing SAPS such that these are not counted toward the exemption threshold cap;
- allowing more limited 'grandfathering' of SAPS deployed under the exemption framework, but in situations where a distributor's total annual regulated revenue decreases over time (such that a lower cap could otherwise be deemed to apply).

¹ Our comments concern the component of SAPS services that the AEMC framework deems to be 'Generation Services' as they are provided via a 'Generation System' (ie some combination of solar PV, storage devices, back-up generation). The AEMC framework prohibits distributors from providing this service component, unless approved via the Guidelines.

² SAPN, *Submission to AER Issues Paper on updates to the Distribution Ring-Fencing Guidelines*, 21 December 2020, p.1



1.2 Exemption design

We welcome the Draft Guideline proposing to apply a ‘broad-based’ exemption threshold cap set to the level of generation revenue derived by distributors in delivering SAPS to customers. This is a practical and administratively simple option to enact and monitor.

However, the design of the generation revenue cap proposed should be revisited as it lacks a clear objective basis. If the AER intends to apply a cap with a tiered structure, such that higher or lower caps apply to different distributors, we propose that an objective approach would be to set the cap’s tiers according to the size of each distributor’s regional / rural network as set out in our Table 1 below. This is on the basis that:

- the cap tiers proposed in the Draft Guideline intended to allow circa 75 percent of the SAPS opportunities that distributors each anticipate. However, the figures used by the AER are out of date, have no solid basis as they did not result from any rigorous forecasting, and were supplied for a different context outside of this review. SA Power Networks has not yet undertaken a complete assessment of all SAPS opportunities over the next 5-10 years, and the figures pertaining to our network only concern potential SAPS opportunities that we were immediately aware of;
- the cap tiers proposed in the Draft Guideline result in unreasonably low thresholds for the vast majority of distributors. For example, SA Power Networks with a vast rural and regional network and the only network covering the entirety of a vast state, would be permitted only 4.8 SAPS before having to apply for waivers. These low thresholds would not serve to achieve any of the benefits (as set out above) of implementing an exemption framework in the first place;
- an exemption threshold that considers the size of each distributor’s regional / rural network would be a more objective approach, on the basis that:
 - opportunities for SAPS supply are predominantly likely to be most efficient and prudent in remote areas where there are individual customers, or few customers connected to the end of long powerlines on the edges of our State-wide distribution network;
 - the AER’s Regulatory Information Notices collect information that can readily be used to determine the size of each distributor’s regional / rural network—we propose using short and long rural route line length divided by total route line length; and
 - the resulting grouping of distributors into regional / rural tiers appears more intuitive, with category 1 pertaining to predominantly rural networks, category 2 to networks with urban and large rural networks, and category 3 pertaining to predominantly urban networks.
- while there is no clear objective means of apportioning a revenue cap percentage to each tier, our proposal, set out in Table 1, mostly applies the percentages proposed in the Draft Guideline. This produces a more reasonable indicative number of SAPS that can be deployed by each distributor, noting that these figures represent the total number of SAPS that each distributor would be permitted to provide in total in perpetuity.

The Draft Guideline also proposes that distributors maintain a register of SAPS deployed commensurate with the exemption. We support the register as providing transparency to stakeholders. However, requirements to report information on whether the distributor has sought offers from third parties should be kept a minimum and perhaps to a yes or no answer noting:

- this avoids duplicating the waiver process that this exemption framework is aiming to avoid; and
- the AER can at any time ask questions of distributors if it requires further information.



Table 1: SA Power Networks proposed alternative exemption thresholds

Category	DNSP	Rural proportion ³	Basis of category	SAPS revenue cap %	Indicative 20kW SAPS ⁴
Category 1	Ergon Energy	95.5	80-100% rural proportion	0.20% of ARR	1492.4
	AusNet Services	92.6			776.6
	Power and Water Corporation	92.2			211.0
	Powercor	91.6			735.9
	Essential Energy	88.5			961.2
Category 2	SA Power Networks	79.9	50-80% rural proportion	0.07% of ARR	339.3
	TasNetworks	55.5			151.3
Category 3	Evoenergy	49.0	0-50% rural proportion	0.02% of ARR	15.3
	Endeavour Energy	48.6			97.8
	Ausgrid	44.4			157.0
	Energex	37.3			172.9
	Jemena	26.2			32.5
	United Energy	26.0			50.6
	CitiPower	0.0			36.2

1.3 Waivers

The Draft Guideline proposes other amendments to support an exemption framework. We support these amendments on the basis that:

- providing distributors the option to apply for a waiver to increase their revenue cap threshold, will allow the AER and stakeholders to publicly consider any jurisdictional specific plans for larger roll-outs of SAPS, such as where a whole community is proposed to be supplied via SAPS; and
- allowing waivers to apply for terms decoupled from regulatory control periods, allows the AER to consider waivers that align to the life of the SAPS assets, and that provide greater investment certainty, where this is warranted.

It is also important that the waiver assessment criteria allows the AER to consider not only if there is a third party tendering for a SAPS service, but also the competitiveness of that tender, relative to what a distributor can provide. Assessments must extend to price and non-price factors (following standard procurement practice) that may determine what will promote the best service outcome for customers.⁵

³ Data sourced from 2019-20 and 2020 Economic Benchmarking RINs – Table 3.7.2

⁴ Calculated based on information sourced from Appendix C (SAPS general revenue cap calculation) of the AER Draft Electricity Distribution Ring-Fencing Guideline – Explanatory Statement, May 2021.

⁵ Non-price factors could include: previous project performance; safety record; contractual terms such as warranties and indemnities; scheduling and completion dates; safety, quality and post completion obligations.



2. Storage devices

Technology is opening up new means of delivering energy services for customers. Large scale storage devices can potentially provide support for distribution networks during times of constraint (i.e. an input to a distribution service), as well as services valued by customers directly⁶ or by the wholesale market.⁷

At a time of service innovation, regulation should aim to be flexible and move beyond the application of simple blanket ring-fencing boundaries that have historically been used. The focus should be firmly on enabling long-term least cost outcomes for customers, rather than assuming that competition will deliver greatest efficiency in all cases. The experience of the metering contestability reforms serve as a reminder of how theoretical assumptions about the benefits of competition may not materialise when hard boundaries between what is regulated or unregulated are poorly formed.

The most efficient means of deploying storage devices across their different potential applications is highly uncertain. For this reason the regulatory framework has, to date, not prescribed the assets that distributors should or should not use, nor prescribed the activities that distributors should undertake in-house or outsource to third parties. This provides scope for innovation, ultimately leading to better customer outcomes.

In this context, it is disappointing that the AER has opted to apply asset-specific regulation, and ban particular models for delivering storage device services, being those involving distributors partnering with third parties to share in the use of storage devices, and those involving distributors using storage devices to directly provide non-distribution services, except where a waiver is granted. In our view:

- the ability to ‘value-stack’ by using storage devices for more than just network support will be key to minimising the cost of distribution services and market services more broadly. Investment in storage is unlikely to be economic on network support grounds alone;
- it is uncertain how ‘value-stacking’ might best be configured, and how multiple parties might best partner in the use of a storage device to deliver multiple value streams. These issues should be left to the industry to determine according to the specific situation, noting that:
 - There are very few cases in the National Electricity Market (NEM) where large scale storage devices have been deployed for network and non-network purposes. The most prominent example is the partnering agreement whereby a retailer shares in the use of the storage device owned by a transmission network (Electranet). This example avoids cross-subsides, reduces costs of transmission services, reduces costs of market services, preserves the ability of the transmission network to safeguard electricity supply, yet is precisely one of the service models that the AER seeks to ban, unless a waiver is granted.
 - It remains to be seen whether it is best for a distributor to own a storage device and lease it out to a third party, or to procure the use of a storage device as a service. A key consideration will be how to ensure that the distributor’s use of a storage device for network support takes precedence in order to avoid network constraints. The optimal configuration of contracts to provide this guarantee, and or the willingness / ability of third parties to provide sufficient access, and insurance coverage and protection against adverse network service impacts, are all still to be determined.

⁶ For example: community storage services, where customers store and retrieve energy from a communal asset service.

⁷ For example, Frequency Control Ancillary Services (FCAS) or Reliability and Emergency Reserve Trader (RERT) services.



- allowing distributors to either partner with a third party to share a storage device, or to deliver non-distribution services directly via a storage device, presents no potential harm to competition. As outlined in Breakout Box 2, there are extensive safeguards for competition in the regulatory framework, and the Draft Guideline has added an additional safeguard that we proposed in our original submission via non-discrimination clauses; and
- the AER should focus on the root-cause of any potential harms to competition rather than imposing outright bans. In doing so, we caution against reliance on anecdotal comments from individual businesses such as expressed at the AER public forum on this review, as there could be any number of factors that may have affected a particular business' bid to a network, and their unsuccessful bid should not be taken as a sign of uncooperative conduct on the part of a distributor.

For the avoidance of doubt, SA Power Networks is not proposing that regulation grant distributors any exclusivity in the deployment of storage devices. Rather, that regulation should be open to a range of service delivery models, noting that there are sufficient safeguards for competition irrespective of the service delivery model adopted. Our business remains open to considering any efficient and prudent proposal from a third party that can minimise the costs of services to our customers.

2.1 Small scale exemptions

Should the AER proceed to ban certain types of service delivery models for storage devices, we propose that consideration should be given to at least providing a pragmatic size-based exemption framework. Our proposed exemption framework entails:

- Size-based exemption—allowing distributors to ‘value-stack’ by using storage devices for non-distribution services provided these devices are at or less than 1 MW. This small threshold is aimed at enabling community-scale storage services, noting the significant interest that community groups across the NEM have voiced in partnering with distributors in this regard; and
- Reporting regime / deemed waivers—a reporting process to provide transparency to stakeholders and the AER. Distributors would be required to publish information of similar scope to the AER draft wavier assessment guidance, published as soon as reasonably practical for each installation. This approach would require distributors to satisfy themselves that their approach is prudent and efficient, noting that the AER could at any time investigate on an ex-post basis. This mirrors the approach taken generally to taxation compliance.

Breakout box 2: competition safeguards

Are there safeguards to competition if distributors are allowed indirect or direct use of storage devices?

Existing safeguards include:

- The AER can assess regulated expenditure proposed by distributors to invest in storage, to determine if the anticipated use for regulated purposes is reasonable to justify the expenditure.
- Distributors must publicly report future network constraints in the Distribution Annual Planning Reports – to be used by third parties wanting to provide network support.
- The Australian Competition and Consumer Commission monitors competitive conduct.
- Distributors must undertake a Regulatory Investment Test (RIT-D) to consider non-network options, allowing third parties to present alternative solutions.
- Distributors have obligations to connect customers under an open access framework, preventing discriminatory conduct.
- Non-discrimination obligations in the Ring-Fencing Guideline require distributor affiliates to not be favoured over third parties.

Additional safeguards in the Draft Guideline:

- Further provisions prohibit a distributor discriminating in favour of itself against competitor storage service providers, such as in respect of the use of the network.



3. Other minor guideline amendments

The Draft Guideline proposes a number of other general amendments. Our views on these are set out in Table 2 below.

Table 2: SA Power Networks comments on minor guideline amendments

Issue	SA Power Networks comments
Office and staff sharing registers	<p>Uncertainty remains as to the information distributors must report in the registers, and we encourage the AER to consider issuing a template register to achieve greater consistency across each distributor. For example, it is unclear what level of detail is expected in relation to staff secondments, which are inherently individualistic. Such reporting would entail disclosing individuals within the business, rather than the current Guideline requirements which are location or position-based criteria and therefore simple to identify.</p> <p>On the frequency of updates to the registers, half-yearly rather than quarterly updates would better balance the benefits of additional transparency with the administrative costs.</p>
Materiality and reporting of breaches	<p>We support extending the breach reporting period from 5 to 15 business days, however:</p> <ul style="list-style-type: none"> ▪ we maintain our view that a ‘materiality threshold’ should remain in place as a practical means of minimising reporting costs; and ▪ we do not support the reporting of all breaches within this timeframe, including the reporting of all trivial breaches, with such reporting serving no purpose for customers to compensate for the increased reporting costs.
Branding and cross promotion	<p>We are disappointed that there are no substantive changes to the branding and cross-promotion provisions. We maintain our view that the current provisions are ambiguous and result in distributors applying broad interpretations and overly conservative policies and procedures. We encourage the AER to revise these provisions, either as part of a separate Guideline review, or through amendments to its Best Practice Manual. As set out in our original submission,⁸ there are a number of examples where a distributor is potentially prevented from ‘co-branding’ in situations where there is:</p> <ul style="list-style-type: none"> ▪ no unfair advantage to a Related Electricity Service Provider (RESP); ▪ no detriment to competitors of a RESP; ▪ no improper inference in the eyes of the public; and ▪ increased administrative cost on the distributor.
Timing of annual compliance reports	<p>We support moving to a calendar year reporting period, and for the first reporting period to be extended by 6 months such that all distributors will be submitting their next compliance report on 30 April 2022 (and other than for Victorian distributors, this will be for an 18 month reporting period).</p>
Information access and disclosure	<p>We support the AER’s proposal to amend the title of the term ‘confidential information’ to ‘ring-fenced information’ to avoid the general misconceptions regarding ‘confidential information’. However, we note that there is no amendment to the original definition, i.e. ‘ring-fenced information’ would be defined as per the current Guideline’s definition of ‘confidential information’.</p>

⁸ SAPN, *Submission to AER Issues Paper on updates to the Distribution Ring-Fencing Guidelines*, 21 December 2020, p.7.

