16 December, 2022

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

Submitted electronically: AERringfencing@aer.gov.au

Dear Mr Feather,

Re: Issues paper: Ring-Fencing Guideline Review (Electricity transmission)

The Snowy Hydro Group welcomes the opportunity to comment on the Australian Energy Regulator's Ring-fencing guideline Electricity Transmission - Version 4 (Draft guideline). We support the Draft Guideline. The AER has made targeted and proportionate changes to the cross subsidy and discrimination provisions that will ensure it is better able to support competitive outcomes in markets within which Transmission Network Service Provider (TNSPs) operate.

Nonetheless technological advances will mean TNSPs continue to have greater scope to offer services outside of their traditional transmission network services creating competition challenges for the AER.

With the markets for contestable energy services within which TNSPs operate being in their early stages of development, an incorrect decision on access by the AER may have serious consequences on long term competition.

As a result, the Draft guideline must be 'fit for purpose.' For this to occur, the AER must resist amending the Draft guideline between now and the final decision in a substantive way that may jeopardise how effective it is.

Below, we highlight the areas of the Draft guideline that should not be amended.

1: Removal of the 5% revenue cap exception and replace with waiver

Open and competitive markets deliver optimal outcomes for consumers so we strongly support a regulatory framework that promotes competition as far as possible. As a consequence, we strongly support ring-fencing arrangements, noting the potential conflict of interest that arises when Transmission Network Service Providers (TNSPs) seek to participate in the market for contestable energy services. This is because they have an incentive to cross subsidise the contestable services they provide by using regulated revenues and discriminate in favour of ring fenced affiliates. This will undermine the development of a competitive wholesale market, particularly for storage services such as batteries and pumped hydro, which is ultimately to the detriment of all consumers.

Snowy Hydro supports the AER's decision to remove the 5% revenue cap exception to the legal separation obligation and replace it with a waiver. This is because TNSPs have projected that by 2050 they would double the size of their Regulatory Asset Bases thus increase their revenue cap values accordingly. Under the 5% revenue cap exception rule, this development would allow them to expand their activities in contestable energy markets significantly. To prevent this from happening and potentially impact competition in these emerging contestable energy markets, the AER has introduced this change.

2: Strengthen the accounting separation and cost allocation arrangements between transmission services and non transmission services

Snowy Hydro supports the AER's decision that requires TNSPs to allocate the costs of transmission services and non-transmission services in accordance with their cost allocation methodologies and the cost allocation principles combined with an independent audit. These changes will provide greater assurance to market participants that the TNSPs are not cross subsidising contestable services with regulated revenues to ensure competitive neutrality in the contestable energy markets that TNSPs operate in.

3: Disallow TNSPs to lease the spare capacity of battery storage they own which provides regulated services without a waiver

Snowy Hydro supports the AER's decision to prohibit TNSPs from leasing any excess battery storage capacity which provides regulated services without a waiver. In short, this decision will support competitive outcomes in the grid scale battery market over the long term. In the absence of these changes:

- TNSPs could lease storage capacity which provides regulated services and 'gold plate' the network in favour of the party leasing the battery in effect giving them preferential access to the wholesale market. To our knowledge, there is nothing in the Rules to prevent.
- TNSP could potentially provide cross subsidised battery storage capacity. This is because battery storage facilities are able to provide regulated and non regulated services almost simultaneously and switch between these services within milliseconds. This would make it almost impossible to accurately determine how costs between the regulated and non regulated services were allocated.

Distribution Network Service Providers (DNSPs) are not permitted to sell excess battery storage capacity from assets already supplying regulated services unless they obtain a waiver under an expedited approval process. Where the AER approves an expedited waiver, the DNSP must demonstrate it has applied the correct cost allocation methodology to the services it provides to prevent any cross subsidisation. The AER appoints an auditor every year to review to confirm compliance

However a methodology for deciding on the manner in which the split between supplying regulated and contestable services of a battery storage facility would be allocated has yet to be developed. We assume that this is due to complexity associated with the allocation of costs to regulated and non regulated services. Given this, we urge the AER to refrain from introducing an expedited waiver process that mirrors the one applied in distribution.

If TNSPs would like to supply battery capacity into the contestable energy services markets, we prefer that they compete in these markets subject to full legal separation through a ring fenced affiliate affiliate. This arrangement will ensure that they compete in a fair and reasonable manner at an arms length on a competitively neutral basis.

4. Support for the separation of prescribed and negotiated transmission services from non regulated transmission services

Snowy Hydro would support a rule change that would require the full division of its prescribed and negotiated transmission services from its non regulated transmission services. Otherwise, TNSPs could potentially use their monopoly power to cross subsidise or discriminate in favour of themselves in terms of supplying transmission connection services.

Given the size of the investment of transmission connection services moving forward, we would support a rule change that would require the full division of its prescribed and negotiated transmission services from its non regulated transmission services. This would mean that TNSPs supply their non regulated transmission services subject to full legal separation through a ring fenced affiliate on a competitively neutral basis.

5. Stronger compliance regime

Snowy Hydro supports the AER's proposal to strengthen the compliance regime; effective regulatory administration is necessary to ensure the ring-fencing framework achieves its objectives. This includes requiring TNSPs to:

- undertake annual compliance reports relating to their ring fencing obligations within 4 months of the end of the calendar year
- report breaches of the Draft guideline within 15 days from the breach
- introduce a civil penalties regime to ensure that the TNSPs comply with the Draft guideline and face financial penalties for any breaches.

Snowy Hydro appreciates the opportunity to respond to the AER's review of the review of ring-fencing arrangements for transmission network service providers (TNSPs). Any questions about this submission should be addressed to [redacted].

Yours sincerely,

[redacted]

Geoff Hargreaves
Regulatory Manager
Snowy Hydro