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Dear John

### **Response to Regulatory Sandbox Arrangements Consultation Paper**

AusNet Services welcomes the opportunity to participate in this review. If an appropriate framework is put in place, AusNet Services considers that regulatory sandbox arrangements could bring substantial benefits through encouraging innovation during this period of energy market transition.

There is a need to encourage innovation at this time. An increasing number of customers are investing in new technologies and expecting energy services to keep pace. New technology enables these services to be delivered to customers in different ways than previously. Innovation is key to maximising the value of these developments across the whole supply chain. Proof-of-concept trials enabled by regulatory sandbox arrangements, where new technologies, products and market models can be tested and validated, could play an important role in facilitating the energy market transition.

It is concerning that, despite having one of the world's highest distributed energy resource (DER) penetration rates, Australian networks have among the lowest per capita expenditure on innovation globally<sup>1</sup>. There are likely several reasons for this – one being, for the regulated networks sector, that unless a regulatory allowance for innovation is granted in a revenue determination, the revenue setting framework truncates the returns to investment and therefore does not provide strong enough incentives for networks to invest in innovation. While the Demand Management Incentive Scheme provides a modest (\$200k plus 0.075% of annual revenues) annual allowance for innovation related to demand management, there are a multitude of other areas (such as the efficient integration of DER into the energy market) where innovation is expected to be equally beneficial but no explicit funding is provided.

Regulatory barriers and risks are another reason for the relatively low level of innovation. In these cases, proof-of-concept trials facilitated by a regulatory sandbox could be a quick way to test whether particular services are viable and provide customer benefits, and therefore whether rule changes to remove these barriers would be beneficial. While the AER is able to issue letters of no action on a case-by-case basis, regulatory sandboxes have the additional advantage of promoting stakeholder confidence as the nature of the temporary exemption and the rationale for this will be clear and transparent. The sandbox concept also has the potential to improve the legitimacy for the AER, and the other institutions, to engage with the trials.

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<sup>1</sup> *Energy Networks Australia*, Network Innovation – Discussion Paper, July 2017 – see Figure 1

The regulatory sandbox framework should complement, and not replace, other routes to enabling innovation. These include the ability for the AER to continue to issue letters of no action.

In setting up the regulatory sandbox framework it is important to balance the need for a robust and transparent assessment process with the need for the framework to support quick decision making and provide flexibility, to accommodate the nature of innovation projects. The framework needs to support innovation, rather than add undue administrative complexity.

In addition, proof-of-concept trials are likely to be relatively small scale and consumer impacts can be closely monitored. This means the risks associated with such trials are relatively low – the framework that is put in place should be designed with this in mind.

### **Relevant Proof-of-Concept Trials**

While AusNet Services' New Reg process trial is currently in operation under the existing Rules, if it is deemed successful, a future trial under the New Reg process may benefit from a regulatory sandbox arrangement to enable the AER to give a greater weight to agreed outcomes incorporated in a Revenue Proposal.

The AER's current ability to issue letters of no action would not assist in these circumstances as the sandbox would be required primarily for the AER in making its revenue determination.

### **Barriers to Proof-of-Concept Trials**

Other trials that are currently restricted by the regulatory framework for new market models may involve network pricing arrangements e.g. peer-to-peer trading. This is because while the Rules currently allow for a trial tariff to be included in a network's annual pricing proposal, the timelines are restrictive – the AER must be notified of this in August and, if approved, the tariff can only apply from the following January.

Many of the proposed peer-to-peer trials are unlikely to generate any substantial benefit to the network in terms of reducing future network investment and so the case for a network to offer a reduced tariff is relatively weak. However, a trial located in a constrained part of the network could yield significant benefits and learnings across the supply chain about customer behaviour in response to network tariffs. In these circumstances, a regulatory sandbox framework would assist to provide greater flexibility around the implementation timeline and to provide transparency over why particular trials are chosen to proceed.

### **Potential Design of Formal Regulatory Sandbox Arrangements**

The objective of formal regulatory sandbox arrangements should be to facilitate proof-of-concept trials to occur, where the concept being tested has potential to result in substantial customer benefits. These benefits should be broadly defined and could include reduced costs, improved reliability and/or energy security, or the ability to generate more value from new technologies, including solar PV, batteries or electric vehicles. The potential benefits may be realised over the medium- or longer-term.

The success of regulatory sandbox arrangements could be measured based on a range of metrics. These could include the number of applications received for projects to be subject to these arrangements. The confidence of stakeholders, and in particular consumer advocates, in

the robustness and transparency of these arrangements is also an important metric, as the regulatory framework operates within the long run interests of customers.

In designing criteria for accessing these arrangements, we consider that the scope of application of the sandboxes should be very broad. However, on an annual basis priority areas of innovation that are likely to have broader benefits across the energy sector could be publically identified, taking into account the views of groups including the ESB, AEMO, ARENA, the AER, ECA and the ENA. For example, the integration of distributed energy resources and standalone power systems may be two areas where innovation is currently likely to lead to customer benefits.

In some cases, it may be valuable for similar trials to proceed. These would allow a comparison of similar, but not identical, approaches. Where it is necessary to select between similar trials, some judgement will be required. The AEMC, AEMO and the AER could agree on the trials that should occur under these arrangements, with input from other parties including the ECA, ARENA and the ENA.

Aside from the regulatory arrangements that are intended to directly protect the security and operation of the network, all other parts of the National Electricity Rules should be in scope. In some circumstances it may be necessary for the participant to seek regulatory exemptions from other regulatory bodies, such as those administering jurisdictional licencing. To prevent these trials from falling at the last hurdle, it would be helpful if jurisdictional licencing bodies could have a formal role in providing advice and establishing whether their own regulatory requirements could be relaxed to enable the trial to proceed.

AusNet Services looks forward to engaging in the next steps of this review. Please contact me with any questions in relation to this submission.

Yours Sincerely,



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**AusNet Services**