

Ausgrid Submission

AEMC review of the regulatory arrangements for stand-alone power systems – priority 2 – draft report

August 2019



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Lodged online

Dear Ms Toomey

Ausgrid is pleased to provide this submission to the Australian Energy Market Commission (AEMC) Stand-Alone Power Systems (SAPS) Priority 2 Draft Report (the Priority 2 Draft Report).

The AEMC's Priority 2 Draft Report for third party-led SAPS follows closely behind final reports considering regulatory arrangements for embedded networks and distributor-led SAPS. As recent experience has shown, when regulatory arrangements diverge depending on how energy is delivered to customers, forum shopping and arbitrage opportunities often result in poor outcomes for customers.

For this reason, consistency across regulatory arrangements should be a key focus for the AEMC as it develops a framework for third-party led SAPS. Consistent regulatory treatment between third-party and distributor-led SAPS will ensure that the customer experience is the same, regardless of how energy is delivered.

We will continue working with the AEMC to develop solutions for the issues raised in the draft report. Should the AEMC have any questions in relation to this submission, please contact John Skinner, Regulatory Policy Manager on 02 9269 4357 or john.skinner@ausgrid.com.au.

Yours sincerely

A handwritten signature in black ink, appearing to read "Iftekhar Omar", written in a cursive style.

Iftekhar Omar
Head of Regulation

Submission

The AEMC review of the regulatory arrangements for stand-alone power systems (SAPS) is an important step in the evolution of electricity distribution networks. Changes in technology and technology costs mean that SAPS are becoming an increasingly viable option for providing electricity services to customers, particularly in rural and remote locations.

Ausgrid is the largest distributor of electricity on Australia's east coast, providing electricity to 1.7 million connected customers. While our network includes some of Australia's most densely populated areas, it also services sparsely populated areas of the Central Coast and Hunter Regions of NSW. This means that we will see SAPS emerge in our network area over time.

Our submission provides views on various issues raised in the Priority 2 Draft Report. In particular, we focus on ensuring consistent customer outcomes, as well as issues relating to the transition of customers to third party SAPS and implementation of an operator of last resort (OoLR) scheme.

Assessment framework for third-party SAPS

In our March submission to the AEMC's February 2019 SAPS Priority 2 Consultation Paper, we submitted that consistency of approach across distributor led SAPS, embedded networks and third-party led SAPS should be a priority, and that this would allow customers to more easily determine their consumer protections and supplier obligations.¹ Many submissions, including that of Ausgrid, also cautioned against allowing customers to trade away their consumer protections, given that a safe, reliable energy supply, backed by a comprehensive set of consumer protections, has long been considered an essential service.

In its Priority 2 Draft Report, it is interesting to note that 'consistent and transparent' regulatory arrangement is at the bottom of the list of assessment criteria being used by the AEMC in its review of regulatory arrangements for third-party led SAPS.² This seems to be reflected in the AEMC's recommendations in the Priority 2 Draft Report, which promotes competition and consumer choice above consistent consumer outcomes and consistency across regulatory approaches.

In its Priority 2 Final Report, we recommend that the AEMC reconsider the weighting with which it applies the assessment criteria used to determine its regulatory approach for third-party SAPS. Consistency and transparency should receive the same weighting as the objective of promoting competition and consumer choice. This will ensure that outcomes for customers are as consistent as

¹ Ausgrid, *Submission to Stand-alone power systems – priority 2, Consultation Paper*, March 2019, p.3

² AEMC, *Stand-alone power systems – priority 2, Draft Report*, June 2019, p.20

possible and that energy suppliers operate on a level playing field, regardless of the way energy is delivered to the end customer. Not only will this avoid forum shopping and arbitrage opportunities, it will ensure that customer protections and supplier obligations are more easily determined.

National v jurisdictional treatment of third party SAPS

An issue discussed at some length in Priority 1 of the SAPS review is whether national or jurisdictional arrangements should apply to the regulation of SAPS. We remain of the view that the AEMC should aim for national arrangements wherever possible, including in areas that remain the responsibility of state jurisdictions. In these circumstances, the AEMC could design a national SAPS framework and jurisdictions would then be free to opt in to the new arrangements. The SAPS framework designed by the AEMC could be as consistent as practicable to the framework for customers covered by the NERL and the NERR. Following adoption by each jurisdiction, all customers within that jurisdiction would be covered by a similar set of consumer protections, regardless of whether they receive supply from a SAPS or the national distribution network.

Under the Priority 2 Draft Report recommendations, however, a significant portion of the third-party SAPS framework relies on jurisdictional arrangements. This significantly increases the risk of divergent regulatory arrangements. For example, two customers with similar energy profiles could each receive a very different energy experience and different consumer protections, simply because of when and how they received their SAPS energy supply. Not only could this situation result in confusion for the customer, it could lead to confusion for distributors, governments, regulators, retailers and ombudsmen.

Classification of SAPS

Consistent with the IPART framework recommended by Ausgrid and Energy Networks Australia, the AEMC has proposed a three-tiered framework for the classification of third-party SAPS.³ In contrast to the IPART approach, however, which used a risk-based framework, the AEMC appears to have employed an economic and competition-based framework to determine the SAPS categories:

- Under the IPART approach, determining which category an electricity supply system would fall into would depend on a risk-based assessment considering factors such as potential customer impacts, system complexity, and the skills required to safely manage and operate the technical assets in the installation. IPART considered that low voltage embedded networks such as high rise residential towers and industrial centres would be category 2, while caravan parks and small unit blocks would more likely be category 3.

³ IPART, Submission to Discussion Paper, Protecting Consumers in a changing energy world, December 2017

- Under the AEMC approach, however, determining which category an electricity supply system would fall into would depend on the ability of the AER to conduct a regulatory determination and the potential for retail competition.

As a result of this change in approach, categorising SAPS as either category 1, 2 or 3 will present some difficulties. The AEMC considers that smaller towns would be considered category 2 SAPS, while the IPART framework only considered that high rise towers and industrial centres would be category 2.

In our view, the fact that a microgrid is large enough to warrant a regulatory determination by the AER and retail competition may not be the appropriate criteria on which to assign the appropriate regulatory treatment of SAPS. As we outlined in our March submission, applying IPART's risk-based approach to microgrids might result in the following categories:

- Category 1: Very large third party microgrids (for example, covering an entire town)
- Category 2: Microgrids covering a group of households or businesses
- Category 3: A SAPS serving an individual, or a microgrid with a very small number of customers

Category 2 SAPS under this classification are clearly smaller than that proposed by the AEMC. As there is clearly further work to do on this issue prior to the Priority 2 Final Report, the AEMC should consider conducting further consultation, perhaps through a stakeholder workshop, on this issue.

Operator of last resort

Consistent with our March 2019 submission, we remain of the view that the local distribution network service provider is likely to be best placed to become the Operator of Last Resort (OoLR) for customers being supplied by a third-party SAPS in their distribution area. However, distributors, and therefore their customers, should not bear the risk and potential costs of being the OoLR.

In the Priority 2 Draft Report, the AEMC raises the possibility of a competitive market developing for OoLR services. While an OoLR scheme could be established in each jurisdiction and a competitive tender carried out to appoint an OoLR provider, it is not clear that the cost of doing so would outweigh any benefit. In each jurisdiction, a process of risk allocation, insurance and ongoing fees would need to be established. Again, the AEMC seems to have prioritised the development of competition in the market for operator of last resort (OoLR) services over the other assessment criteria, including that the regulatory arrangements are fit for purpose and proportional to the risks they seek to mitigate.

While an OoLR scheme is designed for when a SAPS operator fails, the failure of a SAPS operator is likely to become most acute when a SAPS fails. Particularly in regional and remote areas, if a SAPS was to fail, the local network service provider is likely to be the only party that can restore power quickly and safely. The AER recognised that allowing the local DNSP to restore power quickly and safely results in the best customer outcomes in its April 2019 final determination for the NSW DNSPs. In those decisions, the AER gave the NSW distributors permission to fix simple behind the meter faults, recognising that the local DNSP is likely to be the first party on site and that this solution will result in the best customer outcomes.

In our view, a far simpler way of funding the OoLR scheme is to introduce some sort of indemnity or bank guarantee maintained by the SAPS operator. In NSW, this would be similar to the Accredited Service Provider (ASP) scheme, under which ASPs must provide Ausgrid with a bank guarantee when performing contestable connection works on behalf of a customer. These arrangements are set out in section 6 of the ASP Level 1 Authorisation Agreement.⁴ Ausgrid may call for payment under a bank guarantee in certain circumstances, including when the ASP fails to rectify any defects in the connection work or is responsible for any loss or damage. Similar arrangements could be set up to cater for OoLR.

Transitioning to third party stand-alone systems

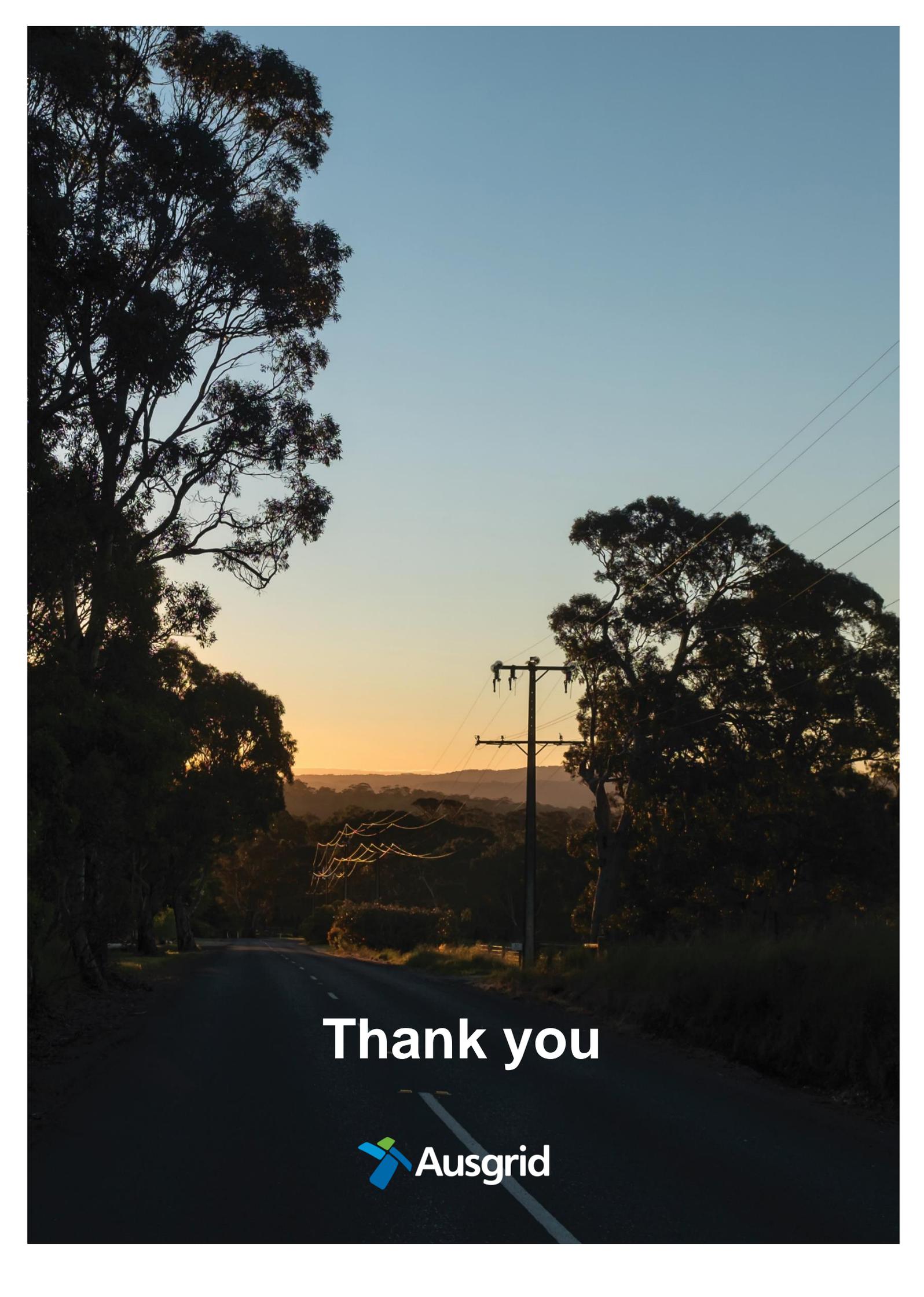
In the Priority 1 Final Report, the AEMC confirmed that transfers of assets between the DNSP and a third party would be governed by commercial negotiations between the DNSP and the third party.⁵ The AEMC also indicated that the AER will have an oversight role on how the DNSP accounts for the asset transfers, stranded assets and asset re-allocation through the revenue determination process but did not provide detail on how this would work in practice. The AEMC indicated that the commission would develop proposed changes to the NEL to allow rules to be made regarding compensation requirements during Priority 2.⁶

However, in its Priority 2 Draft Report the AEMC has not provided any detail regarding the rules regarding compensation requirements. This is important, as the valuation of transferred assets, the identification of stranded assets, and the calculation of efficiency losses are likely to be contentious. The AEMC may need to consult on this issue prior to issuing its Priority 2 Final Report.

⁴ <https://www.ausgrid.com.au/-/media/Documents/ASP/Authorisation/ASP1-Authorisation-Agreement-August-2017.pdf>

⁵ AEMC, *Stand-alone power systems – priority 1, Final Report*, May 2019, p.113

⁶ AEMC, *Stand-alone power systems – priority 1, Final Report*, May 2019, p.xv

A scenic photograph of a road at sunset. The sky is a mix of blue and orange, with the sun low on the horizon. Large trees are silhouetted against the sky, and power lines run across the scene. The road is dark and leads into the distance.

Thank you

