



## Review of stand-alone power systems — priority 2

**The AEMC has published the final report for its review of the regulatory frameworks to support the provision of stand-alone power systems by third-parties while providing protections for consumers.**

The final report sets out the Commission's recommendations on the regulatory frameworks that should apply to stand-alone power systems (SAPS) provided by parties other than the local distributor in the National Electricity Market (NEM). These "third parties" could include a wide range of potential providers including community groups, local councils, developers, ring-fenced affiliates of the local distribution business or NEM market participants.

### Context for this review

In August 2018, the AEMC was asked by the COAG Energy Council to provide advice on the regulatory arrangements required to allow for the use of SAPS. Under the terms of reference, the review was structured around two priorities:

- Priority 1 focused on the development of a national framework for customers that are moved from grid-connected supply to SAPS by the local DNSP.
- Priority 2 focused on the development of a framework to support the supply of electricity from SAPS provided by parties other than the local DNSP (third parties).

A final report for priority 1 was published on 30 May 2019. It recommended changes to the national energy laws and rules to allow NEM distribution businesses to use SAPS where it is economically efficient, under regulatory arrangements that would closely follow existing national energy frameworks to enable customers receiving stand-alone systems to retain their current consumer protections.

### Overview of the final report

The final report for priority 2 presents and explains the Commission's recommendations for the regulatory framework that should apply to third-party SAPS.

In developing this framework, the Commission has sought to apply consistent principles between the electricity supply models considered under priority 2, priority 1 (distributor-led SAPS), and the Commission's recommended framework for embedded networks, as well as standard supply. These principles relate to each of the key areas of regulation, including registration and licensing, consumer protections, economic regulation and access and connections. However, how those principles are applied to the regulation of third-party SAPS in practice will vary, depending on:

- the size of the system (for example, only large systems are likely to be able to support retail competition and justify the costs of economic regulation) and
- whether it is regulated under national or jurisdictional rules (noting that regulation of third-party SAPS is currently the responsibility of jurisdictions).

The approach aims to provide a more flexible framework capable of accommodating the broader range of providers and circumstances that could be associated with third party systems. In contrast to priority 1, customers will generally be making a choice to receive supply from a SAPS provided by a third-party or to move to premises supplied by a third-party system. Additionally, service providers themselves are likely to be much smaller and less well resourced than distribution businesses in the NEM, and may operate under a variety of ownership structures and operating models.

On this basis, the Commission considers that a one-size-fits-all approach is unlikely to be appropriate for the regulation of third-party SAPS. Rather, the most appropriate approach to regulating third-party SAPS is through a tiered regulatory framework which enables regulation to be applied in a proportionate way.

### Three-tiered framework

The recommended framework covers three broad categories of systems. Third-party SAPS which meet a coverage test would be classified as category 1 and regulated under the national framework in an equivalent method to standard supply. All other SAPS would fall within categories 2 and 3 and would be regulated under jurisdictional frameworks to allow for the flexibility and proportionality necessary to accommodate the wide variety of circumstances under which third-party SAPS may emerge.

- **Category 1** would comprise very large microgrids, in particular those large enough to warrant regulatory determinations by the AER. The existence of network tariffs arising from the regulatory determinations, together with the likelihood of a relatively large number of customers, would mean that such systems should also be able to support effective competition in generation and retail. The existing national laws and rules would be extended to apply to these systems, as should relevant existing jurisdictional frameworks, so they are regulated in equivalent manner as standard supply.
- **Category 2** microgrids would range from those connecting more than a handful of customers to those supplying smaller towns. Microgrids under category 2 will generally be expected to be vertically integrated on the basis that their size is unlikely to be able to support meaningful competition in generation and retail where they do not form part of a larger regulated entity. The AER revenue determination process to set network tariffs would be disproportionately burdensome if applied to an individual category 2 microgrid, and it would not be cost effective for competing retailers to develop specific retail tariffs. Comprehensive consumer protections, safety standards and operational obligations should be imposed on the operators of these systems through jurisdictional regulation, which would provide the flexibility and proportionality necessary to accommodate the potential breadth of circumstances.
- **Category 3** would encompass very small microgrids with a handful of customers, microgrids only supplying large customers and individual power systems where there is a sale of energy. These SAPS are likely to have a much lower regulatory risk, and failure of the energy provider would impact a much smaller number of customers. In addition, customers are likely to have a higher degree of control over system specifications and requirements, and greater bargaining power. A proportionate framework would have some minimum consumer protections, such as billing requirements, as well as energy-specific safety requirements, basic metering requirements and some technical standards provided through jurisdictional conditions.

### Background

A stand-alone power system is an electricity supply arrangement that is not physically connected to the national grid. The Commission uses the term to encompass both microgrids, which supply electricity to multiple customers, and individual power systems, which relate only to single customers. Changes in technology and technology costs are leading stand-alone power systems to become an increasingly viable option for providing electricity services to customers.

Currently, the national energy laws and rules only apply to the interconnected electricity grid on the east coast of Australia that forms the NEM. Where there are stand-alone systems not connected to this grid, these are subject to regulation by states and territories at the jurisdictional level. State and territory regimes for SAPS differ quite widely, and regulation is not necessarily comprehensive. Enhancements to the regulatory framework are required to allow customers to take advantage of new technology and approaches, and enable the adoption of future advancements in technology.

**Category 1 third-party SAPS should be regulated under national arrangements, and category 2 and 3 third-party SAPS should be regulated under jurisdictional frameworks.**

## Implementation and next steps

Implementation of the recommended framework for third-party SAPS will require a package of changes to the national energy laws and rules, and to jurisdictional legislative instruments. The Commission has prepared recommended drafting instructions for amendments to the National Electricity Law and National Energy Retail Law for consideration by the COAG Energy Council.

The next stage of work involves the development of detailed revisions to the National Electricity Rules and the National Energy Retail Rules to apply the final recommendations for the regulatory framework for category 1 SAPS, and to allow for customers to transition from the grid to third-party SAPS. The regulatory framework for category 1 third-party SAPS will not be implemented until the complete package of national energy law and rule changes have been made.

The Commission anticipates that the implementation of the requisite rule changes will follow the same approach as priority 1. Following endorsement of its recommendations by the COAG Energy Council, the Commission could commence work to develop rules to implement the recommended framework that would subsequently be made by the South Australian Minister.

Although the development of category 2 and 3 jurisdictional regulatory frameworks are not a prerequisite to implement the national changes, it is not until jurisdictions develop new (or amend existing) jurisdictional regulatory frameworks, including SAPS specific licensing regimes, that third-party providers will be able to operate in a jurisdiction under the Commission's recommended framework. For this reason, the Commission encourages jurisdictions to commence this process as soon as possible.

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