

23 July 2026

Anna Collyer
Chair
Australian Energy Market Commission
Level 15, 60 Castlereagh Street
Sydney NSW 2000

Dear Ms Collyer

Electricity Network Regulation Review – Package 1 (Ref: EPR0106)

The Australian Energy Market Operator (AEMO) welcomes the opportunity to comment on the *Electricity Network Regulation Review – Package 1* (the Review) Consultation paper, which seeks feedback on whether the current service classification and ring-fencing framework in the National Electricity Rules (NER) continues to promote the long-term interests of consumers.

AEMO would like to make the following points regarding the issues under consideration:

1. Service classification and the revenue setting framework for Distribution System Operators

- There are three elements to regulating non-traditional network services: (1) a defined rule obligation (or equivalent) to provide the service, (2) a matched revenue mechanism, and (3) a ring-fencing adjustment at the boundary between the regulated service and contestable markets. Regarding the establishment of Distribution System Operators (DSO), these three elements are currently being pursued through separate processes. AEMO's view is that it is critical that this Review and the DSO policy framework rule change being progressed by the Commonwealth DCCEEW align so that service classification, funding and ring-fencing land as one decision.
- Service classification is currently determined by the AER for each DNSP at each revenue reset, which leads to potentially different classifications across DNSPs and a lag of up to five years before a newly recognised DSO service could be brought into the regulatory envelope. The Review should consider that the NER provide for presumptive, nationally consistent classification of foundational DSO services, available intra-revenue period rather than at each revenue reset. This is particularly important for services on which system security depends, where a minimum standard of capability and interoperability with AEMO's systems is required from all DNSPs across the NEM.
- DSO services should be differentiated by their contestability and security-criticality, with the classification, funding and ring-fencing consequences designed appropriately for each category. International practice generally supports three categories, as outlined in the table below:

Categories	Example services	Potential treatment
1. Regulated, security-critical	- Transmission–Distribution (T–D) coordination services - System security response services - CER conformance and compliance services	Classified as regulated with matched funding; mandatory for all NEM DNSPs
2. Market-interface	Flexibility procurement	Regulated provision with neutral-facilitator conditions attached to the classification itself and specified in the NER

Categories	Example services	Potential treatment
		(e.g. the UK prohibition on DNOs bidding their own assets into their own flexibility tenders, New York's non-discriminatory DER onboarding under the Distributed System Platform, and California's prohibition on the utility acting as counterparty in DER procurement)
3. Contestable	- DSO-led EV charging infrastructure - DSO storage ownership/ community batteries	Default unclassified/contestable, with DNSP entry only through a codified market-failure test (eg. EU Directive 2019/944, Articles 33 and 36: tender first, NRA approval, periodic re-testing and divestment or a defined asset boundary such as New York's "make-ready" doctrine).

- The service classification framework should recognise services that provide system security that may carry a net economic cost. Several foundational DSO services, for example emergency backstop, transmission-distribution observability and minimum system load responses, exist to keep the system secure and a conventional net economic benefits test may not be the appropriate investment test. As the system operator, AEMO's ability to manage lack of reserve and minimum system load conditions increasingly depends on these distribution-level capabilities existing consistently across the NEM. The classification framework should provide an explicit basis for classifying and funding this class of service.
- Services related to coordination across the transmission-distribution operational boundary should be considered as classified services that fall within the regulatory envelope. The technical detail should be specified in binding subordinate instruments, rather than subject to voluntary uptake or reset-by-reset negotiation. AEMO's Transmission-Distribution Coordination Program, approved by the ECMC, will develop the guidelines and procedures that define how the coordination functions are performed. These real-time coordination functions include, for example, observability of CER and distribution operating zones, exchange of information on capacity and constraints, curtailment advice and the control hierarchy for system security. For example, if aggregated sub-5 MW storage units are leased to third-party operators, these operators are not currently required to comply with the obligation to notify AEMO of any circumstances which could be expected to adversely affect the secure operation of the power system (NER 4.8.1 and 4.8.2), therefore the operation of these units leaves the network vulnerable to large aggregate changes in output from production or bidirectional units and escalating cyber security risks.
- In alignment with the M3/P5 CER Taskforce Final Report, AEMO considers that there are some non-traditional and emerging distribution network services that could be considered for classification as regulated services. For example, these services include voltage management, hosting capacity and other data provision, flexibility procurement (including customer/agent interface and emergency backstop), dynamic operating envelope (DOE) publication and operation, transmission-distribution operational interface, CER conformance and compliance monitoring and CER/Distributed Energy Resource Management System cybersecurity assurance.

2. Ring-fencing and asset sharing arrangements for distribution networks

- Each new DSO function that is established as a NER obligation will require careful consideration of the ring-fencing arrangements necessary for that new function. For example, operational requirements to maintain system security, including the calculation and management of dynamic operating envelopes on the distribution network requires arrangements to ensure that an NSP (or DSO) cannot utilise its operational control over DOEs to prioritise its own commercial asset portfolio over other market participants.

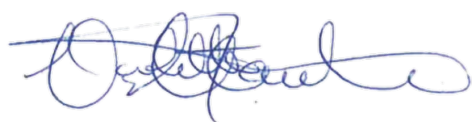
- This Review of ring-fencing arrangements should be cognisant of the implications of emerging business models for multi-service assets. For example, AEMO notes that connection of multiple sub-5 MW batteries clustered at a single substation are creating unintended consequences including reduced transparency of the service to the market and a potential compromise to system security. Disaggregating utility-scale storage units at one site into multiple 4.99MW batteries enables the facility to be exempt from registration under AEMO's Guide to Registration Exemptions and Production Unit Classifications¹. However, the definition in the NER for a 'generating system'² creates ambiguity as systems comprising of multiple sub-5 MW BESS would normally require a registration application. This regulatory misalignment can result in projects bypassing formal registration thresholds, compliance with generator technical standards as well as inclusion in formal network limits advice³ which help maintain power system security. Further, this emerging business model could be used by monopoly NSPs to navigate around regulatory requirements to provide faster connection or access to the network to affiliated businesses, reducing market competition.
- AEMO's view is that any 'market failure test' considered as part of ring-fencing arrangements should consider, among other things, whether the infrastructure or service is necessary for the NSP to fulfil its obligations for the efficient, safe, reliable and secure operation of the system and/or reducing greenhouse gas emissions. There may also be reason to consider ring-fencing exemptions for assets that provide only non-market ancillary services like voltage or reactive-power management.

3. Emerging system operator capabilities

- AEMO recognises that maintaining power system security in an increasingly complex, high-renewables environment will require sustained uplift in the operational capability of NSPs, including operational technology, situational awareness, forecasting, coordination, system resilience and emergency response capabilities. Historically, regulatory frameworks have focused heavily on physical network assets. However, secure operation of the future power system will also depend on the people, processes, systems, data and tools required to plan, monitor, coordinate and operate a highly dynamic electricity system. In many cases, capability uplift may involve significant investments in modelling capability, operational technology, monitoring systems, data and digital platforms, control room tools and associated operational arrangements.
- The ability of NSPs to efficiently develop and maintain these capabilities will be important to supporting power system security and operational resilience. AEMO considers it appropriate for the Review to consider whether the existing revenue setting framework should better support efficient and timely investment in NSP operational capability. This Review provides an opportunity to consider how the regulatory framework can continue to evolve to support these outcomes over time.

Please contact Hannah Heath, AEMO Group Manager – Strategic Market Reform to discuss anything further (hannah.heath@aemo.com.au).

Yours sincerely,



Violette Mouchaileh
Executive General Manager – Policy & Corporate Affairs

¹ Which outlines that 'A standing exemption is available to a person who owns, operates or controls a Generating System or Integrated Resource System with a nameplate rating of less than 5MW when fully connected to a transmission system or distribution system'

² 'a system comprising one or more generating units'

³ Refer to NER 4.3.1(g)