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Total Environment Centre
AEMC Contestability rule changes
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Total Environment Centre's National Electricity Market advocacy

Established in 1972 by pioneers of the Australian environmental movement, Total Environment Centre (TEC) is a veteran of more than 100 successful campaigns. For nearly 40 years, we have been working to protect this country's natural and urban environments: flagging the issues, driving debate, supporting community activism and pushing for better environmental policy and practice.

TEC has been involved in National Electricity Market (NEM) advocacy for ten years, arguing above all for greater utilisation of demand side participation — energy conservation and efficiency, demand management and decentralised generation — to meet Australia's electricity needs. By reforming the NEM we are working to contribute to climate change mitigation and improve other environmental outcomes of Australia's energy sector, while also constraining retail prices and improving the economic efficiency of the NEM — all in the long term interest of consumers, pursuant to the National Electricity Objective (NEO).

Introduction

Pursuant to its ECA grant *Networks + batteries: what's best for consumers?*, TEC is interested in the AEC and COAG EC contestability rule changes because contestability offers the prospect of facilitating high penetrations of solar energy supported by storage in local grids to complement the rollout of large scale renewables. In the short to medium term the success of these rule changes is most likely to assist

- Solar owners who are considering installing a battery not only for self-consumption but also to interact with the grid.
- Proponents of grid-scale storage who – with the right regulatory settings – may cooperate with networks to deliver multiple value streams; but equally, if we get these settings wrong, may be forced to enter this market only on terms favourable to networks (which may consequently prove to create a significant disincentive to investment).

So – as we pointed out in our 2016 *Networks + batteries* report and our submission to the AEMC's Consultation paper – we don't think it should be a case of 'anything goes' in the short term to make sure networks – who have been doing some valuable battery trials recently – don't pack up and go home if faced with the prospect of competition. Like the AEMC and the rule change proponents, we favour regulation that restricts the role of monopoly networks from owning consumer-side¹ DER, and wherever possible, encourages competition in grid-side DER as well.

In short, in the draft determination (DD), the AEMC has drafted an excellent response to issues raised in energy storage review last year and the rule change requests. However, in one important respect we consider it could have gone further.

Restrictions on consumer-side assets

TEC supports Part 1 of the DD, which restricts networks from earning regulated returns on consumer-side DER, noting that

- Networks will still be able to effectively compete for consumer-side DER via their ring fenced businesses (assuming ring fencing works as intended).

¹ ie, on the customer's side of the connection point.

- The AEMC is proposing an exemptions provision wherein networks can make a case that they should be able to play directly in that space; however, we would like to see a high bar set for granting such exemptions so that it doesn't become like the AER's retail exemptions provisions, with literally thousands approved.
- If eventually successful, the Western Power Alternatives to grid-supplied network services rule change request would still allow networks to provide services to customers in isolated areas who have been taken off-grid to avoid expensive network investment or maintenance.

Classifying distribution services

TEC agrees with the incremental changes proposed to improve the service classification system, since they should improve the transparency, inclusiveness and flexibility of this system. However, we consider they could go further. In short, it is not clear that the measures proposed in the DD will encourage more competition for grid-side DER.

To explain why this matters, here are two examples of the potential negative consequences of network domination of grid-side storage market:

- You have a home battery and want to sell your surplus energy into the local grid to help reduce peak demand, but the network has its own grid-side batteries already so won't pay for your exports; or, for technical reasons, it has limited exports to the grid in your area.
- You are a DER proponent or retailer wanting to build a midsize battery (100kWh-1MWh) to take advantage of the multiple potential value streams available, but there is no spare capacity on that part of grid because the network has used it for its own batteries; or the network wants to reserve capacity for future batteries, so you'd have to pay connection costs which are prohibitive.

Take, for instance, Ergon's (now Energy Queensland's) innovative 100kWh GUSS batteries, 17 of which have been installed on long skinny feeder lines to reduce the need for augmentation to meet increasing peak demand, and for voltage control. It's apparently still a trial, but if a project like this becomes BAU (which is only matter of time), installations like these will be able to take advantage of other values streams – especially arbitraging and the FCAS (frequency control and ancillary services) market.

We see nothing in the DD to guarantee that such devices, which could be added to networks' asset bases and therefore be the subject of regulated returns for a decade or more, are likely to be procured at lowest cost on the open market. This is not to suggest that EQ or any other network will deliberately inflate the cost of these units to maximise the regulated return from them. Rather, our concerns are that the absence of competitive pressure will de facto lead to higher than necessary costs to consumers; and that the guarantee of regulated returns may disincentivise networks from maximising the various value streams available. This is arguably a missed opportunity for the rest of the market if either some value streams are missed, or if no one other than networks gets to play in that space.

In practice this may not turn out to be a major problem. Since arbitraging and FCAS are likely to be more valuable than network support over the medium to long term, networks may be obliged to contract with third parties to maximise their value (with the spoils divided up via the existing shared asset and cost allocation mechanisms). But if that turns out not to be the case – if, for instance, networks can use RITs to install batteries to provide network support (relating to peak demand and/or reliability) and add them to their assets without involving third parties to capture other value streams; or alternately, if they manage to deal exclusively with their own ring-fenced businesses – then this rule change may not live up to its promise

to improve competition in grid-side DER. The regulatory regime should not be based on assumption that current or foreseeable market conditions will continue ad infinitum; we need rather to plan for worst case scenarios.

This problem arises because (as the AEMC stresses in the DD), while the AEC rule change request identifies the opportunity for greater competition offered by grid-side as well as consumer-side DER, under the current service classification system classifying DER as a separate category of contestable services would mean that the revenue couldn't be recovered under the RAB; thus networks are likely to prefer poles and wires capex solutions instead.²

However, if we can't carve out separate a 'contestable' niche for DER in direct control services (DCS), perhaps we can treat more regulated network investments like DER – ie, as contestable. This could happen by making a creating a new subset of DCS (eg, energy storage services) and requiring that all such services be contestable. The cost of providing them would then recovered via opex, like RIT-D non-network options.

A more radical option would be to make *all* DCS spending including poles and wires and substation kit over a certain threshold - \$1 million or \$5 million – subject to market competition, with the costs recoverable only as opex via contractors for the regulated or effective lifespan of each asset.

Finally, this problem arises in part because concern remains that the rules favour capex over opex spending. We recommend that the AEMC explores whether moving revenue recovery to a totex (capex plus opex) model would remove the capex bias.

Whether or not any of these suggestions proves feasible, we recommend that the AEMC think creatively about how to use the service classification system to encourage competition in grid-side DER.

Yours sincerely,



Jeff Angel
Executive Director

² AEMC, DD, 21.