



# Economic regulation of network services

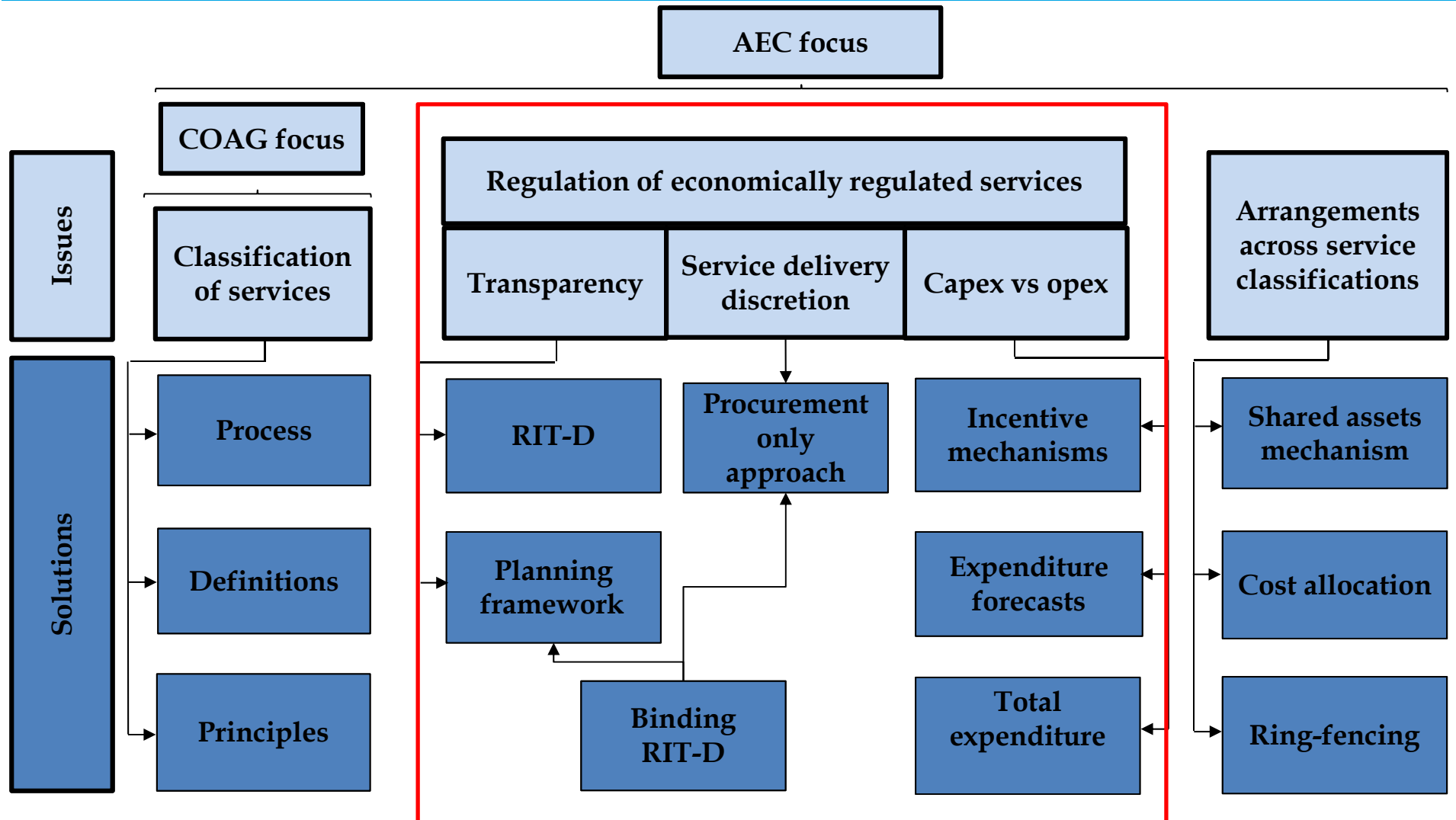
Public Forum on Contestability of Energy Services: 25 January 2017

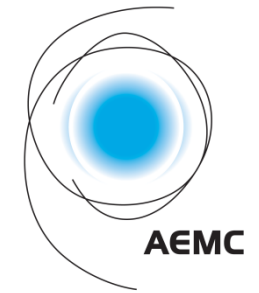


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# Focus for this session

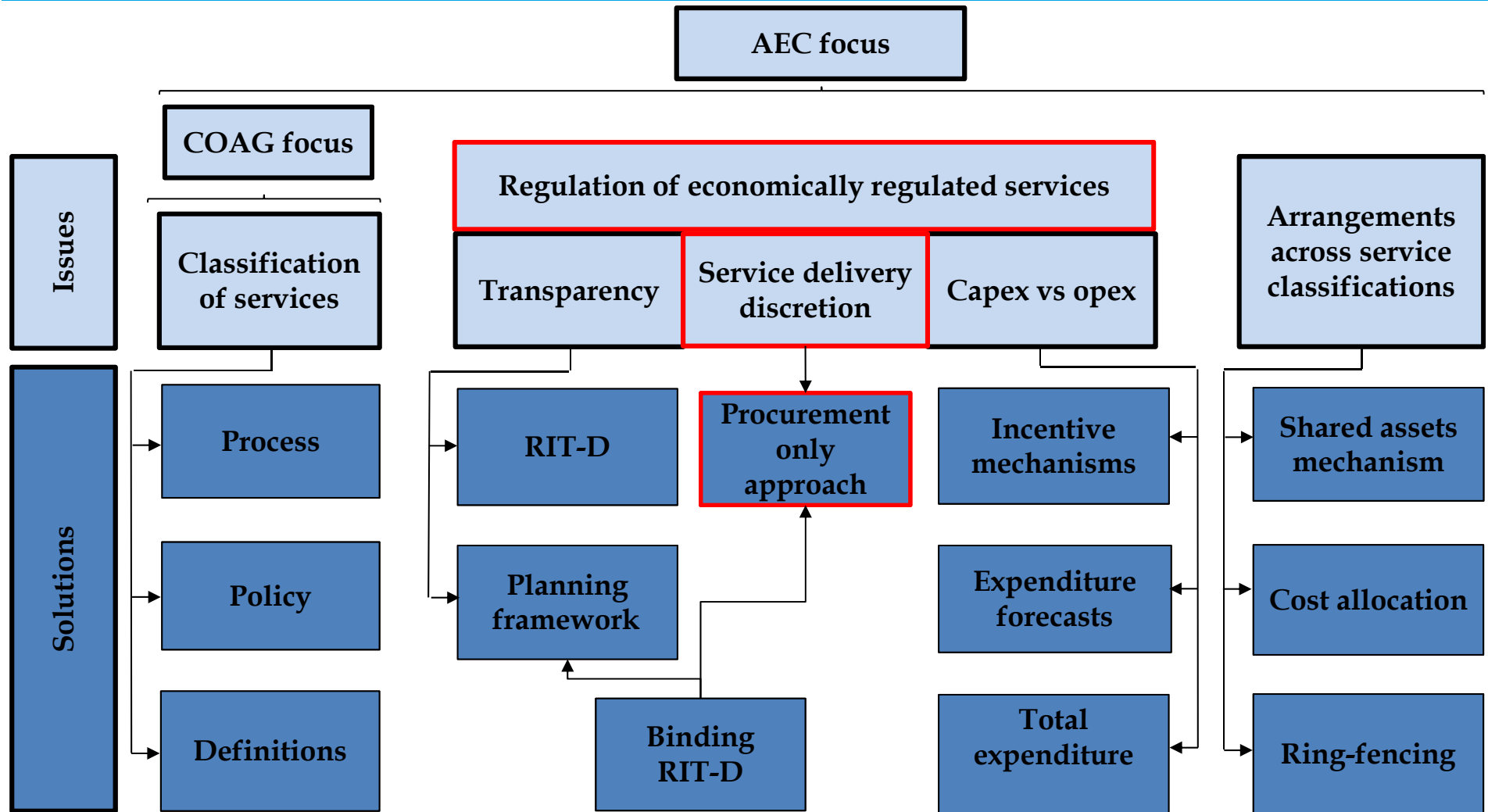




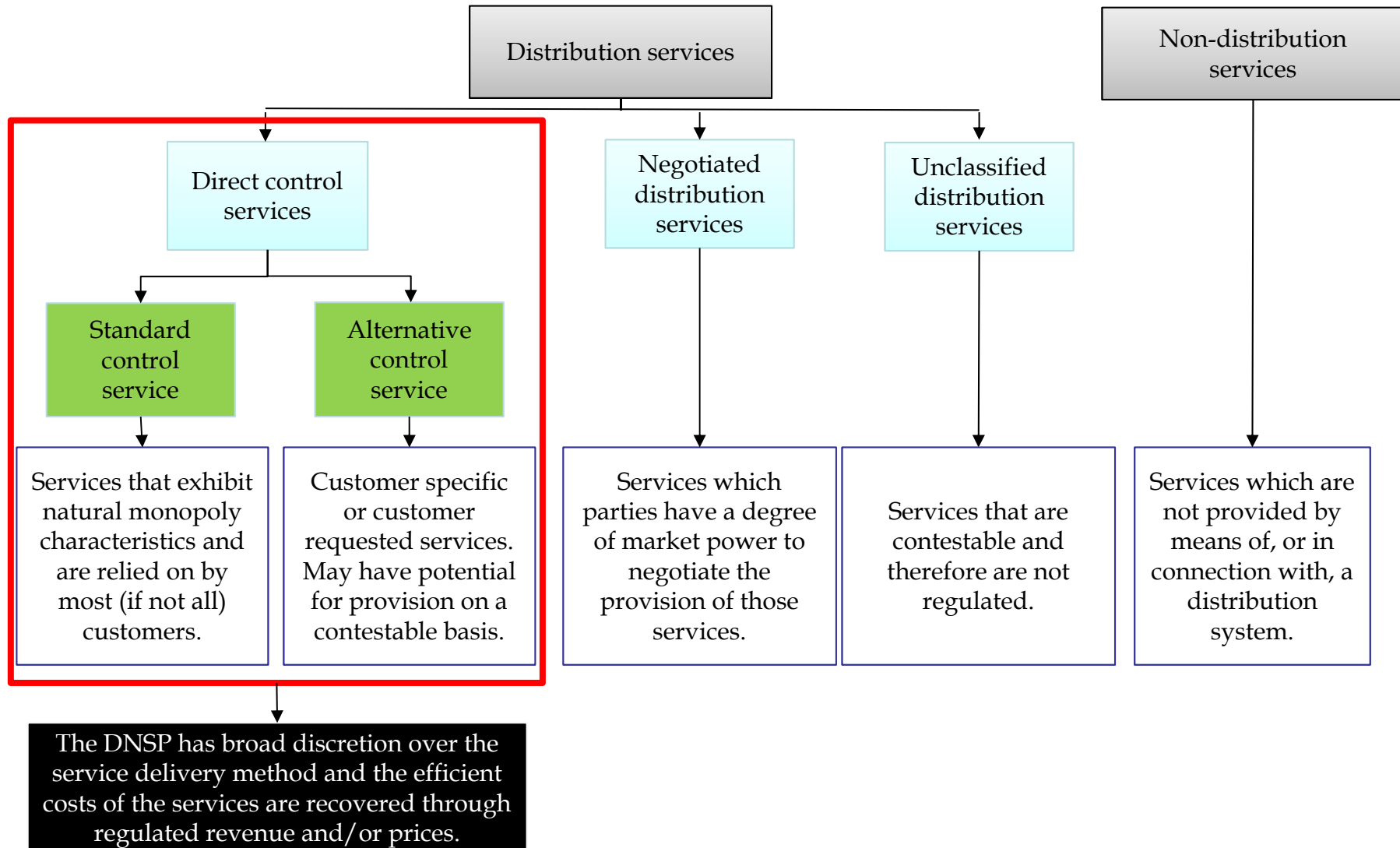
# Economic regulatory framework Part 1: incentives and discretion



# Relevant part of the rule change requests



# Economic regulation



# Key features of economic regulation: Incentives and discretion

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- **The use of incentives to achieve efficient outcomes (as opposed to prescription)**
- **DNSPs have discretion on how they spend the revenue to meet regulatory obligations and provide services using a combination of:**
  - Network vs non-network
  - Capex vs opex
  - In-house build/service vs procuring from third parties or related entities
  - Different types of technologies
  - Location of the assets
- **Incentive schemes - EBSS and CESS**
  - Complementary to the incentive framework

# Issues identified in the rule change request: Procurement of inputs

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- **AEC position:**
  - DNSPs should be required to procure network support, demand management and inputs provided by assets located 'behind the meter' from contestable markets
  - DNSPs should also be prevented from investing in assets that provide the above mentioned inputs
- **AEC rationale** - unique characteristics that distinguishes them from other inputs:
  - Immature technologies – market dominance by DNSPs could potentially inhibit cost reduction, technology improvements and business model innovations
  - Potentially sizable market for services from assets 'behind the meter', this may be able to offset investment in the network
  - services from assets 'behind the meter' are a potential competitor to the distribution network as a means of supplying customers with electricity in the long-term.

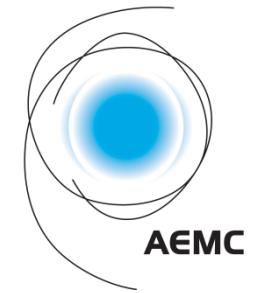
# Questions:

## DNSPs service delivery discretion

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- Is there a problem with DNSPs having service delivery discretion in relation to demand response, network support and other inputs derived from assets located 'behind the meter'? If so:
  - i. What is the problem?
  - ii. How material is it?
  - iii. Provide examples of the problem?
- Is the problem unique to demand response, network support and other inputs provided by means of assets 'behind the meter'?



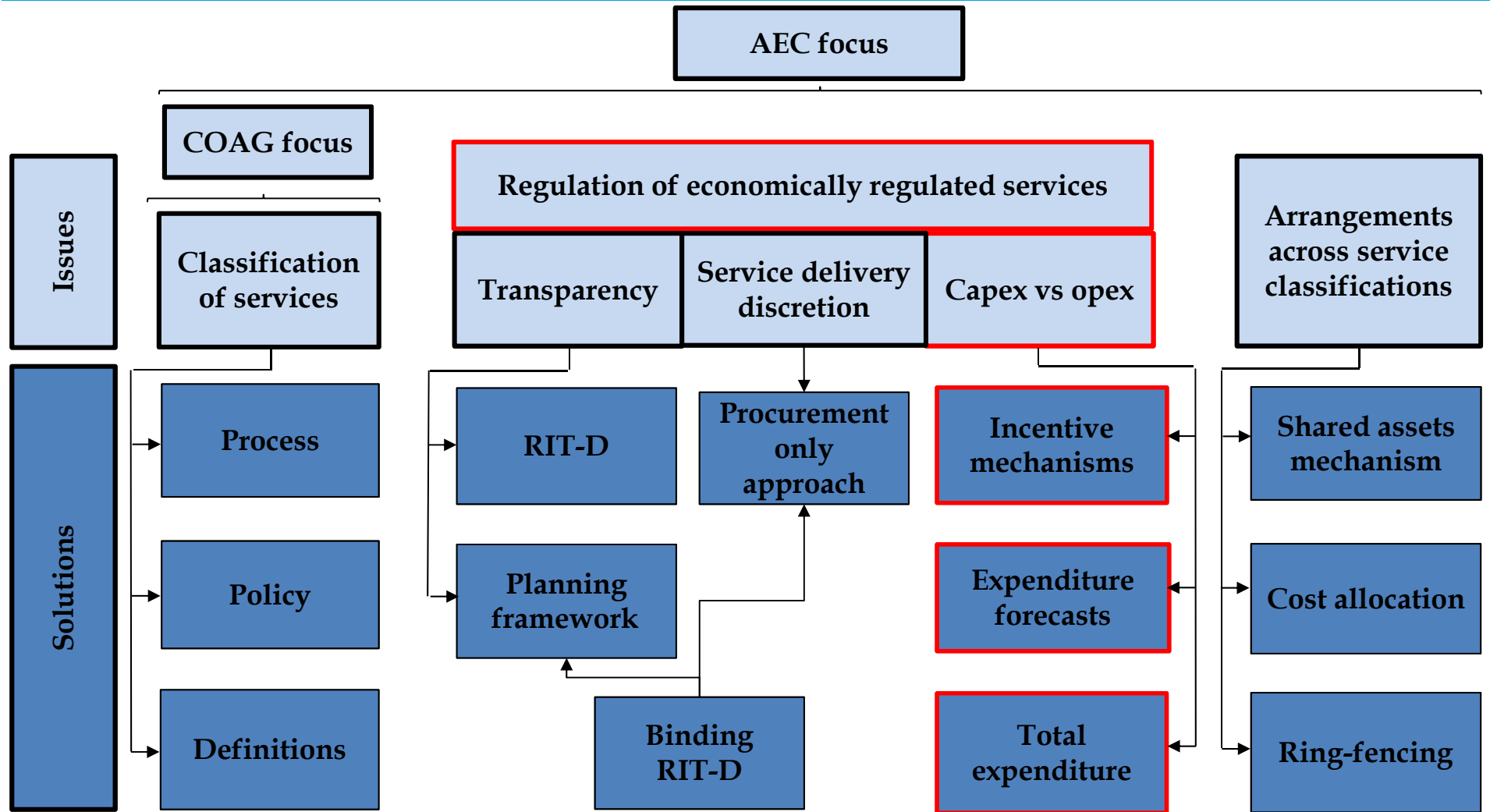


# Economic regulatory framework

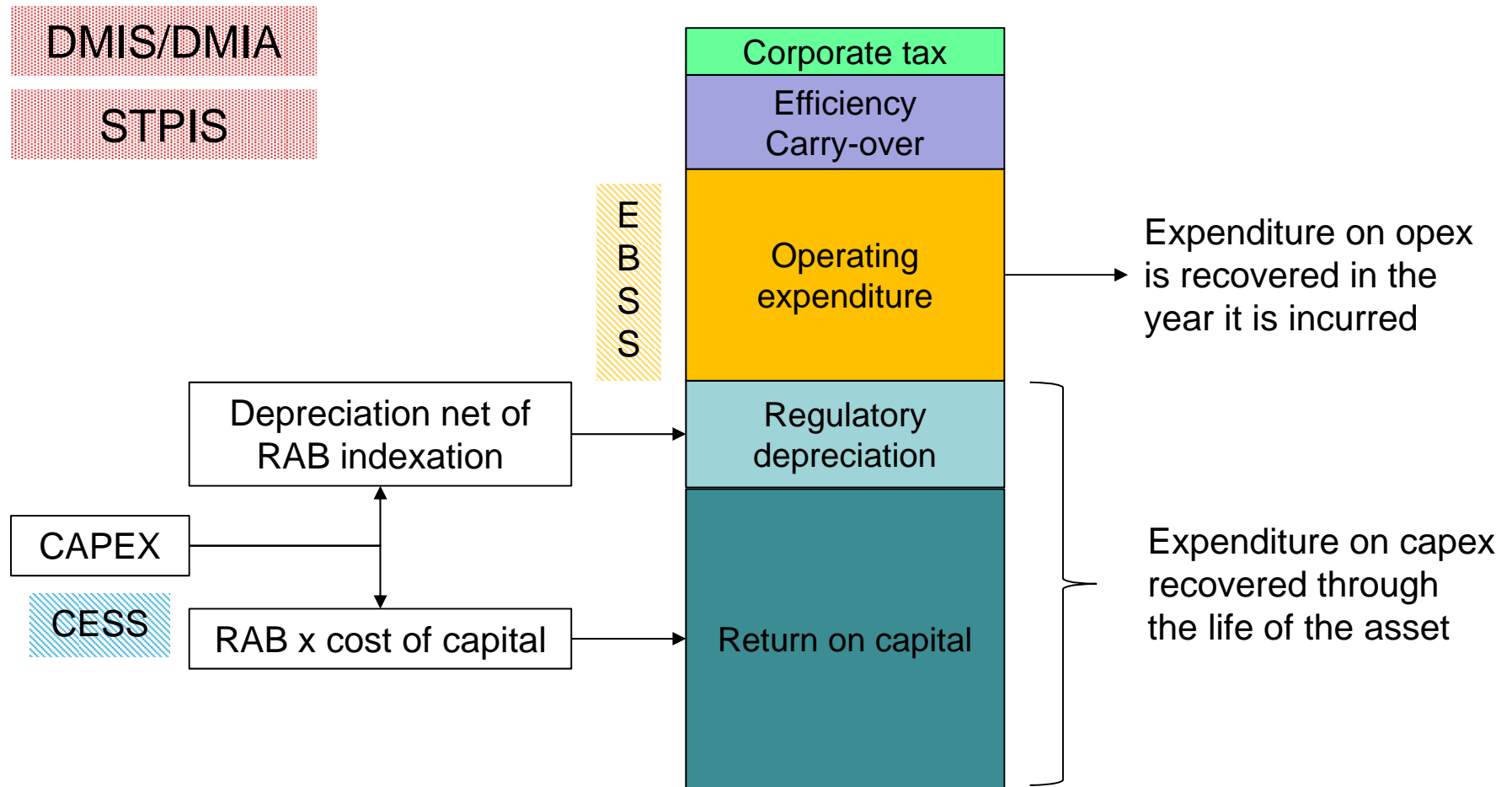
## Part 2: capex vs opex



# Relevant part of the rule change requests



# Revenue determination: the building block



# Issues identified in the rule change request: Balance between capex and opex

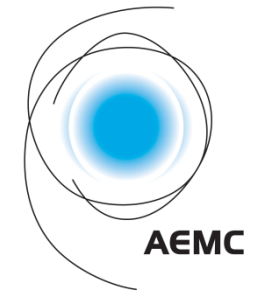
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- **AEC positions:**
  - current framework incentivises DNSPs to favour capital expenditure in order to grow their regulatory asset bases
  - The efficiency benefit sharing scheme (EBSS) and DMIS should be reviewed to ensure that they cannot be "gamed" by DNSPs to share benefits with an affiliate and, thus, gain an advantage over other providers
  - The framework needs to maximise the scope for independent competitive providers to supply network support services to networks. To do this they need to be exposed to the information and price signals that indicate where and when network support services are most valuable

# Questions: Incentives

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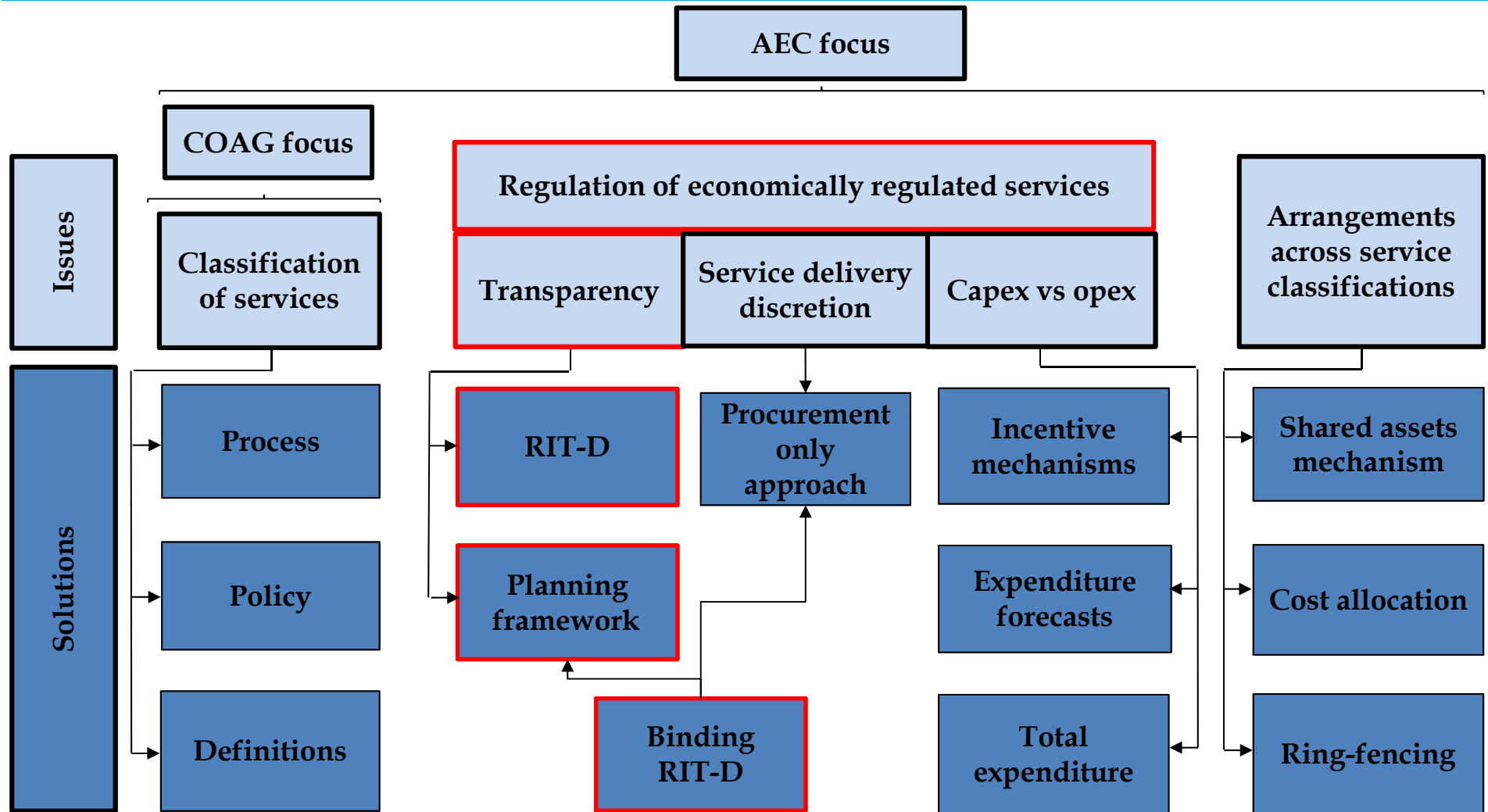
- Does the regulatory framework provide balanced incentives for DNSPs to use the most efficient mix of:
  - i. network or non-network options?
  - ii. capital and operating expenditure?
  - iii. a range of technologies?
  - iv. assets that are positioned behind or in front of the meter?
  - v. providing the services "in-house" or procuring the services from other parties?
  - vi. procuring the services from third parties or related entities?



# Economic regulatory framework Part 3: planning framework



# Relevant part of the rule change requests



# Planning framework: Regulatory Investment Test – Distribution (RIT-D)

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- **RIT-Ds**
  - DNSPs are required to undertake RIT-Ds for distribution (augmentation) projects over \$5 million
  - This is in addition to the standard AER assessment of capital expenditure for the regulatory period (conducted during the revenue determination process)
- **Purpose**
  - Test whether the DNSPs proposed solution is the most efficient
  - Give providers of non-network solutions an opportunity to propose alternatives
- **DNSPs are not required to implement the most efficient solution identified**
- **AER's replacement expenditure planning arrangement rule change**
  - Extend the RIT-D to cover replacement projects
  - AEMC consultation paper was published 27 October 2016



# Planning framework: Annual planning requirement

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- **Distribution annual planning report (DAPR)**
  - Annual report
  - Set out the DNSP review on the expected future operation of its network for the forward planning period of at least five years
- **Recent AEMC rule on local generation network credits**
  - The rule is designed to improve access to system limitation information
  - Requires DNSPs to publish 'system limitation reports' in a consistent format
  - The rule is complementary to the current DAPR requirements

# Issues identified in the rule change request: RIT-D

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- **AEC position**

- an inability of demand response and network support services to monetise the value they produce with regard to both network peak and energy peak [demand]
- the \$5 million threshold of the RIT-D limits the number of opportunities for providers of demand response and network support services to identify where they can provide such value.

- **AEC proposed solution**

- Reduction of threshold from \$5 million to \$50,000
- Truncated RIT-D
- Stricter enforcement

# Issues identified in the rule change request: Annual planning requirement

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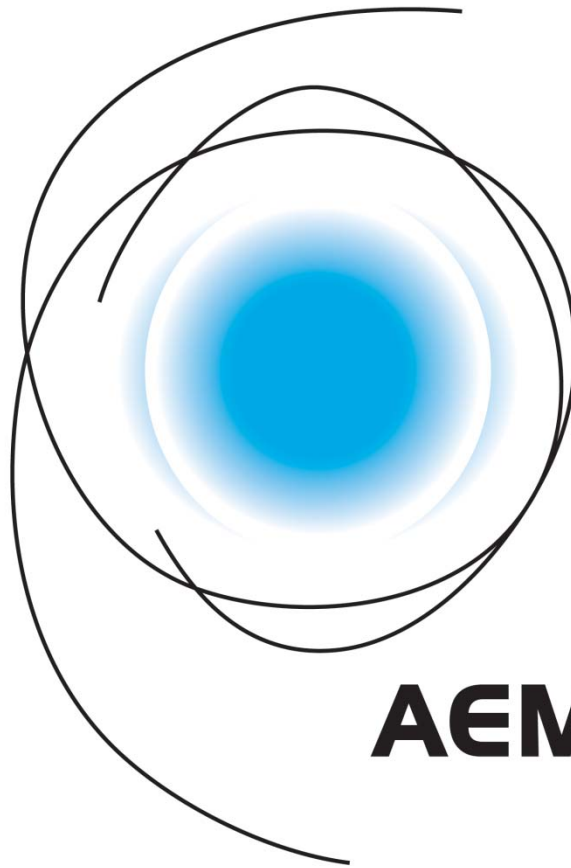
- **AEC position**
  - current annual planning requirements are not adequate for a third party to make decisions about investing in generation, transmission or distribution capacity
- **AEC proposed solution**
  - Standard access obligations to solutions at or near supply points
  - Requirement to provide:
    - all necessary information (network performance data, load data) to competitors that will enable decisions to invest in generation or storage as an alternative to distribution capacity; and
    - technically equivalent access to the network to the competitors of any regulated or related business

# Questions:

## Planning framework

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- Is there a problem with the current planning framework in relation to network support and demand management? If so:
  - i. What is the problem (e.g. the detail or timeliness of relevant information; DNSPs being both the decision-maker of investment decisions and the asset owner)?
  - ii. How material is it?
  - iii. Provide examples?



**AEMC**