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Energex - Applications for Ring-fencing waiver 2016

The Australian Energy Council (the Energy Council) welcomes the opportunity to make a submission to the Australian Energy Regulator (AER) in relation to the two applications from Energex seeking waivers from s. 6.1(b) of the Queensland Distribution Ring-Fencing Guidelines (the Guidelines).

The Energy Council is an industry body representing 22 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia, and sell gas and electricity to over 10 million homes and businesses.

The Energy Council does not support the AER granting these waivers to Energex. To do so would create uncertainty for potential entrants to the emerging market for energy storage services. However, if the AER decides to grant the waiver, the Energy Council recommends that the waiver should end at the start of the national ring fencing Guidelines and that Energex be required to re-submit for a waiver based on the revised national framework. The Energy Council also recommends that any waiver issued should be based on the following conditions:

- It should be a prerequisite for eligibility for a ring fencing waiver that Energex be required to go to tender for the provision of the solar PV and BESS systems as well as the mobile educational exhibit. This would encourage local industry and innovation, and promote confidence in the competitiveness of the commercial terms entered into by Energex.
- All information and learnings of trials funded through regulated revenue should be made publically available. This promotes a competitively neutral environment.

Application of QCA Ring Fencing Guidelines

Under the existing QCA Guidelines a Distribution Network Service Provider (DNSP) must not carry on a related business within that entity without seeking a waiver. A related business is defined as the business of producing, purchasing or selling electricity.

The application argues that even though the Battery Energy Storage System (BESS) project will involve generation, Energex does not, "*consider this constitutes carrying on a related business*"ⁱⁱ because it is not, "*in the business of producing electricity as there is no intention to make a profit*"ⁱⁱⁱ. To the extent that the activity covered in this application involves the introduction of electricity to the grid, it constitutes producing electricity and is therefore a related business. Energex's intention with regard to profit is irrelevant to the guideline, which contains no such caveat.

Energex's intent not to profit from the trial is also intriguing. We estimate that intellectual property flowing from this project will have considerable ongoing commercial value.

New national ring-fencing guidelines

With the AER undertaking a review of the new national Guidelines, pre-empting the outcome of the AER's review by granting an exemption from existing QCA Guidelines is not proper. The precedent of granting an exemption would assumedly apply to other DNSPs seeking similar exemptions prior to completion of the current ring fencing review. Such a consequence should clearly be avoided if we are to ensure that the AER Ring Fencing Guideline is not redundant before it is even published. Hence, any waiver granted prior to the completion of the new national framework should terminate with the commencement of the new framework and the regulated entity required to re-submit the waiver application based on the new framework if deemed appropriate.

The Energy Council submits that all ring-fencing waiver applications must only be provided on an exceptions basis and assessed carefully case by case. Previous decisions of the AER have applied little assessment of the costs and benefits that would arise from such decisions, and in our assessment waivers from the historical ring-fencing guidelines have been applied too leniently in some jurisdictions. This lack of scrutiny in the previous decision to grant Energex a waiver for its Battery Energy Storage System projects and the apparent lack of consideration of the wider costs to consumers arising from the broader market outcomes, such as damaging the confidence of other providers of such services to invest in these opportunities, gives cause for concern.

Expanding on this point, it is important to recognise the consequential impacts on a developing services market when poorly scrutinized waiver applications are approved. We urge the AER to seek full industry feedback on the alternatives to DNSP provided BESS solutions, and to better understand the advantage that waivers deliver to DNSPs. As part of any waiver approval process the DNSP must be able to demonstrate that the delivery of the project / service could not be achieved more efficiently via a competitive tender process. That is the proposed initiative that requires the waiver is the least cost option for the delivery of the service. The Energy Council notes that on the one hand in the RAB solar PV is capitalized and on the other within the BESS solar PV is expensed through regulated OPEX. In terms of the latter, it is not clear whether this charge is based on capacity availability, discharge, or some variant thereof.

The granting of a waiver should be a last resort based on exploring all possible solutions. For example, for this particular application the Energy Council would urge the AER to require Energex to undertake a competitive tender process for both the solar PV and BESS systems as well as the mobile educational exhibit and that all information gathered, including wider energy market outcomes, should be made publically available to all market participants.

The AEMC's recommendations from the Integration of Storage paper released late last year represents a reasonable starting point in terms of the issues that the AER should consider when granting a waiver. However, even with the AEMC's starting point, considerable scrutiny is required to determine whether a waiver from the guidelines is warranted. If waiver applications are granted too easily it could impact the supply of contestable services in emerging markets, to the ultimate detriment of consumers.

Service-level agreement (SLA)

The Energy Council submits that there needs to be greater transparency regarding the information sharing arrangements that form the SLA. While there may be information within the SLA that is of a commercial in-confidence nature, stakeholders need to be aware of the types and reasons why information is being exchanged and under what term. This is important considering Energy Impact may be a participant in contestable energy storage services in the future and its engagement with the network business may provide it with levels of operational understanding not available to other market participants.

Understanding the impact

The AER accepted that Energex's previous domestic BESS pilot project was for research purposes and noted that there is a materiality consideration. The AER concluded that even though the administrative costs of Energex ring fencing the project would be relatively minor compared to Energex's total revenues, they outweigh any potential benefit. The AER concluded that there were unlikely to be material benefits to consumers from requiring Energex to undertake ring-fencing in this instance.

The Energy Council believes a determination of materiality must have been made in the context of its impact on the broader market for the service in question. In this situation it was not apparent what judgments the AER relied upon or applied to determine the public detriment of allowing this waiver and in particular what impact, perceived or otherwise, Energex's direct participation will have on market entry and competition in this emerging market.

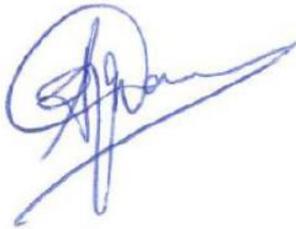
Moving forward

A network business may identify efficiencies and synergies that can be achieved in the operation of its network through battery technology. However the public benefits, including wholesale market benefits, are broader. Accordingly, networks should be compelled to partner with a retailer or other operator to understand and realise them or to outsource them altogether given that these market benefits cannot accrue to the distributor.

The AER has the opportunity to send a strong signal that it will only support a level playing field and competitively neutral outcomes consistent with the principles that underpinned the establishment of ring-fencing. The purpose of ring-fencing is to provide confidence to others that they will be able to compete with an unregulated business on a fair and equal basis. The Energy Council submits that the AER must properly and fully consider the potential detriments to competition before granting Energex waiver applications.

Any questions about our submission should be addressed to Panos Priftakis, by email to panos.priftakis@energycouncil.com.au or by telephone on (03) 9205 3115.

Yours sincerely



Sarah McNamara
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ⁱ Energex, 2016, "Energex Application for a ring-fencing waiver under the electricity distribution ring-fencing guidelines", 18th of May, pg. 2

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