

2 July 2020

John Pierce
Chair
Australian Energy Market Commission
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Ref: EPR0085

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Dear Mr Pierce

Re: AEMC, Electricity network economic regulatory framework 2020 review, Approach Paper, 4 June 2020

AusNet Services consider that the Commission's annual review is a valuable forum for early stakeholder engagement on how the Electricity Network Economic Regulatory Framework (Framework) may respond to emerging trends. We therefore welcome the opportunity to make a submission on the Commission's approach paper for the Electricity Network Economic Regulatory Framework 2020 Review (2020 Review).

Our submission first discusses the existing arrangements covering the integration of Distributed Energy Resources (DER) to date, which was the subject of the 2019 Review. Next we discuss the three focus areas outlined in the Approach Paper of the 2020 Review, namely the risks to customers from costing of large discrete projects arising from ISP, the risk allocation between distribution network service providers (DNSPs) and consumers, and the potential for improved customer engagement through the New Reg process, which AusNet Services has recently trialled. Lastly, we discuss the value and operation of the Framework Review process.

Issues involved in the efficient integration of DER

In its 2019 Review, the Commission explored the integration of DER into the National Electricity Market (NEM) and through this process came up with five essential areas to ensure the integration and optimisation of DER for consumers.¹ As noted in the Approach Paper, the integration of DER remains a significant area of focus in 2020 and is a strategic priority for the Commission with many of the recommendations from the 2019 Review having commenced.

We continue to consider that these reforms remain critical to the efficient integration of DER and to enable DNSPs to effectively meet the expectations of customers. While the Commission seeks to focus on identifying emerging and priority issues beyond DER integration in the 2020 Review, we consider that the 2019 issues identified remain critical and where major advances in the regulatory framework are still required. We therefore welcome the Commission's decision that the 2020 Review will continue to monitor key trends relating to network usage and provide updates on the implementation of key reforms.

Transmission investments in the context of the ISP

A framework for the funding of Integrated System Plan (ISP) priority projects has been established in the specific National Electricity Rules package for the actionable ISP developed

¹ See Box 1, Australian Energy Market Commission, Approach Paper: Electricity network economic regulatory framework 2020 review (4 June 2020), p 3-4.

through the Energy Security Board. Via this framework ISP projects are adopted into the Contingent Project application process for determining required revenues.

AusNet Services supports the robust strategic, system-wide approach to planning for future electricity supply system needs encompassed by the framework for the ISP. We support the use of individual project assessments for these projects, given that they are of potentially significant scale and external to transmission network service providers (TNSP) planning oversight. The contingent project process is a mature approach for assessing revenue requirements.

However, again noting the potential scale of some ISP projects, we support analysis of how the existing economic framework may support investment in this area. While the current regulatory arrangements have only recently been introduced, the 2020 Review could focus on the potential for approaches to ensure that committed major project costs are included in a contingent project revenue determination in a way that mitigates the cost uncertainty risk for network users and TNSP. The Commission should also ensure that the approaches it considers will not impede incentives on TNSPs to deliver projects at efficient cost.

Risk allocation between DNSPs and consumers

The Approach Paper discusses the inherent risks associated with forecasting efficient levels of capital expenditure, which results in risks of under-investment and over-investment, due in part to regulatory obligations for DNSPs relating to connections and reliability standards.

We note that the Commission has conducted a review of planning standards in the past and retained a deterministic planning approach.² During that review process AusNet Services advocated a probabilistic planning process, whereby investments are planned according to improved economic efficiency. Network planning in Victoria continues to use this approach. In our view this delivers better cost outcomes for customers. With significant increases in distributed generation since that review, we suggest that it may be timely to review the effectiveness of different planning approaches.

The Approach Paper concentrates on the allocation of risk from inaccurate demand forecasting. AusNet Services does not perceive this as a material issue for review. Forecasting techniques, tools and data have developed significantly over time and outcomes have been demonstrated as providing high accuracy. Further, the actual forecast underlying a revenue allowance is ultimately determined by the AER. The AER and its consultants have access to detailed data necessary for carrying out a thorough assessment of a networks' forecast. The AER makes this decision amongst a number of component decisions which deliver its overall revenue decision.

The application of probabilistic planning under the current incentive regime minimises the risk that investment will be undertaken based on demand forecasts that turn out to be overstated. Demand forecasts are updated on an annual basis, and investment only occurs where the expected economic benefits exceed the cost of the investment.

In addition, the incentive schemes in their current form (including the Capital Expenditure Sharing Scheme and Service Target Performance Incentive Scheme) work well as a package, providing strong incentives for networks to balance expenditure and reliability outcomes.

While we consider that this risk is not a material issue in today's regulatory framework, we also note that this risk is likely symmetric between networks and customers. That is, given the advanced forecasting techniques applied today, and the thorough assessment carried out by

² Australian Energy Market Commission, Draft Report - National Workstream: Review of Distribution Reliability Outcomes and Standards (28 November 2012).

the AER and its consultants, it is just as likely that demand forecasts prove too low as they do too high.

Need for enhanced consumer engagement

As the Commission notes in the Approach Paper,³ network revenue determination processes have changed significantly in recent years to support enhanced consumer engagement. One key change has been the introduction of the New Reg process which we participated in as an Australian-first trial. As part of this we established a Customer Forum and negotiated parts of our 2022-2026 regulatory proposal for our electricity distribution network.

The Customer Forum was established to represent the perspectives of our customers, drive cultural change across the business and to negotiate and agree key parts of our Revenue Proposal. It was supported by a substantial amount of customer research and engagement, including with end use customers (residential and business), consumer advocates and our Customer Consultative Committee. Material developed for the Customer Forum was published on our website for transparency and we published a Draft Electricity Distribution Regulatory Proposal in February 2019 containing our initial agreed positions for stakeholder feedback.

Reflecting on our experiences of the New Reg process, it is important to note that the effectiveness and efficiency of this process, compared to other forms of regulatory engagement, can only be fully assessed following the AER's Final Decision on our negotiated outcomes contained within our regulatory proposal.

However, the Customer Forum mechanism has allowed us to understand our customers' perspectives in a meaningful, in-depth way to deliver a proposal that reflects customer interests through negotiating outcomes. Given this, there may be an opportunity to shorten the formal process for assessing regulatory proposals post-lodgement with the AER.

We would be pleased to meet with the Commission to discuss our experiences if useful for this review and look forward to participating in further consultation on the implications for the regulatory framework of this trial.

Valuable forum for engagement

This annual review has canvassed many important topics in its three years to date and is a valuable forum for early stakeholder engagement on how frameworks may respond to emerging trends. For example, the regulatory sandbox rule changes emerging from the 2018 review should encourage the testing of innovative initiatives by industry participants once this framework is ultimately established.

However, in considering the Commission's overarching question when conducting these reviews, namely of whether the framework provides 'sufficient flexibility to allow and incentivise networks to adapt to changes in the market',⁴ we note that some framework changes take considerable time to become established. This is due to the requirements for COAG Energy Council and jurisdictional processes to align to the NEL and jurisdictional instruments, as seen for example through the stand-alone power systems supply option.

³ Australian Energy Market Commission, Approach Paper: Electricity network economic regulatory framework 2020 review (4 June 2020), p 6.

⁴ Australian Energy Market Commission, Approach Paper: Electricity network economic regulatory framework 2020 review (4 June 2020), p 1.



AusNet Services encourages the Commission to engage with the relevant government parties to progress these reforms more rapidly in line with the needs of stakeholders and ultimately consumers.

If you require further information about our submission, please contact Victoria Draudins at victoria.draudins@ausnetservices.com.au.

Sincerely

A handwritten signature in black ink that reads "C. Eddy". The signature is written in a cursive style with a long horizontal stroke extending from the end of the name.

Charlotte Eddy
Manager Economic Regulation
AusNet Services