



Contestability of energy services

Publication of final rule and final determination

The Australian Energy Market Commission has made a final rule that facilitates competition in the emerging energy services market and improves clarity and transparency in relation to the distribution service classification framework.

Context

Technology, and the increased choices it offers consumers, is changing the energy sector. In particular, technologies such as battery storage – which can provide multiple services – make it more difficult to draw the line between what is economically regulated and what is provided by contestable markets.

Against this backdrop of change, the Council of Australian Governments (COAG) Energy Council and the Australian Energy Council (AEC) – an industry body representing generators and retailers – submitted rule change requests seeking to facilitate competition in the emerging energy services market as well as improve clarity and transparency in the distribution service classification framework.

Overview of the final rule

The final rule, which is a more preferable rule, has the following key features:

- introduces restrictions on distribution network service providers (DNSPs) earning a regulated return on assets located ‘behind the meter’
- introduces provisions that improve the distribution service classification framework’s ability to respond to technology changes
- introduces a requirement for the Australian Energy Regulator (AER) to develop and publish guidelines that set out the AER’s approach to classifying distribution services.

Reasons for the final rule

Restricting DNSPs’ ability to earn regulated returns on assets ‘behind the meter’

Since the Commission’s Power of Choice reform program started in 2012, its review recommendations and rule changes have focused on increasing the ability of consumers to control how they use electricity and manage costs.

In relation to the energy services market, the Commission considers the best way to support consumers’ ability to make meaningful choices is through robust, well-functioning competitive markets. The final rule safeguards competition in the emerging energy services market by addressing the following concerns about DNSPs’ actions:

- **Favouring network benefits at the expense of maximising value across the electricity system.** Many of the new technologies are capable of providing multiple value and revenue streams, but not simultaneously. In an increasingly connected energy sector, the efficient use of new technologies must not be considered in the distribution sector alone, but across the whole energy supply chain. If DNSPs are in control of assets embodying the new technologies, they may favour network benefits at the expense of maximising value across the electricity system as a whole.

The final rule facilitates competition in the emerging energy services market.

- **Foreclosing competition in the emerging energy services sector system.** The nature of new technologies such as battery storage is such that once installed at a customer's premises, the customer is not likely to install additional assets of the same type. DNSPs, with their incumbent status as monopoly operators of distribution networks, are able to adversely affect the level of competition in the energy services market through the ability to install (and operate) these assets and recover the costs of those assets through regulated revenues.

The Commission considers that the final rule provides an effective and proportionate response to the issues raised by COAG Energy Council and the AEC. Importantly, the final rule does not restrict DNSPs' ability to use 'behind the meter' technologies to deliver network services. It simply requires DNSPs to procure those services from third-parties or from their own ring-fenced affiliates rather than owning and controlling the assets.

Improvements to the processes of classifying distribution services

- **Promoting responsiveness in a changing environment.** It is important the regulatory framework is responsive to the rapidly changing environment. The final rule promotes the regulatory framework's responsiveness to changes through the removal of the provisions in the National Electricity Rules preventing the AER from departing from previous service classification unless a different classification is clearly more appropriate. It allows AER to classify services based on their characteristics and the relevant tests in the law and rules, not a previous classification decision.
- **Improving clarity, transparency and regulatory predictability.** As distribution service classification is a key aspect of the regulatory determination process, the final rule's requirement on the AER to publish a service classification guideline will provide stakeholders with clarity, transparency and regulatory predictability in the service classification process. The final rule retains the AER's discretion to make service classification on a DNSP by DNSP basis so that service classification decisions are appropriate to the circumstances faced by the relevant DNSP.

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