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Mr Ashwin Raj
Project Leader
AEMO

Lodged via email to ashwin.raj@aemc.gov.au

Submission on draft determination and draft rule for Expanding the transmission ring-fencing framework rule change ERC0371

The Clean Energy Council (CEC) is the peak body for the clean energy industry in Australia, representing over 1,000 of the leading businesses operating in renewable energy, energy storage, and renewable hydrogen. The CEC is committed to accelerating the decarbonisation of Australia's energy system as rapidly as possible while maintaining a secure and reliable supply of electricity for customers.

We welcome the opportunity to comment on the AEMC's [draft determination](#) and draft rule for Expanding the transmission ring-fencing framework rule change.

Overview

Given TNSPs' monopoly role in planning, operating and maintaining the transmission network, as well as in providing connections to their networks, it is necessary to have appropriate controls in place to support competitive outcomes in markets within which TNSPs may operate.

It is necessary to ring-fence monopoly services (including those components involved in providing connections to the grid) on the basis that there is a risk that TNSPs could engage in discriminatory behaviour when providing non-contestable services, distorting competition for the provision of contestable services. Regardless of whether or not this has happened in practice, the *very possibility* of such an outcome could materially reduce competition and investor confidence, creating the potential for inflated prices for consumers.

Given the pace of connections is accelerating to achieve the renewable energy transition, and the importance of maintaining investor confidence, we need to set policy defaults to maximise confidence that there are regulatory tools to address the risk of discriminatory conduct, as this is key to driving long run efficient outcomes and maximising dynamic efficiency.

It is better to have the default position that ring-fencing applies automatically, with waivers for limited obligations available only by way of exception, rather than the alternative that ring-fencing is the exception. This will help give investors and developers confidence that there will be effective competition in the contestable connection services market and that projects will not face delays from discriminatory conduct.

The potential harm to competition, and the resulting higher energy costs for consumers, from not having a robust ring-fencing framework planned or in place, which includes all negotiated

transmission services as a default position, would far outweigh any increased administrative costs to TNSPs (if any).

AEMC rule change

We support the AEMC's rule change insofar as it permits the expansion of the scope of the AER's Transmission Ring-fencing Guideline (**Ring-fencing Guideline**) to include **all** negotiated transmission services.

However, we do not support the rule change in so far as it enables the AER to:

- specify some or no obligations in respect of the provision of negotiated transmission services by a primary TNSP; and
- exclude specific categories of negotiated transmission services from the application of any obligations.

In short, we consider the AEMC's approach does not provide adequate certainty to renewable investors regarding prohibition on discriminatory conduct.

The AEMC has adopted this approach to enable the AER to manage the TNSPs concerns about the increased administrative costs of ring-fencing negotiated transmission services (if any). However, we consider that all categories of negotiated transmission services should be included in the Ring-fencing Guideline by default and that TNSPs concerns are better dealt with by specific waivers under the Ring-fencing Guideline by way of exception. Waivers are limited in time and scope and AER retains the regulatory tools to respond flexibly to evolving market conditions, for example, following an oral complaint about discriminatory conduct. In contrast, the carve outs proposed by the AEMC's rule change are unqualified and categories of services carved out cannot be "reincluded" without the AER first following an extensive consultation procedure.

There will be uncertainty as to the scope of the Ring-fencing Guideline for at least 12 months. This is likely to hinder competition in the nascent market for contestable transmission connections. Developers are likely to incur higher costs (including investment costs attributable to the uncertainty) and more delays than if the AER [rule change request](#) had been adopted.

We consider that the AER rule change request, which would include all negotiated transmission services in the Ring-fencing Guideline, is more likely to support effective competition and promote the faster connection of renewable projects at a lower cost. In doing so, it better supports achievement of the National Electricity Objectives (promoting lower costs, reliability through the connection of more batteries and reduced emissions).

For the reasons given above, we recommend that the rule change does not include the proposed clause 6A.21.2(a) which provides:

- (a1) For the avoidance of doubt, in developing the Transmission Ring-Fencing Guidelines, the AER may decide to not impose obligations in relation to negotiated transmission services or specific negotiated transmission services.

Our more detailed comments are given below.

1. **The Ring-fencing Guideline should include all categories of negotiated transmission services**

The AER, AEMC and stakeholders (other than TNSPs) have identified the potential for discriminatory conduct by the TNSP in the provision of (non-contestable) negotiated transmission services and (contestable) non-regulated transmission services.

This may hinder effective competition in the market for contestable transmission connections by discouraging:

- potential competitors from participating in the market for contestable connection services, where potential competitors perceive that the primary TNSP may use its exclusive right to provide non-contestable connection services to obtain a competitive advantage in the market for contestable connections; and
- connecting parties from seeking offers from parties other than the primary TNSP to provide contestable connection services.

Regardless of whether or not this has happened in practice, real harm may result from the perception of discriminatory conduct arising from the failure to have ring-fencing in place.

We note that AER has broad concerns about discriminatory conduct arising from the TNSP providing “all non-contestable components of a transmission connection”: see page 11 of the AER Consultation Paper – Options to address gaps in transmission ring-fencing Framework ([Options Paper](#)). For this reason, the AER requested all negotiated transmission services to be ring-fenced.

Categories of negotiated transmission services

As noted above, there is the potential for TNSPs to engage in discriminatory conduct in providing any of the four categories of non-contestable negotiated transmission services.

Negotiated transmission services are defined in chapter 10 of the NER as:

1. shared transmission services that exceed network performance requirements (category 1)
2. connection services (category 2)
3. services specified to be negotiated transmission services under clause 5.2A.4 of the NER (category 3).

These include providing cut-in works, operation and maintenance services, and setting the functional specification, of an identified user shared asset (IUSA).

4. system strength connection works (category 4).

A Connection Applicant may elect to deal with a project's system strength impacts by paying for the TNSP to carry out system strength connection works.

All these services are not contestable ie the TNSP is the monopoly provider of these services.

There is some potential for the TNSP to engage in discriminatory conduct impacting competition in contestable transmission connections when providing category 2, 3 or 4 of negotiated transmission services as no renewable generation project can be connected without the TNSP providing these services on an exclusive basis.

In relation to category 1 of the negotiated transmission services, there is a potential conflict of interest in the TNSP's role in leasing spare capacity in its battery and its role in approving and connecting other grid-scale batteries. This creates a potential risk that the TNSP could delay connecting grid scale batteries to the grid to enable it to negotiate a better price for the capacity it leases.

Staff involved in leasing arrangements for the TNSP's spare capacity should not be permitted to be involved in the connection of other developer's grid scale batteries to the grid. Information about battery projects in the pipeline is commercially sensitive information and should not be disclosed to any third party, particularly lessees of the spare capacity, as they are potential competitors of the grid scale battery operators. Ring-fencing has a role in ensuring that relevant protections are implemented.

We acknowledge that, following consultation, the AER may decide to impose different obligations for category 1 of the negotiated transmission services under the Ring-fencing Guideline than it imposes for category 2, 3 and 4 of the negotiated transmission services.

Requirements of good economic regulation

As there is the potential for TNSP to engage in discriminatory conduct in providing all four categories of negotiated transmission services, good economic regulation would require that all negotiated transmission services be included in the Ring-fencing Guideline.

The AER at page 11 of its Options Paper states:

"in principle, all services that are provided on an exclusive basis by a single entity should be covered by the ring-fencing framework, where there is a risk of cross subsidisation or discriminatory behaviour".

Focussing on harms from category 2 negotiated transmission service is too narrow

We are concerned that the AEMC has made the "preferential" rule change permitting carve outs of specific negotiated transmission services as it is focussing too narrowly on category 2 negotiated transmission services.

The AEMC states at page 3 of its draft Determination that the focus of this rule change project is on connection services, i.e. category 2 of the definition of negotiated transmission services.

However, it is clear that the AER, in making the rule change request, is broadly looking at the need to ring-fence "all non-contestable components of a transmission connection": see page 11 of the AER Options Paper. For this reason, the AER requested all negotiated transmission services to be ring-fenced.

For example, at page 17 and 19 of its Option Paper, in relation to category 3 negotiated transmission services, the AER refers to:

- Australian Energy Operations concerns about the potential advantages a TNSP could afford to an affiliate in terms of the timing and costs of the "cut-in" to the shared network, or

through the price, terms and conditions associated with the ongoing maintenance of assets the TNSP is required to control; and

- Incentia’s identified potential harms that TNSPs may overstate the cost of maintaining connections that they become responsible for (IUSAs) and could define the Functional Specifications of an IUSA in a manner that imposed additional requirements on competitors or otherwise discriminate in its own favour.

As noted above, cut-in services and operation and maintenance of third party owned IUSA assets are category 3 negotiated transmission services.

Industry members have expressed concern that the TNSP can hold up the completion of a project in failing to provide cut-in services in a timely manner (even through these services represent only a relatively small part of the costs of the entire project).

2. Waiver framework under the Ring-fencing Guideline is a preferable framework for dealing with TNSP concerns without hindering competition

The AEMC at page 23 of the draft Determination notes that:

“TNSPs could apply for a waiver from the AER to exempt them from the application of obligations under the Guidelines for specific categories of negotiated services. However, we understand that the process for applying for waivers is time-consuming and administratively burdensome. Providing the AER with the ability to carve out specific categories of negotiated services from the application of obligations from the outset would avoid the need for an additional waiver process.”

We consider that the waiver framework under the Ring-fencing Guideline is preferable for dealing with TNSP concerns than the AEMC’s proposed rule change which permits unqualified carve outs from the Ring-fencing Guideline. In particular:

- Waivers that are limited in time and scope are only permitted.

The current Ring-fencing Guideline does not permit waivers from the obligation:

- not to discriminate
- restricting information access and disclosure
- to comply and report on compliance
- to establish and maintain separate accounts
- in respect of cost allocation and attribution
- to respond to complaints about adherence to the Guideline.

Waivers are only permitted in respect of obligations relating to legal separation, staff separation, and constraints on Service Providers under the Ring-fencing Guideline.

It is preferable for the AER to have the ability to reassess a waiver’s impact on competition within a defined time frame in a market undergoing rapid technological and structural change.

- AER retains the regulatory tools to respond flexibly to evolving market conditions (including risks of discriminatory conduct) and can revoke the waiver upon giving 40 calendar days’ notice. The AER can take into account oral stakeholder feedback.

In comparison, the AER could only “re-include” a category of negotiated transmission service once carved out from the Ring-fencing Guideline (under the AEMC’s proposed rule change), for example, so as to respond to discriminatory conduct, after formal consultation which takes at least 110 business days and the AER can only invite and consider written submissions (which developers may be reluctant to provide): see transmission consultation procedure under clause 6A.20 of the NER.

This ability to consider oral feedback under the waiver process, rather than written feedback only under the transmission consultation procedure, is absolutely central to effective monopoly regulation. Network monopolies hold all the power when it comes to connection negotiations with generators. It follows that developers will be extremely unlikely to publicly raise concerns regarding any discriminatory conduct for fear of negatively impacting current and future connections.

The AEMC must factor in this power imbalance when making its final decision. Good economic regulatory practice means policy positions should be set to a default that counters inherent power imbalances. A framework based around exemption (ie, the waiver framework) is therefore more consistent with good economic regulatory practice.

- The waiver framework allows the specific concerns and circumstances of TNSPs to be taken into account.

In assessing a waiver application under the current Ring-fencing Guideline, AER must fully consider the TNSP’s costs, relative size, the specific controls which the TNSP proposes to implement, the risk of discriminatory conduct or cross subsidisation in light of the proposed controls, the National Electricity Objectives and whether the benefits to consumers from increased competition would be outweighed by the cost of the TNSP complying with the obligation. The waiver regime will therefore allow the AER to critically consider whether the TNSP’s costs of complying with specific obligations can be minimised, taking account the circumstances and proposed controls, provided competition in nascent markets is not hindered.

3. Uncertainty as to the scope of the Ring-fencing Guideline is likely to hinder competition and result in delayed projects delivered at higher costs

The AER has 12 months to consult on, and update, the Ring-fencing Guideline. Permitting the AER to carve out specific categories of negotiated transmission services creates uncertainty as to the scope of the Ring-fencing Guideline during this period. This is likely to:

- hinder the development of a nascent market for contestable transmission connections
- result in renewable generation projects being delivered more slowly and at a higher cost without the certainty of a robust ring-fencing framework to deter discriminatory conduct
- increased risk premiums for projects as investors and developers will not have confidence that developers will be able to connect to the grid at an efficient cost without undue delays without a robust ring-fencing framework
- higher consumer costs (from developers passing on higher connection costs and from delays in the availability of zero cost generation lowering wholesale costs).

We are in a critical period in the clean energy transition. We need to support more renewable generation connecting to the grid more quickly if we are to meet the target of 80 per cent renewable by 2030 and at an efficient cost (as connection costs can be ten per cent of overall project costs).

In making its “preferential” rule change, the AEMC has given considerable focus to the increased administrative costs of TNSPs in complying with, and seeking waivers to, obligations under the Ring-fencing Guideline (if any). However, the potential harm to competition, and the resulting higher energy costs for consumers, from not having a robust ring-fencing framework planned or in place would far outweigh any increased administrative costs to TNSPs.

We note ring-fencing all negotiated transmission services may not result in a material increase in the TNSP’s costs of compliance. This is because ring-fencing obligations to a large extent already overlap with, and are required, by TNSP’s obligations under Chapter 5 of the NER and because of incentive regulation.

4. Ring-fencing all negotiated transmission services would improve competition and promote National Electricity Objectives

The AER recognised the potential for a robust ring-fencing framework to improve competition:

Even if few ring-fencing measures were ultimately imposed on the provision of negotiated transmission services under the Transmission Ring-fencing Guideline, we consider there would still be merit in amending the rules. Simply having the above tools in the regulatory toolkit would help curb potential discriminatory behaviour by TNSPs and promote competition in contestable connections services. Knowing that more costly measures could be imposed would provide an incentive for TNSPs to avoid operating in a way that could be viewed as discriminatory. pages 28-29 Rule Change Request.

Ring-fencing can incentivise compliance with regulatory obligations

The AER in its Rule Change Request Submission (at page 27- 28) outlines obligations which could be adopted under a revised Ring-fencing Guideline. This includes requiring additional reporting on TNSP’s compliance with obligations under Chapter 5 of the NER and annually requiring TNSP to provide connection information, including connections tendered for, connections proceeding with a non-incumbent provider, and connection timeframes and costs.

We support the adoption of a robust ring-fencing framework with monitoring obligations and recommend that the AER, when consulting on the Ring-fencing Guideline, seek feedback from industry on their concerns and the connection information that should be sought.

Ring-fencing can incentivise compliance with regulatory obligations as demonstrated by the example below.

We have heard concerns from CEC members about the lack of transparency in the costs for operation and maintenance of IUSAs, which makes it difficult to negotiate a reduction in costs. Seeking additional information on whether indicative prices for non-contestable services are negotiated could shed light on whether there is compliance with:

- clause 5.2A.5(c) of the NER (which requires a TNSP and a Connection Applicant to provide information (including commercial information) reasonably required by the other party that would facilitate *effective negotiation* for the provision of a negotiated transmission service in a timely manner); and
- clause 5.2A.6(b) of the NER (which requires a TNSP to identify and demonstrate to a Connection Applicant that the charges for providing a negotiated transmission service reflect its reasonable costs).

We consider that process of reporting on whether costs have been negotiated is likely to incentivise the TNSP to provide greater transparency in its pricing to ensure compliance with the NER.

If prices are not being negotiated, the AER has a range of tools, including issuing a compliance letter providing its expectations in breaking down costs and outlining assumptions made.

More generally, we note that the obligation not to discriminate overlaps with and reinforces the requirements of Chapter 5 of the NER and that Tier 1 civil penalties introduced for breaches of the Transmission Ring-fencing Guideline would also provide a strong motivator for complying with regulatory obligations.

It is essential that reporting covers all stages of the connection approval process, in particular, the stages after the connection application has been lodged, when the TNSP and its affiliates have been made aware that they are not providing the contestable work.

Potential conflicts of interest

The Ring-fencing Guideline can also support competition by permitting the monitoring where there is a potential conflict interest in the TNSP roles. For example:

- TNSP are paid system strength charges in respect of infrastructure it has built to deal with future projects' impact on system strength. TNSP is incentivised for developers to pay this charge, otherwise the costs of under-utilised infrastructure will be borne by consumers. At the same time a developer may elect to self-remediate rather than pay the system strength charge. Despite the conflict of interest, TNSPs have control over a developer's self-remediation scheme for addressing system strength impacts and is responsible for assessing and approving the modelling the developer is required to submit demonstrating that the self-remediation addresses the project's system strength impacts.
- TNSPs build their own batteries but also approve others. There is a risk that TNSP could get more favourable treatment during the process to connect their batteries to the transmission system, than other projects (including grid-scale batteries), for example, in the timing of connection or in assessment of GPS compliance. This may not be intentional but through 'unconscious bias' in the treatment of projects.

National Electricity Objectives

For the reasons elaborated upon above, we consider the AER's requested rule change (in so far as it would include all negotiated transmission services under the Ring-fencing Guideline) is more likely to speed up the connection of renewable generation to the grid at lower cost and thereby promote the National Electricity Objectives (reducing the cost of electricity to consumers (with more zero cost generation), promoting reliability (with more batteries coming online) and reducing emissions).

As always, Clean Energy Council welcomes further engagement with the AEMC on this reform. Further queries can be directed to Diane Staats on dstaats@cleanenergycouncil.org.au.

Kind regards

Christiaan Zuur
Director, Energy Transformation