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3 March 2023

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## Consultation on the structure of participant fees for the NEM 2025 reform program

Energy Networks Australia (ENA) welcomes the opportunity to provide input to AEMO's Consultation Paper and Engagement Plan on the structure of participant fees for the NEM 2025 reform program declared NEM project.

ENA represents Australia's electricity transmission and distribution and gas distribution networks. Our members provide more than 16 million electricity and gas connections to almost every home and business across Australia.

### Key messages

It is critical that AEMO's declared NEM2025 fee structure is designed in a way that promotes the long-term interests of consumers of electricity. To achieve this it is important to allocate costs and risks to the parties best placed to manage them, while balancing the principles AEMO is required to consider in setting fee structures.

To summarise ENA's response, we support:

- » further efforts from AEMO to contain its declared NEM project and other costs.
- » using the existing fee categories to recover declared NEM project costs until the next general fee determination takes effect from mid-2026, noting:
  - Declared NEM project fees should be allocated within existing fee categories in a manner that is consistent with the NEO and the principle of allocation based on the involvement of the participant. This requires weighting the allocation of fees to the causers and beneficiaries of the costs. Only a small portion of costs should be allocated to core NEM fees.
  - This approach is simpler and avoids discriminating against participant classes based on their ability to recover costs. It is also more efficient and cost effective for customers because it does not allocate costs to parties that are not able to manage them.
- » changes to the fee structures in the next general fee determination so that, for the long term, they are more closely aligned with the NEO and the relevant fee principles. This could include considering whether some fees should shift away from a c/kWh metric if this means that causers of the costs pay less. Significant collaboration with industry is required to ensure any changes are enduring and fit for purpose.
- » fees being charged from the 'go live' dates for projects and for the first relevant declared NEM reform project.

- » AEMO's proposed engagement plan, including the creation of an industry working group to explore different approaches to post-2025 declared NEM project fee structures and to help develop participant fee structures heading into the general fee determination.

## Electricity networks have varying abilities to recover the cost of AEMO participant fees

Distribution network service providers (DNSPs) and transmission network service providers (TNSPs) are regulated to ensure their costs to deliver network services are prudent and efficient. This means they forecast their operational expenditure and capital expenditure on a five-yearly cycle, as approved by the Australian Energy Regulator (AER). The regulatory periods for networks business' start in different years so that their cycles are staggered.

Costs that are not forecasted and included in a revenue determination cannot be recovered except under specific circumstances where:

- » they have been nominated in a pass-through category, and
- » the amount of the variance in costs is greater than one per cent of the business' maximum allowable revenue for the relevant year.

DNSPs and TNSPs are in materially different positions with respect to their ability to recover AEMO fee costs. The reasons for this are historical:

- » TNSPs were allocated core NEM fee costs in the most recent fee determination, with cost recovery delayed for TNSPs until mid-2023. The delay was to allow TNSPs to pursue a rule change request that would allow them to pass those costs on to customers. The AEMC determined that TNSPs should be allowed to adjust their revenue to recover those costs from customers during a transition period, after which the costs would need to be forecasted and recovered through incentive regulation.
- » DNSPs were not allocated fees in the most recent fee determination and they generally do not have nominated pass through categories that include this type of cost within scope. Even if AEMO fees were nominated as potential pass-through events, it is unlikely that in any given year the costs would meet the materiality threshold for recovery. It is also uncertain whether an allocation of fees would be considered a regulatory change event, triggering the ability to recover the costs.

The rule change that would allow TNSPs to recover the costs of new AEMO participant fees, including a potential new fee category for post-2025 declared NEM project fees, does not apply to DNSPs. An allocation of fees to them could deny them the opportunity to recover their efficient costs as required under the revenue and pricing principles in the National Electricity Law.

The extent to which TNSPs and DNSPs are allocated costs in the future and the ability for them to recover those costs will also depend on how stable and forecastable they are. The traditional approach taken by AEMO of setting fees that apportion a percentage of costs to a participant class, with actual costs varying year on year, will not be sufficient to allow TNSPs and DNSPs to recover their fee costs over the long term. This exposes them to forecasting risks and it is imperative that there is cost certainty. TNSPs and DNSPs do not have control over AEMO's transformation project costs and, if they were allocated these costs, would be taking risks for costs that they have no control over. Greater predictability and transparency of future costs are important to provide them the opportunity to recover their costs.

Further efforts are also required from AEMO to contain its costs. In the absence of the economic regulation of AEMO, there is limited incentive on AEMO to stay within its forecasts of its costs. ENA suggests that more transparency tracking AEMO's forecast and actual costs is required to help incentivise cost control.

### AEMO should use existing fee categories to recover declared NEM project costs

AEMO should use existing fee categories to recover declared NEM project costs until the next general fee determination takes effect from mid-2026. This approach is preferable in the short term because it better meets the NEO because it is more efficient and cost effective for customers. It also better meets the relevant principles of simplicity, non-discrimination and cost recovery based on participant involvement.

We disagree with AEMO's assessment of the extent to which the two options meet the relevant principles in Table 2 of the consultation paper. ENA's assessment of the options against the relevant principles is set out at a high level in the table below, with detailed reasons further below. The traffic light colour key is the same as used in AEMO's table.

Option	Simplicity	Involvement	Discriminate	Recovery	NEO
Use existing fee structures	Green	Yellow	Yellow	Green	Green
Create a new NEM 2025 fee	Yellow	Yellow	Red	Green	Yellow

#### *Simplicity*

Using existing fee categories is administratively simple for AEMO and the industry to implement.

The alternative approach of designing a bespoke fee structure requires the rapid development of new ways to apportion fees and metrics for recovering costs. As noted below, we agree fee structures require reform in the long-term. We also consider that such reform should be achieved through sufficient consultation and testing to make sure the arrangements are workable and fit for purpose. This is not achievable in the timeframes required to develop a new fee structure for declared NEM project costs given the level of uncertainty and complexity.

#### *Reflective of involvement*

Neither option can apportion costs perfectly with respect to the level of *involvement* of participants. The question is, which option will be better at apportioning based on involvement?

The concept of involvement is broad. It encompasses interactions with AEMO, use of AEMO outputs, receipt of AEMO outputs, and benefitting from AEMO outputs. It also extends to the *causes* of AEMO's revenue requirements. The concept of involvement incorporates aspects of 'user pays', 'beneficiary pays', and 'causer pays' cost recovery approaches. AEMO can exercise discretion in how it chooses to allocate costs to participants based on this principle. ENA considers that AEMO should exercise its discretion in interpreting this principle in a manner that best promotes the NEO. More detail on assessment against the NEO is provided below.

Given the above, both options can meet the principle of reflective of involvement. It is preferable however to use existing fee structures for the time being as it is too early to observe what the detailed design of many individual post-2025 reforms will be. It is therefore too early to determine the level of involvement of different participants. Indeed, most reforms are still with policy makers for consideration and detailed design before rules are made (or not made) by the AEMC or Ministers.

While using existing fee structures would not perfectly align with the level of involvement of participants, the difference would be marginal at best between that option and creating a new fee structure based on the limited information currently available. AEMO should be able to allocate declared NEM project costs to existing participant fee categories in a manner that broadly reflects the level of involvement of participants and is consistent with the other principles. Noting our comments further below in relation to non-discrimination and application of the NEO, we consider this is likely to be weighted towards causers and beneficiaries of AEMOs costs (e.g. wholesale market participants and market customers). AEMO could use, for example, the Electricity Retail Markets fee and the DER program fee.

The consultation paper suggests that Participant Impact Assessments (PIAs) conducted through the Reform Delivery Committee (RDC) could be used to inform AEMO of the level of involvement of participants. This approach is unlikely to produce efficient outcomes because it weights towards a 'user pays' approach, not a causer or beneficiary pays approach. As noted above, it is still unclear who the providers of inputs to AEMO and users outputs from AEMO will be. However, DNSPs and TNSPs are likely to be increasingly interacting with AEMO to provide them with inputs that will help with the operation of the wholesale market. The causers of the increased interactions and the beneficiaries are wholesale market participants and customers. DNSPs and TNSPs have little ability to control or manage their level of interaction with AEMO, nor should they have an incentive to reduce their level of interaction.

### *Non discrimination*

It is likely that the creation of a new participant fee category for the declared NEM project would discriminate against some participant classes.

AEMO describes the term *discriminate* as including both:

- » the treatment of people or categories of people differently or unequally, or
- » the treatment of people or categories of people who are different in a material manner, in the same or identical fashion.

We agree with this characterisation when interpreting the principle that AEMO should not discriminate between participants or participant classes in its fee determinations, including in setting the fee structure for the declared NEM project.

Our view that a new fee structure for the declared NEM project would not meet the non-discrimination principle assumes that the new fee structure would likely allocate a proportion of fees to DNSPs. If that is the case, the fee structure would discriminate against DNSPs by not allowing them the same opportunity to recover their costs as other participant classes. DNSPs would not be able to recover their costs, while:

- » participants in competitive markets, such as generators and retailers, would be able to recover these costs by adjusting their bids or retail prices respectively (which at times may be constrained by hedging or retail contracts, but usually not materially so), and

- » TNSPs would be able to recover their costs due to the transitional arrangements in the recent *Recovering the cost of AEMO's participant fees* rule change process.

Allocating declared NEM project fees to DNSPs would be an example of treating participants that are materially different in a manner that is identical. It would discriminate between the participant classes in the material outcome that some are able to recover their costs and others are not. This would breach the principle of non-discrimination and accordingly we have marked this in red in the table above.

It could be possible to create a new category of participant fees to recover the declared NEM project costs that does not allocate fees to DNSPs. This would be consistent with the principle of non-discrimination, but the fee allocation outcomes would likely then be no different to simply allocating costs to existing fee categories, taking care to broadly allocate them in a manner consistent with the principle of *involvement*.

### *Recovery of AEMO's budgeted requirements*

We agree with AEMO's assessment that both options would equally meet the principle that AEMO should recover its budgeted requirements.

### *Consistency with the NEO*

AEMO rightly notes that the heart of the NEO is the promotion of efficient outcomes that are in the long-term interests of consumers. Many principles of good regulatory design to support efficient outcomes are encapsulated in the specific fee principles discussed above, such as the principles of simplicity and non-discrimination. Others, such as the principle of allocation based on involvement, should be guided by established regulatory principles that promote efficient outcomes as envisaged by the NEO.

An important regulatory economics principle that supports efficient outcomes is that costs and risks should be borne by those best able to manage them, or else should be passed on directly to the parties who ultimately pay them (i.e. the customer). With respect to the structure of AEMO's fees and to the allocation of fees for the declared NEM project, the allocation of costs to parties unable to manage them or pass them on will not result in efficient outcomes. Unmanageable and unrecoverable costs create risks that can increase the cost of delivering services, or reduce the services delivered. Allocation of these costs to DNSPs would likely create risks and costs that cannot be managed, which over the long term would be passed on to consumers as higher prices or reduced services.

Furthermore, causer and beneficiary pays approaches should be preferred for recovery of AEMO's costs because this promotes more efficient behaviour. The causers and the beneficiaries of AEMO's costs are varied, for example:

- » all customers are beneficiaries of AEMO's costs, while customers that are investing in solar PV, home batteries, electric vehicles and other controllable or significant demand side devices are causing an increase in AEMO's costs, and
- » wholesale market participants both procuring greater portions of renewable generation and new renewable generators and large-scale storage entering the market are causing a shift in wholesale market dynamics that is a significant driver of AEMO's costs, including requiring significant reform to reliability and security frameworks.

Allocation of costs to causers and beneficiaries is a more cost reflective approach to cost recovery, which is likely to result in more efficient overall outcomes. AEMO should take this into

account when either allocating costs to existing fee classes or developing the structure of a new fee structure for the declared NEM project. Allocation of costs to users, or producers of data for AEMO's use, risks creating incentives for participants to share less data and information with AEMO.

## Fee structure reform is required for the 2026 general fee determination

While we note above that the declared NEM project fees should be recovered through existing fee structures, we also consider that the current fee structures will require updating in the next general fee determination. At this time more information will be available on the level of involvement of different participant classes in AEMO's costs to deliver the transition.

In reforming AEMO's fee structures it will be important to do so in a manner that best promotes the efficient outcomes envisaged under the NEO. We consider the application of the NEO in greater detail in the section above, including the appropriate allocation of costs and risks. With respect to the recovery of AEMO's costs, we conclude that this should be weighted toward recovery from causers and beneficiaries.

TNSPs and DNSPs are not the major causers or beneficiaries of AEMO's costs. Furthermore, they have little influence over AEMO's costs, particularly those that are driven by the need to transform the market and energy system to enable the transition to net zero emissions. Future approaches to cost recovery will also need to recognise the difference between the ability of networks to recover costs and other participants. Options to change the approach to fee structures and cost recovery could include:

- » recognising the difference between business-as-usual costs that are more stable, and transformation or change project costs, that can be more variable
- » developing cost-smoothing mechanisms for participants that do not have an equal ability to recover changes in costs, for example:
  - providing fixed cost paths for TNSPs and DNSPs that align with their regulatory periods (with the variable balance paid by other participant classes better able to manage cost variability), or
  - providing better forecasting of costs to reduce the risk of incorporating AEMO fee costs in regulatory proposals.
- » changing the metrics for cost recovery (for example to a \$ per customer approach) to recognise that the causers of some of AEMO costs, such as those households with solar PV and batteries, pay less under the current c/kWh charging approach.

Such approaches would also be consistent with the fee principle of non-discrimination because it would be treating participants with different characteristics differently, and in doing so to give them the same opportunity to effectively recover their costs.

The AEMC considered in its recent decision on TNSPs' recovery of AEMO participant fees that it is important that TNSPs have an incentive to influence AEMO's costs. We agree that it is important to maintain these incentives to reduce AEMO's costs and should work towards this outcome. These incentives are not promoted where TNSPs and DNSPs are managing costs and risks that they are unable to influence or control. It will be important in any new fee determination to effectively separate the matters that TNSPs and DNSPs are able to effectively influence, and those that they are not able to influence. This approach will create a much clearer incentive for



TNSPs and DNSPs to influence AEMO's costs and would avoid the misallocation of costs and risks. This would produce more efficient outcomes in the long term interests of consumers.

We would welcome constructive engagement with AEMO to develop approaches to the recovery of AEMO's costs in the next general fee determination that seek to achieve these outcomes.

### Cost recovery period

We support AEMO's proposed approach of:

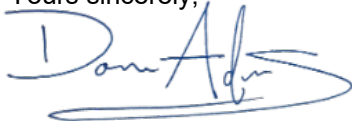
- recovering project costs for individual reforms from the 'go-live-date' for the reform, and
- beginning the cost recovery period for the overall declared NEM project from the go-live-date of the first relevant reform.

### Engagement plan

We support the proposed engagement approach and plan. We consider it would be helpful to create a NEM 2025 participant fee consultative committee to workshop the fee structure, as well as to leverage existing committees and forums to engage with stakeholders. We also advise that the fee committee should continue to work towards the next general fee determination.

If you have any questions or would like to discuss specific topics further, please do not hesitate to contact me - [dadams@energynetworks.com.au](mailto:dadams@energynetworks.com.au).

Yours sincerely,



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