Unlocking the value of community batteries

Response to AER Ring-fencing Class Waiver Initiation Notice

January 2023

Energy Networks Australia

Contents

Contents		2
Key messages		3
1	Overview	3
2	Realising value stacking	4
3	Class waiver	6
Appendix A I Summary of key positions		11

Energy Networks Australia www.energynetworks.com.au
Unit 5, Level 12, 385 Bourke Street Melbourne VIC 3000
P: +61 3 9103 0400 **E:** info@energynetworks.com.au
Energy Networks Association T/A Energy Networks Australia
ABN: 75 106 735 406

Key messages

- To meet consumer and community support and demand for network-led roll-out of technologies such as community batteries, **ENA strongly supports the development of a class waiver** that allows DNSPs to lease battery capacity to third parties under government projects.
- Realising the **value-stacking of batteries maximises the services and benefits that a community battery can provide to the electricity grid, and therefore, to electricity customers**. It reduces the cost to all customers of DNSPs providing distribution services and would foster the energy storage market and support retail competition.
- Implementation of a class waiver, however, does not imply that all DNSPs will seek or be awarded government funding for these community batteries, which is instead subject to a separate rigorous independent process.
- ENA has **proposed amendments to the final class waiver**, including:
  - a simplified **cost allocation approach directly linked to customer benefits**,
  - a **broadening of the waiver to also capture jurisdictional government community battery programs**, ensuring that government funding for community batteries, irrespective of whether it is led by the Commonwealth or jurisdictional governments, is treated on a consistent ring-fencing basis under the same class waiver, and
  - fit for purpose **reporting requirements that provide the AER and stakeholders with the required transparency** without imposing significant costs on electricity customers.

1 Overview

Energy Networks Australia (**ENA**) appreciates the opportunity to respond to the Australian Energy Regulator's (**AER**) ring-fencing class waiver initiation notice for the Commonwealth Government's Community Batteries for Household Solar Program (**Commonwealth Program**).[1]

ENA is the national industry body representing 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.

To meet consumer and community support and demand for network-led roll-out of technologies such as community batteries, ENA strongly supports the development of a class waiver that allows distribution network service providers (**DNSP**) to lease battery capacity to third parties under government projects.

Realising the value-stacking of batteries maximises the services and benefits that a community battery can provide to the electricity grid, and therefore, to electricity customers. It reduces the cost to all customers of DNSPs providing distribution services and would foster the energy storage market and support retail competition.

[1] AER, Ring-fencing class waiver initiation notice – Community Batteries for Household Solar Program, December 2022.

ENA has proposed amendments to the final class waiver, including a simplified cost allocation approach which ensures that:

- the costs to electricity customers do not exceed the benefits that they receive from the installation of community batteries, and
- for those assets partially funded by electricity customers, customers share in benefits that the DNSP may receive from leasing the battery capacity to a third party.

This approach meets the AER's key policy intent to ensure that:

- costs to regulated electricity customers do not exceed the benefits, and
- non-network services are not cross-subsidised through the provision of network services.

Additional reporting requirements will also provide the AER and stakeholders with transparency over the use of the battery and the revenue that the DNSP receives from leasing battery capacity to third parties.

Importantly, however, implementation of a class waiver does not automatically provide DNSPs with exclusivity over service provision, nor does it imply that all DNSPs will seek or be awarded any Commonwealth funding for community batteries, which is instead subject to a separate rigorous independent process. Rather, it enables the potential for more service delivery options within the tight constraints of the regulatory framework.

2 Realising value stacking

Australia's energy system is undergoing a significant transition, moving away from large, centralised coal and gas generation to smaller scale dispersed generation that is increasingly renewable generation.

Distributors have an important role to play in facilitating the customer-driven transition to distributed energy, which is a significant part of Australia's move to a low carbon future. The practical role that DNSPs will play in the roll-out of community battery projects under the Commonwealth Program is recognised in the AER's class waiver initiation notice and the Commonwealth's recently released Grant Opportunity Guidelines, developed to deliver the program.[2]

ENA strongly supports the development of a class waiver that allows DNSPs to lease battery capacity to third parties under government projects. Without the class waiver, DNSPs will be unable to partner with third parties to realise the full battery value stack, which will limit the services and benefits that the community battery can provide to the electricity grid, and therefore, to electricity customers.

A class waiver will, for example, allow a smaller third-party retailer that may not have the resources or investment capital to rollout a community battery directly to instead partner with a DNSP to provide energy storage services to its customers, thereby supporting retail competition.

Importantly, implementation of a class waiver does not automatically provide DNSPs with exclusivity over service provision, nor does it imply that all DNSPs will seek or be awarded any Commonwealth funding for community batteries, which is instead subject to a separate rigorous independent process. Rather, it

[2] Department of Climate Change, Energy, the Environment and Water, Grant Opportunity Guidelines: Community Batteries for Household Solar Program – Delivery of Election Commitments Stream 1, December 2022.

enables the potential for more service delivery options within the tight constraints of the regulatory framework.

The AER introduced the class waiver provision to improve the practicality of its waiver process and enable a more efficient solution.[3] A reliance instead on the AER's individual streamlined waiver process will unnecessarily slow down the roll out of the Commonwealth Program, introduce additional uncertainty, and require a material increase in resources and costs to develop and assess each individual battery waiver proposal.

2.1 Strong consumer safeguards

The Electricity Distribution Ring-fencing Guideline (**Distribution Guideline**) was updated in 2021 and places a number of obligations on DNSPs to address concerns around cross-subsidisation and discriminatory behaviour.

The Distribution Guideline[4]:

- prevents DNSPs from discriminating in contestable markets in favour of themselves or affiliated entities,
- ensures DNSPs handle ring-fenced information appropriately,
- requires a DNSP to adhere to the Cost Allocation Principles in the National Electricity Rules and its AER-approved Cost Allocation Method as a safeguard against cross-subsidisation, and
- requires DNSPs to prepare and submit annual ring-fencing compliance reports to the AER that include an assessment of compliance undertaken by a qualified independent party. These reports are available publicly on the AER's website, and the AER also publishes an annual ring-fencing compliance report.

In addition, ring-fencing waivers include a number of additional conditions and criteria that a DNSP must meet in order to comply.

The existing regulatory framework also includes obligations on DNSPs such as:

- information disclosure obligations through the Distribution Annual Planning Report and network opportunity maps, which requires the publication of information to all parties on emerging network issues and constraints, and
- obligations to connect customers in the National Energy Retail Law and associated connection timeframes.

[3] AER, Electricity Distribution Ring-fencing Guideline: Explanatory Statement – Version 3, November 2021.

[4] AER, Electricity Distribution Ring-fencing Guideline: Version 3, November 2021.

3 Class waiver

The sections below address the detailed requirements of the class waiver and, in particular, proposes a simplified cost allocation proposal for Class B projects which ensures that:

- the costs to electricity customers do not exceed the benefits that they receive from the installation of community batteries, and
- for those assets partially funded by electricity customers, customers then share in any benefits that the DNSP may receive from leasing the battery capacity to a third party.

The approach meets the AER's key policy intent to ensure that:

- costs to regulated electricity customers do not exceed the benefits, and
- non-network services are not cross-subsidised through the provision of network services.

3.1 Cost allocation approach

The initiation notice splits the class waiver into two classes:

- **Class A projects** that have no allocation to a DNSP's Regulatory Asset Base (**RAB**), and
- **Class B projects** that have an allocation to a DNSP's RAB, and therefore a corresponding cost allocation approach.

ENA supports the AER's proposed Class A but does not support the AER's Class B draft cost allocation approach due to its potential complexity in its application, including that:

- the draft approach requires forecasting of unregulated revenues in all circumstances, which may have a high degree of uncertainty given the relatively undeveloped community battery market and uncertainty in energy markets coupled with the expected life of the asset and therefore required time period of the forecast, and
- the draft approach requires the DNSP to provide customers with the forecast lease benefit (i.e., unregulated revenue that the DNSP expects to receive from leasing the battery capacity to a third party) upfront. This imposes a potential disadvantage to customers if the actual lease revenue obtained over the life of the asset is greater than what is forecast, and additional risk on the DNSP should that funding not materialise.

3.1.1 Class B projects – ENA's customer benefits model for cost allocation

ENA has therefore proposed an alternative simplified customer benefits approach to cost allocation for Class B projects included in **Box 1** below.

Box 1: Proposed customer benefits approach (Class B projects – cost allocation)

The RAB allocation will be no greater than the quantified regulated customer benefits with a maximum ceiling that the RAB allocation cannot be more than the residual cost of the asset, where:

- the regulated customer benefit is equal to the quantified benefit derived from the deployment of the asset for *direct control services*, calculated with reference to the AER's DER Integration Expenditure Guidance Note[5] and in particular, the benefit streams identified therein.
- the residual cost of the asset is equal to the cost of the asset net of any government funding received by the DNSP.
- the DNSP must develop a revenue sharing arrangement to ensure that regulated electricity customers share in any benefits accrued to the DNSP from the deployment of the asset for *other distribution service* and *other services* over its economic life – for example, a proportionate share in any revenue that the DNSP receives from leasing battery capacity to third parties.
- a DNSP's revenue sharing arrangement should ensure that regulated electricity customers share in no less than 10 per cent (as the minimum floor) of any benefits accrued to the DNSP from the deployment of the asset for *other distribution service* and *other services* over its economic life[6], weighted by the proportion of cost allocated to the RAB (i.e., the proportion of the asset that regulated electricity customers have funded). Importantly, no materiality threshold can be applied to this revenue sharing arrangement.

In applying this customer benefits approach, ENA understands that:

- any government funding is treated as a zero-dollar capital contribution to the RAB,
- when quantifying the regulated customer benefits, the 'other benefits' value stream in the AER's DER Integration Expenditure Guidance Note may include items such as innovation funding, where justified, and
- the Demand Management Innovation Allowance (**DMIA**), if approved, may be used for community battery projects given the novel and innovative nature of projects.

This approach ensures that:

- any capital expenditure that is allocated to the RAB, and therefore funded by regulated electricity customers, reflects the benefits that these customers will receive from the community battery. Importantly, an additional ceiling is also applied so that this amount is capped at the cost of the asset minus the government funding that the DNSP receives, even in circumstances where the quantified customer benefits are higher.
- when regulated electricity customers fund a portion of the community battery via the RAB, they are guaranteed a share in any revenue that accrues to the DNSP from leasing battery capacity to third parties. Importantly, under the proposed revenue sharing, if additional unregulated benefit streams are realised, or the value of the leasing revenue is increased due to potential further market development over the life of the asset, regulated electricity customers will benefit (compared with an approach that depends on forecast revenues).

[5] AER, DER Integration Expenditure Guidance Note, June 2022.

[6] For example, any revenue that the DNSP receives from leasing battery capacity to third parties.

The class waiver will also require a DNSP to adhere to the Cost Allocation Principles in the National Electricity Rules and its AER-approved Cost Allocation Method.

In addition, to receive any government funding for a community battery project in the first place, applicants will be required to demonstrate value for money for consumers. For example, the Guidelines issued by the Department of Climate Change, Energy, the Environment and Water (**DCCEEW**) require applicants to demonstrate how the proposed project will put downward pressure on household electricity costs, and in order to be competitive, outline the proposed financial arrangements for the operation of the community battery including costs and revenue.

3.2 Government programs

ENA supports the AER's draft position that the class waiver should apply to Class A and Class B projects administered by both DCCEEW and the Australian Renewable Energy Agency (**ARENA**) under the Commonwealth Program.

However, in acknowledgment of the substantial focus on community batteries at a jurisdictional level, there is an increasing need for the class waiver to also capture jurisdictional government community battery programs. Examples of these type of jurisdictional government programs include, but should not be limited to, the

- Victorian Government Neighbourhood Battery Initiative, with funding for additional neighbourhood batteries recently announced,
- Queensland Government Energy and Jobs Plan, which includes funding for community batteries, and
- ACT Government Big Canberra Battery, with Stream 3 for the rollout of neighbourhood scale batteries.[7]

The inclusion of both Commonwealth and State/Territory community battery programs will ensure that government funding for community batteries, irrespective of whether it is led by the Commonwealth or jurisdictional governments, is treated on a consistent ring-fencing basis under the same class waiver.

3.3 Waived obligations and time period

To enable value-stacking of the battery and facilitate DNSPs leasing battery capacity to third parties, ENA supports the AER's proposed ring-fencing obligations to be waived for both Class A and Class B projects:

- clause 3.1 [Legal separation],
- clause 4.2.1 [Functional separation – Physical separation / co-location], and
- clause 4.2.2 [Functional separation – Staff sharing].

[7] Victoria: https://www.energy.vic.gov.au/grants/neighbourhood-battery-initiative and https://www.premier.vic.gov.au/powering-potential-neighbourhood-batteries [accessed 12 January 2022].

Queensland: https://www.epw.qld.gov.au/__data/assets/pdf_file/0031/32989/queensland-energy-and-jobs-plan-overview.pdf [accessed 12 January 2022].

ACT: https://www.climatechoices.act.gov.au/policy-programs/big-canberra-battery/get-involved-in-the-big-canberra-battery-project [accessed 12 January 2022].

For critical infrastructure security reasons, and to ensure an efficient delivery of these services, a DNSP's network control systems (for example, a DNSP's Advanced Distribution Management System) will likely be utilised to operate the asset, and it is not economically or operationally efficient to separate out this functionality from a DNSP's normal operation of network assets and therefore the three clauses above should be waived.

Note that the class waiver will still require a DNSP to adhere to the Cost Allocation Principles in the National Electricity Rules and its AER-approved Cost Allocation Method.

The Commonwealth Government's Community Batteries for Household Solar Program is scheduled to run from 2022-23 to 2025-26[8]. Therefore, to align the class waiver with the expected economic life of community batteries (15 years), ENA proposes a modification to the time period that the class waiver applies – from 30 June 2038 to 30 June 2041. This update will allow for community batteries installed in the last financial year of the program (2025-26) to also be covered under the class waiver.

3.4 Transparency and reporting requirements

3.4.1 Third party contracts

For both Class A and Class B projects, ENA supports the AER's proposal for DNSPs to provide the AER with information as to the terms and conditions of the contracts entered into with third parties for the leasing of battery capacity.

This information should be provided to the AER within 20 business days of the contract being formally entered into and provided on a commercial in confidence basis.

This information should also include how the DNSP selected its market partner. However, we do not support the AER mandating a competitive tender process to select the third-party market partner in all cases. Instead, the class waiver should allow for a range of third-party engagement processes, including a competitive tender process, a request for proposal process, and partnership models with community groups and local councils. Importantly, when providing the AER with this information, the DNSP should outline why the specific process was undertaken and, if applicable, why a competitive tender process was not run.

3.4.2 Annual reporting

ENA also supports the AER introducing additional transparency and reporting requirements for Class B projects (i.e., those projects with a RAB allocation) as part of a DNSP's regular annual ring-fencing compliance reporting. However, we have proposed modifications to the AER's proposal to ensure that the reporting is fit for purpose and provides the required transparency without imposing significant costs on electricity customers.

Rather than requiring an additional stand-alone audit report, a DNSP's annual Ring-Fencing Compliance Independent Assessment report (undertaken by a qualified independent party) should include the total financial benefit derived from the deployment of the asset from *other distribution services* and *other services* over the most recent financial year – for example, any revenue that the DNSP receives from

[8] Budget October 2022-23, Budget Measures: Budget Paper No. 2, Page 69, 25 October 2022.

leasing battery capacity to third parties. Note that this may be provided to the AER on a commercial in confidence basis.

A DNSP should also be required to publish (appropriately deidentified) data, subject to security and privacy requirements, regarding the usage of the battery (volume and frequency) by the DNSP and by its retail partner (or other third party). The data on the battery usage will be most useful for policy makers and future investors, and therefore costly annual audits on the data will likely not be necessary.

In addition to the AER's class waiver transparency and reporting requirements, the Commonwealth Program will also require successful applications to submit reports. For example, DCCEEW's Guideline[9] requires the successful applicant to submit reports in line with the grant agreement, which is expected to include:

- progress against agreed project milestones,
- project expenditure, including expenditure of grant funds, and
- contributions of participants directly related to the project.

Post project reporting to DCCEEW will also be required and cover the ongoing outcomes and community benefits of the project, and DCCEEW also retains the discretion to request an independent audit of claims and payments.

[9] Department of Climate Change, Energy, the Environment and Water, Grant Opportunity Guidelines: Community Batteries for Household Solar Program – Delivery of Election Commitments Stream 1, Section 12.2, December 2022.

Appendix A I Summary of key positions

The table below provides a brief summary of ENA's key positions. For more information, including the rationale, please refer to the body of this submission.

Item	AER class waiver proposal	ENA Position
Cost allocation **Section 3.1**	» Class A: no RAB allocation » Class B: Proportionate share approach	» **Class A: Support** » **Class B: Do not support** – proposed a simplified cost allocation approach linked to customer benefits.
Application **(Class A & B)** **Section 3.2**	» Waiver applies to Class A and B projects administered by both DCCEEW and ARENA under the Commonwealth Program.	» **Support** application to both DCCEEW and ARENA. » **However, the waiver should be widened to also include jurisdictional government programs**, for example (but not limited to): – Victorian Government Neighbourhood Battery Initiative, with funding for additional neighbourhood batteries recently announced, – Queensland Government Energy and Jobs Plan, which includes funding for community batteries, and – ACT Government Big Canberra Battery, with Stream 3 for the rollout of neighbourhood scale batteries.
Waived obligations **(Class A & B)** **Section 3.3**	» Proposed ring-fencing obligations to be waived: – clause 3.1 [Legal separation] – clause 4.2.1 [Functional separation – Physical separation / co-location] – clause 4.2.2 [Functional separation – Staff sharing]	» **Support** the proposed waived obligations in order to enable value-stacking of the battery and facilitate DNSPs leasing battery capacity to third parties.

Item	AER class waiver proposal	ENA Position
Time period **(Class A & B)** **Section 3.3**	» Period of class waiver: 30 June 2038 [approx. 15 years]	» **Proposed amendment to the proposed timeframe**: 30 June 2041 » Assuming an expected battery life of 15 years, this allows for community batteries installed in the last financial year of the Commonwealth Program (2025-26).
Contract information **(Class A & B)** **Section 3.4.1**	» DNSP must provide the AER with information as to the terms and conditions of the contracts entered into with third parties for the leasing of battery capacity. » The AER expects DNSPs would undertake a competitive process to select a third party.	» **Support provision of third-party contract information**, however, this should be provided to the AER on a commercial in confidence basis within 20 Business Days of the contract being entered into with third party. » **Do not support a mandated competitive tender process** to select a third-party market partner in all cases, and instead the DNSP should be required to outline to the AER what specific process was undertaken and, if applicable, why a competitive tender process was not run.
Reporting requirements **(Class B)** **Section 3.4.2**	» As part of that DNSP's regular ring-fencing annual compliance reporting, DNSPs must submit an independent audit report that covers actual benefits derived and actual usage	» **Support introduction of additional transparency measures for Class B projects, however, proposed amendments** to ensure that the reporting is fit for purpose and provides the required transparency without imposing significant costs on electricity customers.