5 February 2019

Owen Pascoe
Director
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Mr Pascoe,

Submission to consultation paper on regulatory sandbox arrangements

The Public Interest Advocacy Centre (PIAC) is an independent, non-profit legal centre based in New South Wales. Established in 1982, PIAC tackles systemic issues that have a significant impact upon people who are marginalised and facing disadvantage. We ensure basic rights are enjoyed across the community through litigation, public policy development, communication and training. The Energy + Water Consumers' Advocacy Program represents the interests of low-income and other residential consumers, developing policy and advocating in energy and water markets.

PIAC welcomes the opportunity to respond to the AEMC's consultation paper.

The industry is transforming

The energy sector is in a major transformation in terms of technology, economics, business models, consumers' willingness and ability to take a more active role in their energy supply, and, necessarily, the supporting regulatory arrangements.

This transformation can deliver more efficient energy services to individual consumers and also deliver system- and economy-wide savings by allowing more cost-effective ways of providing affordable, sustainable and reliable energy services. But at the same time, it presents new risks, to both consumers and investors as well as challenges to existing regulatory arrangements.

Regulation must balance preventing consumer harms with realising potential benefits

The current transformation will require energy policy and regulatory frameworks that balance appropriate levels of protections so consumers continue to enjoy energy supply now while enabling the innovation and investment needed for the future. These frameworks will be key to realising the potential benefits and managing any risks associated with the transformation.

While the policy and regulatory framework for energy is complex and imposes burdens on businesses, the essential question to consider is whether these burdens are proportionate to the harms they intend to prevent.

The potential harms to consumers stem from the fact that electricity is an essential service in a modern society. Broadly speaking, these harms are:

- Unnecessarily high prices due to inefficient markets and networks – consumers may fail to receive the benefits of competitive markets due to a variety of factors including concentration of market power, barriers to new entrants, the existence of perverse incentives or a lack of transparency allowing for excessive profits to some participants.

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- Inability to make informed choices – a lack of transparent, accessible and understandable information for consumers means that many are unable to choose products and services which reflect their actual preferences.

Innovation through advice and regulatory sandboxes have a role to play

In determining whether and how to aid navigating energy regulations, there is unlikely to be a one-size-fits-all solution. Instead, PIAC considers there are two predominant likely cases:

- An established energy market player looking to modify their offers where providing energy services is the primary concern. Being already established in the NEM, these businesses would likely already have their own regulatory advice in-house or be more readily able to procure this advice externally if needed and therefore, might find more value in proceeding to developing a regulatory sandbox to justify the case for a rule change.

- A new entrant to the energy market with a business model that involves an innovative energy-only service, or where the provision of those energy services is a secondary consequence of a non-energy related service being offered.[1] For these cases, it would be of more use for a market body to be able to provide quick and accessible, non-binding advice on the impact of energy regulations. Depending on the outcome of this advice, the business may or may not pursue a formal a regulatory sandbox.

In order to address potential harms to consumers, energy regulations must strike a balance by providing appropriate levels of protection whilst also removing barriers to entry and providing the long-term certainty to facilitate the innovation and investment needed to unlock the full benefits possible in the current transformation in energy.

Therefore, a well-designed regulatory sandbox must include:

- an appropriate assessment prior to commencing the trial to determine:
    - a robust justification that the greater benefits from conducting the trial outweigh the cost and potential risk to sandbox consumers
    - which regulations need to be relaxed
    - by how much
    - how long for
    - what (additional) protections may be required for customers within the trial – for example if the technology were to develop a fault or the trial is forced to close earlier than expected
    - what are the sunset clauses on the sandbox offer(s) – for example on warranties or ongoing support services for products, or ongoing subscription fees for participating customers
- ongoing monitoring of the trial including the effectiveness of the product/service being trialled and the effectiveness of the consumer protections
- post-trial review including sharing of data/lessons learnt, and informing any other (ongoing or subsequent) sandbox trials. Ideally these reviews should specifically seek to identify any failures in the realisation of the concept, including any unintended impacts upon consumers.

[1] For instance, where the primary service may be related to transportation or accommodation but, as a consequence of bundling a number of services together, the business model technically also includes the sale or distribution of electricity.

Attached is PIAC's responses to the AEMC's consultation which discusses these matters in further detail.

Continued engagement

PIAC would welcome the opportunity to meet with the AEMC and other stakeholders to discuss these issues in more depth.

Yours sincerely,

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ATTACHMENT: Responses to Consultation Questions

QUESTION 1: OTHER SANDBOX EXAMPLES

Are there other examples of regulatory sandbox arrangements that are relevant when considering these arrangements for the NEM?

In addition to those listed, other examples of regulatory sandboxes worth considering are:

- The NSW Government's regulatory sandboxes to improve business innovation more broadly;[2] and
- The energy-specific sandbox run by Singapore's Energy Market Authority.[3]

In addition, it is essential that in searching for examples, the AEMC also consider the case where a regulatory sandbox was not implemented for an innovative trial. In these instances, it would be instructive to consider factors such as:

- Why a regulatory sandbox was not used;
- The outcomes of the trial in terms of customer and business experiences;
- The relevant lessons or insights gained from the trial and whether these were useful for informing future regulatory or policy reform; and
- Inferring whether the use of a regulatory sandbox would or would not have materially altered the outcomes either for the better or worse.

QUESTION 2: OTHER RELEVANT TRIALS

What other proof-of-concept trials are relevant when considering formal regulatory sandbox arrangements for the NEM?

No comment

QUESTION 3: BARRIERS TO PROOF-OF-CONCEPT TRIALS

(a) Are proof-of-concept trials being inhibited by current market regulations or processes?

(b) If so, what are the potential barriers to proof-of-concept trials that might be addressed by a regulatory sandbox initiative?

No comment

QUESTION 4: ACCESS TO GUIDANCE ON THE REGULATORY FRAMEWORK

(a) Is there a lack of access to guidance for innovative new entrants on navigating the energy regulatory framework?

(b) If so:

- **What type of guidance is needed?**
- **Who should provide it?**
- **Should guidance be coordinated across the AER, AEMO and AEMC?**
- **How should the provision of guidance be funded?**
- **Should an application be required in order to gain access to detailed guidance? If so, what criteria should apply?**

Anecdotal evidence suggests yes. However, as noted earlier in this submission, while the policy and regulatory framework for energy is complex and imposes burdens on businesses, the essential assessment remains whether these burdens are proportionate to the harms they intend to prevent.

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2 https://www.innovation.nsw.gov.au/regulatorysandboxes

3 https://www.ema.gov.sg/Sandbox.aspx

The complexity of energy regulation and policy in the NEM (noting the combination of national and state-specific regulations) is likely exacerbated where an innovative new entrant to the energy market seeks to develop a product or service which provides more than solely energy services. In such cases, it may not be clear how the energy-specific obligations interact with other obligations.

In determining whether and how to aid navigating energy regulations, there is unlikely to be a one-size-fits-all solution. Instead, PIAC considers there are two predominant likely cases.

The first case is an established energy market player looking to modify their offers where providing energy services is the primary concern. These businesses, being already established in the NEM, would likely already have their own regulatory advice in-house or more readily procure this advice externally if needed. Therefore, they may see less benefit from receiving fast, non-binding advice from a market body. Instead they might find more value in proceeding to developing a regulatory sandbox to justify the case for a rule change.

The second is a new entrant to the energy market which may involve an innovative energy-only service. However, many may be business models where providing energy services are secondary and is, instead, a consequence of the primary service being offered. For instance, it could be a telco, transport, or ride-sharing business looking to provide a service or product which technically requires the sale of energy in some form or other. For these cases, it would likely be of more use for a market body to provide quick and accessible advice on the impact of energy regulations. As a consequence, this advice would have to be non-binding. Depending on the outcome of this advice, the business may decide to procure more thorough advice and there may or may not be merit in more formally examining a regulatory sandbox.

PIAC has not yet formed a view on more detailed matters such as the coordination of guidance between the market bodies, its funding arrangements or the application thresholds. However, we would welcome working further with the AEMC and other stakeholders in developing these ideas.

(c) Is there a role for binding advice from market bodies on certain aspects of the regulatory framework to support proof-of-concept trials?

Not at this stage – PIAC considers there would be a stronger case for market bodies providing fast but non-binding advice.

While there will definitely be a need for binding advice for any innovative new offering, PIAC is not yet convinced that this would be a role for market bodies to provide. Instead, it may be more appropriate for the innovating business to procure this advice themselves, or potentially with external funding support if needed.

QUESTION 5: TRIALS UNDER AER ENFORCEMENT DISCRETION

(a) Is the AER's ability to issue no action letters, provide waivers and exemptions, and use its enforcement discretion sufficient to facilitate proof-of-concept trials in the NEM? If not, why?

PIAC considers that relying solely on no action letters to facilitate proof-of-concept trials may leave substantial innovative potential unrealised.

While the AER's use of no action letters can help to facilitate innovation and proof-of-concept testing, it is important to note the subtle yet important distinction between no action letters and a well-designed regulatory sandbox. No action letters are, by their very nature, compliance-based

with the starting premise of whether or not to issue one being compliance with the regulatory status quo. A well-designed regulatory sandbox, by contrast, starts from the premise that, if a proposal is likely to be in the long-term interests of consumers, it then seeks to determine how to make it part of the regulatory status quo. While the two approaches could potentially result in the same outcome in some cases, they are not inherently interchangeable.

This difference is amplified by the fact that a well-designed regulatory sandbox should include a number of ongoing and post-trial reporting requirements (see PIAC's response to Questions 6 and 7) whereas a no action letter may not necessarily require a similar level of transparency and analysis.

(b) Is there a need for a more formal process for proponents of proof-of-concept trials to seek a no action letter?

No comment

(c) Should no action letters that facilitate innovation or proof-of-concept trials be made public?

By default, such no action letters should be made public.

It provides important transparency regarding the application of regulatory obligations and, by inference, the appropriateness of current regulations in response to developments in the market. For example, the number of no action letters issued (or requested) relating to a particular regulatory obligation may suggest that the particular obligation should be reviewed.

If there are significant and legitimate concerns regarding making the no action letters public, the onus should be on the affected party to establish this. Further, we note that, if there are proven confidentiality concerns, those sections alone of the no action letter could be redacted rather than the entire document being kept confidential.

QUESTION 6: THE NEED FOR A FORMAL REGULATORY SANDBOX
(a) Would formal regulatory sandbox arrangements, where some regulatory requirements are relaxed on a time-limited basis whilst appropriate safeguards remain in place, serve to better facilitate proof-of-concept trials in the NEM?
(b) What other regulatory tools are needed to facilitate proof-of-concept trials?

Yes, however, as noted earlier in this submission, while the policy and regulatory framework for energy is complex and imposes burdens on businesses, the essential question remains the proportionality of burdens to the harms they intend to prevent.

To this end a number of related tools and obligations would be required including:

- an appropriate assessment prior to commencing the trial to determine:
    - a robust justification that the greater benefits from conducting the trial outweighs the cost and risk to sandbox consumers
    - which regulations need to be relaxed
    - by how much
    - how long for
    - what (additional) protections may be required for customers within the trial – for example if the technology were to develop a fault or the trial is forced to close earlier than expected
    - what are the sunset clauses on the sandbox offer(s) – for example on warranties or ongoing support services for products, or ongoing subscription fees for participating customers

- ongoing monitoring of the trial including the effectiveness of the product/service being trialled and the effectiveness of the consumer protections
- post-trial review including sharing of data/lessons learnt, and informing any other (ongoing or subsequent) sandbox trials. Ideally these reviews should specifically seek to identify any failures in the realisation of the concept, including any unintended impacts upon consumers.

QUESTION 7: DESIGN OF A FORMAL REGULATORY SANDBOX ARRANGEMENTS, IF REQUIRED

(a) If required, should the objective of the formal regulatory sandbox arrangements be to facilitate further proof-of-concept trials in the NEM? If not, what should the objective be?

PIAC considers that the objective of any well-designed regulatory sandbox should be to help inform the need for, and direction of, any reforms to the existing regulatory and policy frameworks in order to ensure they remain fit-for-purpose. Proof-of-concept trials are one of a number of ways of achieving this.

Furthermore, proof-of-concept trials are a means to an end and not the end in and of itself. Defining the objective of sandboxes to be facilitating further trials risks divorcing its operation from the ultimate outcome of being in the long-terms interests of consumers.

(b) If required, what metrics should be used to measure the success of a formal regulatory sandbox arrangement?

- The degree to which the high-level criteria listed below have been met
- The experience of participating customers – including the effectiveness of customer protections implemented and the responsiveness of these arrangements to customer feedback or changing conditions
- The appropriateness of consumer protections for participating customers
- The degree to which consumers as a whole (not merely a narrow consumer cohort or participating consumers) are likely to benefit from the proof-of-concept
- The degree to which the NEM as a whole is likely to benefit from the proof-of-concept

(c) If required, what should be the high-level criteria for accessing a regulatory sandbox arrangement?

- The product, service or business model being tested must be genuinely innovative and ready for proof-of-concept testing
- The proponent must demonstrate that a regulatory sandbox is the most suitable option (most efficient, with proportionate level of risk) available to test the proof-of-concept
- The scope must be well-defined in terms of which regulations are to be waived and for what period of time and/or location
- Potential harms for participating consumers are identified and appropriate consumer protections are proposed including boundary conditions for participation and entry-exit clauses
- There must be a demonstrable benefit from conducting a proof-of-concept, such as:
    - The reasonably likely benefit to consumers as a whole – for example by developing a technology or business model which can reduce the cost of the electricity system or provide better service to participating customers
    - The reasonably likely benefit to the NEM as a whole – for example by better defining the need, if any, for regulatory or policy reforms
- An appropriate monitoring and compliance process must be proposed

(d) How could fairness be addressed in the case where proponents of similar trials apply to access sandbox arrangements but only a limited number of trials can be accepted?

PIAC has not yet formed a view on this. However, we would welcome working further with the AEMC and other stakeholders in developing potential options.

(e) If required, what should be the key features of a formal regulatory sandbox arrangement for the NEM?

- **What regulatory arrangements should be within scope to consider for relaxation?**
- **What should be the safeguards for consumers?**
- **What obligations should be placed on the participants (e.g. knowledge sharing requirements)?**

See PIAC's response to Question 6.

QUESTION 8: TRIALLING INNOVATIVE REGULATORY PROCESSES
How could formal regulatory sandbox arrangements be used to trial changes to regulatory arrangements to guide adoption of reforms across the market?

As noted in the consultation paper, a well-conducted regulatory sandbox can help to provide the evidence base to determine whether a regulatory reform, such as a rule change, would be in the long-term interests of consumers.