

11 March 2016

Ms. Catherine Cussen  
Queensland Productivity Commission  
PO Box 12112  
George St QLD 4003

## Electricity Pricing in Queensland Draft Report

Dear Ms. Cussen

The ENA welcomes the opportunity to make a submission to the Queensland Productivity Commission (QPC) in response to the *Electricity Pricing Inquiry Draft Report* published by the QPC on 3 February 2016.

The ENA is the national industry association representing the businesses operating Australia's electricity transmission and distribution and gas distribution networks. Member businesses provide energy to almost every household and business in Australia.

The Draft Report makes 54 recommendations. ENA responses to key issues are provided below.

### **Supply chain productivity (Recommendations 1-3)**

The ENA supports Recommendation 1-3. Emissions reduction policies which give preference to specific technologies limit the ability of market participants and investors to explore the full range of potential economic solutions. Emission reduction policies should be outcome focused and technologically neutral. The ENA agrees with the QPC that government intervention should be limited to circumstances of clear market failure and that cost-benefit analysis should be used to assess any new policy initiatives.

The ENA would support the Queensland Government, in conjunction with network businesses, keeping emerging technology issues, such as increased use of batteries and the uptake of electric vehicles, under active review.

### **Renewable energy & carbon abatement (Recommendations 9-11)**

The ENA supports the QPC's recommendations 9-11. ENA notes that the Acil Allen modelling shows that the QRET (using large scale feed-in tariffs) would require a subsidy of about \$10.8 billion (real) over the period to 2030. "The 10.8 billion QRET subsidy consists of \$8.6 billion (present value \$5.2 billion) for 6,300 MW of additional large-scale investment, and \$2.2 billion (present value \$1.5 billion) for small scale investment. The subsidy includes payment to those rooftop PV installations that are already expected to occur in the base case between 2018 and 2030, as well as the additional 300 MW expected to come forward in the QRET case"<sup>1</sup>.

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<sup>1</sup> Queensland Productivity Commission Electricity Pricing Inquiry Draft Report, February 2016, p. 55.  
<http://www.qpc.qld.gov.au/files/uploads/2016/02/EPI-DRAFT-REPORT-Final.pdf>

ENA notes that “compared to the base case, the additional QRET renewable investment displaces about 1,600 MW of investment in gas-fired capacity. This is a result of a QRET targeting renewables rather than emissions reduction, which results in gas-fired generation rather than coal being displaced”. This is the basis for the ENA’s position that emission reduction policies should be outcome focused and technologically neutral. The Queensland Government should focus on supporting emission reduction rather than specific technologies.

ENA notes that both the Government’s Emissions Reductions Fund and the former Government’s carbon price provide lower cost abatement than the proposed QRET and hence the ENA agrees with the QPC that the Queensland Government should work co-operatively with the other jurisdictional governments and the Australian Government on emissions reduction policy. ENA supports the COAG Energy Council’s recent agreement to develop a national approach to better integrate carbon reduction and energy policies in the interests of consumers<sup>2</sup>.

ENA notes that the Acil Allen modelling shows that the proposed 3000 MW of solar (or one million rooftops) is projected to be met by 2022 in the absence of any further Government subsidy and that “the tariff level required to bring forward investment to meet the target by 2020 would facilitate a very large transfer of wealth from other electricity consumers to owners of rooftop solar PV”<sup>3</sup>.

NERA undertook a solar case study for the AEMC which illustrates that for example a South Australian consumer with a 2.5 kilowatt north-facing solar panel system currently pays about \$200 a year less in network costs than a similar consumer without solar panels. North-facing solar panels generate about 18 per cent of their maximum capacity during the time of peak network demand and as a result the reduction in network costs is about \$80. This consumer therefore pays about \$120 a year less than the costs of providing the consumer network services. That \$120 is recovered by other consumers facing higher prices”<sup>4</sup>.

### ***Issues affecting network businesses (Recommendations 12-16)***

ENA welcomes the leadership of the Queensland Government working within the COAG Energy Council to seek to ensure Australia’s energy regulatory frameworks remain relevant and continue to promote the long-term interests of consumers during a period of dynamic change. Work undertaken to date to conduct a regulatory ‘stress-test’ of the existing regulatory framework provides a sound basis for governments to consider the diverse range of scenarios that may emerge, and associated priority issues.

ENA plans to further progress these issues throughout 2016 through the second stage of a collaborative partnership between the ENA and the CSIRO called the Network Transformation Roadmap. The initial stage of this project identified critical areas for future government and regulatory decision-making around issues of the scope of economic regulation, ensuring appropriate risk allocation between consumers and market participants, the importance of a sustainable and efficient universal service obligation, and maintaining strong consumer protection around new technologies and services.

### ***Market structure and competition***

As recognised by the QPC’s report, the market for energy services is experiencing a process of significant transformation affecting energy networks, retailers and a range of other service providers. These transformation trends arise due to rapidly evolving technologies, consumer demands, markets and business models.

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<sup>2</sup> COAG Energy Council Communique December 2015, p.1. <http://www.scer.gov.au/publications/4th-coag-energy-council-meeting-communique-4-december-2015>

<sup>3</sup> Queensland Productivity Commission Electricity Pricing Inquiry Draft Report, February 2016, p. 61. <http://www.qpc.qld.gov.au/files/uploads/2016/02/EPI-DRAFT-REPORT-Final.pdf>

<sup>4</sup> Distribution Network Pricing Arrangements Rule Change <http://www.aemc.gov.au/getattachment/de5cc69f-e850-48e0-9277-b3db79dd25c8/Final-determination.aspx>

The key starting point for regulatory and policy considerations in this area should be maximising the long-term benefits of benefit for consumer. In order to develop and deliver valued services to consumers in this changing market, networks need to have the capacity to flexibly meet evolving customer expectations around direct service offerings to customers. A further key principle is that networks need to be free to deliver regulated network services to customers with the most efficient mixture of technologies, assets and commercial arrangements available, in order to meet the needs of consumers and achieve efficient levels of network charges.

The ENA notes the QPC's recommendations in relation to ring-fencing between competitive and monopoly functions, as well as exercising caution in pursuing new business models. The ENA agrees with the QPC that it is essential that the electricity networks in Queensland continue to deliver reliable and safe supply to their customers. Queensland electricity networks face strict legal obligations under State and Federal laws and rules to continue to focus on the safe, reliable and efficient delivery of core network services.

The ENA considers that the scope of separation between the energy services business and the electricity distribution businesses' activities requires careful and evidence-led assessment processes. This is required to assess the benefits, costs and risks of alternative proposed approaches. The primary guiding principle in these assessments should be that new markets should be being served by a diverse range of market participants and competing business models, to maximise the benefits of competition to consumers. A careful assessment process is required to ensure that there are no unintended consequences of any proposed approaches that have the effect of discouraging efficient participation by networks in emerging contestable markets. This may potentially deprive consumers of access to a range of innovative network services that they would value highly.

In many cases, the evolution of business models, emerging technologies, and a competitive environment may mean network businesses are the party that can most efficiently meet evolving customer needs. Furthermore, alternative services may allow network businesses to improve the quality and reliability of network services, including achieving existing service obligations in more cost-effective ways. Arbitrary technology based restrictions that foreclosed networks being able to use, configure and own emergent technologies to support efficient delivery of core regulated services would create a significant risk of imposing higher costs on all connected energy consumers.

The ENA notes that the existing regulatory regime provides ring-fencing elements, thereby reducing the need for additional actions in this area. Current arrangements are focused in particular on ensuring appropriate cost allocation between the regulated and other activities of network businesses, and providing the Australian Energy Regulator (AER) with detailed information on the costs incurred by network businesses in delivering regulated services.

In addition, the National Electricity Rules empower the AER to reduce the annual revenue requirement for a regulated business to reflect the costs of the regulated assets which are used in providing an unregulated service. The AER has established Shared Asset Guidelines to give effect to the Rules' requirement. These long-standing regulatory tools already address a range of existing circumstances in which assets serve a dual purpose, and deliver both network-related services and services to unregulated competitive markets.

### ***Incentives for efficient network decision-making***

The ENA recognises the role of both tariff and non-tariff demand management programs in minimising or deferring network capital expenditure, as per QPC's recommendation 16. It is important to note however, that the regulatory framework contains a suite of other relevant incentives to encourage efficient investment decisions:

- » The Rules require network businesses to apply the RIT-T and RIT-D before significant augmentation or expansion of network infrastructure. These tests require alternatives to network augmentation or expansions to be appropriately considered with a requirement to examine feasible network and non-network options.
- » Under the Capital Expenditure Efficiency Sharing Scheme (CESS), a network business will retain 30 per cent of any underspend or overspend in capex while consumers will retain 70 per cent of the underspend or overspend. This means that in net present value terms a business bears around 30 per cent of any overspend, even if the expenditure is subsequently deemed efficient. However, if the AER finds that the overspend is inefficient, *ex post* reviews mean the business will bear 100 per cent of the cost of the inefficient overspend. The key policy goal of the AEMC and AER in introducing and designing the CESS was to provide that incentives for opex and capex are balanced and constant thereby encouraging network firms to make efficient expenditure decisions.
- » If a business's capex exceeds the regulator's forecast, the AER will examine its spending and can disallow some or all of the capex overspend to be included in the regulated asset base (RAB). The network firm faces the possibility of never obtaining a return on these assets, but continuing to bear the costs of their upkeep and maintenance.
- » The new Demand Management Incentive Scheme is expected to create a new incentive framework for energy network businesses undertaking innovative demand management activities, following its introduction in 2016.

### **Reforming the Queensland Solar Bonus Scheme (Recommendation 17)**

The ENA supports recommendation 17 which suggests that the Queensland Government should consider the merits of an earlier end to the Solar Bonus Scheme (SBS) than the planned 2028 closure.

As mentioned previously, the ENA supports technology neutrality. The ENA notes that the QPC is undertaking a review into Solar Feed-In Pricing in Queensland and that the Victorian Essential Services Commission is undertaking an Inquiry into the true value of distributed generation to Victorian consumers. The AEMC has also received a City of Sydney/Total Environment Centre Rule Change on Local Generation Network Credits. These inquiries will consider the value of solar generation and will also consider for example "the most appropriate policy and regulatory mechanisms for compensating different benefits of distributed generation, including considering their practicalities and costs"<sup>5</sup>.

Any scheme that recovers its costs from distributors will add to electricity prices and reduce electricity sector productivity. This should be avoided in the design of future schemes.

ENA believes the best way to recover network costs associated with demand more efficiently and equitably is for consumers to be charged a price that reflects the efficient costs of providing that service. The distribution network pricing objective and the distribution pricing principles will ensure that prices better reflect the costs of the network service and that consumers can make more informed decisions about how they use electricity.

Australia's world leading rates of rooftop solar installation are both an opportunity and a threat to fair and more efficient prices for customers, with up to a further 7 million customers projected to install solar panels by 2034<sup>6</sup>. Solar panels usually require advanced meters that measure the time of energy use, so there would be no additional metering investment needed to provide a fair network tariff. However, if

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<sup>5</sup> Essential Services Commission Inquiry into the true value of distributed generation to Victorian Consumers Terms of Reference <http://www.esc.vic.gov.au/getattachment/0a3f1608-ac62-43a1-83e4-7123262a9851/Terms-of-Reference.pdf>

<sup>6</sup> ENA Position Paper: Towards a national approach to electricity network tariff reform. p. ii. December, 2014

network tariffs remain unchanged the result will be over-investment in distributed energy resources and higher community costs of up to \$17.7 billion by 2034<sup>7</sup>.

### ***Deregulation in South East Queensland (Recommendations 22-28)***

The ENA supports retail price de-regulation where competition is shown to be effective. Hence the ENA supports the QPC's Recommendation 22 and 23. The ENA agrees with the QPC that "if price deregulation is to commence on 1 July 2016, any planned customer engagement activities should be implemented as soon as practicable to maximise success and help ensure a smooth transition"<sup>8</sup>.

The ENA supports recommendation 24 concerning a planned customer engagement campaign. ENA agrees that the campaign should

- » "provide sufficient advice and information to consumers to assist with comparing offers, and be tailored to address the needs of vulnerable customer groups; and
- » provide assistance to NGOs to assist vulnerable and disadvantaged consumers to fully participate in the market"<sup>9</sup>.

The ENA supports recommendations 25 to 28. ENA agrees that the currently proposed market monitoring arrangements are adequate and that monitoring the efficiency and effectiveness of standing offers should form part of the Queensland Government's market monitoring arrangements for SEQ.

The ENA also agrees that the Queensland Government should monitor the impact of deregulation on vulnerable and low income customers.

### ***Options for Increasing Competition in Regional Queensland (Recommendations 29 – 35)***

It is expected that de-regulating electricity retail prices will encourage new retail market entry to drive competition for customers and so place downward pressure on prices. Implementing this reform in regional Queensland is particularly complex because of the longstanding Uniform Tariff Policy ("UTP") and the Community Service Obligation ("CSO") arrangements which operate to support it. As the QPC notes, the current arrangement under which the Government makes the CSO payment to Ergon Energy (Retail) means that other retailers cannot compete in regional Queensland. The QPC also observes that the arrangement is complex: the UTP has no clearly stated public policy objective, the CSO's method of calculation is opaque and detailed information about the categories of customers who benefit and the sizes of their subsidies is not public. Consequently, public understanding of the UTP and CSO is so limited that there is scant discussion of the efficiency and effectiveness of arrangements which involve substantial public expenditure.

The ENA therefore supports the QPC's recommendations (29 and 30) that the UTP and CSO arrangements be made transparent and that payment of the CSO be shifted from Ergon Energy (Retail) to Ergon Energy (Network). The ENA recognises that implementing a network CSO will not be cost neutral (imposing additional costs on either the State budget or customers, or both), and therefore supports recommendation 31 for the State Government to find measures to mitigate the financial effects of the reform.

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<sup>7</sup> Network Pricing and Enabling Metering Analysis - Prepared by Energeia for the Energy Networks Association, November 2014 p.5.

<sup>8</sup> Queensland Productivity Commission Electricity Pricing Inquiry Draft Report, February 2016, p.115. <http://www.qpc.qld.gov.au/files/uploads/2016/02/EPI-DRAFT-REPORT-Final.pdf>

<sup>9</sup> Ibid. p.116.

Given the complexity of the CSO arrangements, the ENA agrees that it might require several years to implement a network CSO and supports the QPC's recommendation (32) that this be completed no later than 1 July 2019.

The energy market is undergoing significant change with the entry of distributed resources such as rooftop solar PV and battery storage units. Distribution Network Service Providers have for many decades provided "behind the meter" services such as load control of hot water systems to manage network load at times of peak demand. These services have thereby enabled DNSPs to optimise network investments and therefore minimise the costs they have to recover from customers in the future. Distributed resources add to DNSPs' long-standing load control capacity to manage network load and optimise investment programs. Compelling DNSPs to buy these network-related services from other businesses would simply add to the cost of providing the services and potentially increase their costs relative to other network solutions.

Further, it is clear that the distributed resources product market is a competitive market. Preventing DNSPs from offering distributed resources products for network service purposes would only diminish competition in that broader market. To the extent that a DNSP's sale of a product to provide a network services delivers the best value for a customer, then that must be the most efficient means of delivering the product. Arguments by other market participants that DNSPs should be excluded from selling distributed resources should be examined very closely to ensure that they are not being made with the objective of removing a competitor at the expense of customers. The ENA also recognises that DNSPs should not be afforded special benefits in this competitive space by virtue of being an incumbent DNSP, and not be permitted to cross-subsidise, for example, through the use of regulated revenue allowances to enter new or adjacent markets. As noted previously, a range of regulatory tools and mechanisms already exists to avoid these types of outcomes (such as cost allocation, ring-fencing, and sharing guidelines).

#### ***Rural and Regional Industries (Recommendation 36-40)***

The ENA supports the QPC's recommendations 36-40. The ENA strongly supports moving toward cost-reflective network pricing. However, the ENA also recognises that, to ensure movement toward cost-reflectivity is sustainable, customers whose business models rely on historic below-cost tariffs must be assisted to manage the transition. The provision of tailored information, advanced meters and assistance with efficiency measures including capital investments are all measures which should be considered as part of developing the transition program.

#### ***Role of local service providers (Recommendations 41-43)***

The ENA supports the development of a consistent and flexible national regulatory framework to provide for innovative new fringe of grid and isolated system developments that can efficiently meet the needs of customers.

The Draft report clearly highlights the key issues that arise in respect of the participation of local service providers. It is of critical importance that frameworks that are developed in this area:

- » provide the right economic incentives to promote efficient price, reliability and safety outcomes to both the affected local community and grid-connected customers as a whole
- » provide for regulated networks to discharge their obligation to supply through flexible customised community solutions using the full range and most efficient mixture of new technologies, and ensure resulting savings are passed through to both local communities and those remaining on the grid, in circumstances where assets are decommissioned

- » do not result in the creation of regulatory risks and which allows for flexible recovery of existing assets that are, or are at credible risk of, having economic lives that are shorter than original regulatory assumptions
- » take account of the need for the costs of universal service obligations (or supplier of last resort obligations) to be sustainably recovered in a way that minimises inefficient investment and usage decisions

The Draft Report correctly identifies the critical need to develop and rely upon national rule frameworks and bodies in any policy development relating to recognising the value of local generation with the electricity market. This approach will minimise the potential for a fragmentary and inconsistent set of policies and pricing signals being introduced at State or Territory level, with potentially costly and distortionary impacts on investment and consumer usage decisions. For this reason, the ENA is actively engaging in the AEMC's local generation network credit rule change process, and encouraging the AEMC to consider the issues in a national context. In this context, the ENA has observed that appropriate sequencing – and progressing cost reflective pricing outcomes at a consumption level – is a critical pre-condition for any consideration of introduction of localized 'export' pricing signals.

#### ***Electricity Concessions Framework (Recommendations 44-51 and 54)***

The ENA would support the Queensland Government developing a clear policy intent for its concessions framework and assessing the design of the framework against the principles of adequacy, equity, adaptability and transparency. As mentioned in our submission to the QPC's Electricity Pricing Inquiry's Issues Paper, ENA supports the effective targeting of government assistance based on need. As part of this process ENA would support extending the eligibility for the general Electricity Rebate to recipients of the Commonwealth Government Health Care Card. Equity and budgetary considerations may mean targeting of the general Electricity Rebate is necessary.

The ENA would support the Queensland Government considering if there is a case for providing additional support for households with dependent children, as consumption increases with the number of people in a household. The ENA would also support the QPC's recommendation 48 concerning a proposed review of the Medical Heating and Cooling Electricity Concession Scheme and the Electricity Life Support Rebate and recommendation 49.

Financial assistance to support eligible, vulnerable, customers with their energy bills varies by jurisdiction. In addition to the recommendations made by the QPC the ENA would recommend

- » harmonising the value of government assistance across jurisdictions;
- » providing assistance to finance household or community investments in technology or energy efficiency improvements;
- » improving customers' access to information and decision tools<sup>10</sup>;
- » transitioning vulnerable customers to more cost reflective electricity network pricing, including the option of 'social tariffs'.

As stated in our previous submission, ENA would support a national review of vulnerable energy customer financial assistance. The national review, to be undertaken by the COAG Energy Council prior to the introduction of cost reflective pricing from 2017, could consider:

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<sup>10</sup> Supporting Vulnerable Energy Customers – ENA Information Paper p. 1 available at: [http://www.ena.asn.au/sites/default/files/ena\\_information\\_paper\\_-\\_supporting\\_vulnerable\\_energy\\_customers\\_may\\_2015.pdf](http://www.ena.asn.au/sites/default/files/ena_information_paper_-_supporting_vulnerable_energy_customers_may_2015.pdf)

- » the effectiveness of current assistance measures, including whether it is reaching those most in need;
- » the appropriate eligibility criteria for customers requiring assistance;
- » the basis for energy concessions, whether as a percentage of the energy bill or a flat rate;
- » the forms of assistance that could be provided;
- » maintaining the relative value of energy concessions over time;
- » the advantages and disadvantages of harmonising eligibility for assistance and the value of assistance across jurisdictions.

ENA would support Recommendation 50. The administration of energy concessions would be delivered more efficiently through the Australian Government social security system. The ENA agrees that jurisdictional governments should address the impacts of tariff reform on vulnerable customers by ensuring concessions are well targeted.

The ENA would support Recommendation 54; that the Queensland Government should investigate:

- » placing a requirement on landlords to meet certain standards of energy efficiency and demand management in their housing stock; and
- » funding a complementary assistance program to subsidise the purchase price of energy and demand efficient appliances for vulnerable customers that have accessed the Home Energy Emergency Assistance Scheme due to the breakdown of their existing appliances.

This could also perhaps be more efficiently achieved through action at the Australian Government level through the National Energy Productivity Plan and the Australian Government social security system respectively.

If further information is sought on this matter, please contact Ms. Kate Healey, Director Regulation, on 02 6272 1516 or by email on [khealey@ena.asn.au](mailto:khealey@ena.asn.au)

Yours sincerely,



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