

Ms Kate Reid
Senior Adviser
Australian Energy Markets Commission
PO Box A2449
Sydney South, NSW, 1235

Project Reference RPR0006

17 May 2017

By email: aemc@aemc.gov.au

Dear Ms Reid,

Re: AEMC Review of Regulatory Arrangements for Embedded Networks, Consultation Paper

The Australian Energy Council (AEC) is an industry body representing 21 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia, and sell gas and electricity to over 10 million homes and businesses.

Review Objectives

In practice, regulatory frameworks should operate with a purpose to limit market failure and to deal with market power that may threaten the delivery of safe, and secure competitively priced energy to customers. Embedded networks, along with Distributed Energy Resources (DER), will continue to create challenges in the design and coverage of both the technical and commercial regulatory frameworks.

The AEC would like to see the review address consistency in the scope and application of the regulatory frameworks, in particular minimum retail standards, as this is key as to whether or not the overarching framework is, or remains, fit for purpose. The review can assess this by whether the regulatory arrangements for embedded networks can accommodate various business models, can be consistently applied, will limit compliance complexity and cost and will not proliferate further tiers of registrations, authorisations and exemptions

Finally, just like any competitive framework, any regulatory framework is probably imperfect. In determining whether a regulatory framework is fit for purpose, firstly its objective should be clear. Clear objectives should simplify regulatory requirements and limit any need for a proliferation of further tiers of registrations, authorisations and exemptions to accommodate minority or unique business models.

Summary

In establishing minimum standards applicable to embedded networks, regulators should look to the minimum required:

- Standards in the National Energy Retail Law (NERL)¹;

¹ Section 34(2) (3) of the NERL, Section 36 of the NERL

- Technical and quality of supply standards; and,
- Safety Standards.

Such minimum standards allow regulatory policy goals to be met and will provide the benefits delivered from competitive priced energy, choice, safe and secure supply. These minimum standards also provide appropriate focus on what needs to be regulated. If inducements to introduce further layers of exemptions exist, then clearly the standards are not at the minimum.

Minimum standards reduce the need for multiple tiered regulatory frameworks. Multiple tiered regulatory frameworks that can be applied differently according to the provider's business model are often popularised as lowering barriers to entry and improving competitive outcomes. At least that's the theory. In practice, exemptions that lower the cost of compliance for certain business models, when compared to those of say an authorised retailer, create regulatory arbitrage leading to distorted incentives and price signals. Further, the tiers contribute to problems of confidence in the regulation; legitimate concern that if a regulatory requirement can be waived for certain types of service providers then that same requirement should not be imposed on other types of suppliers for essentially the same product and service. Arguably in such cases any exempted regulatory requirement should be waived for all service providers to ensure a level playing field and minimised regulatory costs.

Multiple tiered regulatory frameworks which impose differing benchmarks of regulatory obligations may inadvertently provide a litmus test of the true need for a specific regulatory intervention. Multiple tiered regulatory frameworks also highlight the risk that overregulation of authorised retailers may result in lost opportunities to them for growth, investment and job creation.

Recent changes to embedded network regulation have placed defined roles of responsibilities, established more consistent obligations of safety and the minimum expectation of metering provision. Combined with efforts to provide customer access to competitive offers, these changes have gone some way to ensure embedded networks offer choice and secure and safe energy supply to the customers within. However jurisdictional restrictions such as those in the ACT, Tasmania and Queensland, have limited the benefits of choice to only those jurisdictions that allow embedded network customers access to competitive offers. We stress the importance of removing these impediments so that all customers can enjoy the benefits from a choice of supplier.

The Two Tiered Regulatory Framework

Two tiered regulatory frameworks are commonplace in Australia in both technical and commercial regulation, such as the Therapeutic Goods Administration and the Financial Regulatory Framework. Such tiered approaches generally account for the risk of adverse outcomes of registrations or exemptions by product type. Broadly speaking these two tier arrangements ensure any regulatory restrictions exist only where they are necessary to achieve the public interest, and to achieve this with as little regulation as possible.

Energy supply and sales agreements are subject to a high level of regulation and oversight, consistent with the view of its essential nature. Decades of review have gone into developing the mandated one size fits all consumer protection framework, or NECF. In many two tiered regulatory regimes, such as therapeutic goods, the subject of the differing regulation is the product itself, not the supplier. This product based approach means that compliance obligations are uniform across suppliers of the product. In the energy exemptions framework, it is the supplier that is subject to differing authorisation and regulation, even though the product of retailed energy is the same.

This two tiered approach extends to the treatment compliance monitoring and the consequences of non-compliance of the regulations. The enforcement regime points to more severe penalties on

licensed retailers than for exempt sellers for comparable contravention of regulatory obligations around retailing the same good – electricity. The two tiered supplier authorisation is clearly not fit for purpose where it would permit, in practice that lower consumer protections and differing penalties for identical compliance breach can apply to a class of retail energy customers based solely upon their connection characteristics.

Alternative Regulatory Arrangements

The discipline of the market provides broad protections on price and service but may fail to set minimum standards for supply and sale to individual consumers (the policy objective).

When considering the retail exemption framework it is most appropriate to focus on what needs to be regulated (the minimum standards) rather than introduce further layers of exemptions. If there are regulations that can be ‘peeled off’ by the exemptions framework then we can broadly assume they are superfluous to the minimum standard. The question of who makes the offer available to a customer is much less important in this context. Regardless of the seller or their business model, there should be no inconsistency in the agreement with the NERL’s benchmark conditions of supply.²

Efficient investment and incentive regimes

Theoretically the conditions of natural monopoly created by the embedded network could allow the embedded network to exercise its market power by setting prices higher, and performance lower, than would occur in a competitive market.

The exemption framework does not incentivise efficient infrastructure investment. This is because the regulatory regime fails to incentivise the embedded network owner to perform (or not perform) an action. Instead the embedded network has its own motivations and specifications for its infrastructure investment that cater for its connected customers. An example might be multiple redundancies in cabling and substations at an international airport.

In practice therefore a regulatory assessment seeking to establish that the exemption framework at current levels hinders (or promotes) efficient investment in embedded network infrastructure would be a marginal exercise at best.

Access to Competition & Risk Allocation

Consumers must be able to access information easily to improve their informed choices.

Embedded network customers (other than those in the ACT, Queensland and Tasmania) gained a number of benefits from access to the competitive retail market in 2015. This access to competitive retailing effectively allocates risks between exempt sellers and embedded network customers in the same manner as any other retailer/customer risk allocation in that state.

It is unfortunate that embedded network customers in the ACT, Tasmania and Queensland continue to have costly regulatory impediments in place that require them to connect directly to the network should they wish to access retail market offers, the practical effect of which is to deny the customer access to competition. We support a review by the AEMC to explore ways that regulation changes can be expedited to ensure these customers are able to benefit from choice of supplier.

² Section 34(2) (3) of the NERL, Section 36 of the NERL

We observe that the embedded network child connection minutes off supply (i.e. non DNSP), and child connection quality of supply data is not available either for the consumer or for wider analysis. It's therefore difficult to ascertain embedded network service provider risk allocation in the absence of that type of data.

We also observe that should embedded networks choose to expose their customers directly to some form of embedded network use of system charge, such charges would not unreasonably be limited to a tariff no greater than the tariff that would apply if the customer is supplied directly by the DNSP.

Exemption Frameworks

The exemption framework should allow the retailing of energy to a small number of retail customers, whilst also ensuring the NECF governs the sale and supply of energy to retail customers. Given the extant obligations on authorised retailers, presumably the interests of customers are unacceptably compromised where any gaps exist between the minimum standards required of an authorised retailer and any off market embedded network energy supply agreement. The objective of the retail exemption framework should be to ensure that the clear minimum standards govern the sale and supply of energy to retail customers.

Consumer Protection

In theory, the implementation of the NECF was expected to provide efficiencies and reduce the regulatory burden for energy businesses operating across various jurisdictions that are part of the national energy market (NEM). In practice, NEM jurisdictions saw it as unacceptable for consumers in their state to be materially disadvantaged by the move to the NECF. For this reason material gaps and differences in the NECF emerged through jurisdictional derogations.

We note that consumers or small businesses in embedded networks are also not covered by the Energy and Water Ombudsman Scheme in all states. Exempt owners and operators are not required to be members of the scheme, though they are required to provide a comparable dispute resolution forum. A national approach to access to complaint and dispute resolution services remains a gap and should be examined in the review.

Minimum Standards

Short of an examination of each off market embedded network energy supply agreement, specific gaps may be difficult to identify. However the issue remains that the interests of customers are, in the apparent view of the NEM states, unacceptably compromised where any gaps exist between minimum standards required of authorised retailers and any off market embedded network energy supply agreement.

Retailers who are not exempt sellers may also provide broader services than electricity to their customers. For authorised retailers the terms of any agreement to purchase energy cannot be enforced upon non-energy sales agreements. This requirement should reasonably apply to off market embedded network energy supply agreements, bundled or not.

Finally, if there is no evidence of poorer outcomes due to differences in consumer protections provided by the multi-tiered regulatory approaches then that this may represent a hypothetical case that the existence of the authorised retailer agreements creates an effective floor to minimum standards. If this hypothesis is incorrect, and/or there is evidence of poorer consumer outcomes

on embedded networks, then the interests of customers are compromised and therefore the retail exemption conditions should not prevail.

Gas Embedded Networks

Gas embedded networks present unique technical and safety challenges, such as safety case obligations. Retail sale agreements for gas embedded networks would be best aligned with those determined for embedded networks.

Should you have any questions in relation to this rule change request please contact David Markham, telephone 03 9205 3111 or david.markham@energycouncil.com.au.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Sarah McNamara', with a long horizontal stroke extending to the right.

Sarah McNamara
General Manager Corporate Affairs