



PO Box 4136
East Richmond VIC 3121
T 131 806
F 1300 661 086
W redenergy.com.au

PO Box 632
Collins St West VIC 8007
T 1300 115 866
F 1300 136 891
W lumoenergy.com.au



3 June 2016

Dr Ron Ben-David
Chairperson
Essential Services Commission of Victoria
Level 37, 2 Lonsdale Street
Melbourne VIC 3000

Submitted electronically

Dear Dr Ben-David,

Re: The Energy Value of Distributed Generation

Red Energy (Red) and Lumo Energy (Lumo) welcome the opportunity to make a submission to the Essential Services Commission's (the Commission) Distributed Generation Inquiry Stage 1 Draft Report (the Draft Report).

Red and Lumo are 100% Australian owned subsidiaries of Snowy Hydro Limited. Collectively, we retail gas and electricity in Victoria and New South Wales and electricity in South Australia and Queensland to approximately 1 million customers.

Red and Lumo oppose the recommendations put forward in the Draft Report. We are particularly concerned that regulating a highly complex energy value is not in the best interests of all Victorian consumers, and will increase the price of energy state wide.

Energy retailers in Victoria must, in accordance with Victorian legislation, make "an offer to sell electricity to an renewable energy customer at the same tariffs and on the same terms and conditions that it would offer to the customer if the customer was not a renewable energy customer"¹. This requirement limits the ability of an energy retailer to recover the efficient costs of supply attributable to this particular group of customers in their energy pricing, so as such, the costs are cross-subsidised, including by vulnerable customers least able to afford them.

Deregulation of payments to distributed generation owners

Red and Lumo strongly believe that the feed in tariff (FIT) in Victoria must be deregulated. Regulation should be limited and applied to markets where there is a clear market failure or the existence of market power.

Generally speaking, markets need to be given an opportunity to work and evidence of a market failure before any form of regulated solution is implemented. As markets deliver the most efficient and reasonable value for the price of goods by allocating finite economic resources in a more efficient way compared to regulated solutions. In addition, they also encourage innovation and lead to a broader range of service offerings for consumers.

The Commission has yet to provide any evidence to demonstrate the existence of a market failure in the Victorian distributed generation market. As such, the assumption that

¹ Section 23C of the Electricity Industry Act 2000 (Victoria)

a regulated solution is required for the Victorian distributed generation market appears to be flawed.

Red and Lumo understand that the Terms of Reference (TOR) of the Inquiry prohibit the consideration of deregulating the FIT. Nevertheless, we consider that the Commission must not disregard the important principles contained in the Australian Energy Market Agreement² by enshrining price regulation in Victoria by overcomplicating the tariff with no evidence of market failure.

At a time when the evolution of energy markets has seen regulators and policy makers favouring deregulated approaches to energy market design, the decision to enforce a more complicated regulated solution in a market with no clear failure is odd. The implementation costs associated with the various components of the regulated solution proposed by the Commission have the potential to be very high, and unwinding them should the position of the Government change in the coming years seems a disproportionate cost considering the benefits accrued.

Unfortunately, it will be consumers that will be required to pay for this implementation.

Red and Lumo's preference for the regulated tariff

Given that the TOR for this Inquiry prohibit the Commission allowing the market to set the price of FIT, we prefer that the current flat mandated FIT remain in place.

We believe the complexity in implementing time based and locational FIT's when compared to the benefits realised is not in the long term interests of Victorian consumers. We consider simplicity and cost efficiency as key reasons for maintaining the flat FIT, as outlined below.

Simplicity

The current FIT is very simple, making it easy for consumers to understand. This allows consumers to easily understand the value that their solar panels are providing, and make efficient decisions regarding the opportunity costs of consuming energy at any point in time.

The implementation of any time and location based FITs will create unnecessary complexity, with the potential benefits likely to be disregarded as immaterial by consumers given the financial impacts on consumers.

Cost efficiency

Red and Lumo believe elements of the Commission's proposed FIT will be particularly costly to implement. While time based FIT's may be a relatively low cost solution, the additional complication presented by locational tariffs that disregard distribution zones, critical peak FITs, and social and environmental values are significantly more costly.

Red and Lumo strongly recommend the Commission undertakes in depth analysis of the costs associated with implementing the various changes required to make the proposed framework available to the market. These costs should be weighed against the potential benefits of each particular element of the framework before any decision is made on whether to proceed with these changes.

² Australian Energy Market Agreement s14.11

Critical peak FIT

Red and Lumo strongly oppose the proposal to include a critical peak component into the regulated FIT. Mandating a tariff that requires a retailer to implement the wholesale price into its billing system without any advice as to the plausibility and cost of doing so is inconsistent with good regulatory practice. Even at this stage we are unclear on the scope of changes required to our billing engine for this to occur, if it were even possible.

Red and Lumo urge the Commission to undertake comprehensive analysis, including on the costs, benefits, and feasibility of the proposal prior to making any further determinations on this matter.

Environmental and social value of distributed generation

Red and Lumo believe that a new retailer funded payment to distributed generation owners for environmental and social benefits will add unnecessary costs with irreconcilable benefits.

Owners of distributed generation are compensated for avoided emissions under the Small-scale Renewable Energy Scheme (SRES). The SRES contributes to the Renewable Energy Target's objective of reducing emissions of greenhouse gases in the electricity sector. We are not convinced that just because the relevant Commonwealth legislation does not make explicit that SRES payments are exclusively for avoided emissions that they should be disregarded when considering whether to compensate Victorian distributed generation owners for an environmental benefit. On this basis, we consider this recommendation to be unjustified.

Opt in

Should the Commission decide to implement time and location based FIT's in line with its proposal, we would request that it is not mandated. Retailers should have the choice whether or not to offer a more granular tariff to consumers, or allow consumers to stay on the current mandated flat FIT that applies in Victoria today.

Given the competitiveness of the Victorian market, we expect that if there be a demand for this type of product, retailers will adapt to offer consumers the more granular time and location based pricing they desire.

Red and Lumo thank the Commission for the opportunity to respond to this consultation. Should you have any further enquiries regarding this submission, please call Con Noutso, Regulatory Manager

Yours sincerely

Ramy Soussou

General Manager Regulatory Affairs & Stakeholder Relations

Red Energy Pty Ltd

Lumo Energy Australia Pty Ltd