22 April 2016

Angus Bruce
Essential Services Commission of South Australia
GPO Box 2605
Adelaide SA 5001

Lodged by email: escosa@escosa.sa.gov.au

Dear Mr Bruce,

RE: Review of the South Australian electricity retailer feed-in tariff – Issues Paper

Origin welcomes the opportunity to respond to the Essential Services Commission of South Australia's (the Commission) Issues Paper on the Review of the South Australian electricity retailer feed-in tariff.

We have long advocated for the introduction of deregulated feed-in tariffs in competitive retail markets like South Australia.[1] Evidence from other states suggests that the market can be left to deliver a range of offers for solar PV customers and there is no reason to believe that this won't be the case in South Australia given the large number of residential customers with solar PV. In Origin's view, deregulation of the retailer feed-in tariff will benefit consumers through better competition and product innovation.

We address the questions raised by the Commission in more detail below.

Is the solar PV segment of the electricity market competitive in South Australia, in your view? Why or why not?

Origin believes that the South Australian solar feed-in tariff market is effectively competitive and that mandatory regulation of the retailer feed-in tariff is unnecessary in an otherwise deregulated retail electricity market. In Origin's view, governments do not need a solar export pricing policy where effective competition exists in their retail electricity market for feed-in tariffs. Price regulation is not as effective at determining efficient and fair prices as an effectively competitive market is. There is no compelling reason to set policy parameters for the regulation of the value of solar energy where the market is working to offer customers a range of feed-in tariffs. This reflects the situation in South Australia where over 28% of customers have installed rooftop solar PV systems.[2] We note that the Queensland market, with only marginally more customers in percentage terms than South Australia, has a competitive deregulated feed-in tariff market in the south east segment. As the New South Wales Independent Pricing and Regulatory Tribunal (IPART) has noted in the context of the NSW feed-in tariff market:

> *[In] a competitive market any retailer (regardless of whether it is a gentailer or not) has an incentive to offer a fair price for a customers' PV exports. If it doesn't offer a fair price for PV exports, then it risks losing these customers to competitors and having to pay the same, or a higher price, to someone else for that electricity.*[3]

In both South Australia and south east Queensland, retailers risk losing a significant share of the market if they do not make available reasonable retailer feed-in tariff offers. The incentive for retailers

---

[1] See for instance Origin's submission to the 2014 Retailer feed-in-tariff determination: http://www.escosa.sa.gov.au/library/2014111-RetailerFiTDraftPriceDeterminationSubmission-OriginEnergy.pdf

[2] Australian PV Institute. Accessed here: http://pv-map.apvi.org.au/historical#4/-26.67/134.12

[3] Independent Pricing and Regulatory Tribunal, *Draft Report: The subsidy-free value of electricity from small-scale solar PV units from 1 July 2014*, April 2014, p.10.

Origin Energy Limited ABN 30 000 051 696 • Level 45, Australia Square, 264-278 George Street Sydney NSW 2000
GPO Box 5376, Sydney NSW 2001 • Telephone (02) 8345 5000 • Facsimile (02) 9252 9244 • www.originenergy.com.au

to offer a competitive retailer feed-in tariff will only continue to rise along with the anticipated increase in PV installations.

The spread of offers in South Australia is analogous south east Queensland. In south east Queensland, there is a spread of retailer offers from 4-11 cents/kWh, a diversity that indicates healthy competition among retailers; in South Australia, there are presently fourteen retailers offering retailer feed-in tariffs from the minimum of 6.8 cents/kWh to 12 cents/kWh. In the past, the Commission has indicated a lack of satisfaction with the range of offers available but this is evidently no longer the case in South Australia, where there are five different rates available. In any event, we believe that a mandated minimum price may artificially limit the diversity of offers because it creates a focal point around which the market converges. Deregulation of the retailer feed-in tariff is likely to introduce more competition and greater incentives to promote greater offer diversity. Despite the current regulation of the retailer feed-in tariff, the market has reached a level of effective competition that would benefit from further deregulation.

The level of the feed-in tariff is only one element for customers to consider when choosing a retailer. Some customers may place a high store of value on the level of a feed-in tariff, while others with solar PV may emphasise a preference for other features of energy products (such as a discount or fixed pricing for their energy supply). The Commission may be concerned that retailers, in a deregulated market, might offer consumers a rate that is lower than what might have been the mandated minimum. However, a retailer in these circumstances may choose to offer customers a low feed-in-tariff in conjunction with highly competitive electricity tariffs and discounts. A customer in South Australia that uses, rather than exports, most of its electricity would in fact benefit from this if a retailer is offering a lower electricity tariff and/or higher discount than the general market. Retailers may benefit from purchasing the solar electricity at a lower than expected rate but equally if the customer does not export much energy then they benefit from the low electricity tariffs. This option is presently not available to South Australian customers as the mandated minimum constrains the ability of retailers to set their own minimum rate that is offset by a competitive electricity tariff. Accordingly, regulating feed-in tariffs restricts retailers from offering competitive products to their customers.

As such, customer valuation of the level of a feed-in tariff will vary according to these preferences. Regulating a minimum feed-in tariff constrains the ability of retailers to innovate and may create a sub-optimal price ceiling for some customers seeking to export electricity to the grid. Additionally, a retailer may wish to propose a time varying feed-in tariff to distinguish itself from its competitors, but they will be constrained in setting such tariffs by the mandated minimum rate exceeding the value of solar PV at certain times. These unintended consequences arise as a result of regulation in otherwise competitive markets.

Government intervention in the retail electricity market to mandate a minimum-feed-in tariff may also stifle competition by acting as a barrier to entry for new retailers; this in turn may restrict the overall availability and quality of products offered. For instance, a small retailer may wish to enter a market and compete for customers without solar PV by offering attractive prices for their general tariffs to non-solar customers. As IPART has stated in a solar feed-in tariff determination:

> *"In our view, a competitive market is the best way to provide the fair value for PV exports, and the market should determine the fair value of PV exports through competition. We consider that mandating minimum feed-in tariffs will lead to fewer offers that consumers can choose from and less incentive for retailers to innovate…. Mandating minimum feed-in tariffs will also not guarantee that PV customers will be better off … because feed-in tariffs are only one component of a retailer's market offer."*[4]

[4] Independent Pricing and Regulatory Tribunal, *Final report- Solar feed-in-tariffs- The subsidy free value of electricity from small scale solar PV units from 1 July 2014*, 16 June 2014, p. 9.

The market for solar customers has evolved over the last two years to include new product offerings and finance models. For instance, Origin offers customers the choice to purchase solar systems upfront or to consider our “Solar as a Service” product where customers are offered a solar power purchase agreement for a defined contract period. These products are further evidence of a competitive retail market. It is also important to consider how regulation of feed-in tariffs might restrict product development; regulated pricing introduces risk for retailers because they cannot control the minimum price for exporting solar. For instance, a small retailer may wish to enter a market and compete for customers without solar PV by offering attractive prices for their general tariffs to non-solar customers. The introduction of a mandated minimum feed-in tariff will act as a disincentive to such new entrants and may decrease the value proposition of their non-solar products by increasing the cost of the feed-in tariff. Similarly, an alternative energy seller may not agree with the prescribed minimum feed-in tariff and decline to enter that market. Accordingly, mandated minimum feed-in tariffs may raise market barriers to entry, for both retailers and alternative energy sellers, at a time where solar energy markets are undergoing significant change with new products and technologies increasingly in the market.

Commission objectives not promoted by continued regulation of R-FIT

Under the *Electricity Act 1996,* the Commission is granted a discretion whether it will make a price determination for the R-FIT. In assessing whether to make a determination, the Commission must consider its objectives under section 6 of the *Essential Services Act 2002*. The primary objective of the Commission under section 6(a) is the “protection of the long term interests of South Australian consumers with respect to the price, quality and reliability of *essential services*.”[5] Whilst the supply of electricity to customers constitutes an essential service, Origin would argue that the decision to install a rooftop solar PV system does not. A residential solar PV system is an addition to the essential service of supplying electricity. The regulation of this service does not actually assist the Commission with meeting its primary objective under section 6(a).

Furthermore, as the table below indicates, continuing to regulate the R-FIT does not assist the Commission with meeting its additional objectives under the section 6(b) of the Act.

Objective of ESCOSA	**Impact of regulated R-FIT**
Promote competitive and fair market conduct.	Limits ability of firms to compete by mandating a minimum price.
Prevent misuse of monopoly or market power.	No evidence of monopolies forming in the market.
Facilitate entry into relevant markets.	Mandated feed-in tariffs create a barrier to entry for smaller retailers; if the rate is set higher than the efficient cost then they may find it difficult to meet those obligations to customers.
Promote economic efficiency.	Efficiency is limited because the market is not allowed to set the most efficient price for solar power.
Ensure consumers benefit from competition and efficiency.	Reduces competition and economic efficiency; if feed-in tariff is set too low then consumers are underpaid, and if set too high then all consumers pay cost through higher electricity tariffs.

[5] Emphasis added.

Objective of ESCOSA	Impact of regulated R-FIT
Facilitate maintenance of the financial viability of regulated industries and the incentive for long term investment.	Regulatory burden does not encourage long term investment by retailers (particularly new entrants) and does not make the industry more viable.
Promote consistency in regulation with other jurisdictions.	The direction of policy in feed-in tariffs, and energy more broadly, is towards deregulation of price controls and feed-in tariffs.

Is the methodology proposed by the Commission appropriate for assessing the level of competition in the market appropriate?

Switching rates

In its feed-in-tariff determination for 2015-16, the Commission provided data that demonstrated lower switching rates for PV customers compared with non-PV customers.[6] Although switching rates are a useful barometer of competition in the broader energy market, in Origin's view this is not necessarily the case with respect to solar PV customers. For those customers who do not have access to the Distribution feed-in tariff (D-FIT), the overwhelming economic benefit of installing a PV unit is the avoided cost of purchasing energy from their retailer. Customers are better off consuming the energy they generate from their panels because it is cheaper than purchasing it from their grid supplier. Indeed, the growing Solar Power Purchase Agreement market is predicated on the customers purchasing energy from the solar system when it is generating electricity, rather than from their grid-supplied retailer. This reduction in energy use generally leads to an overall lower bill for consumers, diminishing their incentive to switch retailers. The incentive is especially diminished for the customers on Class 1 and Class 2 D-FITs, where rates of 44 cents/kWh and 16 cents/kWh can entirely negate a customer's energy bills.

Furthermore, customers are more likely to switch retailers for reasons other than the price they receive for their exported solar energy. The level of the feed-in tariff is only one element for customers to consider when choosing a retailer. For customers on a retailer feed-in tariff, other features of energy products, such as a discount or fixed pricing for their energy supply, are likely to rate as higher considerations for choosing their retailer. A retailer may offer the highest feed-in tariff in the market but this does not mean that customers are better-off switching to them if their competitors have more favourable rates or discounts.

Incidence of minimum payments

Origin presently offers the mandated minimum feed-in tariff rate to customers. We note that the largest retailer in the state also offers the minimum rate. The Commission would be wrong to conclude that this reflects an absence of effective competition in the market for two reasons: firstly, because other retailers offer higher rates that customers may switch to if they place such a high value on their feed-in tariffs; secondly, a mandated minimum signals to the market what a fair price is, and retailers tend to cluster around that value accordingly.

Incidence of Market Offers to PV customers

Origin offers its market solar customers the same tariffs and discounts that it offers to its non-solar customers.

[6] Essential Services Commission of South Australia, *2015-2016 Retailer Feed-in Tariff Final Price Determination: Statement of Reasons*, December 2014, p. 37.

Evidence from other jurisdictions

As the Commission is aware, both New South Wales and Queensland have feed-in tariffs that are set by the market rather than regulation. The Queensland Productivity Commission (QPC) recently affirmed this preference in its Draft Report to the Queensland Government on solar feed-in pricing.[7] As we discuss above, Origin believes that the south east Queensland market is analogous to South Australia insofar as there is a wide range of prices offered by a similar number of retailers; in each market, most customers belong to the largest two retailers, but competition is still strong due to the different price levels offered by retailers.[8] Switching rates and the level of customers on market offers are also similar in each retail electricity market.[9] If anything, the south east Queensland market has a broader scope of offers to feed-in tariff customers, which we would attribute to the fact that they are not regulated. After all, prices remain regulated in the broader south east Queensland market, and we would expect competition to increase once deregulation is aligned in both markets. Similarly, we would expect South Australian customers to benefit in terms of choice if the Commission decided to align deregulation in the retail electricity market with feed-in tariffs.

Do electricity retailers differentiate electricity prices charged to solar and non-solar customers? Does the setting of a minimum RFiT incentivise such behaviour?

Origin does not differentiate its electricity tariffs between solar and non-solar customers. Whilst our new Predictable Plan product is not available to solar customers, it is different to most other energy plans insofar as it does not bill customers according to a kilowatt per hour tariff for their electricity consumption. Where customers are on kilowatt per hour tariffs, solar customers have access to the same electricity offers as non-solar customers. Hence, Origin offers its market solar customers the same tariffs and discounts that it offers to its non-solar customers.

A minimum feed-in tariff could impose additional costs on retailers where the regulated value exceeds the market wholesale cost of that electricity. In that situation, retailers would have to make their own decisions about how they recover the costs associated with an excessive regulated feed-in tariff. In theory, these costs could be recovered directly from those solar customers, or they would be recovered through general retail tariffs available to all customers. In these hypothetical circumstances, this is a commercial decision for each retailer to determine how they will recover their costs.

Are the costs and obligations of an electricity retailer any different between servicing solar customers and non-solar customers? If yes, is there any evidence to support this?

An additional cost to service may not necessarily arise as a consequence of solar customers but the regulatory risk introduced by mandated minimum prices. If solar customers do cost more than other customers—for instance, if they were to file additional ombudsman complaints or contact a retailer more frequently—then these costs would, like any other customer class, need to be recovered through either the general tariff or feed-in tariffs. This is a commercial decision for retailers to make. We note that unlike in the general electricity market, which is deregulated, retailers may be constrained in recovering costs due to the mandated minimum feed-in tariff.

Are there any other matters the Commission should consider?

The Commission is proposing to consider whether the benefits of regulation exceed its costs. Origin agrees that this is a necessary step. However, it is not clear to Origin what the case is for continued regulation of the retailer feed-in tariff; regulation may be the status quo position in South Australia but it does not follow that a need to intervene in the market still exists. Whilst the Commission is correct to assess whether there is effective competition in the market before making a decision to deregulate, it equally needs to consider whether continued regulation is justified. Hypothetically, if the Commission

[7] Queensland Productivity Commission, *Draft report: Solar feed-in pricing in Queensland*, March 2016.
[8] Ibid, p. 47.
[9] Australian Energy Market Commission, *2015 Retail Competition Review*, June 2015, pp. 242 and 254.

concluded that competition was not effective in the feed-in tariff market, it does not necessarily follow that regulation is the most effective solution for generating the necessary levels of competition or for guaranteeing that consumers receive a fair value for their exported solar energy.

As the state of the South Australian market following retail price regulation demonstrates, removing mandated levels of pricing injects additional competition into the market. Since retail prices were deregulated in South Australia, tier two retailers have increased their market share, new retailers have entered the market, customer satisfaction rose and ombudsman complaints have fallen.[10] Price deregulation has improved customer outcomes and we would expect the same to occur if mandated minimum retailer feed-in tariffs ceased to be regulated. Origin believes that if the Commission were to conclude that the South Australian feed-in tariff had not reached the threshold of “effective competition”, but acknowledged that there was still a reasonable level of competition in the market, then they should consider whether deregulation would in fact generate additional competition that would be in the long-term interest of consumers. In these circumstances, we would anticipate that the costs of regulation outweigh the benefits, even if competition was not effective.

Closing

Origin would be pleased to discuss any matters raised within this response with the Commission. Please contact Timothy Wilson (Retail Regulatory Analyst) in the first instance on (03) 8665 7155.

Yours sincerely

Keith Robertson
Manager, Wholesale and Retail Regulatory Policy
(02) 9503 5674 Keith.Robertson@Originenergy.com.au

[10] Australian Energy Market Commission, *2015 Retail Competition Review*, June 2015, p. 192.