



30 October 2014

Con Carellas
Essential Service Commission of South Australia
GPO Box 2605
Adelaide SA 5001

Via online lodgement

Dear Mr Carellas,

2015-2016 Retailer Feed-in-Tariff- Draft Price Determination

Origin Energy (Origin) welcomes this opportunity to respond to the Essential Service Commission of South Australia's (the Commission) draft price determination on the 2015-2016 Retailer Feed-in-Tariff (R-FIT).

Mandated feed-in-tariff

Effective competition in the market for R-FIT

Origin believes that the South Australian solar feed-in-tariff market is effectively competitive and that mandatory regulation of the R-FIT is unnecessary in an otherwise deregulated market. 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.¹

This reflects the situation in South Australia where nearly a quarter of customers have installed rooftop solar PV systems. Retailers risk losing a significant share of the market if they do not make available reasonable R-FIT offers. The incentive for retailers to offer a competitive R-FIT will only continue to rise along with the anticipated increase in PV installations.

The Commission notes that nine of the thirteen retailers only offer the R-FIT at the mandated minimum and concludes that there is a lack of effective competition in the market. Rather than being a symptom of insufficient competition, the mandated minimum price tends to create a focal point around which offers in the market converge. Deregulation of the R-FIT is likely to introduce more competition and greater incentives to promote greater offer diversity. As IPART stated in its recent 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."²

¹ 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.

² 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.

Despite the current regulation of the R-FIT, the market has reached a level of effective competition that would benefit from further deregulation. The Commission highlights the fact that AGL offers a R-FIT of 8 cents per kWh as part of a strategy to distinguish itself to customers from other retailers. The Commission minimises the significance of this and suggests that it represents a mere marketing strategy rather than a retailer opting to pay the full value of the exported solar energy. However, without the competition that has been engendered by full retail contestability and price deregulation there would be less incentive for AGL to offer a higher rate. In Origin’s view, the fact that the biggest retailer in the state has opted to offer a higher rate – regardless of the reason - highlights the maturity of South Australia’s energy market and the potential for further competition should the R-FIT be deregulated.

Switching rates of solar PV customers not right measure for market competition

In its analysis of market competition, the Commission over-emphasises the switching rates for solar PV customers. Although switching rates are a useful barometer of competition in the broader energy market, this is not necessarily the case with respect to solar PV customers. For those customers who do not receive the benefit of a Distribution feed-in-tariff (D-FIT), the overwhelming economic benefit for customers installing a PV unit is the reduced need to draw on energy from the grid. 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 bill.

Commission objectives not promoted by continued regulation of R-FIT

Under the *Electricity Act*, 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.”³ 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 or suggestion 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.

³ Emphasis added.

Objective of ESCOSA	Impact of regulated R-FIT
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.
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.

Encourage review of decision to regulate the R-FIT for both 2015 and 2016

We therefore ask the Commission to reconsider its draft decision to regulate the R-FIT for 2015. There is effective competition in the South Australian market and removing regulation of the R-FIT could only support the increased availability of different offers for solar PV customers. It would also assist with maintaining competition in the otherwise deregulated retail energy market, as a layer of regulation in the R-FIT only acts to stifle innovation in the products that retailers can offer.

Should the Commission decide to continue regulation for the next calendar year, then Origin encourages the Commission to reconsider its decision to regulate prices for 2016 also. The Commission intends to continue its price monitoring role. It will be in a position to use this data to assess the state of the market and the ongoing need for regulation next year rather than waiting two years. Given the benefits from moving to a deregulated market, there is merit providing for that review and decision sooner rather than later.

Method for determining the R-FIT

In essence, ACIL Allen's view "is that the value to a retailer of exported PV output is:

1. *the wholesale spot price of electricity projected using PowerMark as described in section 4.1*
2. *weighted by the net system load profile projected using the process in 4.2*
3. *adjusted for network losses*
4. *adjusted for market and ancillary service fees."*⁴

Whilst Origin accepts the third and fourth factors above, which are consistent with other state regulators, we have concerns with the method applied under the first and second factors.

Forecasting spot prices

ACIL Allen develops a spot price forecast to determine the value of exported solar power. The mechanics of this price forecast lack transparency and are dependent entirely upon the consultant's knowledge and skill in determining input parameters. In regulatory decisions that rely upon modelling results it is important that the inputs and the sensitivity of results are explained and open to stakeholder comment. While an outline of ACIL's methodology has been provided Origin is unable to comment on the inputs as these have not been provided. In Origin's view, given that there is a forward market traded by retailers, to forecast spot prices it would be more appropriate to use baseload swap electricity contracts as traded on the ASX (adjusting for any price differential in historical prices for the

⁴ ACIL Allen, *A Report to the South Australian Essential Services Commission: The Fair and Reasonable Value of Exported PV Output*, 2014, p. 16.

repeat of the carbon price). This is the approach undertaken to assess the "Market value of solar PV exports" by Frontier Economics who were engaged by IPART to determine the NSW solar feed in tariff.⁵

Method of weighing pool prices

Under ACIL Allen's methodology, the wholesale spot price of electricity is weighted by the Net System Load Profile (NSLP). This is the load shape of small customers without interval meters. In Origin's view, it would be more appropriate to weigh the pool prices by the solar PV export profile. This would reflect the volume weighted price captured by solar exports. Again this approach is undertaken in the "Market value of solar PV exports" as prepared by Frontier Economics who were engaged by IPART to determine the NSW solar feed in tariff.⁶ In Origin's view, ACIL Allen's approach risks overstating the volatility in the average spot price that is used in the NSLP. Our understanding is that high price events outside the profile of solar generation might be weighted up, increasing the estimate avoided costs of retailers. Origin would welcome the opportunity to explore this element of the analysis further ahead of the final determination.

Price-monitoring

Origin will continue to support the use of publicly available information in order to monitor market developments in the R-FIT and competition for solar PV customers generally. We hope that this information will ultimately assist the Commission in its decision to allow a market-based determination of the R-FIT.

Timing of the determination

We note that last year the Commission advised stakeholders of its final decision for 1 January 2014 on 17 December 2013. We would appreciate it if the Commission could make its decision earlier to provide retailers with an adequate amount of time to update necessary procedures prior to 1 January. A decision by 5 December 2014 would be appreciated.

Closing

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

Yours sincerely

David Calder
Regulatory Strategy Manager
(03) 8665 7712 David.Calder@Originenergy.com.au

⁵ Frontier Economics, *Market value of solar PV0020exports: A final report prepared for IPART*, June 2014, p. 15.

⁶ *Ibid*, pp. 7-8.