



23 September 2011

Determination of Solar Feed-in Tariff Premium
Essential Services Commission of SA
GPO Box 2605
Adelaide SA 5001

Lodged (by email/online): escosa@escosa.sa.gov.au

ESCOSA's Determination of Solar Feed-in Tariff Premium Issues Paper

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Essential Services Commission of South Australia's (ESCOSA) Issues Paper on the determination of a solar feed-in tariff (FIT) Premium in South Australia.

esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of over 40 electricity and downstream natural gas businesses. These businesses own and operate some \$120 billion in assets, employ over 52,000 people and contribute \$16 billion directly to the nation's Gross Domestic Product.

esaa is fuel and technology neutral and has therefore consistently argued against the introduction of FITs that provide a significant and arbitrary premium over the economic value of the energy supplied after accounting for any avoided costs. Many of the FITs introduced by states and territories over the past few years have been at excessive rates which has led to dramatically quick rates of uptake and put pressure on electricity networks to maintain voltage levels.

The Parliament of South Australia has recently enacted legislation to change the feed-in tariff scheme. The new scheme has been introduced via the Electricity (Miscellaneous) Amendment Bill 2011. As a result, ESCOSA is now required to determine an amount (the FIT Premium) for all retailers to pay consumers with eligible solar photovoltaic (PV) generators. This amount is intended to reflect the fair and reasonable value to a retailer of electricity fed into the network.

Benefits of a light-handed approach

It is unfortunate that the terms of reference for this review are so narrow and that ESCOSA is required to establish a fixed value for electricity generated by solar PV and exported to the grid. The Association argues that there are a variety of issues that could otherwise be considered in determining a FIT.

esaa notes that the Independent Pricing and Regulatory Tribunal of New South Wales is also undertaking a review of FITs for electricity generated by solar PV that

will consider other ways to implement a FIT in NSW than just setting a mandatory price. esaa considers that a similar process could also be of benefit to South Australia.

Establishing a fixed, FIT Premium results in a series of risks that otherwise could be avoided by using a light-handed approach which allows for consumers and retailers to negotiate a fair value rather than one being imposed on both. esaa contends that ESCOSA should be allowed to consider alternative mechanisms that act as a guide for consumers and retailers. Mechanisms such as a benchmark price, or a benchmark range could be used in order to provide information to consumers, while providing for active competition and minimising risks. By avoiding a highly prescriptive mandatory tariff for electricity generated by residential solar PV, retailers can offer a range of products that best suit customers, rather than relying on ESCOSA to provide a 'one size fits all' tariff.

Risks of a high or low FIT Premium

Setting the FIT Premium too high risks forcing retailers to pay above what is a fair and reasonable value for electricity generated by solar PV. This could disadvantage retailers who are forced to pay more than a fair price, as well as consumers who may then be faced with reduced competition in the retail electricity market if retailers do not wish to take on customers with solar PV. The costs faced by retailers through a FIT set too high would presumably be passed on to all of that retailer's consumers.

On the other hand, setting a FIT Premium "too low" simply creates a floor price for solar PV energy. Setting a relatively low FIT Premium could, in fact, have advantages. If retailers are able to price solar PV generation above the FIT, then competition in the sector could intensify as retailers actively seek and compete for customers with solar PV.

In this way ESCOSA would be taking a light-handed approach to setting a FIT Premium for customers. This would allow for greater flexibility for both retailers and customers, and the market may update prices as regularly as it needs to, without waiting for the intervention of an external agency through regular reviews. Retailers would also have the opportunity to develop products and services specifically tailored to customers rather than relying on a one-size-fits-all approach. This could negate the need for ESCOSA to determine different prices for different customers, and result in a more efficient outcome for retailers and consumers.

Setting a price

A variety of factors need to be considered when establishing a fair and reasonable value for a solar PV FIT Premium, noting that the asymmetric risks described above suggest erring on the side of a lower rather than higher price. This could be done by assessing the financial gain to retailers if there were no FIT Premium or the wholesale market value of the electricity customers with PV export to the grid. The costs of solar PV on electricity networks should also be considered when determining a value for the electricity generated by solar PV and exported to the grid.

ESCOSA poses the question as to how the variability in the value of energy should be reflected in setting a FIT Premium. As the Issues Paper notes, there is little

correlation between peak solar PV output and peak electricity demand. Solar PV output peaks around noon while residential demand tends to peak at around 6-8pm. Household PV may therefore have limited impact on mitigating peak demand from a distribution network perspective. So the value is likely to come mostly from the wholesale value of electricity at the time of PV output.

Another issue to consider in setting a FIT Premium based on peak prices is that it may not be appropriate to value such electricity at peak rates when most customers in SA pay flat-rate tariffs for electricity consumed from the grid. Mixing and matching a peaking profile for export with flat import tariffs may create a distorted set of incentives for customers. The reverse may also be true.

To the extent that the FIT Premium determined by ESCOSA is related to wholesale prices in the National Electricity Market (NEM), changes in wholesale prices could be used to review the level of the FIT Premium periodically. For example this could be done based on the previous year's average price, or a multiple year rolling average could be used to avoid the impacts of extreme prices in any given year. Whatever method is chosen, it is important that it is flexible enough to adjust in line with wholesale price changes

Acknowledging that the value of generation from solar PV is not solely based on wholesale electricity prices, and there are influences from networks to consider, there could be additional components to the FIT calculation, either positive or negative. Such components will in practice be estimates, and it may be preferable to minimise the compliance costs by carrying out periodic reviews of these estimates, rather than annual re-sets.

ESCOSA also asks whether the benefits of solar PV to retailers, in the form of lower overall costs, should be extended to all electricity customers or just those with solar PV systems. It is difficult to make an assessment about this without having details on what this would entail. To the extent that the mechanism for achieving this is to impute a benefit as a lower regulated retail price, this runs the risk of resulting in tariffs that are not cost-reflective. This is particularly so if any perceived benefits are not capable of accurate measurement or their incidence is not the same for all retailers. In any case, if solar PV does in fact reduce loss factors, to take the example used in the Issues Paper, this will be reflected in market offers due to the competitive nature of the market and it will be reflected in the loss factors used in subsequent regulated price determinations. Accordingly no additional action would be required by the regulator.

Conclusion

It is commendable that ESCOSA is undertaking a review to determine a fair and reasonable FIT Premium for electricity generated by solar PV. Many state and territory feed-in-tariffs have been overly generous, resulting in fast uptake and, as a result, the premature closure of programs. By carefully designing a FIT Premium which allows the market to determine the value of solar PV generation to retailers, a policy can be implemented which can be of benefit to retailers, networks and consumers.

esaa advocates for ESCOSA to set a FIT Premium which can allow for maximum flexibility for both consumers and retailers. This would reduce the risks of setting a tariff at an inappropriately high level, and could promote competition in the retail sector.

Any questions about our submission should be addressed to Kieran Donoghue, by email to kieran.donoghue@esaa.com.au or by telephone on (03) 9670 0188.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Clare Savage', with a stylized flourish at the end.

Clare Savage
Interim Chief Executive Officer