

CORRECTED VERSION

ECONOMIC, EDUCATION, JOBS AND SKILLS COMMITTEE

Inquiry into community energy projects

Melbourne — 20 March 2017

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Witnesses

Dr Ron Ben-David, Chairperson,

Dr John Hamill, Chief Executive Officer, and

Mr David Young, Director, Energy, Essential Services Commission.

The CHAIR — Welcome to the public hearing for the Economic, Education, Jobs and Skills Committee’s Inquiry into community energy projects. All evidence taken at this hearing is protected by parliamentary privilege. Any comments you make outside the hearing are not afforded such privilege. Hansard is recording today’s proceedings. We will provide a proof version of the Hansard transcript so you can correct any typographical errors. Please state your name before you start and allow us some time for questions.

Dr BEN-DAVID — I am Ron Ben-David. I chair the Essential Services Commission. We are the state’s regulator for energy, but amongst other things we are also the regulator for water, the port and, for the moment, taxi fares. We also administer the state’s Victorian energy efficiency scheme—that is the one where they come round to your house and change your light bulbs—so we do all the back office of that, and we also administer the state government’s local government rate-capping regime. So we have got quite a broad ambit.

In terms of energy, because energy is an essential service there is specific legislation dealing with the supply of energy. Energy suppliers need to be licensed unless they are exempt, and I will explain that in just a moment. We grant licences under the powers provided to us under the state’s legislation, and the conditions of those licences either come directly from the legislation or from us in interpreting that legislation. Our objective is to promote the long-term interests of Victorian consumers, and since the beginning of last year it has also been to promote protections for Victorian consumers, particularly those in payment difficulty. So in developing the conditions of a licence, we take all of that into account.

There are various codes that we administer that outline the obligations of the retailers or distributors in their operations in Victoria, and then we monitor compliance with those obligations and we report on that from time to time—usually once a year, but we are actually moving to reporting more frequently. In fact we have here our first report. When I say our first report, it is the first time we have produced it in this form. We have produced various other reports, but what we have done is we have compiled them all into a single, comprehensive report. So that tells you pretty much everything that we know about the energy market in Victoria. Now, it is a very long document, so do not be terrified by that. It is really the first part of the report, which is probably about 30 pages, which really gives a feel for how the whole thing works. So the previous speaker referred to the costs of distribution, the costs of transmission et cetera. We discuss things like that. I would not inflict the whole report on you, but certainly the first 20 or 30 pages are a good read if you want to get a good understanding of how the market operates in Victoria.

The licensing framework that we administer is a product of its time, and it is a very regimented framework. It assumes the market consists of generators, the power stations; transmission companies—that is the big pylons you see crisscrossing the countryside; distributors, who are the guys who run the poles and wires out here; and then retailers, the people who send you your bill for your energy.

What we have realised in the last few years is that that model is breaking down. The advent of new technology, the emergence of new technology, has allowed new business models to emerge such as community projects, and so our licence framework is looking out of date, and we know that and we have been working on that. In fact in June 2015 we put out an issues paper identifying exactly that issue—that the framework was designed for a 1980s and 1990s view of the market, but the market has changed and is continuing to change, probably at an ever-increasing rate. So we put out a paper, and we discussed some options of how we might go about regulating or licensing energy companies in Victoria. What we proposed was two main things.

The first was that, instead of regulating based on whether someone is classified as a retailer, a distributor, a transmission company or an energy generator, we should stop forcing companies into these very clear-cut categories, because those categories do not work anymore. So instead of forcing you to be a retailer or forcing you to be a distributor, what we would do is produce a licence that said, ‘Right, do you want to deliver these type of activities? You can get a licence for that activity or group of activities’, so it was much more flexible to the different business models that are emerging. I am sure you have started to hear about some of those.

The second thing that we proposed was the introduction of a small-scale licence. So the current licences are—I suppose you would call it—a ‘one size fits all’. If you are a generator, whether you have just got a small plant or a plant the size of Loy Yang, you get the same licence, and so it has got the same conditions attached to it. Again in the modern world that we are now facing we said, ‘Let’s make available small-scale licences’, so licences for a smaller scale of operation without all the regulatory obligations that come with a full-blown licence. That was a way of trying to promote entry into the market, allow people or companies to get established

and, if they grow, then maybe they would move to a full-scale licence, but in the meantime they can operate on a small-scale licence.

As I said, that was about a year and a half ago. We received some submissions, which were generally quite supportive, but what they did not like was the small-scale licence, which I have to admit took me a little by surprise. The main reasons for the push back on the small-scale licence: one argument was, ‘Everyone should have the same level of obligation; it should be an even playing field. Why should a small-scale provider have a lower level of regulatory obligation than a larger provider?’. The second concern was not just the regulatory obligations but the protections from a customer’s point of view—why should a customer with one type of provider have a different level of protection from a customer with a different type of provider? There was also a view that even with the small-scale licence there was too much regulatory obligation, too much regulatory burden, being placed on the licensee. Even though we were trying to make it a lighter touch licence, even that was seen as imposing too much burden.

We have kind of put that project on hold. We are still thinking about it, but we have not actually done anything. Remember how I said you either had to be licensed or exempt from licence? The exemption comes under ministerial order, so it is not something that we control. It is something that is issued by the minister, by the government, and the government is currently reviewing what is called the exemption order—the general exemption order. We are waiting to see where that lands, because depending on where that lands, that will tell us what we are really dealing with as far as the licensing framework going forward.

Mrs FYFFE — We have heard a lot about the national framework and that everything we do is governed by the national framework. What you are talking about and the changes that you are thinking of making, are they not controlled by the national framework?

Dr BEN-DAVID — No.

Mr YOUNG — No. Victoria is completely unique in that we have maintained an obligation for all energy businesses to be licensed, and in addition we impose the conditions of those licences. In the national framework those things are dealt with by different bodies—the AEMC sets the rules and the AER administers them. In Victoria the Commission both sets and administers the rules. Therefore we can adjust the rules as technology evolves and as business models evolve and as the need for consumer protection evolves. That said, some things that we do: when we grant a licence for a distribution business it means that they become subject to the national rules for pricing—for what we call the economic regulation. That is mainly for distribution businesses and the generation sector, so the generation businesses that participate in the national market and the distribution businesses that actually have their prices determined by the Australian Energy Regulator. Once we have licensed them, those economic functions go to the national scheme. The schemes are linked, but there is no duplication: we do the licensing and non-economic regulation and they do the economic regulation.

Dr BEN-DAVID — Unfortunately it is messy and it is confusing...

Mrs FYFFE — We have heard it is very confusing.

Dr BEN-DAVID — It is very confusing, and it takes a while to get your head around it, but at the retail level—the bit that people see; you would get your bills from different power companies—we fully regulate retail in this state. That was never handed over to the national framework. Distribution—they do a bit; we do a bit—but we license them, so if a distributor wants to operate in this state, they have to be licensed.

Just to finish off—I have only got one more point to make in my opening remarks—what we are trying to do with this licence framework review is to promote innovation because we want new business models coming in. We want new ways of delivering services to customers because we want customers to have choice, we want customers to be able to source the power from the sort of companies that they are interested in dealing with and we want competition, because we think competition does drive better outcomes for customers—and I mean genuine competition, not faux competition. We can talk about that. And compliance: we want to make sure that we have got a framework that we can administer and that we can hold companies to account so that they are delivering on their obligations to Victorian consumers. I think I will leave it there for the moment. I am happy to take any questions.

The CHAIR — Doctor, thank you for your contribution. The growth of renewable energy generation has created some challenges for the Commission. How have these challenges been dealt with?

Dr BEN-DAVID — Renewable energy?

The CHAIR — Yes.

Dr BEN-DAVID — Interestingly for us the way we go about licensing a renewable energy company is no different to how we would go about licensing, say, if someone wants to open up a new coal-fired power station or a gas-fired power station—the application process is exactly the same. We apply effectively three tests to any licensee. First, they must demonstrate they have the financial capacity to manage the service. Because running these companies is a complex financial operation, they have to demonstrate to us that they have the financial resources to accommodate the risks involved in their operations. So for renewable energy, for example, say if we are talking wind, the biggest risk is the volatility in the wind. So they have to demonstrate to us that they can manage the risk that there will be times when they are producing a lot of energy and times when they are producing very little energy. So that is financial capacity. The second is technical capacity, so that they have the skills within the company, on the board and in the management, to operate a business of this type. The third is a fit and proper person test, so to make sure that they are the sort of people that we want delivering services to Victorians.

We have a constant stream of licence applications. I do not know how many we have got in the pipeline at the moment, but usually at any time there is probably half a dozen or so. Some we can deal with quite easily, and some take quite a long time, because if we are not satisfied on those things, we do not just say, ‘No—no licence’; we put questions back to them. We always give the companies or the applicants the opportunities to come back with better information and fuller information.

Mr CRISP — I know you are not only dealing with the price but the security of supply. As we move to distributed generation with, in some places, less energy consumed off the grid, how do we maintain the grid going forward in the future?

Dr BEN-DAVID — That is clearly a very, very good and very, very important question. It is one that largely does not fall within our remit. We do not manage the grid in Victoria; that is managed by one of these national bodies, so AEMO—the Australian Energy Market Operator—is responsible for making sure energy gets from where it is produced to where it is needed. We do not really have a role there. Having said that, we have just completed a review for the Government, and that review is scheduled to be released sometime in the next week or two, on distributed generation: how small-scale distributed generators can participate in the market more readily, because for now if you are a small-scale generator, you can get paid a feed-in tariff—which we also set, by the way—but distributed generators can provide services other than just the power they produce. They can provide support services for the network operators to keep the network stable, but they have got no way to sell those services at the moment. So what this report does is highlight what those services are and talks about how a market could be established, but it will be up to the Government to respond to that as to how they want to take that work forward.

Dr HAMILL — They are the sorts of services that are provided already at a transmission level, but what the new technologies create is the potential for smaller scale if you aggregate it or if you operate it in the right way to begin to provide similar sorts of services. That is where that kind of sits. Really the point I was making was that they are the kinds of services to the network that are already provided at a larger scale level, at the transmission level, but because of the new nature of technology, the ability to manage information more smartly becomes more possible at a smaller scale level.

Mr CRISP — That will need new network control mechanisms in order to realise that value. Have you given that any consideration?

Dr BEN-DAVID — No. Again this is where it gets so confusing. Traditionally the way that distribution companies worked was: ‘We’ve got demand or we’ve got risks to manage, so let’s go build a bit more infrastructure’, and they would build up what is called their regulatory asset base and they would just build things. What they are now required to do is not only look at what can you build, but what other options have you got to manage that which might be cheaper.

This whole ability to buy services from small-scale operators is something that we are keen to make available to those distribution companies when they are looking at how to manage the network, particularly the unreliability issues because of renewable energy coming in and out. So there are large operators, as John said, in the field that provide these services, but not small-scale operators, and what the Government was asking us to do was say, ‘How can you get small-scale operators to participate in this market?’.

Dr HAMILL — There is some debate as to whether you need a system operator at the distribution level in a range of jurisdictions at the moment, but I do not think that issue has at all been resolved as to whether it is really necessary or not.

Mr CRISP — The \$64 question at the end now: is a target the best method of achieving it or do you allow the market to develop up these distributed renewable services out there according to market dictates or should you set targets and force it?

Dr BEN-DAVID — Maybe David and John disagree, but I do not think targets serve the purpose, because this is about saying, ‘How do you keep the network stable?’. So you might get a fluctuation because suddenly wind comes in or wind drops out, or we saw what happened in South Australia, when the system became unstable, so these are the services to create stability. That stability has to come in when it is needed. It is not a matter of having a target. For the actual energy produced, there could be a target. For example, in the renewable energy target there is a quantum of energy that is being pursued, but that is meeting a different objective if you like.

Mr YOUNG — So what we found was that the value of distributed generation varies geographically considerably in different parts of the state. It varies across the times of day significantly, and it also varies from year to year, which does not really make it suitable for a statewide target. It is something that has to be looked at at the network level, at what we call the substation level or below. I did note that your previous speaker had on the slide there the absence of information or insufficient access to information about the way the network operates. We would certainly concur with that, and our inquiry itself was limited by the lack of information available in the public domain. So there is certainly a view that if you are going to allow a market to operate in the areas of Victoria in which it is needed, it is going to need to be supported by proper and reliable information about that network and about the constraints and about the voltage variation and all of the technical stuff that no doubt you have heard lots about.

Mrs FYFFE — Battery storage is something that is beginning to bother me now during this inquiry. How will household battery storage affect the Victorian energy industry and consumers, and will the commission be overseeing the regulation of battery storage? I see us moving down a path where you will have a greenfield housing estate of 250 houses—solar, battery storage; you end up with a mini power station. How is that going to be overseen and regulated?

Dr BEN-DAVID — That is something we are basically learning, and one of the things in terms of the distributed generation review that we are thinking about is the role of trials and pilots. Because this is all so new, we are all trying to work out how it is going to work. But you are absolutely right—batteries will have the potential to revolutionise the way the whole system works and the way people engage with energy.

For us one of the challenging issues is: an electron is an electron, so whether you charge up your battery using your solar energy source or your mains, does that affect the feed-in tariff you should get when you release that energy? In some states in the US, you know, once you install a battery you are no longer eligible for a feed-in tariff, because if the purpose of a feed-in tariff is to promote solar but you cannot be assured the current coming out of a battery originated with solar, the easiest way to do it is to say, ‘You’ve got a battery; you’re not eligible anymore’. But that is a matter for policy; it is not a matter for the regulator to decide. So that will be something for Government and the Department to work out.

Mr MELHEM — What changes to legislation may be required to encourage community energy projects? I know you talked about the paper you are releasing next week or the week after, so what would be your thoughts on any changes you would like, particularly to protect consumers?

Mr YOUNG — There are some important aspects of what we have covered already. If I just pick up on something Ron said earlier, the Government decides which technologies are covered by the feed-in tariff. At the moment it has only applied it to solar. The existing legislation would allow the Government to decide that

battery storage should be included as well, and it can also issue us with guidance as to methodologies that we might need to use to be able to calculate properly the value of that battery storage.

So in a sense what I am suggesting there is that some things may not need any legislative change because the machinery is already in place. I would also say that there are many things that are not good about our licensing framework, but the legislation that sits above it is actually very flexible. It allows for regulation of energy supply end to end. It does not prescribe the form of organisation, the technology or any of those sorts of things, so it is actually quite a flexible piece of legislation.

We could already license battery storage, and in fact in one particular case we already have—so a partnership between a small retailer with 20 customers that we licensed, working with United Energy to pilot, as Ron said, solar battery storage and control systems to allow that to feed into the grid.

So in a sense the legislative framework is actually pretty robust in lots of ways in Victoria, and in particular, going back to my earlier point, because we have the capacity to evolve the rules as we need to, unlike in the national jurisdiction.

One last quick point I would come back to is this issue about information: the requirement and the need to ensure that the market is informed about the network constraints and the opportunities that might be available for people to supply distributed generation to assist with those constraints.

Dr BEN-DAVID — A customer usually receives, but when a customer puts a solar panel on their roof and starts exporting energy or any other services, we are very concerned that their protections as a customer do not change, because suddenly they are a producer. You have may have heard this awful term, ‘prosumer’.

Mrs FYFFE — No.

Dr BEN-DAVID — None of you know ‘prosumer’?

Mrs FYFFE — It does not sound like an English word.

Dr BEN-DAVID — Exactly right. I am the son of an English teacher; I cannot stand it. So it is someone who is both a consumer and a producer. What we are saying is that in the future market we are going to have a lot of people who are both consumers and producers, and we want to ensure that by becoming a prosumer—pardon me—they do not lose their protections when they are operating as a consumer. That is something that we think is really very, very important.

Mr CRISP — I am seeking your thoughts on how to protect low-income earners against price rises in energy going forward.

Dr BEN-DAVID — I wish I was smart enough to have the answer for that one. We are currently doing a very large piece of work on what we call the payment difficulty framework, or the old name is hardship. We started this project in the middle of 2014. We did an inquiry into: is it working or is it not working? We came to the conclusion it was not working very well at all, and we made some recommendations to Government about a way forward. The Government said to us, ‘Get on and do it’, and that is what we have been working on. Now, that does not go to controlling prices; we do not have any role in controlling price. But it is saying: what must retailers do...

Mr CRISP — But you must have some because you control the price of the feed-in tariff.

Dr BEN-DAVID — It is the only price we control. When you get your bill from your energy company, we have no control over that price; it is completely set by the market. But what we do control are the processes that they must go through to assist customers. That is what we are working on.

Mrs FYFFE — And that is in here. You have got tables in here, have you not?

Dr BEN-DAVID — I think it cracks a mention in there, but it is not detailed in there. It is a whole inquiry.

The CHAIR — I take it that this copy has been tabled. Is that correct?

Dr BEN-DAVID — Yes.

Dr HAMILL — The other thing we do indirectly is providing for innovative models for the supply of energy in the retail sector. Through the licensing mechanism you create potential lower cost models coming into the market, but it is a very indirect way—it is not primarily the influence on prices, but it has that potential benefit.

Dr BEN-DAVID — That is why I said one of the reasons for that licence framework is to allow innovation, to promote innovation, because as John said, we would like innovation to deliver lower cost models of production. But we might be waiting a while.

Mr CRISP — Because of time constraints, can you send us a little bit on your rationale for the 11.3? Could you send that to the Committee?

Dr BEN-DAVID — Sure. Just a couple of pages?

Mr CRISP — Thank you. Yes.

Mrs FYFFE — Of the feed-in tariff.

The CHAIR — Gentlemen, on behalf of the Committee, I would like to thank you for your time and contribution. Thank you very much.

Dr BEN-DAVID — Thank you for the invitation.

Witnesses withdrew.