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Economic Regulation Authority
PO Box 8469
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Dear sir or madam

INQUIRY INTO REFORM OF BUSINESS LICENSING IN WESTERN AUSTRALIA

Synergy welcomes the opportunity given by the Economic Regulation Authority (**ERA**) to participate in the above inquiry. As Western Australia's largest licensed generator and energy retailer Synergy has a strong interest in licensing frameworks and arrangements. In response to the various matters the ERA has requested feedback, Synergy advises as follows:

1. What are the priority areas for reform of business licensing in Western Australia? Why? What effects do they have on you? What reforms would you recommend?

Repeal of electricity generation licences

The Public Utilities Office (**PUO**) in 2015 advocated amendments to the *Electricity Industry Act 2004 (Act)* to repeal the requirement for generation licences. In December 2015 the PUO published its consultation paper outlining a proposal to remove section 7(1) from the Act that imposed a requirement on those who construct and/or operate electricity generating works to obtain an electricity generation licence. The paper considered whether the benefits of the generation licencing regime were outweighed by the costs. The PUO subsequently concluded generation licences could be removed from the Act, the rationale being:

- Majority of small generating works in Western Australia operate at a capacity level (< 30 MW nameplate) that is already exempt from the generation licence requirement.
- Generation licence obligations comprise less than 10 percent of all electricity licencing obligations and of this share there are no type 1 (material customer impact) obligations.



- Generation licensees incur substantial costs directly related to licence administration including licence application charges, annual licence fees, standing charges, periodic performance audit and asset management review costs and internal licensee compliance costs.
- Generation licensee compliance history is strong and the ERA rewarded good compliance by extending performance audit and asset management system review periods for the large majority of generation licence holders beyond the standard two years.
- Network connected generators are subject to legislative requirements under technical rules and access arrangements with these arrangements being subject to ERA approval and oversight, independent of the generation licencing scheme.
- Removal of generation licencing would not diminish generators' obligations to comply with wholesale electricity market (**WEM**) rules. The WEM rules are subject to oversight by the Australian Energy Market Operator and the ERA, independent of generation licencing scheme.
- Licence repeal would not affect generator obligations under the *Environmental Protection Act 1986* and the safety of electrical equipment and contractors under *EnergySafety* legislation (WA).

The PUO concluded there are sufficient regulatory and commercial arrangements in place to effectively manage the operation of generating works, without the need to licence generators. In response to the PUO's issues paper eleven public submissions were received expressing unanimous support for the repeal proposal.

The proposed legislative changes were introduced into Parliament on 14 September 2016 under the *Licensing and Other Authorisations Amendment Bill 2016* however, due to other legislative priorities the bill did not receive Parliamentary approval. Since the Bill's lapse compliance amongst generation licence holders remains strong with the ERA increasing the audit and review periods for an additional eight licensees, seven of which were extended to the maximum period of 60 months.

Synergy submits the justification for generation licence repeal has not diminished and is in the long terms interests of consumers for this to occur.

Application of electricity retail licences

A gas trading (retail) licence¹ is only required for the sale of gas to < 1TJ/a customers on the basis customers \geq 1TJ/a have sufficient market power to safeguard their commercial interests. The limited scope of gas trading licences was introduced from the inception of that licensing scheme in 1999 and since that date there has been no demonstrable market failure that warrants extending the licence scope to the sale of gas to all customers.

In contrast an electricity retail licence is required to sell electricity to any customer irrespective of size. Unlike a gas trading licence an electricity retail licence extends the monitoring and auditing framework to large use customers. Synergy considers this unnecessary.

Synergy notes under the current electricity licensing framework in Western Australia customers consuming more than 160MWh/a have sufficient market power and capacity for dispute resolution and are therefore not subject to specific energy market regulatory protections that apply to small use customers.²

¹ Issued by the ERA under the *Energy Coordination Act 1994*.

² In Western Australian the threshold for application of electricity customer protections is \leq 160MWh/a. Such protections include the code of conduct, regulated standard form contracts, obligations to offer to supply and the Energy and Water Ombudsman scheme.

It is questionable whether the sale of electricity to large business and industrial customers requires an electricity retail licence. From Synergy's perspective the threshold applicable to an electricity retail licence could safely be reduced to 160MWh/a without any real risk to large customers largely because of the contractual arrangements that exist between those customers and a retailer. Synergy considers limiting the scope of an electricity retail licence to customers who consume less than 160MWh/a to be in the long term interests of consumers as it avoids unnecessary costs for regulating an activity that does not need to be regulated on the basis of no evidence of demonstrable market failure.

2. Is business licensing used too freely to address problems and risks? If so, why is this the case?

The energy market is dynamic and is changing rapidly due to new technology, asymmetry of information and changing customer attitudes towards energy supply specifically a shift to consumer partial self-sufficiency. Customers are now changing the way they participate in the energy market and in response the range of new products and services being offered is proliferating.

From Synergy's experience licensing is implemented with good intent but is not necessarily evidenced by market failure. Synergy rarely sees a business case for regulatory change that demonstrates regulation is in the long term interests of consumers i.e. the benefits of regulation outweigh the costs.

Synergy is concerned with the advent of smart meters, behind the meter battery, electric vehicles, standalone power systems, micro grids etc, the energy industry could face a new wave of licensing regulation. Synergy's view is licensing should only be implemented where it is the most appropriate form of intervention to meet a clearly identified market failure and where the benefits of licensing outweigh its cost. Often a proposal for energy regulatory change does not involve a regulatory impact statement and it is often left to market participants to argue the counterfactual against change rather than the proponent for change evidencing the business case for regulatory intervention.

3. What shapes the way regulatory agencies and licensees interact?

From Synergy's experience the licence framework design and a licensee's compliance performance determines how regulatory agencies and licensees interact. Examples of regulator / market interaction include annual compliance and performance reports, performance audits, asset management reviews and the statutory reviews of regulatory instruments.

4. What types of issues hinder reforms of business licensing? What can be done to make business licensing reforms more likely to be progressed?

- *Lack of transparent licensing objectives.* It is very important the objectives of any licensing regime are transparent and easily understood as objectives provide a necessary reference point to measure whether the framework and its application meets the stated objectives. For example in relation to energy licensing Synergy considers an effective licensing framework should: ensure customers are effectively and adequately protected; the framework should not stymie competition and market entry; and minimise unnecessary compliance and administrative burden.
- *Regulatory design.* Prescriptive regulation reduces flexibility and innovation because it is focussed on process rather than outcome. In contrast outcome based regulation moves away from reliance on detailed, prescriptive rules and relies more on high-level, broadly stated rules or principles to set the standards by which regulated entities must conduct business. Under such a framework required outcomes are specified within regulation, targets or objectives are set and incentives (or penalties) established to deliver the required

outcomes. As energy markets are fluid in nature, outcome based regulation provides flexibility to deliver a solution that provides a greater degree of “future proofing” enabling regulation to respond to new issues as they arise without having to amend or create new legislation. By encouraging organisations to recognise the business advantages of complying with regulated outcomes and regulating their behaviour accordingly, regulators can minimise regulatory intervention and reduce red tape. If regulated entities do not achieve the required outcomes then more prescriptive regulation can be expected in response.

- *Risk based regulation.* Regulation should be commensurate to the level of risk (likelihood and consequence) that the licensed activity poses. For example in electricity retailing there is understandably a strong focus on protecting life support customers. In the case of electricity generation the focus is keeping plant workers, general public and the environment safe. However, in some activities low risk activities can be extensively regulated. For example, Synergy is subject to legislation (via its retail licence) that requires approximately 44 different matters to be included on customer bills notwithstanding it is in a retailer’s legitimate business interest to ensure its bills are easily understood. Licensing should be applied on a risk basis to address a clearly identified market failure and not perception or jurisdictional consistency especially where incidents elsewhere have not occurred in Western Australia.
- *Applicable laws vs energy specific laws.* Where obligations are duplicated via activity specific conditions in a licence, there is a risk that in the event external obligations are amended over time, this will result in an inconsistency with a licence. This in turn creates additional compliance costs and the potential for competitive disadvantages. Regulation which duplicates existing law should be removed or modified. For example given current federal Australian consumer laws is it questionable whether there is a need for so much specific energy customer protection. Synergy’s view is energy specific legislation should occur when there is demonstrable evidence of gaps in applicable laws. Also refer Q.5 below

5. What are some examples of successful reforms of business licensing?

From Synergy’s experience:

- Gas trading licence scope (refer Q.1 above).
- Removal of regulatory duplication from *the Code of Conduct for the Supply of Electricity to Small Use Customers 2016*³ (**Code of Conduct**) (electricity retail licensing). In the past, the ERA has amended the Code of Conduct to remove duplication with existing laws such as the Australian consumer law and privacy laws that has reduced an energy licensee’s compliance costs without diminishing customer protection.
- Outcome based regulation under the Code of Conduct (electricity retail licensing). Previously, hardship regulation was very prescriptive in terms of how a retailer was required to assess a residential customer for financial hardship. The ERA amended the Code of Conduct to adopt a more outcome based form of regulation enabling retailers to have greater flexibility to undertake hardship assessments that focussed on the customer’s need for assistance rather than a prescriptive regulatory process to determine whether the customer was eligible for assistance.

³ A licensee must comply with the Code as a condition of its electricity retail licence.

6. Which licensing schemes should be a high priority for review and reform? Why? What effects do they have on you?

(a) Environmental licensing

Prescribed premises such as a power station require a licence under the *Environmental Protection Act 1986 (EP Act)* to legally operate. These licences come with a number of conditions that set emissions limits/targets, monitoring and management requirements and have been subject to a modification and review process over the last three to five years that has resulted in improvements to effectiveness and consistency.

The Department of Water and Environmental Regulation (**DWER**) has occasionally taken an inconsistent approach to licence changes. An example is the emission monitoring requirements for the Kwinana power station since the closure of the coal fired portion of the station and the ceasing of coal burning at the site in April 2015. When coal burning ceased the emissions of sulphur dioxide (**SO₂**) effectively decreased to zero. Synergy, following a period of engagement with DWER and the Kwinana Industries Council submitted a licence amendment to remove all licence requirements associated with coal burning recognising SO₂ emissions no longer occurred at the Kwinana site. Natural gas and low sulphur diesel are still used in the gas turbines but neither fuel has any significant levels of sulphur meaning emissions of SO₂ are effectively zero at the site. DWER amended the environmental licence to remove a number of requirements regarding stack emissions and limits as SO₂ was no longer emitted from the decommissioned Kwinana coal fired power station.

The DWER did not however remove the costly ambient SO₂ monitoring requirements citing issues with an Environmental Protection Policy (**EPP**) in place for the Kwinana region. Synergy has made various representations and obtained independent advice to substantiate its case for change but this issue has still not been resolved. Some progress has been made by trying to use a redetermination process for emissions allowed for in the EPP to remove the requirements, however this itself is complicated and time consuming. In Synergy's view policy content needs to be redesigned to allow for a simpler process to change requirements, resolving an obvious anomaly that is leading to unnecessary and costly regulation of Synergy's operations in this particular instance.

(b) **Repeal of generation licences** (refer Q.1 above).

(c) **Scope of electricity retail licences** (refer Q1. above).

7. Please provide evidence about the effects of the licensing scheme(s), including:

Refer Q1 and 6.

8. What reforms would you recommend for these licensing schemes?

Refer Q.6.

9. Which licensing schemes have been reviewed over the past five years? Were these reviews effective? Why/why not? Have recommendations for reform been implemented?

Economic Regulation Authority electricity licence review 2018. The review had a limited scope focussing on electricity licence content and format only. Stakeholders were not given prior opportunity to input into the scope review. Consequently, the scope did not enable market participants to provide feedback on the licence framework under the *Electricity Industry Act 2004* nor did it permit a review of various licence instruments such as the ERA's compliance reporting manual or performance audit and asset management guidelines. Synergy considers the licence review would have been more effective had the review scope been more broad.

10. What should the ERA consider to select case studies to assess against the analytical framework?

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Generally the interests of consumers will be maximised by having competitive markets provided all costs and benefits are captured in market outcomes. In instances where this does not occur due to a lack of a competition or the presence of externalities this typically necessitates regulatory intervention where there are no alternative means for achieving these outcomes.

Synergy's view is regulatory intervention via licensing is justified when there is demonstrable evidence of market failure and regulatory intervention leads to a superior outcome in the long term interests of consumers and the benefits of the intervention exceeds the costs (**public interest test**). However, regulatory intervention is rarely evidenced on this basis.

Synergy advocates the ERA should focus its attention on determining whether licensing policy makers and licensing administrators consider or address the public interest test in terms of:

- the decision to licence;
- the decision to continue to licence;
- consideration of licensing alternatives;
- whether licensing frameworks specify objectives or outcomes that can be measured for effectiveness and whether retrospective assessment occurs; and
- whether the decision to licence was transparent, adequate, consistent and evidence based.

Please contact me should you wish to discuss the above matters further.

Yours sincerely,



SIMON THACKRAY
MANAGER REGULATION AND COMPLIANCE