



**public interest**  
ADVOCACY CENTRE

**Submission to the draft report  
AEMC Review of regulatory arrangements for  
embedded networks**

17 October 2017



# Introduction

## The Public Interest Advocacy Centre

The Public Interest Advocacy Centre (PIAC) is an independent, non-profit legal centre based in New South Wales. Established in 1982, PIAC tackles systemic issues that have a significant impact upon disadvantaged and marginalised people. We ensure basic rights are enjoyed across the community through litigation, public policy development, communication and training.

Our work addresses issues such as:

- homelessness;
- access for people with disability to basic services like public transport, education and online services;
- Indigenous disadvantage;
- discrimination against people with mental health conditions;
- access to energy and water for low-income and vulnerable consumers;
- the exercise of police power;
- the rights of people in detention, including the right to proper medical care; and
- government accountability, including freedom of information.

PIAC is funded from a variety of sources. Core funding is provided by the NSW Public Purpose Fund and the Commonwealth and State Community Legal Services Program. PIAC also receives funding from the NSW Government for its Energy and Water Consumers Advocacy Program and from private law firm Allens for its Indigenous Justice Program. PIAC also generates income from project and case grants, seminars, donations and recovery of costs in legal actions.

## Energy and Water Consumers' Advocacy Program

The Energy + Water Consumers' Advocacy Program (EWCAP) represents the interests of low-income and other residential consumers of electricity, gas and water in New South Wales, developing policy and advocating in energy and water markets. PIAC receives policy input to the program from a community-based reference group whose members include:

- Council of Social Service of NSW (NCOSS);
- Combined Pensioners and Superannuants Association of NSW;
- Ethnic Communities Council NSW;
- Salvation Army;
- Physical Disability Council NSW;
- Anglicare;
- Good Shepherd Microfinance;
- Financial Rights Legal Centre;
- Affiliated Residential Park Residents Association;
- Tenants Union; and
- Mission Australia.

## **AEMC Review of regulatory arrangements for embedded network**

PIAC welcomes the opportunity to comment on the AEMC's Draft Report for the Review of regulatory arrangements for embedded networks (the Review).<sup>1</sup>

The growth in the number and size of embedded networks in Australia presents a variety of regulatory challenges. PIAC concurs with the AEMC and other stakeholders that the two-tier embedded network regulatory framework is often ineffective.

The current regulatory system provides embedded network consumers with considerably less information and fewer protections compared with those on standard supply contracts. PIAC considers fixing this imbalance to be an important function of the Review.

To this end, PIAC supports the AEMC's recommendations overall, but argues that competition should be considered a means to more affordable energy for consumers, rather an end in itself.

PIAC recommends that the AEMC enact consumer protection reforms ahead of the broader reforms to the regulatory framework. This would ameliorate the worst impacts of the current framework with the most urgency.

This submission provides feedback on the AEMC's proposed reforms, structured around the three themes identified in the Draft Report:

- Access to competition for legacy embedded networks;
- Elevating embedded networks into the national framework; and
- Better consumer protections for new and legacy embedded networks.

## **Improving access to competition in legacy embedded networks**

PIAC is concerned that the AEMC's focus on access to competition treats competition as a goal in itself, rather than as a method for improving consumer outcomes, given that

- retailers may have little or no interest in acquiring child-metered embedded network customers, especially those in smaller networks where they would have to contract with the embedded network operator;
- in some embedded networks, the cost of enabling access for contestable retail (including metering, metrology, and electrical works), may outweigh the benefits of having an embedded network in the first instance.

Broadly stated, the argument for increasing retail competition is that when a variety of retailers are competing for the business of consumers, they will provide more efficient and innovative

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<sup>1</sup> AEMC, Draft Report, Review of regulatory arrangements for embedded networks, September 2017, <<http://aemc.gov.au/getattachment/08fa7747-e165-4bd6-9691-d43e82c2213e/Draft-report.aspx>>.

services to gain a competitive advantage, driving down prices to result in better consumer outcomes.

Recent experience in the retail energy market outside of embedded networks suggests that this has not been the case. Instead, the complexity of the retail energy market has consistently mitigated against informed choices by consumers and resulted in what has been called a ‘confusopoly’. For many consumers, inability to effectively engage with the market means they default to very expensive energy contracts with high retail margins.

For this reason, PIAC contends that the AEMC should only require retail competition in embedded networks where it provides clear consumer benefits that outweigh the costs.

### ***Recommendation 1***

*PIAC recommends that the AEMC only require retail competition in embedded networks where it provides clear consumer benefits that outweigh the costs.*

### **Build it and they may not come**

PIAC doubts that these proposed reforms will result in retailers entering embedded network markets:

- Issuing and registering National Metering Identifiers (NMI) to all child connections in embedded networks with an embedded network manager (EMN); and
- Allowing retailers serving embedded network customers to pay ENSPs a network tariff that is equal to the standard published LNSP tariff that would apply if there was no intermediate embedded network.<sup>2</sup>

PIAC agrees with the AEMC that these reforms would reduce the transaction costs associated with retailers approaching embedded network consumers by making them more visible and aligning their network tariffs with those the retailer already pays. Even so, PIAC considers it unlikely that retailers would choose to serve these consumers.

The AEMC concedes this, stating that “in practice there is unlikely to be workable competition” for many consumers in legacy embedded networks.<sup>3</sup>

In PIAC’s view, retailers are very reluctant to offer market contracts to small groups of consumers that would require them to make changes to their internal systems. Even with the proposed reforms, other costs that are likely to discourage retailers from approaching embedded network consumers. For example, retailers would still have to change their systems to pay network tariffs to considerably more NSPs than the limited number of LSNPs they currently deal with.

Given that high transaction costs mean retailers are often reluctant to offer market contracts to small groups of customers, PIAC considers it unlikely that they would choose to make the system changes necessary to offer retail competition in embedded networks, particularly small ones.

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<sup>2</sup> Ibid, v.

<sup>3</sup> Ibid, 114.

If proposed reforms are implemented and retailers still do not offer market contracts to embedded network consumers, there is considerable cost risk. The proposed requirement for embedded network managers to assign NMI and register and maintain information in MSATS will involve costs to the ENSP. As with any costs related to network operation, they will be recovered from the consumer. If the reforms result in effective retail competition, the costs may be offset by the lower prices and other benefits associated with competition. However, if retailers still choose not to serve embedded network consumers these costs will be paid by consumers without any benefit.

To minimise the risk associated with competition-related reforms, PIAC recommends that the AEMC take two actions. Firstly, competition reforms should only be enacted when there is sound evidence that retailers are providing services in embedded networks. Secondly, after they are enacted, the AEMC should conduct a review into the effectiveness of competition in embedded networks to ensure that the reforms are actually working as intended.

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### ***Recommendation 2***

*PIAC recommends that the AEMC not proceed with reforms to facilitate competition without evidence that retailers will offer consumers competitively priced services in embedded networks.*

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### ***Recommendation 3***

*PIAC recommends that, assuming the reforms to facilitate competition are enacted, the AEMC review their effectiveness after a period of two years.*

## **Elevating new embedded networks into the national framework**

PIAC agrees with the AEMC and other stakeholders that the current two-tier regulatory framework is no longer fit for purpose. While the practice of exempting embedded networks from the framework was suitable when they served a small number of consumers, the AER reports that there are currently over 3,000 networks with exemptions.<sup>4</sup> These networks are highly diverse, with some servicing small communities and others providing network and retail services to large groups of consumers.

For these reasons, PIAC supports the intent of the AEMC to regulate embedded network service provision and on-selling under the national registration and authorisation framework. However, there are a number of issues raised by the elevation of new embedded networks into the national framework that PIAC wishes to bring to the attention of the AEMC. These issues are:

- Network charges and cost recovery;
- On-seller exemptions;
- Exemptions for small embedded networks, particularly those providing community energy services.

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<sup>4</sup> AER, Public register of network exemptions, 2017 <<https://www.aer.gov.au/networks-pipelines/network-exemptions/public-register-of-network-exemptions>>.

## Network charging and cost recovery

PIAC contends that some ENSPs should be allowed to recover network costs through network charges.

In the current exemption framework, ENSPs are prohibited from recouping the costs associated with network infrastructure through energy bills.<sup>5</sup> PIAC understands that this will continue to be the case under the new embedded network framework, as the network tariff that is paid to the ENSP will be a direct pass-through of the local DNSP's network tariff. In both cases, this means that the ENSP's means of recouping network costs is generally limited to leasing agreements with consumers.

PIAC considers that it may be appropriate to remove this prohibition in some circumstances. In many residential parks, for example, internal embedded network infrastructure was not developed as an up-front capital project as it would be in shopping centre or apartment building embedded networks. Instead, network infrastructure has been built up over time, often decades, as parks have transitioned from exclusively holiday accommodation to places of permanent residence, greatly increasing the demands on these embedded networks. In a recent consultation park residents advised PIAC that the embedded networks are often in poor repair, unreliable, do not comply with current wiring rules, and are potentially unsafe. For example, some even use household extension leads in the place of hard wiring.

In these cases, the need to repair, maintain or upgrade infrastructure may result in considerable unforeseen capital expenditure, at short notice, that has not been factored into existing rent payments. Given the high proportion of park residents on fixed incomes, they are unlikely to be able to afford dramatically increased rents or fit-out charges. In these circumstances, it would be preferable for the ENSP to have the option to progressively collect network management costs through an extra ENSP network charge over a longer period of time.

In the past, this practice has been prohibited for two reasons. Firstly, it is impractical for ENSPs to go through an AER determination of network charges because of their small size. Therefore, there has not been a mechanism through which to regulate what individual ENSPs charge consumers to maintain the network. Secondly, lease agreements have been considered appropriate.

Clause 4.6.3 of the AER's network exemption guideline considers this appropriate because:

the AER considers the network development costs to have been met in the initial establishment of the facility. Such costs are capital in nature and are normally recoverable through fit-out charges or the like.

PIAC recommends this be changed for two reasons. Firstly, while a full revenue determination for each ENSP is clearly impractical, recovering the costs through lease payments provides no more regulatory protection than having them recovered through energy bills. In fact, other the recommendations in the Draft Report indicate the opposite will be the case. In Chapter 9, the AEMC recommends giving the AER increased embedded network monitoring and enforcement responsibilities, meaning that there would be a level of protection in the form of regulatory

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<sup>5</sup> Ibid, 64.

oversight of costs recovered through energy charges. Conversely, the AER has no jurisdiction over private rental agreements and has no monitoring and enforcement powers over embedded network cost recovery through lease payments. Therefore, PIAC contends that, if anything, cost recovery through energy charges would result in better regulatory protection for embedded network consumers than recovery through lease payments.

Secondly, while the up-front costs of network development can be easily added to lease payments, this becomes more difficult when considering ongoing maintenance of an aging embedded network such as those in residential parks. The potential for expensive works in these networks has the potential to create considerable consumer detriment through a sudden increase in non-energy charges by the ENSP.

PIAC recommends that the rules give the AER discretion to allow registered ENSPs to recover networks costs through energy bills where there is a demonstrable consumer benefit.

Given that it is not practical for each ENSP to have a full regulatory determination, this should be regulated on an application basis. An ENSP would apply to the AER if they thought it was appropriate to charge in this manner and the AER could either approve the practice or not based on a consumer benefit test. Through this process, the AER could direct that the funds collected be used only for network maintenance and upkeep, and undertake or initiate enforcement if this is not followed.

#### ***Recommendation 4***

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*PIAC recommends that the AEMC give the AER discretion to allow registered ENSPs to recover network costs through energy charges where there is demonstrable consumer benefit in doing so.*

#### **Exemptions for registered on-sellers**

The AEMC recommends that the AER be given limited discretion to exempt on-sellers from some authorisation requirements. PIAC supports this recommendation on the basis that some obligations placed on authorised retailers are likely to be too onerous for small on-sellers to comply with. For example, PIAC does not consider it appropriate for authorised on-sellers to be required to pay registration fees to AEMO when they do not participate in the wholesale market.

However, as the AEMC notes, there are some key consumer protections for which the AER should have no discretion to exempt on-sellers. The Alternative Technology Association (ATA) recently produced a report assessing consumer protections in emerging energy markets.<sup>6</sup> In this report, they produced a list of fundamental protections, stating that all consumers should be confident that:

- They will be able to connect to an energy supply;
- Their energy supply will meet minimum reliability, quality, and safety standards and they will be compensated if it doesn't;

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<sup>6</sup> ATA, *Empowering the future – Appropriate regulation and consumer protections in emerging energy markets*, 2016, <[http://www.ata.org.au/wp-content/uploads/2016/11/Empowering-the-future-appropriate-regulation-and-consumer-protections-in-emerging-energy-markets\\_ATA.pdf](http://www.ata.org.au/wp-content/uploads/2016/11/Empowering-the-future-appropriate-regulation-and-consumer-protections-in-emerging-energy-markets_ATA.pdf)>.

- Sufficient notice will be given for any planned interruptions to supply, and special consideration given to people reliant on life-support systems;
- They will be given clear information about the service they are purchasing, a cooling-off period for any contract they sign (for more novel supply arrangements), a limited right to exit a contract and revert to their previous contract;
- The basis of all energy supply charges is clear and subject to regulatory oversight;
- They have access to historical billing data;
- They have access to discounts on their energy costs if they are eligible for concessions;
- If they come into payment difficulties, they will be given support and flexibility and only disconnected as a last resort and according to a regulated process;
- They have access to an external dispute resolution service if they are unable to resolve a dispute with their energy supplier;
- During billing disputes, they can stay on supply and not have to pay the disputed amount; and
- If their supplier ceases trading, their supply is uninterrupted.<sup>7</sup>

PIAC contends that these protections should always apply to both standard supply and embedded network consumers. PIAC recommends that the AEMC adopt this list as the basis for designating the minimum set of consumer protection conditions for on-seller authorisations in embedded networks.

#### ***Recommendation 5***

*PIAC recommends that the AEMC adopt the ATA's list of fundamental consumer protections as its minimum set of consumer protection conditions for on-seller authorisations.*

#### **Embedded network exemptions for community energy projects**

PIAC contends that exemptions from some embedded network arrangements should be provided for innovative projects.

In PIAC's view, an important feature of effective markets and competition in the future energy system, will be that willing communities of consumers are able to establish innovative energy projects. Where, for example, these projects are based around solar PV and/or battery installations, having an embedded network can be essential to realise the cost benefits.

Embedded networks may be of benefit to communities of consumers by

- enabling more cost effective, scale-efficient shared energy generation and/or storage infrastructure;
- increased onsite consumption of generated and/or stored energy reducing import from the grid; and
- collective bargaining power for better prices for energy purchased from, or exported to, the grid.

Many of these networks would not benefit from access to contestable retail within the embedded network. As a result, despite their clear benefits, a potential inability to meet registration costs and the absence of a need for competitive retail, may mean these projects are not be able to

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<sup>7</sup> Ibid, 8.

receive an exemption under the AEMC's proposed framework, which would limit exemptions to embedded networks to those

- supplying infrastructure;
- related parties such as subsidiary companies; and
- the owners of short duration accommodation with simple network arrangements.<sup>8</sup>

While PIAC supports the AEMC's intent to limit exemptions where possible, we contend that community projects with a demonstrable consumer benefit should be added to the list.

### ***Recommendation 6***

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*PIAC recommends that the AEMC allows exemptions for innovative projects, such as community energy projects, that have demonstrable consumer benefits and whose business cases are reliant the establishment of an embedded network.*

## **Better consumer protections for new and legacy embedded networks**

Regardless of access to competition or the regulatory framework employed, all consumers should enjoy a basic level of protection. In submissions to the Consultation Paper stage of the Review, PIAC and other stakeholders identified significant gaps in the consumer protections framework for embedded networks.<sup>9</sup> Consumers in many embedded networks are currently treated as second class energy citizens, with far fewer protections than their standard supply counterparts.

PIAC contends that the AEMC should prioritise protections for exempt embedded network consumers and not wait for other regulatory reforms to provide vital consumer protections to currently under-protected consumers.

Assuming that a list of protections similar to that listed above is included in the new framework as non-exemptible, PIAC agrees with the AEMC that elevating ENSPs and on-sellers into the national registration and authorisation framework will provide an adequate level of protection for consumers in embedded networks created after the proposed reforms are enacted.

However, this does not apply to embedded networks already in existence, those created between now and when the reforms are enacted, or, potentially, those that will still be given exemptions under the new framework. For these consumers, PIAC supports the AEMC's approach to consumer protections. The AEMC should recommend reforms that provide all embedded network consumers with access to dispute resolution and concessions, while extending existing standing offer price cap to off-market customers of authorised on-sellers and improving the ability of the AER to monitor and enforce compliance with its exemption guideline.

### ***Recommendation 7***

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*PIAC recommends that the AEMC proceed with the proposed consumer protection reforms separately to the framework reforms and enact them as a matter of urgency.*

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<sup>8</sup> AEMC, Draft Report, Review of regulatory arrangements for embedded networks, 90.

<sup>9</sup> Ibid, 41.

## Further engagement

PIAC would welcome the opportunity to discuss the issues raised in more depth. For any queries please contact Energy Team Leader, Craig Memery at [cmemery@piac.asn.au](mailto:cmemery@piac.asn.au) or on (02) 8898 6522.