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Review Secretariat
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To whom it may concern

Consultation on proposed legislative changes to incorporate an emissions reduction objective into the national energy objectives

Thank you for the opportunity to submit to this review into the introduction of an emissions reduction objective into the national energy objectives. There can be no doubt that this is an important step in modernising the legislative and regulatory frameworks governing the national energy markets, but it is only a first step. This brief submission identifies two supporting measures required to ensure the proposed objectives drive a successful energy transition – that is, a transition that accords with policymakers' expectations and is aligned with community interests.

1. Interpretative guidance

While this review will propose newly worded objectives in the relevant energy laws, it is also important that the regulatory authorities (or 'market bodies' as they are commonly described) be given clear guidance about governments' expectations in how the new objectives are to be interpreted.

The guidance should contain:

- principles the regulatory authorities must follow when exercising their functions and making their decisions, and
- specific examples that demonstrate how the objectives and principles should be applied in particular circumstances.

There are many cases where such principles would provide helpful clarity to the regulatory authorities about the intended operation of the new objective. For example:

- *Principles guiding the counterfactual scenario to be adopted by regulatory authorities when assessing the merits of an investment option.* The status quo is often treated as the counterfactual against which an investment proposal is considered. This is unlikely to be a realistic methodology during the transition. At a minimum, regulatory authorities should apply a shadow carbon price in the modelling of all investment options (including when the status quo is assumed). The shadow carbon price should be set and reset by policy makers through an appropriate process and instrument.
- *Principles addressing the regulatory treatment of sunk assets which are at risk of stranding during the decarbonisation of the energy system.* At present, regulatory authorities operate on the basis that investors in networks are fully indemnified by consumers. This may have been a reasonable approach in the past when the energy system was in steady-state and there was comparatively little risk of stranding. No such assumptions can be sustained during the energy transition. Principles guiding the allocation of risk between investors and consumers (and potentially, taxpayers) during the energy transition are urgently required.¹

It may be worth considering embedding in legislation the principles required to support the new emissions reduction objective. Doing so may, however, limit the flexibility available to policy makers wanting to update the principles as the energy system and market evolve during the transition. A more flexible option would involve implementing the principles via regulation. An even more flexible approach would see the principles transmitted to the regulatory authorities via a lesser instrument (for example, a statement of ministerial expectations). More flexible options should suffice if regulatory authorities are made sufficiently accountable for their actions to ministers and the public.

The energy transition is bearing down on the market and its regulators. Consumers pay for regulators' decisions. There is simply no time left for the regulatory bodies to embark on their own 'voyages of discovery' given the scale and speed with which the energy system needs to transform. The objectives (and principles) must be unambiguous and actionable from the day they receive Royal Assent. Regulatory authorities must be left in no doubt about ministerial expectations about how the objectives (and principles) are to be applied.

¹ For further discussion, see: Consumer Challenge Panel (18 February 2022) *CCP28 Advice to the AER. Victorian Gas Transmission System Access Arrangement 2023–27*. Chapter 7. Available at: <https://www.aer.gov.au/system/files/CCP28%20-%20Advice%20to%20AER%20on%20APA%20VTS%202023-27%20AA%20Proposal%20-%2018%20February%202022.pdf>

2. Consumers are part of the energy transition

So far, the regulatory response to the energy transition has been to treat households and businesses as ‘market participants’ rather than as straightforward consumers of energy.

Nearly every regulatory decision directly affecting consumers contains embedded assumptions about how ‘*consumers-as-participants*’ will respond to the new markets, business models and pricing structures being enabled by those regulatory decisions. These assumptions about consumers are rarely spelled out; and no attention is given to the consequences for consumers if they fail to act in accordance with these assumptions.² What is certain, however, is that many (and maybe most) households and small businesses will not act in line with regulators’ silent assumptions about them. Designing a market for imaginary participants is surely an exercise in futility.

Of course, some highly effective customers will benefit under these new arrangements but it will likely be at the expense of those households and businesses who, for whatever reason, do not astutely participate in the energy market. Inevitably, this latter group of customers will feel betrayed when they realise the market for an essential service is driving large welfare transfers away from them.

In the two papers referenced below, I have outlined how the rapidly increasing complexity of the consumer-facing energy market greatly increases the likelihood of consumers entering contracts that do not align with their interests. In other words, the energy market is at risk of becoming a significant source of consumer harm.

My papers propose a suite of measures that would assist in avoiding the energy market becoming a source of consumer harm. Most importantly, this includes:

- establishing a duty of care requiring all energy-related service providers to act in the best interests of their customers; and
- introducing a harm minimisation objective in the national energy law(s) that would sit above, but not displace, other objectives such as the promotion of efficient investment in, and use of, the energy system.

² Similarly, no discussion is offered about the consequences for the energy transition if households and businesses fail to participate as the regulatory authorities assume. Such outcomes are simply not countenanced in the regulation of the national energy markets. Put bluntly, the regulatory authorities are ‘betting the house’ on a singular, idealised view about ‘*consumers as participants*’ – a view that is not well supported by 20 years of experience with retail competition.

Amending the national energy objectives to include an emissions reduction objective is intended to propel the energy transition forward. But, there can be no successful energy transition if consumers lose confidence in the energy market and all those responsible for its governance and operation.

Ben-David, Ron (27 May 2022) ***Energy market uncertainty, consumer protection, and a new duty of care.*** Available at:

<https://www.aer.gov.au/system/files/Ron%20Ben-David%20Submission.pdf>

Ben-David, Ron (17 November 2022) ***Minimising consumer harm for a successful energy transition.*** Available at:

https://www.ipart.nsw.gov.au/sites/default/files/cm9_documents/Ron-Ben-David-Minimising-Consumer-Harm-IPART-30-year-conference-%2817-November-2022%29.PDF

I would welcome the opportunity to discuss this submission with the secretariat. In the meantime, I wish you well in your endeavours.

There is no information in this submission subject to a confidentiality claim.

Yours sincerely

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