



Ms Elizabeth Molyneux
Deputy Secretary Energy
Department of Energy, Environment and Climate Action
Level 3, 8 Nicholson Street
EAST MELBOURNE VIC 3002

22 February 2023

Dear Ms Molyneux,

REGULATORY IMPACT ASSESSMENT FOR FEES FOR THE VICTORIAN ENERGY UPGRADES PROGRAM

I would like to thank your staff at the Department of Energy, Environment and Climate Action (the Department) for working with the team at Better Regulation Victoria to prepare a Regulatory Impact Statement (RIS) for fees for the Victorian Energy Upgrades Program (the proposed fees). The proposed fees will replace the existing fees which are due to expire on 19 October 2023.

As you know, the Commissioner for Better Regulation provides independent advice on the adequacy of the analysis provided in all RISs in Victoria. A RIS is deemed to be adequate when it contains analysis that is logical, draws on relevant evidence, is transparent about any assumptions made, and is proportionate to the proposal's expected effects. The RIS also needs to be written clearly so that it can be a suitable basis for public consultation.

I am pleased to advise that the final version of the RIS received by us on 20 February meets the adequacy requirements set out in the *Subordinate Legislation Act 1994*.

Background

The Victorian Energy Upgrades (VEU) program is an incentive scheme for households and businesses to upgrade to energy-efficient products. Upgrades are installed by accredited providers (APs) who generate Victorian Energy Efficiency Certificates. Each certificate represents one tonne of carbon abated. Greenhouse gas reduction targets are set every five years, with the currently set targets reaching 7.3 million certificates in 2025. Energy retailers are required to purchase a number of these certificates each year according to how much energy they purchase on the wholesale market.

The VEU program was established in 2009 under the *Victorian Energy Efficiency Target Act 2007* (the VEET Act). The Department oversees the program, while the Essential Services Commission (ESC) administers and regulates the program.

The ESC carries out several functions for the VEU program, including:

- validating the creation of certificates for registration on the market;
- accrediting persons to create certificates under the program;
- assessing applications to generate certificates from large and custom upgrade projects;
- approving energy efficient products that can be installed under the program; and
- reviewing energy acquisition statements lodged by energy retailers.

Section 73 of the VEET Act enables the Minister for Energy and Resources to set fees for the administration of the VEU program in consultation with the Assistant Treasurer. Currently, the ESC's costs to administer the program are funded through a \$1 per certificate registration fee, a one-off \$500 fee to apply for accreditation, as well as direct government funding. The ESC does not currently charge fees for other VEU Program services. The current fees will lapse on 19 October 2023 due to provisions in the *Essential Services Commission (Compliance and Enforcement Powers) Amendment Act 2021*.

Problem analysis and objectives

The ESC is currently under-recovering the costs of its activities related to the VEU program. This will be exacerbated due to the introduction of new functions and powers for the ESC under the *Victorian Energy Efficiency Target Amendment Act 2022* (VEET Amendment Act), such as increased oversight and controls over APs. The VEET Amendment Act also introduced new fee-making powers, so that the ESC's costs can be recovered from more of its services. The Department explains that if the ESC maintains its existing fee structure, it is expected to face an average annual revenue shortfall of

\$11 million per year for the next three years. ESC activities relating to certificate creation account for approximately 83 per cent of ESC's costs.

The Department explains that adopting a full cost recovery fee structure is appropriate because the program requires regulation to ensure that created certificates are genuine, energy retailers meet their obligations, and consumers are protected from harm. Furthermore, program participants benefit from participating in the market.

The Department explains that, in setting fees, it has considered four key objectives:

1. Competition and innovation: fees should not limit access to the market, particularly for small operators, as well as innovative products and projects;
2. Horizontal equity: fees should minimise cross subsidies between taxpayers and VEU program participants as well as between smaller and larger program participants;
3. Compliance: fees should drive compliant behaviour and lower regulatory costs; and
4. Simplicity: fees should be easy to understand and administer.

Analysis of options

All options are based on activity-based costing (ABC) analysis that ESC conducted of the tasks it conducts as part of its administration and regulation of the VEU program. All options aim to fully recover the costs of service provision by the ESC. All options set fees for a three-year period (from July 1, 2023 to June 30, 2026). The options are estimated to raise between \$54.2 million in total over three years, which is more than double the current total fees. The options are:

- **Option 1** (*activity-based fees*) — *charge fees to directly recover the costs of each service and function the ESC undertakes.* This approach is simple and avoids cross subsidies, but results in very high fees for small APs.
- **Option 2** (*discounted fixed fees*) — **(the preferred option)** *lower upfront fees such as accreditation fees, with higher certificate fees to achieve full cost recovery.* This results in some cross-subsidising of smaller APs by larger APs, but encourages competition and innovation within the industry.
- **Option 3** (*fee waivers for small APs*) — *provides accreditation fee waivers to APs generating less than 7,600 certificates per year.* To ensure larger APs are not incentivised to decrease the number of certificates created to below the threshold, these smaller APs are charged a higher certificate fee.

The table below compares the options to the current fees and demonstrates the key differences between the options. In particular:

- Option 1 has the lowest certificate fees, but the highest upfront fees;
- Option 2 has low upfront fees for all APs, but a higher certificate fee; and
- Option 3 charges certificate fees at registration rather than creation, and has different accreditation fees depending on how many certificates an AP creates.

Fee	Current fee	Option 1	Option 2	Option 3
Certificate creation	n/a	\$2.05	\$2.33	n/a
Certificate registration	\$1	n/a	n/a	\$2.83 for small APs \$2.09 for other APs
Application of accreditation	\$500	\$17,218	\$3,000	\$0 for small APs \$17,218 for other APs
Annual reaccreditation	n/a	\$5,162	\$1,000	\$0 for small APs \$5,612 for other APs
Variation of accreditation condition	n/a	\$6,026	\$1,500	\$0 for small APs \$6,026 for other APs
Annual reaccreditation late lodgement	n/a	\$0	\$14,814	\$14,814
Project-based activity impact report	n/a	\$3,778	\$500	\$3,778
Product Application	n/a	\$766	\$500	\$766
Lodging an energy acquisition statement	n/a	\$3,122	\$3,122	\$3,122
Opening an account to hold and trade certificates	n/a	\$2,332	\$2,000	\$2,332
Review of a reviewable decision	\$200	\$2,500	\$750	\$0

The Department analyses the options using a Multi-criteria Analysis (MCA) utilising the four objectives above as equally weighted criteria. The options are assessed against a base case of the current fees being allowed to expire.

The Department explains in the RIS that Option 2 is the preferred option because it best balances the Department's objectives: in particular, it discourages competition and

innovation less than the other options relative to the base case. Option 2 is also expected to produce the highest compliance rate, while being simple to understand and administer. However, Option 2 has the highest cross-subsidy between large and small APs, of \$5.9m over three years. On balance, the Department assesses Option 2 as best achieving its objectives.

Implementation and Evaluation

The proposed fees are scheduled to commence on 1 July 2023 and be in place for three years. The Department explains that the proposed commencement date will allow the ESC to establish the necessary administrative processes and to communicate the new arrangements to the sector. New fees under the VEET Amendment Act will be phased in over time, with 12-month transitional periods for current APs and certificate traders.

The RIS explains that the ESC will have responsibility for monitoring the cost recovery of the program, and publishing Performance Reports on the program.

In the RIS, the Department commits to a broad review of the VEU program in 2024 to inform setting targets for 2026 through to 2030. The Department will work with the ESC in 2024 to evaluate the proposed fees as part of the broad review of the VEU program. Some of the specific metrics that will be used to monitor implementation and evaluate the proposed fees include:

- effective fees per certificate for APs, that is, the total fees paid by each AP divided by the number of certificates they create;
- certificate creation volumes;
- AP registration and participation levels; and
- the number of registered products in the VEU program and the number of certificates created for each product.

Should you wish to discuss any issues raised in this letter, please do not hesitate to contact my office on (03) 7005 9772.

Yours sincerely



Anna Cronin

Commissioner for Better Regulation