

Regulatory Impact Statement for proposed fees for the Victorian Energy Upgrades Program

2023



Author

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Acknowledgment

We acknowledge and respect Victorian Traditional Owners as the original custodians of Victoria's land and waters, their unique ability to care for Country and deep spiritual connection to it. We honour Elders past and present whose knowledge and wisdom has ensured the continuation of culture and traditional practices.

We are committed to genuinely partner, and meaningfully engage, with Victoria's Traditional Owners and Aboriginal communities to support the protection of Country, the maintenance of spiritual and cultural practices and their broader aspirations in the 21st century and beyond.



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Table of contents

Table of contents	1
Executive summary	5
Glossary	8
1. Introduction	9
1.1 Background	9
1.2 Power to set fees for the program	9
1.3 Current and new program fees	9
1.4 Assessment and consultation requirements	10
1.5 About this Regulatory Impact Statement	10
1.6 How to provide feedback	11
2. What is the problem being addressed?	12
2.1 Policy context	12
2.1.1 VEU is helping to decarbonise and electrify Victoria	12
2.1.2 Strengthening the VEU program	12
2.1.3 Costs and benefits of the VEU program	14
2.2 Why cost recovery?	14
2.2.1 The Victorian Pricing Principles	14
2.2.2 Legislation requires the ESC's VEU program to fully recover costs	14
2.3 Changes to the ESC's costs	15
2.3.1 Current fees do not fully cost recover the ESC's costs	15
2.3.2 The ESC's role is expanding	15
2.4 The base case - what would happen if no action were taken?	16
3. Factors considered in designing options to address the problem	18
3.1 Context	18
3.1.1 Victorian Government pricing principles	18
3.1.2 VEET Act objectives	18
3.2 Supporting competition and innovation	18
3.2.1 Application for accreditation fee	19
3.2.2 Annual re-accreditation fee	19
3.2.3 Variation of accreditation condition fee	19
3.3 Horizontal equity	20
3.3.1 Lodging energy acquisition statement fee	20
3.3.2 Opening an account to hold and trade certificates fee	20
3.3.3 Product application fee	20
3.4 Compliance	20

3.4.1 Fees at the point of certificate creation or registration	21
3.4.2 Late lodgement of applications to renew accreditation fee	22
3.4.3 Project-based activity impact report fee.....	22
3.5 Simplicity	23
3.6 Ensuring access to review of decisions	23
4. Costing methodology	24
4.1 Identifying relevant services	24
4.2 Allocating costs to services	25
4.3 Relevant costs	28
4.4 Resourcing estimates	29
4.4.1 Accreditation	29
4.4.2 Registration of certificates	29
4.4.3 Compliance and scheme monitoring	29
4.4.4 Enforcement and legal advice	30
4.4.5 Engagement, communication, and education	30
4.4.6 IT and governance	30
4.5 Cost and revenue escalation	30
5. Objectives.....	31
5.1 Victorian policy objectives	31
5.2 VEET Act objectives	31
5.3 VEU Fee-setting objectives	31
6. Options	32
6.1 Factors that are varied between options to explore trade-offs	32
6.1.1 Application for accreditation fee	32
6.1.2 Annual re-accreditation fee.....	32
6.1.3 Variation of accreditation condition fee	32
6.1.4 Fees at the point of certificate creation or registration	33
6.1.5 Project-based activity impact report fee.....	33
6.1.6 Late lodgement of applications to renew accreditation fee	33
6.1.7 Opening an account to hold and trade certificates	33
6.1.8 Product application fee	34
6.1.9 Reviewable decision fee.....	34
6.2 Options to be evaluated.....	34
6.2.1 Option 1: Activity-based costing.....	34
6.2.2 Option 2: Discounted fixed fees—the preferred option.....	35
6.2.3 Option 3: Fee waivers for small APs.....	35
Comparison between proposed fees and existing fees	37

6.2.4 Change in fees for typical stakeholders	38
6.3 Consultation questions for this chapter	38
7. Assessment of options	39
7.1 Approach to assessment of options	39
7.1.1 Consideration of discount rates	40
7.2 Detailed evaluation	40
7.2.1 Cost impacts per certificate for varying AP service levels and AP sizes	40
7.3 Summary of multi-criteria analysis evaluation outcomes	45
7.3.1 Competition and Innovation	45
7.3.2 Horizontal Equity	45
7.3.3 Compliance	46
7.3.4 Simplicity	47
7.3.5 Conclusion	47
7.4 Ensuring access to review of decisions	47
7.5 Consultation questions for this chapter	48
8. Implementation, monitoring and evaluation	49
8.1 Implementation	49
8.1.1 Transitional arrangements	49
8.2 Monitoring	50
8.3 Evaluation	50
8.4 Consultation questions for this chapter	50
9. Consultation questions	51
Appendix A: How the VEU program works	52
Appendix B: Forecast volume of certificates, accredited providers and services performed	54
Sensitivity analysis (if the cost variables change)	55
Appendix C: Impacts on electricity prices	56

List of tables

Table 1: Comparison of fee options evaluated	5
Table 2: Summary of multi-criteria evaluation of fee options	6
Table 3: Administrative decisions of the ESC under the VEU program	16
Table 4: ESC's services under the VEU program	24
Table 5: Timing of introduction of new and expanded services under the VEU program	25
Table 6: ESC costs and tasks	26
Table 7: Allocation of task costs to services.....	27
Table 8: VEU program costs over 2023-24 to 2025-26 (nominal).....	28
Table 9: Summary of fee options assessed	34
Table 10: Fee summary under option 1, activity-based costing (2023-24 – 2025-26, \$ nominal)	34
Table 11: Fee summary under option 2, Discounted fixed fees (2023-24 – 2025-26, \$ nominal)	35
Table 12: Option 3 – cost for fee waiver threshold for smaller APs	36
Table 13: Fee summary under option 3 for different size APs (2023-24 – 2025-26, \$ nominal)	36
Table 14: Fees paid by other stakeholders under option 3	37
Table 15: Comparison to existing fees	37
Table 16: New fee categories to be introduced.....	37
Table 17: Criteria in multi-criteria analysis.....	39
Table 18: Criterion score standards	39
Table 19: Annual cost impacts for existing APs with basic service level	41
Table 20: Annual cost impacts for existing APs with full service level	43
Table 21: Annual cost impacts for new APs with basic service level	44
Table 22: Summary of MCA evaluation of fee options	45
Table 23: Consultation questions	51
Table 24: Forecast certificates, accredited providers, and services	54
Table 25: Assumptions made in forecasting certificates, accredited providers, and services	54
Table 26: Sensitivity analysis on certificate creation volumes 20% lower than forecast.....	55
Table 27: Sensitivity analysis on certificate creation volumes 20% higher than forecast	55
Table 28: The range of impacts on electricity bills for energy consumers from option 2	56

List of figures

Figure A: Change in fee collection point.....	21
Figure B: ESC VEU program costs by tasks—total cost for three-year fee period	28
Figure C: Cost impacts per certificate for existing APs with basic service level	41
Figure D: Cost impacts per certificate for existing APs with full-service level	42
Figure E: Cost impacts per certificate for new APs with basic service level	44
Figure F: How the Victorian Energy Upgrades program works.....	52

Executive summary

This Regulatory Impact Statement (RIS) sets out the reasons for, and the basis of, proposed new fees payable to the Essential Services Commission (ESC) as the administrator and regulator of the Victorian Energy Upgrades (VEU) program.

The VEU program, established under the *Victorian Energy Efficiency Target Act 2007* (the VEET Act), offers financial incentives to businesses and households to voluntarily undertake energy efficiency upgrades. Private businesses accredited under the program (accredited providers [APs]) provide these upgrades and create Victorian Energy Efficiency Certificates (certificates) that they sell to energy retailers, who are obliged to obtain and surrender a set number of certificates each year. The ESC's costs to administer the program are currently covered by a combination of fees and discretionary government budget allocations. The VEU program fees have not changed since the program started in 2009. They currently apply to creating certificates, becoming accredited under the program, and applying for a review of an ESC decision.

In 2019, the Department of Treasury and Finance (DTF), which has responsibility for the ESC, reviewed the organisation's overall funding model and recommended the VEU program fees be reviewed and set with the aim of full cost recovery. In 2022, a VEU Code of Conduct was introduced to establish minimum protections for consumers under the program. In addition, the VEET Act was amended to expand the range of tools available to the ESC to effectively administer the scheme, monitor compliance of companies working in the program, and pursue enforcement where necessary to protect Victorian consumers and ensure the program meets its goals.

As a result of these changes, the costs to the ESC to administer the VEU program are expected to increase from \$16.2 million in 2023-24 to \$19.4 million in 2025-26. If the current fee structure were to remain unchanged, it could result in an estimated average annual revenue shortfall of \$11 million per year for three years. Under section 73 of the VEET Act, the Minister for Energy may fix fees to cover the costs of administering the VEU program in consultation with the Assistant Treasurer, who has oversight of the ESC. The fees need to be reviewed and reset before the current fees lapse on 19 October 2023. The RIS structure requires proposed amendments to the fees for the VEU program to be assessed against a hypothetical 'base case.' Given the current fees expire on 19 October 2023, the Department of Energy, Environment and Climate Action (the department) has defined the base case as no fees being recovered for the program. That is, the ESC would receive no revenue from fees as they would not exist.

Three fee options were explored to fully recover the costs of the VEU program over 2023/24 to 2025/26:

- **Option 1: Activity-based costing**, which allocates the incremental costs of providing each ESC service and an annual fee that recovers fixed costs. This is the most cost-reflective option.
- **Option 2 (preferred): Discounted fixed fees**, which manages the impact of fee increases on smaller APs (by setting most fees at between \$500 and \$3,000) and then increases certificate fees to offset this and achieve full cost recovery.
- **Option 3: Fee waivers for small APs**. Costs are allocated in the same manner as per option 1, with the addition of fee waivers for small APs (those generating less than 7,600 certificates per year) for certain up-front fees. This results in higher certificate fees for all APs (to ensure full cost recovery). The certificate fees for the small APs that benefit from the waiver in up-front fees is substantially larger than those for larger APs (to ensure bigger APs do not artificially reduce their certificate creation to fall under the waiver threshold and avoid up-front fees).

The types of fees and their nominal costs over 2023/24 to 2025/26 are set out in Table 1 below.

Table 1: Comparison of fee options evaluated

Fee	Current fee (where applicable)	Option 1: Activity based	Option 2 (preferred): Discounted fixed fees	Option 3: Fee waivers for small APs
Certificate creation/registration (cost per certificate)	\$1 for registration	\$2.05 for creation	\$2.33 for creation	\$2.09 (or \$2.83 for a small AP) for registration

Application for accreditation	\$500	\$17,218	\$3,000	\$17,218 (or \$0 for a small AP)
Annual re-accreditation	-	\$5,612	\$1,000	\$5,612 (or \$0 for a small AP)
Late lodgement of applications to renew accreditation	-	\$0	\$14,814	\$14,814
Variation of accreditation condition	-	\$6,026	\$1,500	\$6,026 (or \$0 for a small AP)
Project-based activity impact report	-	\$3,778	\$500	\$3,778
Product application	-	\$766	\$500	\$766
Lodging an energy acquisition statement	-	\$3,122	\$3,122	\$3,122
Opening an account to hold and trade certificates¹	-	\$2,332	\$2,000	\$2,332
Review of a reviewable decision	\$200	\$2,500	\$750	\$0

Each option is allocated a score on a scale of -10 (performs significantly worse than the base case) to +10 (substantially achieves criterion) against four equally weighted criteria to achieve an overall score. The scores are assessed by comparing outcomes for each option to the base case of no policy action being taken (i.e. no fees are collected from the participants in the program). The base case is given a score of 0 against each criterion.

The criteria are:

- competition and innovation (fees should not limit program access)
- horizontal equity (the program and individual services recover costs)
- compliance (fees drive compliant behaviour and lower regulatory costs), and
- simplicity (fees are easy to understand and administer).

Table 2 compares the scores for options 1, 2 and 3.

Table 2: Summary of multi-criteria evaluation of fee options

Criteria	Option 1: Activity based	Option 2 (preferred): Discounted fixed fees	Option 3: Fee waivers for small APs
Competition and innovation	-10	-3	-4
Horizontal equity	10	7	8
Compliance	6	8	5
Simplicity	-3	-3	-6
Total weighted score	0.75	2.25	0.75

¹ For those who are not APs and who want to hold and trade certificates, i.e. certificate traders. APs and energy retailers do not need to pay this fee.

All options score more highly than the base case because they produce much better outcomes for horizontal equity and compliance than allowing the fees to lapse.

Option 1 is based on an activity-based costing, where fees reflect the incremental costs of providing each service, and an annual fee that recovers fixed costs. Although fully cost recovering each activity through the fee charged for that activity sends accurate price signals and therefore would be expected to be the most horizontally equitable and economically efficient in the short term, this does not consider the long-term effects of this fee structure. The high fees for various services in option 1 are expected to discourage market entry and product and service innovation, which would have long-term negative effects on the economic efficiency of the program. Additionally, since this option has a certificate creation fee but no fee for the late lodgement of an annual accreditation renewal application, this option receives a moderate score for compliance. Option 1 scores equal to option 3 but lower than option 2, as a result, option 1 is not recommended.

As stated previously, option 2 is intended to avoid excluding small APs by setting most fees at between \$500 and \$3,000 (except for the lodging of an energy acquisition statement which is a fee to retailers). The certificate fee is increased to achieve full cost recovery. This variation means that option 2 reduces barriers to entry for APs with limited ability to pay, thus increasing competition and innovation. However, it would mean that large APs subsidise smaller APs due to the greater reliance on certificate fees for cost recovery than option 1 which reduces its score for horizontal equity. Overall, option 2 achieves the best balance across each of the four criteria compared to the other options and receives a higher score than the other options. Therefore, option 2 is the preferred option.

Option 3 is an alternative way to support smaller APs, by creating an annual threshold for certificate creation, below which small APs would pay zero fees for accreditation and all APs would pay zero fees for reviews of a reviewable decision. Other APs are charged at full cost recovery for most fees, and slightly more than full cost recovery for certificate registration fees to ensure full cost recovery is achieved, which introduces a cross-subsidy between large and small APs. The certificate fee is also higher for smaller APs to ensure there is no incentive for APs to reduce their certificate creation to fall under the threshold. However, option 3 introduces complexities that would be very difficult for the ESC to administer and for APs to understand and comply with. Option 3 scores equal to option 1 but lower than option 2, as a result, option 3 is not recommended.

The new fee structure will be given effect after a notice is published in the *Victoria Government Gazette*. The new fees are proposed to apply from 1 July 2023, replacing the current fees before they lapse on 19 October 2023.

The ESC will implement the required system processes, communicate the new fees to APs and retailers, implement data analytics and monitoring and report on program cost recovery, including through publishing annual performance reports. The Department of Energy, Environment and Climate Action (the department) will work with the ESC to evaluate the new fees as part of a broader review of the VEU program in 2024.

Glossary

Acronym	Definition
Activity-based costing	The costing methodology used to determine the salary and oncost expenses identified in this document
AP	Accredited provider (also known in the VEET Act is an accredited person)
Base appropriation	Government budget funds allocated to an institution's ongoing operations
BRV	Better Regulation Victoria
CBR	Commissioner for Better Regulation
Corporate costs	The costs of providing corporate services, including the cost of human resource management, financial services, infrastructure maintenance and communications costs
CPI	Consumer Price Index
The department	Department of Energy, Environment and Climate Action. As of 1 January 2023, the Department of Environment, Land, Water and Planning (DELWP) became known as the Department of Energy, Environment and Climate Action (DEECA) following machinery of government changes.
DTF	Department of Treasury and Finance
ESC	Essential Services Commission
ESC Act	<i>Essential Services Commission Act 2001</i>
ESC Amendment Act	<i>Essential Services Commission (Compliance and Enforcement Powers) Amendment Act 2021</i>
Fees	Fees charged by the Essential Services Commission in accordance with section 73 of the <i>Victorian Energy Efficiency Target Act 2007</i>
FTE	Full-time equivalent
Operating expenses	Operating expenses cover a range of costs, including: <ul style="list-style-type: none"> • training • information and communications technology costs • accommodation, court room costs and facility management costs • security • corporate costs: Commissioners and executives, human resources, and finance services • pro-rata share of the costs of Commissioners.
RIS	Regulatory Impact Statement
VEU	Victorian Energy Upgrades program
Certificate	Victorian Energy Efficiency Certificate
VEET	Victorian Energy Efficiency Target
VEET Act	<i>Victorian Energy Efficiency Target Act 2007</i>
VEET Amendment Act	<i>Victorian Energy Efficiency Target Amendment Act 2022</i>

1. Introduction

This RIS sets out the reasons for, and the basis of the fees payable to the ESC as the regulator of the VEU program. The proposed fees will take effect from 1 July 2023 and will replace the current fees, which lapse on 19 October 2023.

The ESC provided the department with all costings and options to inform this RIS. The ESC administers and regulates the VEU program in accordance with the VEET Act. The department develops and implements energy efficiency policy related to the VEU program. This division of responsibilities means that the ESC identified the costs to be recovered and developed the fee options for their continued regulation of the program in consultation with the department, whilst the department prepared the RIS.

1.1 Background

The VEU program, established under the VEET Act, is a market-based incentive mechanism that offers financial incentives to households and businesses to voluntarily undertake energy efficiency upgrades. Private businesses accredited under the program (APs) provide these upgrades and create Victorian Energy Efficiency Certificates (certificates) that they sell to energy retailers, who are obliged to obtain and surrender a set number of certificates each year. A certificate represents one tonne of carbon abated. The program is part of the Victorian Government's commitment to reduce greenhouse gas emissions. It is overseen by the department. See Appendix A for more details about the VEU program.

The VEU program is administered by the ESC in accordance with section 10(k) of the *Essential Services Commission Act 2001* (ESC Act). The ESC Act states the ESC is to perform the functions conferred on it by the VEET Act, being the administration of the VEU program.

1.2 Power to set fees for the program

The Minister for Energy and Resources may make fees for the VEU program under section 73 of the VEET Act, which provides that the Minister, after consultation with the Assistant Treasurer, may fix fees for the purposes of the VEET Act or regulations made under it².

In fixing fees, consideration may be given to the administration and operation of the VEU program or more specifically, the costs the ESC incurs (as the regulator) to administer the VEU program. Consideration may also be given to legislative requirements and obligations.

1.3 Current and new program fees

The current VEU program fee structure was set on 11 December 2008³ ahead of the program commencing in 2009 and has remained the same since that point. This includes fees for three services:

- application for accreditation—\$500
- registration⁴ of a certificate—\$1 per certificate
- request for review of a reviewable decision—\$200.

The current fees have not changed since 2009 and do not include indexation. The current fees are set to lapse on 19 October 2023 (see section 2.2.2 for further details). Changes to the VEU program, including the introduction of a code of conduct and changes to the ESC's role and responsibilities have also been considered in setting the fees (see chapter 2 below).

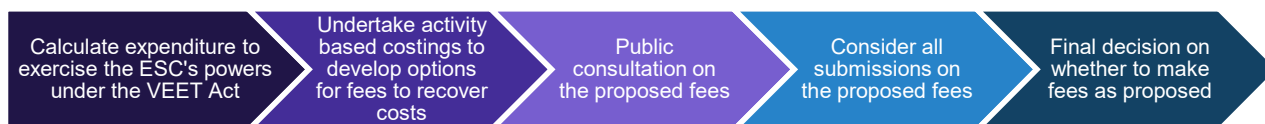
2. Section 73(1) of VEET Act.

3. Government of Victoria (2008) *Victoria Government Gazette* G 50, 11 December 2008, see <http://www.gazette.vic.gov.au/gazette/Gazettes2008/GG2008G050.pdf>.

4. Certificates have a 'registered' status after the ESC has validated the activity documentation

1.4 Assessment and consultation requirements

Before new fees are made, the VEET Act and the *Subordinate Legislation Act 1994* require an assessment of the following:



The ESC calculated the revenue it needs to cover its administration of the VEU program and designed options to achieve full cost recovery. The ESC's three key considerations when determining the setting of fees were:

- the costs incurred by the ESC for each service,
- the nature of the potential response to fee changes by program participants,
- and the implications of this behavioural change on regulatory and policy objectives.

To assist parties to comment on proposed changes to fees, the *Subordinate Legislation Act 1994* requires a RIS to consider the impact of changes where they impose a potentially significant economic or social burden on a sector of the public. A RIS must:

- state the objectives of the proposed changes
- explain the effect of the proposed changes
- identify other practicable means of achieving those objectives, including other regulatory as well as non-regulatory options
- assess the costs and benefits of the proposed changes and of any other practicable means of achieving the same objectives
- state the reasons why the other means are not appropriate.

The department prepared this RIS based on the costings and options provided by the ESC and will publicly consult on them and consider stakeholder feedback in consultation with the ESC. The Minister for Energy and Resources will then set the VEU program fees.

1.5 About this Regulatory Impact Statement

This RIS explains the method used to estimate the costs relating to the ESC's regulatory and administrative functions as they relate to the VEU program. This RIS also describes how the proposed fees were subsequently developed and evaluated.

The RIS takes into consideration the Victorian Government's *Pricing for Value Guide*⁵, which states that there should be full cost recovery for regulatory fees unless this would substantially undermine other important objectives. It has been prepared through consultation and engagement with Better Regulation Victoria (BRV) and as described above, the ESC.

The Commissioner for Better Regulation, who independently assesses RISs in accordance with the *Victorian Guide to Regulation*, has determined this RIS meets the requirements of the *Subordinate Legislation Act 1994*.

This RIS is structured as follows:

- This chapter sets out the background to this RIS, its purpose and how to provide feedback.

⁵ DTF, Pricing for value guide, <https://www.dtf.vic.gov.au/sites/default/files/document/Pricing%20for%20Value%20Guide%20-%20Pricing%20Principles.pdf>.

- Chapter 2 gives an overview of the current regulatory environment and describes the key problems that the proposed amendments to the fees seek to address.
- Chapter 3 describes the policy issues considered in this RIS.
- Chapter 4 explains the methodology used to identify the ESC's costs.
- Chapter 5 describes the objectives the proposed regulations will achieve.
- Chapter 6 describes the policy options considered in this RIS, how they were selected and why other options were deemed not feasible.
- Chapter 7 summarises the costs, benefits, and competition impacts of the preferred and alternative options.
- Chapter 8 provides further detail on how the preferred option will be implemented and evaluated.
- Chapter 9 lists consultation questions that the department are seeking feedback on.

1.6 How to provide feedback

Interested parties and stakeholders are invited to make submissions to the department on the proposed fees and regulations by **26 April 2023**.

All relevant materials and information on consultation forums can be accessed through the Engage Victoria website. For further assistance or to obtain a copy of the RIS, please call 136 186.

Submissions can be made online, via email or via hard copy as follows:

Options for submission	Detail
Engage Victoria's website	https://engage.vic.gov.au/revised-victorian-energy-upgrades-fees
Email	energy.upgrades@delwp.vic.gov.au
Post	Manager, Demand Side Policy Energy Demand and Efficiency Policy Branch Department of Energy, Environment and Climate Action PO Box 500 EAST MELBOURNE VIC 8002

The department will consider all submissions received in response to the proposed fees. Following this, a notice of decision and statement of reasons will be published.

See chapter 9 for specific consultation questions the department is seeking feedback on.

2. What is the problem being addressed?

This chapter discusses the policy, economic, and legislative implications in support of the need for action and describes the key problems that the proposed regulations seek to address.

Significant reforms to the VEET Act that governs the VEU program have resulted in changes in the ESC's costs to administer the VEU program. Therefore, the fees for the program need to be reviewed and revised accordingly.

2.1 Policy context

2.1.1 VEU is helping to decarbonise and electrify Victoria

Climate change is one of the most critical issues facing Victoria and the global community. Risks for Victoria from unmitigated climate change include an average annual temperature increase of up to 2.4 degrees Celsius, sea levels rising by around 24 centimetres and a doubling of the number of very hot days and high fire danger days⁶. The Victorian Government has committed to taking a leadership role on climate change and playing its part in this global effort. In 2020, Victoria's total net emissions were 83.3 million tonnes of greenhouse gas emissions (carbon dioxide equivalent, or CO₂-e)⁷. The Victorian Government have set a target to reduce greenhouse gas emissions by 50 per cent from 2005 levels by 2030⁸ and have announced their intention to set the 2035 emissions reduction target to reduce emissions by 75-80 per cent⁹.

The VEU program plays a crucial role in achieving the government's climate change policy objectives, as well as the broader agenda for a clean and affordable energy system. The VEU program reduces greenhouse gas emissions by decreasing the total demand for energy by residential and business consumers. This reduction in demand is achieved by improving the energy efficiency of premises, or the appliances and equipment used within the premises. Since the VEU program was established in 2009, it has reduced Victoria's greenhouse gas emissions by over 60 million tonnes CO₂-e and supported more than two million households and 140,000 businesses to upgrade their appliances and equipment.

The program is significantly contributing to the achievement of Victoria's interim emission reduction targets established under the *Climate Change Act 2017* and key commitments under *Victoria's Gas Substitution Roadmap*¹⁰, by providing incentives for Victorians to move from gas to energy efficient electrical appliances.

2.1.2 Strengthening the VEU program

The key role the VEU program has in decarbonising Victoria has resulted in several changes to the program and to the ESC's role and therefore its costs. The targets for 2022 to 2025 for the VEU program are:

- larger than any previous targets, up to 7.3 million certificates in 2025
- generating greater energy savings as the energy system decarbonises, with each certificate representing more energy
- anticipated to result in more substantial upgrades and deeper energy savings at each premises (as low-hanging-fruit upgrades such as lighting are phased out)
- anticipated to result in a more diverse range of upgrades.

Because of all these changes, the current \$1 per certificate will no longer support the ESC's costs to administer and regulate the VEU program.

⁶ Victoria's Climate Science report, 2019, see: <https://www.climatechange.vic.gov.au/victorias-changing-climate>.

⁷ Victorian Greenhouse Gas Emissions Report 2020, see: https://www.climatechange.vic.gov.au/data/assets/pdf_file/0036/598257/Victorian-Greenhouse-Gas-Emissions-Report-2020.pdf (released 20 September 2022).

⁸ DEECA Climate action targets, 2023, <https://www.climatechange.vic.gov.au/climate-action-targets>

⁹ Victorian Labour media release, 20 October 2022, see: <https://www.danandrews.com.au/news/putting-power-back-in-the-hands-of-victorians>

¹⁰ Victoria's Gas Substitution Roadmap, 2022, <https://www.energy.vic.gov.au/renewable-energy/victorias-gas-substitution-roadmap>.

As noted in section 1.3 the fees have remained the same since the program commenced in 2009. In historic reviews of fees for the program (in 2012 and 2015), it was found that ESC's costs would increase in line with the target increasing (i.e., the \$1 per certificate fee collected \$2.7 million in fees in 2011 when the target was 2.7 million certificates and increased to \$5.4 million in 2012 when the target was 5.4 million certificates). Therefore the \$1 per certificate fee was not changed.

However, the trends of greater energy savings per certificate, more diverse range of upgrades and more complex upgrades have all changed this and ESC's costs will not match the growth of the targets between 2022 and 2025. Additionally, the ESC fees have not been adjusted to account for inflation (indexed) since 2009 and the ESC is no longer able to absorb these growing costs without reducing service levels.

The role of the ESC has also been expanding. To ensure the broadest participation in the VEU program and provide all Victorian households and businesses the opportunity to decarbonise, the VEU program must have strong consumer protections. Strong enforcement is also critical to achieving the Victorian Government's objectives for the VEU program; if certificates are created improperly, the program's emissions reduction goals will not be achieved.

The VEET Act was reviewed in 2021 to:

- strengthen the statutory framework for the program
- support delivery of the program targets
- provide further certainty for the VEU program
- set it up for the future.

More than 80 stakeholders participated in a consultation on consumer protection issues, and enforcement, compliance, and administration. This included a webinar held on 9 November 2021. A response to the consultation on the Code of Conduct was published on 13 January 2022.

Following the review, the VEET Amendment Act has expanded the range of tools available to the ESC to:

- effectively administer the program,
- monitor compliance of companies working in the program,
- and pursue enforcement where necessary to protect Victorian consumers and ensure the program meets its goals (section 2.2.3 provides more detail).

These changes will ensure the VEU program has a robust compliance framework that enables the program regulator, the ESC, to effectively administer the scheme, monitor compliance of companies working in the program and pursue enforcement where necessary to protect Victorian consumers and ensure the program meets its goals.

In order to support these new functions for the ESC, the VEET Amendment Act provides for new fees from 1 July 2023. These new fees will allow the ESC to recover costs for these new services, including for:

- renewal of accreditation¹¹
- the late lodgement of an application for renewal of accreditation¹²
- an application to vary the conditions of accreditation¹³
- opening an account to hold and trade Victorian Energy Efficiency Certificates¹⁴
- the approval of a product.¹⁵

11. Section 17 of the VEET Amendment Act.

12. Section 17 of the VEET Amendment Act.

13. Section 17 of the VEET Amendment Act.

14. Section 27 of the VEET Amendment Act.

15. Section 65 of the VEET Amendment Act.

In addition, a VEU Code of Conduct was introduced to establish minimum protections for consumers under the program. The Code of Conduct was made via regulations and came into effect on 1 July 2022.

The ESC's costs to administer the VEU program are expected to increase as a result of these additional functions and reforms. Consequently, if fees remained unchanged, there would be an average annual revenue shortfall for the ESC. Therefore, the new fees will need to cover that revenue gap.

2.1.3 Costs and benefits of the VEU program

On 7 December 2021, Governor in Council made amendments to the *Victorian Energy Efficiency Target Regulations* setting the program's energy saving targets for 2022 to 2025. The energy saving targets will increase substantially over the next four years—from 6.7 million certificates in 2022 (up from 6.5 million in 2021) to 7.3 million certificates in 2025. Modelling that informed the development of these targets estimated a net benefit of \$4.4 billion to the Victorian economy and savings to energy consumers of \$1.3 billion.¹⁶

The VEET Act requires that energy saving targets for 2026 to 2030 be set by May 2025. This has three implications for the fee setting review:

- A full program cost benefit review is not warranted or feasible as part of this fee setting analysis, since the department will fully evaluate the VEU program's costs and benefits in 2024 as part of the future target setting process. Instead, this RIS analyses the choices relating to the program fees.
- The fees are being set for a period of three years as fees in future years will be considered as part of the target setting process for 2026 to 2030 and will be set in line with the ambition of those targets.
- To provide certainty for stakeholders the fees in this analysis were set for the period to 30 June 2026, six months longer than the currently set VEU targets to align with the end of the financial year. This analysis includes a simplifying assumption that the targets continue at the 2025 level for 2026 (7.3 million certificates). This is indicative only and is not intended to signal likely targets beyond 2026. This RIS does not seek to pre-empt what the future targets may be; however, it is necessary to apply an indicative assumption to complete the analysis. It is unlikely that the outcomes of the analysis on the preferred fee option would change significantly if the 2026 targets differed substantially from the indicative target, given the short timeframe.

2.2 Why cost recovery?

2.2.1 The Victorian Pricing Principles

The Victorian Government's approach to fees and cost recovery is set out in the *Pricing for Value Guide*. The guide states there should be full cost recovery for regulatory fees unless this would substantially undermine other important objectives.

The services the ESC provides in accrediting providers and validating and registering certificates, allows those providers to trade those certificates and seek to create profit. Similarly other stakeholders benefit from their participation in the VEU program, including product manufacturers who can access discounts for products that the ESC adds to a VEU product register or businesses who trade in certificates. It is consistent with the pricing principles that these businesses should pay for the services that benefit them.

2.2.2 Legislation requires the ESC's VEU program to fully recover costs

The ESC regulates a wide range of services for Victoria, including energy, water, and transport, in addition to their role administering the VEU program. In 2019, the Department of Treasury and Finance (DTF), which has responsibility for the ESC, reviewed how the ESC was funded to support all these functions. The review recommended that the ESC be directly funded through fees collected from those it regulates. These recommendations were then implemented through legislation in the *Essential Services Commission (Compliance and Enforcement Powers) Amendment Act 2021* (ESC Amendment Act). This Act established an:

¹⁶ Regulatory Impact Statement VEET Amendment Regulations 2020, see: <https://engage.vic.gov.au/project/victorian-energy-upgrades/page/targets>

- operating fund
- enforcement fund where certain fees are collected for use by the ESC in enforcement.

These changes mean the ESC's VEU division will move to being fully directly funded through fees collected from program participants. This is in line with other government programs, where stakeholders whose activities result in costs of administering or regulating a program contribute to those costs. This is consistent with the *Pricing for Value Guide*, as noted above.

The DTF review also recommended the VEU program fees be reviewed and set with the aim of full cost recovery, to the extent suitable in accordance with Victorian pricing principles. This recommendation was also made into law to ensure that new program fees are established. The current VEU program fees will lapse on the second anniversary of the day on which the ESC Amendment Act received Royal Assent (19 October 2021)¹⁷. Therefore, the fees for the VEU program must be reviewed and new fees in place before 19 October 2023.

The ESC considers that all costs associated with the administration of the VEET Act and regulation of participants, including ancillary support organisational functions, should be fully cost recovered via fees in alignment with those principles.

2.3 Changes to the ESC's costs

2.3.1 Current fees do not fully cost recover the ESC's costs

The ESC has three major sources of funding for the ESC services that relate to the VEU program:

- discretionary government budget allocations and budget bids
- fees from certificates
- existing base level of government funding appropriation (where fees are insufficient).

Currently, the ESC recovers¹⁸ some of its costs for the VEU program through a \$1 certificate registration fee and a \$500 fee to apply for accreditation. The difference is made up by allocations from the general revenue of the Victorian Government (referred to as an existing base appropriation).

The ESC can also seek discretionary government budget allocations for specific purposes or projects in addition to the fees and allocations from the Victorian Government.

The ESC's additional functions arising from the VEET Amendment Act together with a more diverse range of upgrades under the VEU program mean the program's administration costs will increase. The ESC has advised the department that if fees were to remain unchanged, it could result in an estimated average annual revenue shortfall of approximately \$11 million per year for three years.

2.3.2 The ESC's role is expanding

The costs associated with the administration of the VEU program are set to increase as a result of additional functions introduced under the VEET Amendment Act. These additional functions were well supported by stakeholders during the consultation period for the VEET Amendment Act. The ESC functions ensure the program maintains strong consumer protections, compliance and consumer trust in the program, which are essential to ensuring the program benefits continue to be realised.

These additional functions include:

- investigating and enforcing additional types of breaches and offences in the VEU program, for example AP marketing in a manner that does not meet Code of Conduct requirements

17. Section 77(b) of the ESC Amendment Act states that any existing fees for the VEU program continue in effect until fees are revoked or two years after the ESC Amendment Act came into force. Therefore, the existing fees, as described in chapter one of this RIS, will lapse on 19 October 2023.

18 Prior 2022 and the implementation of the ESC Amendment Act, fees for the VEU program went to consolidated revenue, rather than ESC receiving the funds directly.

- providing additional powers and enforcement tools to the ESC, for example accreditation suspensions or accreditation cancellations
- introducing penalties for third parties or scheme participants in the VEU program
- requiring APs to annually renew their accreditation
- introducing annual accreditation assessments such as the ‘fit and proper person’ and ‘competent and capable person’ tests
- introducing VEU registry account restrictions
- introducing the requirement for independent assurance audits.

2.4 The base case - what would happen if no action were taken?

Without action to set new fees on or before 19 October 2023, the current fees will cease to exist and the VEU division of the ESC will have insufficient revenue to conduct its regulatory and administrative functions, which are necessary for the basic functioning and integrity of the program (Table 3). The assumption underpinning the analysis in this RIS is that the ESC must be funded to deliver against their statutory obligations to regulate and administer the VEU program. Accordingly, in the hypothetical base case scenario that the fees lapse, and no new fees are established under the program, the ESC would seek to receive funding from an alternative source (i.e., budget funding from consolidated revenue) to ensure the ESC can deliver on its statutory obligations and the program can continue to operate. This would require a subsidy from taxpayers of \$54.2 million across the three years.

In the event the fees remain unchanged, there would be an average annual revenue shortfall in the order of \$11 million per year.

The operational arrangements for the VEU program contained in the VEET Act and regulations give the ESC the power to make administrative decisions (e.g., accreditation of providers) necessary for the basic functioning of the program and its integrity. These are summarised in Table 3 below.

Table 3: Administrative decisions of the ESC under the VEU program

ESC obligations under the VEET Act	ESC’s discretionary powers under the VEET Act
<ul style="list-style-type: none"> • Maintain an electronic system to allow APs to create and transfer certificates • Maintain registers of information, including a register of APs, a register of certificates, and a register of approved products • Decide if certificates are eligible for registration and register certificates • Approve or refuse applications to be accredited • Publish guidelines • Annually report on the performance on the VEU program to the Minister and publish information about the surrender of certificates each year • Confirm, vary, or set aside decisions for which a review is requested • Assess energy retailers’ compliance with the requirements for surrender of certificates to meet the target 	<ul style="list-style-type: none"> • Request information, evidence, or records, conduct site visits or otherwise investigate to substantiate information provided under the VEET Act or to determine if the VEET Act has been complied with • Bring proceedings for an offence under the VEET Act or regulations • Require certificates created unlawfully to be surrendered • Require an AP to undertake a compliance audit

As discussed above, The Victorian Government would need to ensure the ESC’s legal obligation under the VEET Act could be met, which would require subsidising the increase in VEU program costs from general government revenue, including taxation, which would be inconsistent with the DTF’s recommendations and the *Pricing for Value Guide* (section 2.2.1).

The VEET Act and regulations clearly intend for the ESC to have the resources necessary to use its discretionary powers. The structure of the legislation is such that the effective operation of the VEU program relies on the ESC having sufficient resources to undertake its discretionary powers, such as validating certificates to ensure they have been correctly created and undertaking compliance and enforcement actions. If the ESC did not have the resources to apply these powers, errors and outright fraud would not be identified or prevented. This could result in a cost to consumers (via retailers) without a benefit being realised for consumers (improved energy efficiency with associated energy savings and greenhouse gas abatements).

Therefore, the VEU program's significant benefits (see section 2.1.3) rely on the ESC having the resources to effectively administer the program and without this resourcing these benefits may not be achieved. The VEU program is a fundamental part of delivering key government commitments on energy affordability and emissions reduction. In the base case the Victorian Government would honour its commitments to strengthen and expand the VEU program. Therefore, it is reasonable to assume for the purpose of this analysis, that VEU program costs would be met with alternative sources of government revenue if no fees were set.

3. Factors considered in designing options to address the problem

Chapter 2 of this RIS established that the fees for the VEU program need to be reviewed and to achieve full cost recovery for the program to meet its legislative requirements. This chapter will set out the key policy issues we are seeking to explore as options for different approaches to setting the fees as part of this public consultation.

3.1 Context

3.1.1 Victorian Government pricing principles

As noted in the previous chapter, the *Pricing for Value Guide* establishes a whole of government framework to ensure that price-setting is transparent, efficient, effective, and consistent with legislative requirements and government policy. In developing the options, this RIS seeks to balance competing pricing principles in the guide and considers the objectives of the VEET Act.

The starting pricing principle is that agencies should aim to recover the full costs of service provision to promote efficient consumption and, in turn, the efficient allocation of resources by sending appropriate price signals about the value of resources required to provide the good or service. The pricing guide recognises this is one of several principles.

The second pricing principle is that the cost-of-service provision should be borne by those who benefit from it. Fees should be specific to the task or service being provided, rather than having cross-subsidisation across different services. Setting of fees should consider not just the direct costs required to deliver a particular service, but also the indirect costs such as salaries and utilities, using an activity-based costings methodology.

For the VEU program, APs are the key people who benefit financially from the services the ESC provides, which enable them to create and trade certificates. The services the ESC provides for energy retailers, product manufacturers, and people trading certificates may also be relevant to consider.

3.1.2 VEET Act objectives

As noted in the previous chapter, VEU is a key policy to address climate change and reduce energy bills. In addition to the pricing principles, it is important that the fees support the VEET Act objectives. The nature of a program that seeks to encourage innovation and investment is that many participating businesses may start at a small scale and be sensitive to upfront costs.

In considering how ESC's costs that will be passed on to the consumer of those services (e.g., APs) it is important to ensure these businesses have economic incentives to enter the market and invest in the energy efficiency industry.

This RIS seeks to define and assess options that take a range of different approaches to costs for small APs and considers the impacts of fees on small businesses.

3.2 Supporting competition and innovation

As noted above, to achieve the third objective of the VEET Act (to “*encourage investment, employment and technology development in industries that supply goods and services which reduce the use of electricity and gas by consumers*”), the program needs to have low barriers to entry and support small-scale businesses who may be sensitive to upfront costs (section 2.4.1).

The current pool of APs includes large corporations and very small operators. The current fee structure supports this range, with APs paying from less than \$100 per year to more than \$700,000, depending on how many certificates they create.

Currently, to become an AP, a person must apply to the ESC once for an ongoing accreditation and pay a one-time fee of \$500. This approach means that accreditation is a small portion of the services ESC provides and a small portion of fees paid by APs.

However, this will change in two ways when the requirements for the VEET Amendment Act commence:

- To enter the program, a prospective AP must submit an application to the ESC that meets its new accreditation standards.
- APs must apply for their accreditation to be renewed once every 12 months.

High fixed annual fees or entry fees might discourage small operators from participating in the program, having a negative impact on industry development and employment. To reduce this risk, the fixed fees might need to be reduced.

3.2.1 Application for accreditation fee

Once the requirements for the VEET Amendment Act commence, APs will need to satisfy the ESC that they are fit and proper people who are competent and capable of complying with the program requirements.

These criteria will require the ESC to conduct more extensive checks for the initial application than for accreditation extensions or renewals. Therefore, the initial accreditation cost is higher than the annual re-accreditation costs.

However, upfront fees may represent a barrier to entry into the VEU program, especially for smaller businesses. The development of options will consider different ways to structure accreditation costs to explore the trade-offs that need to be made to support competition and innovation by reducing barriers to entry into the program.

3.2.2 Annual re-accreditation fee

Once the requirements for the VEET Amendment Act commence, accreditations for APs will expire after 12 months. APs must apply for their accreditation to be renewed every 12 months.

APs will need to satisfy the ESC that they are still fit and proper people who are competent and capable of complying with the program requirements as part of their re-accreditation. To reach the point of applying for an accreditation renewal, an AP will have already been assessed as part of their initial accreditation application. This means the evaluation process for accreditation renewal can be less resource intensive than the new accreditation process without introducing significant compliance risks.

A risk-based approach to this process could mean that APs with a history of non-compliance may be flagged each year for detailed accreditation renewal checks, while APs with a demonstrated history of compliance may face less detailed checks.

Similar to the accreditation fee, upfront annual fees may represent a barrier to ongoing participation in the VEU program for small businesses. The development of options will consider different ways to structure re-accreditation costs to explore the trade-offs which need to be made to support competition and innovation.

3.2.3 Variation of accreditation condition fee

Certificates can be created under the VEU program for any one of 36 different activities. If an AP seeks to change their accreditation to allow them to participate in a new prescribed activity that was not a part of their initial accreditation, they must apply to the ESC for a variation of their accreditation condition. The fee is payable for each additional activity requiring accreditation.

Examples of common activities include lighting upgrades, water heating upgrades and space heating upgrades. APs are likely to seek to become accredited in all activities at the outset, which they believe they may wish to perform and can demonstrate evidence of suitable competency in.

Currently, the ESC does not charge fees for applications for variations of accreditation conditions. Once the VEET Amendment Act changes come into force, the ESC will be able to charge fees for these applications.

An application for a variation of accreditation conditions requires the AP to have already successfully applied for a new accreditation, making the evaluation process less resource intensive compared to a new accreditation.

Upfront fees for expanding into delivering new types of upgrades may represent costs to businesses investing in new activities. The development of options will consider different ways to structure accreditation variation costs to explore trade-offs to support competition and innovation.

3.3 Horizontal equity

Fees should aim to minimise cross-subsidies between different VEU program participants. There are several program participants who are currently not subject to any fees. This means their participation in the VEU program is being cross subsidised by the fees paid by APs. All options in this RIS will include new fees for these participants.

In addition to the consideration of horizontal equity between different classes of participants, i.e., product suppliers and APs, the analysis section of this RIS will also consider the cross-subsidisation between the same class of participants, such as different size APs.

3.3.1 Lodging energy acquisition statement fee

Each year, energy retailers who are relevant entities under the VEET Act, must submit their energy acquisition statements indicating their gas and electricity liabilities. ESC staff evaluate each statement to ensure accuracy and compliance. Activity-based costing analysis indicates the resources required to process each energy acquisition statement is \$3,122. All options set the fee for lodging an energy acquisition statement at that level to reflect these costs.

3.3.2 Opening an account to hold and trade certificates fee

Once the requirements for the VEET Amendment Act commence, persons seeking to open a registry account for the purpose of holding and trading certificates will need to be found to be fit and proper by the ESC.

APs will have already been assessed as fit and proper in order to become accredited and open a registry account and will therefore not need to pay this fee in order to hold and trade certificates¹⁹. A range of other stakeholders hold and trade certificates, including certificate brokerage companies, banks and those purchasing certificates as carbon offsets for voluntary surrender. These stakeholders will need to pay this fee once in order to establish their account.

Activity-based costing analysis indicated that the ESC's costs to process each application will be \$2,332.

3.3.3 Product application fee

For a product to be added to the VEU product register (and hence be eligible to be used under the program), an application must be submitted for the ESC to approve. Currently, the ESC approves many products that are never installed as part of a prescribed activity. This indicates that ESC resources used to evaluate these applications may have been deployed unnecessarily. In recommending a fee for product applications, the ESC aims to reduce this problem by reflecting the costs required to process product applications.

For example, of the approximately 9,000 products registered under activities 1 and 3 (water heating upgrades), about 1,000 have ever been used as part of a VEU upgrade. The businesses registering these products may receive benefit from having their product on the register of energy efficient products regardless of if it is installed under the program, therefore there should be a fee specifically for this service, rather than cross subsidising this service from fees collected from elsewhere.

3.4 Compliance

Another pricing principle is that the structure of fees should encourage regulated parties to engage in desired behaviours, such as improved punctuality, timeliness, accuracy, and compliance. It is important to send accurate price signals about the relative effort of different regulatory activities to avoid excessive, inefficient demand for some regulatory services that would lead to the inefficient use of resources and market distortions, such as some APs intentionally 'gaming' the program to lower their own costs at the expense of other APs.

¹⁹ Please note, to open a VEET registry account, they have to pass a 'fit and proper' test only, whereas APs applying for accreditation need both a 'fit and proper person' and a "competent and capable person " test as per Act Part 3, div6, s26a and sections 10C.

Under the current VEU fee structure, an AP who is fully compliant when they create certificates will pay the same fees as an AP who creates certificates with inaccurate or incomplete information. An AP who creates certificates with inaccurate information can withdraw them to rectify the mistake and then create new certificates with correct information without incurring any extra fees, however this creates additional work for the ESC. Charging a fee at the point of certificate creation, would incentivise accuracy and compliance for APs.

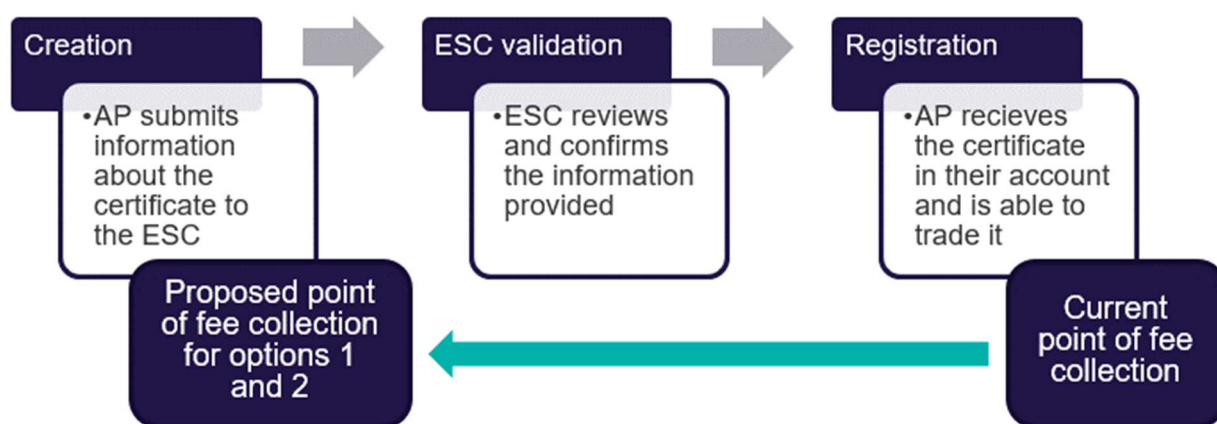
Additionally, some negative behaviours can generate extra costs or delays in program administration. For example, an AP submitting a late application for their annual accreditation renewal would require ESC to divert staff from their usual roles to assess the late application, leading to additional costs. Where practical, these fees should be borne by the relevant parties.

Pricing should support compliance and regulatory outcomes. Fees should disincentivise ‘free riding’ behaviour, poor-quality applications, and poor internal quality control processes. Such behaviours transfer costs and risks from APs to the ESC and are economically inefficient.

3.4.1 Fees at the point of certificate creation or registration

One of the choices explored in this analysis was between setting fees for APs creating certificates at the start or end of the process (Figure A). When an AP *creates* a certificate, the ESC begins work validating that the certificate was created in compliance with the requirements of the VEET Act. This involves assessing energy upgrades to ensure the AP supplied accurate details and evidence that meet the requirements. Certificates that the ESC deems valid are *registered*; certificates deemed invalid are not registered.

Figure A: Change in fee collection point



As illustrated by Figure A, under the current fee structure, the certificate fee is charged only upon certificate registration. This aligns the timing of the AP paying the fees more closely with the time they can trade the certificates, minimising the impact on cashflow.

Charging a certificate fee at the creation phase (rather than at the registration phase under the current arrangements) better reflects when the ESC incurs most costs and incentivises APs to provide all relevant documentation up-front. The certificate fee would not be refunded if the ESC did not validate the certificate, for example if the AP provided insufficient evidence. Where certificates are withdrawn by the AP or not validated by the ESC, the AP would have to pay a second certificate creation fee if they later rectified the issues and created a second set of certificates for the same installation. Charging a certificate fee at the creation phase is cost reflective, since the ESC incurs costs for each certificate created and evaluated regardless of whether it is ultimately registered.

This shift in the timing to the fee being payable at the creation phase will result in APs having to pay for ESC to validate the certificate before it can be sold. ESC will only begin the process of registration validation assessment after issuing a certificate invoice fee for the creation fee and receiving payment for that invoice.

Under the current system, the ESC has a risk-based approach to managing this timing, with a target timeframe of seven days to process the lowest risk certificates and up to 60 days to process higher risk certificates. The ESC aims to complete the validation within two days of the target timeframe. APs would be incentivised to have high rates of compliance so they can be assessed as lower risk and subsequently receive their certificates sooner.

The time between paying the fee and selling the certificate may present potential cashflow management implications for some businesses. APs may consider updating their business models and contracts with installers and lead generators to mitigate any potential cashflow impacts. APs currently successfully manage their cashflow regarding upfront payments of materials and labour costs whilst they wait for registration of their certificates so that they can sell them. These existing costs are significantly larger than the proposed certificate creation fees.

The development of options will consider different ways to structure certificate fees to explore differences between a fee at the point of registration or creation.

The option of having fees for both certificate creation and registration was considered and discarded. Splitting the certificate costs between certificate creation and registration would introduce significant administrative complexities and associated risks for the ESC. A split fee would also create more administrative burden for APs.

3.4.2 Late lodgement of applications to renew accreditation fee

Once the VEET Amendment Act requirements commence, APs will be required to apply to renew their accreditation 90 days before their current accreditation expires. This provides sufficient time for ESC to assess the application. Note a late lodgement prior to the expiry of the accreditation does not risk an AP's accreditation lapsing on the date their accreditation expires. The AP will remain accredited until the ESC has made an assessment on their late application to be re-accredited.

Under transitional requirements, the ESC will nominate an expiry date for all existing AP accreditations within 12 months of the requirements commencing. The ESC will be able to charge a late lodgement of application to renew accreditation fees when an AP applies for an accreditation renewal less than 90 days before their accreditation expires, as outlined in the VEET Amendment Act.

The ESC's intention is that a late lodgement would trigger a detailed assessment of the applicant to address concerns about the nature of the applicant's processes that led to their late submission. The fee is intended to cover the costs the ESC will incur to procure the temporary resources required to complete a detailed assessment at short notice. The detailed assessments will include but are not limited to:

- an assessment of the applicant's organisational structure
- participation in other government energy efficiency programs
- proposed program service delivery arrangements
- history of compliance with the VEU program
- record keeping
- quality assurance protocol
- training and development protocol
- and other policy and procedural considerations.

The development of options will include options without a late fee and options with a late fee to ensure we receive stakeholder feedback on a range of options.

3.4.3 Project-based activity impact report fee

Project-based activity (PBA) impact report fees will be charged at the third and final stage of the PBA approval process – the impact report. Charging a fee for PBA impact reports is intended to reflect the ESC's costs and incentivise high quality applications.

There is a potential risk this PBA application fee might discourage applications and reduce the number of PBA projects. This may introduce risks to achieving the objectives of the VEET Act and achieving the full benefits of the VEU program.

PBA projects have delivered more than 300,000 certificates since they were first introduced in 2017, a relatively small but important and growing part of the overall VEU program. As the VEU program looks to support a more diverse range of upgrades and deeper retrofits, the PBA approach will likely have a larger share of activities undertaken in the program. However, PBA projects do require greater oversight from the ESC and therefore represent greater costs compared to other methods for creating certificates under the program. Therefore, it is appropriate to consider fees to minimise cross subsidisation.

Historically, more than 75 per cent of PBA projects have generated more than 1,000 certificates per project (equivalent to \$73,000 of incentives at a certificate price of \$73). The average project should be large enough to support the introduction of fees, however it is important that fees do not have a perverse effect on participation in smaller PBA projects.

Currently PBA projects must submit a project scope and a project plan before undertaking works on site and then an impact report after upgrades have been installed and energy savings demonstrated. The impact report stage is the final stage before certificates are created for a PBA project and therefore the proposed stage for fees to be collected.

The development of options will consider different approaches to facilitate stakeholder feedback.

3.5 Simplicity

In addition to the factors listed above, the options should also be designed to illustrate a range of options in terms of simplicity. Pricing structures should be easy to understand and simple to administer. The fees should not impose a disproportionate burden to administer or be a barrier for stakeholders to understand and predict.

The guide encourages simplicity and efficiency in pricing arrangements. Simpler fee structures are preferable to overly detailed and precise arrangements.

In some cases, the principle of simplicity may be in tension with the principle that the service should be borne by those who benefit from it. This RIS seeks to define options that take different approaches to balance this tension.

3.6 Ensuring access to review of decisions

It is important to maintain fairness and the perception of fairness in the operation of the market (i.e., participants are treated fairly by the ESC in terms of fees and access to justice). If a person is subject to an ESC decision, that person has a right to request the decision be reviewed internally by the ESC.

Charging a fee for an internal decision review is intended to reflect the costs incurred by the ESC during the review process without limiting access to justice. Activity-based costing indicated the cost of recent decision reviews was approximately \$2,500, not including the costs of external professional advice. Some costs are unrelated to the collection of fees, and they are not included in the estimates. There is some risk that this level of internal decision review fee would restrict access to justice.

For comparison, the Clean Energy Council charges \$750 for an application appeal fee. Analysis indicates this level of fee would prevent frivolous submissions without limiting access to justice.

The development of options will include different fee levels for a reviewable decision to explore the alternative options for access to justice and issues of cross subsidisation. Ensuring access to justice is a principle that only applies to the fee related to reviewable decisions. Therefore, this is assessed separately from the multi-criteria analysis.

4. Costing methodology

This chapter describes the steps taken to analyse the ESC's costs that relate to the VEU program.²⁰ The steps to analyse these costs include:

1. identifying the main relevant services/functions under the VEU program
2. allocating costs to services/functions
3. considering an efficient level of costs to be included in the cost base for the purpose of setting fees
4. considering revenue escalation.

4.1 Identifying relevant services

To allocate the above expenditure to fees for services for the VEU program, the first step was to identify the ESC's services carried out under the VEU program. The ESC's responsibilities under the VEET Act were translated into the services summarised in Table 4, which may be subject to a fee under this proposal.

Table 4: ESC's services under the VEU program

Service	Description of ESC costs allocated to service	Is a fee currently charged?
Application for accreditation	To create certificates under VEU, a person must be an AP under the VEET Act. This fee relates to the costs of assessing an application for accreditation, including whether the documentation complies with section 9 of the VEET Act. The ESC will assess whether applicants are fit and proper, and competent and capable.	Yes
Creating certificates	Includes the costs of validating and creating certificates and various annual activities, including compliance and enforcement, governance, IT, market monitoring, as well as corporate and executive support. Several annual activities are allocated to the cost of creating certificates because they are not related to any other service provided by the ESC to any particular person or program participant, but rather they address the program as a whole.	Yes
Lodging an energy acquisition statement	Each year, energy retailers with scheme acquisitions must submit audited annual energy acquisition statements. These are the costs to review retailer's audited annual energy acquisition statements under Part 5 of the VEET Act.	No
Product application	The costs associated with assessing a proposal to add a product to the Register of Products (e.g., ensuring it meets minimum criteria specified in the VEET regulations).	No
Annual reaccreditation	The costs to assess annual applications for reaccreditation.	New service
Application for variation of accreditation condition	The costs to assess an application to undertake additional activities under the program, additional to the original accreditation application.	New service
Opening an account to hold and trade certificates	The costs to assess and set up a trading account to facilitate the transfer and surrender of certificates.	Expanded service
Project-based activity impact report	The costs to assess impact reports from existing APs to establish energy savings from large and custom upgrade projects.	No

²⁰ The ESC provides a range of other services outside of the VEU program, which are funded through alternative sources.

Review of a reviewable decision	The costs to administer/review reviewable decisions. Part 7 of the VEET Amendment Act outlines which decisions can be reviewed.	Expanded service
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The new and expanded services listed above will apply once the VEET Amendment Act changes come into effect. Most of these changes will come into effect when proclaimed by the Minister for Energy and Resources – this is planned for mid-2023 (Table 5).

Table 5: Timing of introduction of new and expanded services under the VEU program

New service	Timing
Annual reaccreditation	Once Part 2 of the VEET Amendment Act is proclaimed, there will be a transitional period of 12 months for existing APs to move to an annual accreditation (as per section 19 of the VEET Amendment Act). After this, the APs will need to apply annually for reaccreditation and their application will need to be accompanied by the relevant fee.
Application for variation of accreditation condition	Once APs transition to an annual accreditation they may wish to make changes to their accreditation, for example expanding the number of activities their accreditation covers.
Opening an account to hold and trade certificates	Part 3 of the VEET Amendment Act will commence on 1 November 2023. There will be a transitional period of 12 months for existing certificate holders (see section 28 of the VEET Amendment Act), during which time they will need to apply to the ESC and this application must be accompanied by the relevant fee. This fee will only need to be paid once, either on opening an account or transitioning an existing account for those covered by the transitional arrangements. This fee will only be paid by stakeholders who are not APs. AP costs for creating a VEET registry account are covered by accreditation fees.
Review of a reviewable decision	APs are currently able to apply to the ESC for a review of certain decisions made by the ESC. A request for a decision to be reviewed by the ESC must be accompanied by the relevant fee. Once Part 7 of the VEET Amendment Act is proclaimed, APs will be able to seek a VCAT review after exhausting ESCs internal review process. External costs of VCAT reviews will be borne by applicants separately as per VCAT fee structures.

4.2 Allocating costs to services

An activity-based costing approach was used to allocate costs to services. This is a 'bottom up' approach that involves understanding cost drivers for each task and assigning costs for each task to the relevant services.

This process involved assessing how a change in the quantity of a service provided might (or might not) affect the costs for each task. In several cases, the cost of a task directly relates to a single service. For example, the cost of assessing and approving product applications directly relates to the number of product applications received, and no other tasks contribute to this service.

Delivering a particular service may require staff from several different teams, and the ESC identified the number of relevant staff (full-time equivalents [FTEs]) at each salary grade involved in each task. Where staff spend some of their time undertaking a variety of tasks, either related to the VEU program or not, an FTE weight was applied (e.g., 100 per cent if a staff member is dedicated entirely to a particular task, 50 per cent if a staff member spends half their time on a task).

In addition, program costs include a share of indirect costs (e.g., share of corporate services costs). Indirect or common ESC costs (e.g., corporate costs) were allocated using a pro-rata approach, based on the number of staff that work in each of the areas ESC regulates (i.e., water, energy and transport in addition to the VEU program). The ESC estimates that the VEU program's share of corporate costs is 40 per cent.

The costs the ESC provided to DEECA include a range of existing functions, new functions, and indirect costs (Table 6).

Table 6: ESC costs and tasks

Costs for existing ESC tasks	Indirect tasks	Costs for new functions
<ul style="list-style-type: none"> • New/varied accreditations • Validating/creating certificates • Approving products • Approving PBA plans and reports • Retailer and certificate surrenders • Managing enquiries/complaints • Compliance strategy • Compliance operations • Reporting • Enforcement • Policy/program governance • IT systems • Data governance 	<ul style="list-style-type: none"> • Executive office • Corporate support • Legal support • External costs (e.g., recruitment, ongoing IT licensing costs). 	<ul style="list-style-type: none"> • Annual reaccreditations • Account creations • Assurance audits • Managing program changes • Market monitoring

The allocation of task costs to services as provided by the ESC is summarised in Table 7 below. Certificate creation, validation, and registration account for 83 per cent of the ESC’s costs for the VEU program.

It is proposed that common costs be recovered through certificate costs because it is likely that certificate creation has a relatively low-price elasticity of demand, since APs would be able to pass most of these fees on to retailers. These common task costs are allocated 100 per cent to certificate costs in Table 7 below. Most of these tasks can also be directly attributed to the process of certificate creation or registration, for example assurance audits prove that certificates are legitimate and compliance operations disincentivise illegitimate certificates.

Table 7: Allocation of task costs to services

Tasks	Services							
	Application of accreditation	Creating certificates	Energy acquisition statement	Product application	Annual reaccreditation	Variation of accreditation conditions	Opening an account to hold and trade certificates	PBA application
New/varied accreditations	60%				40%			
Annual reaccreditations	100%							
Account creations	100%							
Validating/ creating certificates	100%							
Approving products	100%							
PBA activities	100%							
Retailer and certificate surrenders	100%							
Assurance audits	100%							
Managing enquiries /complaints	100%							
Compliance engagement	100%							
Compliance strategy	100%							
Compliance operations	100%							
Reporting	100%							
Enforcement	100%							
Managing program changes	100%							
Program governance	100%							
Market monitoring	100%							
IT systems	100%							
Data governance	100%							
Executive office	100%							
Corporate support	100%							
External costs	100%							

4.3 Relevant costs

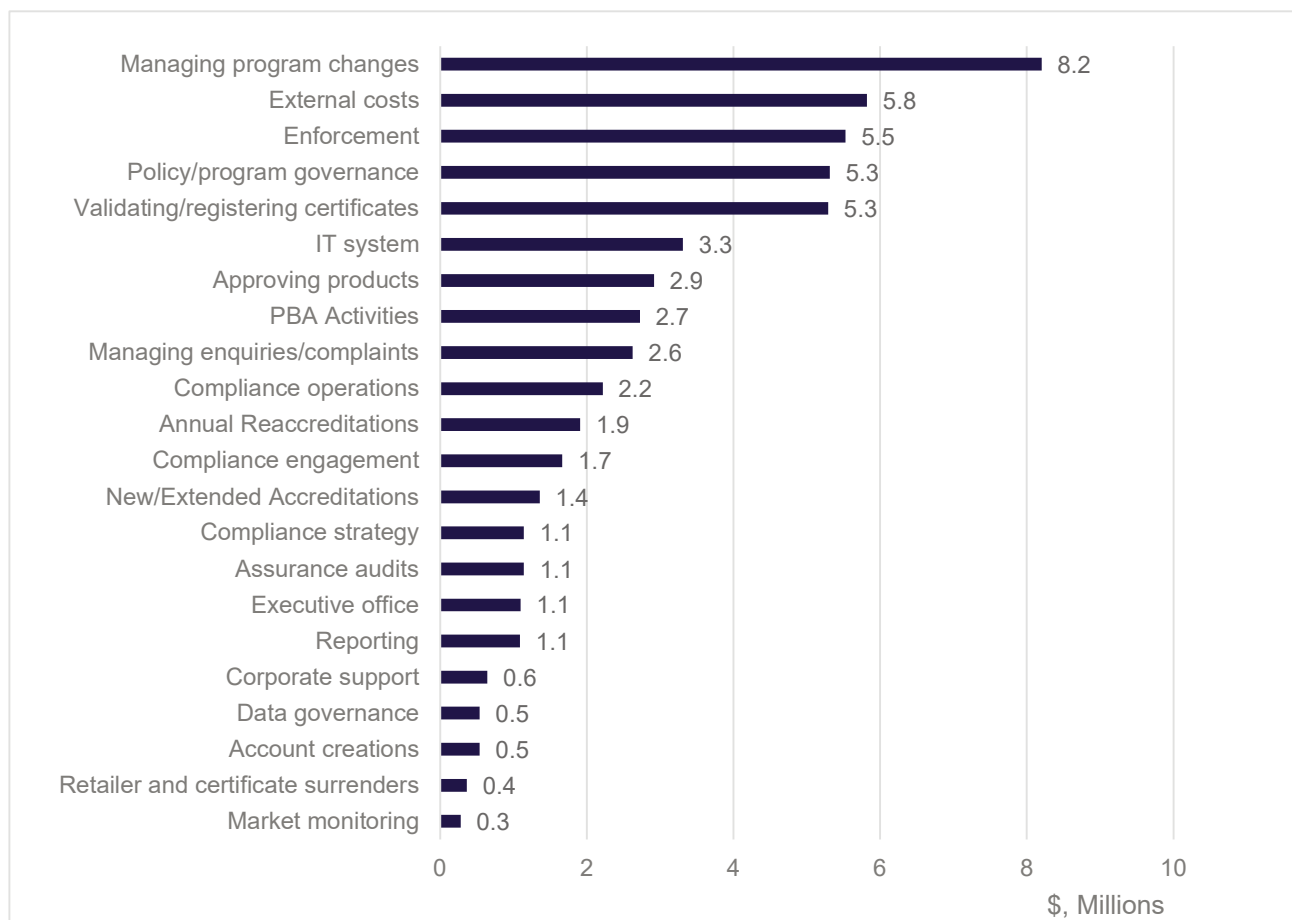
With the introduction of the VEU Code of Conduct and the changes arising from the VEET Amendment Act, the total expenditure attributable to the VEU program is expected to increase from \$16.2 million in 2023-24 to \$19.4 million in 2025-26 (Table 8). This nominal total of \$54.2 million across the three years is equivalent to \$47.2 million using a net present value calculation based on inflation and real discount rate estimates sourced from Reserve Bank of Australia and the Victorian budget.²¹

Table 8: VEU program costs over 2023-24 to 2025-26 (nominal)

Financial year	2023-24	2024-25	2025-26
ESC's VEU program costs	\$16.24 m	\$18.56 m	\$19.40 m

This includes direct costs (such as salaries and operating expenses of staff directly involved in regulation) and indirect costs (such as corporate functions shared across different areas the ESC regulates) (Figure B). The largest cost is salaries (including on-costs and overheads), making up approximately 90 per cent of total costs. The increase in costs represent approximately 30 additional FTE, across a range of Victorian public sector levels performing different services and functions across the VEU team. The costs increase over the three years as the ESC ramps up its implementation of the program reforms.

Figure B: ESC VEU program costs by tasks—total cost for three-year fee period



²¹ This net present value calculation is based on an annual real discount rate of 4%, combined with annual inflation forecasts. The Reserve Bank of Australia's February 2023 Statement on Monetary Policy inflation forecasts used were 3.5% for 2023-24 and 3.0% for 2024-25. For 2025-26, the 2022 Victorian budget projection of 2.5% was used."

4.4 Resourcing estimates

ESC's costs are based on estimates of the number of APs in future years and the assumed number of services that will be provided (e.g., number of accreditations, etc), which are then translated into estimates in increased costs in section 4.3. Further information on the assumed number of services is provided in Appendix B.

These resource estimates are based on several assumptions. Existing trends in current functions were assumed to continue. For example, the current growth rate in consumer complaints related to the VEU program are assumed to continue due to the projected introduction of new residential upgrades.

It was also assumed that the ESC can find internal staffing efficiencies and leverage collaboration between the resources in the new approach outlined below. For example, additional capacity in the compliance team can be utilised by the accreditation team in a flexible manner. Further assumptions and explanations for each process are listed below.

4.4.1 Accreditation

The accreditation process will undergo a significant shift from an assessment of completeness of the information provided in an application. There will be new legal tests on the suitability of the prospective accredited person. That means the processes will require additional rigour and in-depth assessments of certain criteria. In addition, an annual re-accreditation process will be implemented, and ESC will have to administer the imposition of new accreditation conditions to ensure standards do not decline. These new functional requirements have informed ESC's assessment of future costs.

The ESC will use a risk-weighted approach to the re-accreditation of existing APs to minimise operational cost impacts, with higher risk APs undergoing a more detailed process to determine whether they remain 'fit and proper' and 'competent and capable'. This approach will make re-accreditation balanced and efficient.

The significant increase to the rigour of accreditation processes under the *VEET Amendment Act 2022* means that the number of accreditation applications assessed per FTE will decrease. However, the ESC believes that there will be efficiency gains once the estimates account for the higher effort required in the future, and the increased effectiveness of new accreditation processes.

The new process to administer accreditation conditions imposed on accredited persons is fundamental to the regulatory approach. The ESC will implement a risk-based approach to minimise costs of administration, in conjunction with compliance functions (see section 4.4.3)

4.4.2 Registration of certificates

The revised approach to administering the VEU program will involve expanding the team responsible for registering VEECs to meet the anticipated increase in VEECs and program participation. The registration process will also be made more efficient as part of ongoing IT system upgrades. The ESC registration team resource estimate assumes that current VEEC batch numbers will double in the near future, and a small increase on current staffing levels is expected. Anticipated efficiency gains from IT system upgrades means the ESC anticipates that the number of certificate batches processed will increase by about 35% per FTE, compared with the previous 5 years.

4.4.3 Compliance and scheme monitoring

The ESC will create a new compliance team to administer a new independent assurance audit process and panel of auditors, undertake more compliance audits, and monitor the market for VEECs. The compliance team is expected to include some employees that will be redistributed from the existing audit team. Each year the team will analyse information related to 20 escalations, conduct 15 compliance audits, and perform 50 assurance audits. The ESC's flexible approach will allow them to scale the audit function based on the demands of the program. This means the ESC can redirect resources to higher risk APs, utilise resources from other teams if demand peaks or conduct more detailed audits if there is a reduced participation in the

program. ESC analysis indicates that the efficiency would increase by 45% per FTE in the number of audit and compliance actions undertaken compared with the previous 5 years.

4.4.4 Enforcement and legal advice

The ESC will expand its enforcement capability by creating a new enforcement team and revising the enforcement framework to cover the conduct of scheme participants under the VEET Act. The new enforcement powers and regulatory oversight will require additional internal legal advice and involvement in the review process. The enforcement team will conduct targeted investigations into suspected non-compliance of APs and scheme participants. The ESC estimates that additional staff will be required to appropriately resource the enforcement team and provide legal advice for the VEU program. The team is assumed to deal with 10 detailed investigations per year. This will be a qualitative efficiency gain to fulfil the requirements of the *VEET Amendment Act 2022*.

4.4.5 Engagement, communication, and education

As required by the VEET Amendment Act 2022, there will be additional engagement and education functions. The ESC anticipates this function will be expanded. This is based on an expanded approach to communication and proactive outreach for the program, outlined above. It also assumes complaints related to the program continue to increase and that this level of resourcing will allow these complaints to be dealt with faster and more effectively. The resources in this team will be actively shared between the team's two main functions: communications and complaints management.

4.4.6 IT and governance

The ESC anticipates the creation and ongoing maintenance of a new IT system to facilitate the effective administration of the VEU program. The development of a new IT system for the VEU program will result in increased efficiencies in key processes, such as VEEC registration, complaints handling, and fee collection. The new IT infrastructure will allow for the collection and monitoring of more accurate data, as well as facilitating annual reporting and promotional materials about the program.

4.5 Cost and revenue escalation

The proposed fee options were calculated to remain constant in nominal terms over the three-year period of 2023/24 to 2025/26 (that is, they do not need to be adjusted for inflation). The (staffing) cost estimates used in the RIS were derived from the Victorian Public Service Enterprise Bargaining Agreement (EBA) for the periods covered by the EBA. For periods not covered by the EBA beyond 20 March 2024, the ESC made the working assumption that costs would increase by 2.5 per cent annually.

As all options considered in this RIS fully recover the ESC's costs (based on forecast volumes of certificates created, number of APs participating in the program and volume of other services provided), fees will be higher compared to existing fees. Importantly, the introduction of new fee categories under all options better reflects the nature of individual services provided by the ESC under the program and therefore adheres more closely to good pricing principles including horizontal equity, i.e. 'user-pays.'

5. Objectives

This chapter describes the objectives the proposed regulations will achieve.

5.1 Victorian policy objectives

The government's policy objectives relevant to the proposed fees is set out in the recent *Victoria's Climate Change Framework*, discussed in chapter 2. The framework identifies that reducing greenhouse gas emissions through increasing energy efficiency and productivity across the economy will be one of the pillars necessary to achieve broader climate change objectives.

5.2 VEET Act objectives

The objectives of the VEET Act are to:

- reduce greenhouse gas emissions
- encourage the efficient use of electricity and gas
- encourage investment, employment and technology development in industries that supply goods and services that reduce the use of electricity and gas by consumers.

5.3 VEU Fee-setting objectives

In addition to the overarching policy and VEET Act objectives, the following additional fee-setting objectives/criteria were considered as part of options design of the different options as set out in chapter 3 and discussion below in chapter 6:

- competition and innovation
- horizontal equity
- compliance
- simplicity.

These criteria are crucial to achieve the broader program objectives and are important factors in the assessment of fee options (see chapter 7).

6. Options

This chapter describes the policy options considered in this RIS, how they were selected and why other options were deemed not feasible. The three critical considerations that determine the setting of fees are:

- the costs incurred by the ESC for each service
- the nature of the potential response to fee changes by program participants
- the implications of this behavioural change on regulatory and policy objectives.

6.1 Factors that are varied between options to explore trade-offs

As described in chapter 3, the options have been developed to illustrate the differences between different approaches to the trade-offs in setting the fees to inform stakeholder feedback. This section sets out how different fees are varied between options.

6.1.1 Application for accreditation fee

Activity-based costing analysis indicated that the cost of each new accreditation application is \$17,218. Option 1 sets a new accreditation fee that directly reflects this cost. However, this high fee could overly impact smaller prospective APs and impact competition and innovation.

Option 2 includes reduced application fees to reduce the impacts on small APs while ensuring the fee is high enough to incentivise high quality applications. Option 2 is comparable to the \$2,500 accreditation fee charged by the Independent Pricing and Regulatory Tribunal of NSW under the New South Wales Energy Savings Scheme.

Option 3 aims to reduce competition and innovation concerns by waiving the new accreditation fee for APs that create fewer than 7,600 certificates annually.²²

6.1.2 Annual re-accreditation fee

Activity-based costing analysis indicated that the cost of processing the renewal of an AP's accreditation is \$5,612 or roughly one third of the costs of a new accreditation. Option 1 sets renewal of accreditation fees that reflect the cost of this process.

To reduce the risk that this renewal of accreditation fee would overly impact smaller APs and risk competition and innovation, in option 2, the renewal of accreditation fee is \$1,000. This is approximately one third of the new accreditation fee for option 2 to reflect the relative costs of the two processes. This relative cost difference is driven by the ESC having prior experience working with the AP seeking accreditation renewal. The ESC will have conducted the same or similar assessments for the APs original application for accreditation and any previous annual renewals.

Option 3 aims to reduce competition and innovation concerns by waiving the renewal of accreditation fee for APs that create fewer than 7,600 certificates annually.²³

6.1.3 Variation of accreditation condition fee

Activity-based costing analysis indicated that the cost of processing an accreditation variation application (to allow the provider to deliver a wider range of energy upgrades) is \$6,026. This is lower than the cost of new accreditations but higher than the cost of accreditation renewals. Option 1 charges fees that directly reflects the ESC's costs to process each accreditation variation application.

Option 2 includes a reduced variation of accreditation condition fee to reduce the risk of overly impacting smaller APs and risking competition and innovation. In option 2, the variation of accreditation condition fee is

²² Refer to 6.2.3 for further detail on why the specific threshold of 7,600 certificates was selected.

²³ Refer to 6.2.3 for further detail on why the specific threshold of 7,600 certificates was selected.

\$1,500, which is lower than the new accreditation fee but higher than the renewal of accreditation fee to reflect the relative costs incurred by the ESC when processing these different applications.

Option 3 aims to reduce competition and innovation concerns by waiving the variation of accreditation condition fee for APs that create fewer than 7,600 certificates annually.²⁴

6.1.4 Fees at the point of certificate creation or registration

For options 1 and 2, the certificate fee is charged at the creation phase (rather than at the registration phase under the current arrangements). This more accurately reflects when the ESC incurs most costs and incentivises positive behaviour.

To reduce the impact of the proposed fee changes on APs, option 3 charges only a certificate registration fee, consistent with the current fees.

The option of having fees for both certificate creation and registration was considered and discarded. Splitting the certificate costs between certificate creation and registration would introduce significant administrative complexities. Requiring two separate points of invoicing (i.e., ESC provides an invoice, the AP then pays the invoice, the ESC receives and then settles that invoice before providing the relevant service) would add multiple steps and delays to certificate creation and registration. ESC invoicing for both a creation fee and registration fee at the same time would create a different problem; it would mean ESC would not be able to withhold validation until the certificate creation fees were paid (meaning APs could choose not to pay for the fees for the creation of certificates which had not proceeded to the registration stage due to their mistakes or inaccuracies).

6.1.5 Project-based activity impact report fee

Activity-based costing analysis indicated the total cost of processing a PBA impact report application is \$3,778. Options 1 and 3 set PBA impact report fees that reflect these costs.

Option 2 reduces the PBA impact report fee to address the risks that a high PBA application fee might discourage applications and reduce the number of PBA projects. For option 2, the impact report fee is \$500. This figure was based on average sizes of PBA projects, as discussed in section 3.4.3 and in consultation with the ESC's PBA processing team, who indicated that a \$500 fee would be unlikely to reduce the number of PBA projects but would still provide an incentive for high quality applications.

6.1.6 Late lodgement of applications to renew accreditation fee

Activity-based costing analysis indicated the cost of processing a late lodgement of application to renew accreditation would be \$14,814. The late lodgement fee would be paid in addition to the annual reaccreditation fee for an AP who submitted late. The fee is \$14,814 for options 2 and 3 to reflect the costs of processing late renewal applications and provide a strong incentive for APs to submit their applications on time. ESC is able to set the reaccreditation due dates so that their work is evenly distributed over the course of the year and can be completed efficiently with the minimum number of staff—the scale of the late lodgement fee accounts for the fact that late application may disrupt this planning and require ESC to hire additional temporary resources in order to be able to assess late applications.

The fee is \$0 for option 1 as this would minimise costs on small APs. Option 1 would still fully recover costs if there are very few late lodgements, so that ESC would not be required to procure temporary resources to meet the surge demand.

6.1.7 Opening an account to hold and trade certificates²⁵

Activity-based costing analysis indicated that the ESC's costs to process each application is \$2,332. Option 1 reflects these costs.

There is a risk that setting a higher fee to open a registry trading account would limit access to small traders and have a distortionary impact on the certificate market. To reduce these risks, options 2 and 3 reduce the fee to open a VEET registry trading account. The \$2,000 cost of opening an account under option 2 reflects

²⁴ Refer to 6.2.3 for further detail on why the specific threshold of 7,600 certificates was selected.

²⁵ For those who are not APs and who want to hold and trade certificates, i.e. certificate traders. APs do not need to pay this fee.

the proportional discount that was applied to other service fees under option 2. For option 3 traders will pay \$2,332 as per option 1.

6.1.8 Product application fee

Activity-based costing analysis indicated that the costs associated with processing product applications is \$766 per product. Options 1 and 3 set the product application fee to reflect these costs. Option 2 reduces the product application fee to \$500 to address the risk of reduced competition and innovation due to a higher product application fee. Option 2 is the fee level that the ESC believes will reduce risks related to access while also providing an incentive for high quality applications.

6.1.9 Reviewable decision fee

Activity-based costing indicated the cost of recent decision reviews was approximately \$2,500, not including the costs of external professional advice. Options 1 sets the internal decision review fee at \$2,500 to reflect these costs. Option 2 sets it at \$750 to ensure that costs are not a barrier to participants seeking a review of a decision they believe is unfair or unreasonable. Option 3 sets no fee to facilitate broader access to justice.

6.2 Options to be evaluated

There are a wide range of individual choices and small changes that could be made to fees. However, to allow a useful evaluation of options, three options were chosen, each of which primarily focussed on a different consideration (Table 9). This is an evaluation tool only and stakeholders should provide feedback about which elements of the options should be adopted.

Table 9: Summary of fee options assessed

Option	Summary
Option 1—activity-based costing	Fees are based on activity-based costing, which allocates the incremental costs of providing each of the services by ESC.
Option 2—discounted fixed fees	Aims to manage the impact of fixed fee increases on APs by re-distributing cost recovery to certificate fees. The certificate fee is increased in comparison to option 1 to achieve full cost recovery.
Option 3—fee waivers for small APs	Supports small APs (who create fewer than 7,600 certificates annually) by providing them with fee waivers. Small APs are granted fee waivers while other APs pay the same fees as option 1. Small APs pay a higher certificate fee to disincentivise splitting businesses into separate legal entities.

6.2.1 Option 1: Activity-based costing

The fees in option 1 are directly based on the activity-based costing exercise described above and the allocation of costs to services in Table 10. This approach allocates the incremental costs of providing each ESC service to the users of that service. This means there is zero cross-subsidy from larger APs to smaller APs under option 1.

Option 1 emphasises economic efficiency or sending appropriate price signals about the value of resources the ESC uses to provide services and regulatory activities. These options have the most cost-reflective fees. The late lodgement fee is set at zero, which is not cost-reflective, but is expected to only have a minor impact on the overall cost-reflectivity of the option, as it is expected that most APs will be compliant. Furthermore, the lack of cost reflectivity for this activity is unlikely to have a significant effect on the overall cost reflectivity of this option.

Table 10: Fee summary under option 1, activity-based costing (2023-24 – 2025-26, \$ nominal)

VEU Fee types	Option 1 proposed fee
Certificate fee—creation	\$2.05/ certificate
Annual reaccreditation fee	\$5,612

Application of accreditation fee	\$17,218
Variation of accreditation condition fee	\$6,026
Project-based activity impact report fee	\$3,778
Product application fee	\$766
Lodging a retailers' energy acquisition statement fee	\$3,122
Opening an account to hold and trade certificates fee	\$2,332
Review of a reviewable decision	\$2,500
Annual reaccreditation late lodgement fee	\$0

6.2.2 Option 2: Discounted fixed fees—the preferred option

Option 2 aims to manage the impact of fee increases on APs by setting most fees at between \$500 and \$3,000 (except for the lodging of an energy acquisition statement, which is a fee to retailers). The certificate fee is increased to achieve full cost recovery (Table 11).

One of the objectives for the fee setting is to ensure that fees do not act as a barrier to meaningful participation and industry development. The ESC developed option 2 to address this issue. It sets the fee for most services between \$500 and \$3,000 to avoid significant upfront costs.

As several fees are set below the more cost-reflective fees in option 1, the certificate fee is used to recover the remainder of the ESC's total costs. This means the certificate fee is higher for option 2 compared to option 1. Because larger APs create more certificates and therefore pay more in certificate fees, this results in a cross-subsidy from larger APs to smaller APs under option 2 of approximately \$5.9 million over three years.

Also in option 2, the review of a reviewable decision fee is based on benchmarking with the Clean Energy Council's application appeals fee of \$750.

Table 11: Fee summary under option 2, Discounted fixed fees (2023-24 – 2025-26, \$ nominal)

VEU Fee type	Option 2 proposed fee
Certificate fee—creation	\$2.33/ certificate
Annual reaccreditation fee	\$1,000
Application of accreditation fee	\$3,000
Variation of accreditation condition fee	\$1,500
Project-based activity impact report fee	\$500
Product application fee	\$500
Lodging a retailers' energy acquisition statement fee	\$3,122
Opening an account to hold and trade certificates fee	\$2,000
Review of a reviewable decision	\$750
Annual reaccreditation late lodgement fee	\$14,814

6.2.3 Option 3: Fee waivers for small APs

Option 3 supports smaller APs by providing them with fee waivers on fixed fees. Small APs are defined by a threshold of less than 7,600 certificates created annually (Table 12).²⁶

²⁶ Note that this threshold is based on creation, whilst the fees for option 3 are charged based on registration.

Table 12: Option 3 – cost for fee waiver threshold for smaller APs

Small AP threshold (no. certificates per annum)	Estimated no. of current APs that meet threshold	Estimated annual cost of fee waiver
7,600 certificates	22	\$288,180

Option 3 is a hybrid option where larger APs pay more fees based on the activity-based costing analysis, but small APs receive fee waivers. This option results in a lower cross-subsidy from larger APs to smaller APs compared to option 2, a total of \$864,540 over three years.

Small APs are granted fee waivers while other APs pay the same fees as option 1. However, small APs and all ‘other APs’ have different certificate fees under option 3. The certificate fee for ‘other APs’ is set higher to ensure the ESC can achieve full cost recovery (see Table 13).

A lower fee structure for small APs may potentially have an unintended consequence of incentivising a single provider to establish multiple entities each of which seek accreditation as a ‘small AP’. To account for this, the certificate fee for small APs is set higher to ensure there is no incentive for APs to reduce certificate creation to fall under the threshold. A small AP will have no upfront or annual fees but will pay a higher certificate registration cost (see Table 13). Certificate registration is the point that most closely aligns with the ability to trade a certificate and would therefore minimise the cashflow impacts of fees for these small businesses.

The threshold to define a small AP that receives fee waivers was selected to balance the cost of fee waivers with the number of small APs who would benefit from these waivers. The 7,600 certificates created threshold level was the level which ensured a significant number of small APs would benefit and therefore continue their participation in the VEU Program, while also ensuring that the costs of waiving their fees did not present issues with horizontal equity.

To ensure small APs do not face barriers to seeking a review of ESC decisions, the review of a reviewable decision fee is \$0. This is important for small APs as the lost revenue caused by ESC decisions will likely be a larger proportion of total revenue for a small AP, because the AP is delivering a small number of upgrades each year. Similarly, fees to review a decision will represent a greater proportion of a small AP’s revenue. Additionally, to ensure consistent treatment for APs of all sizes, the fee will be \$0 for all APs, ensure equitable access to justice.

Note, fees for project-based activity impact reports, product applications, and lodging retailer energy acquisition statement fees are not related to accreditation and so will not impact lower volume APs, which are unlikely to utilise these services.

Table 13: Fee summary under option 3 for different size APs (2023-24 – 2025-26, \$ nominal)

VEU fee type	Small AP	Non-small AP
Certificate fee – registration (per certificate)	\$2.83/certificate	\$2.09/certificate
Annual reaccreditation fee	\$0	\$5,612
Application of accreditation fee	\$0	\$17,218
Variation of accreditation condition fee	\$0	\$6,026
Project-based activity impact report fee	\$3,777	\$3,777
Product application fee	\$766	\$766
Review of a reviewable decision	\$0	\$0
Annual reaccreditation late lodgement fee	\$14,814	\$14,814

Table 14: Fees paid by other stakeholders under option 3

VEU fee type	Fees
Lodging an energy acquisition statement fee	\$3,122
Opening an account to hold and trade certificates fee	\$2,332
Review of a reviewable decision	\$0

Comparison between proposed fees and existing fees

As required by section 12H(1)(c) of the *Subordinate Legislation Act 1994*, Table 15 and Table 16 compare the proposed and existing fees, including the percentage increase or decrease for each fee.

Table 15: Comparison to existing fees

VEU fee type	Current fee	Option 1	Percentage increase	Option 2	Percentage increase	Option 3	Percentage increase
Certificate fee—creation (per certificate)	n/a	\$2.05	105% (and fee moved to certificate creation rather than registration)	\$2.33	133% (and fee moved to certificate creation rather than registration)	n/a	108% to 248%, depending on the size of the AP
Certificate fee—registration (per certificate)	\$1	n/a		n/a		\$2.83 for small APs \$2.09 for other APs	
Application of accreditation fee	\$500	\$17,218	3,344%	\$3,000	500%	\$0 for small APs \$17,218 for other APs	3,344%
Review of a reviewable decision fee	\$200	\$2,500	1,150%	\$750	275%	\$0	-100%

Table 16: New fee categories to be introduced

VEU fee type	Current fee	Option 1	Percentage increase	Option 2	Percentage increase	Option 3	Percentage increase
Annual reaccreditation fee	n/a	\$5,612	-	\$1,000	-	\$0 for small APs. \$5,612 for other APs	-
Variation of accreditation condition fee	n/a	\$6,026	-	\$1,500	-	\$0 for small APs. \$6,026 for other APs	-
Project-based activity impact report fee	n/a	\$3,778	-	\$500	-	\$3,778	-
Product application fee	n/a	\$766	-	\$500	-	\$766	-
Lodging an energy	n/a	\$3,122	-	\$3,122	-	\$3,122	-

acquisition statement fee							
Opening an account to hold and trade certificates fee	n/a	\$2,332	-	\$2,000	-	\$2,332	-
Annual reaccreditation late lodgement fee	n/a	\$0	-	\$14,814	-	\$14,814	-

6.2.4 Change in fees for typical stakeholders

The impact of these changes will vary depending on the nature of the stakeholder, for instance some APs will have part of their business which seeks to register energy efficient products and will therefore need to pay those fees. Section 7.2 considers the cost impacts per certificate for varying AP size and service level and Table 19, Table 20, and Table 21 set out the change in fees.

6.3 Consultation questions for this chapter

The department is seeking stakeholder feedback on these proposed fees, in particular the questions listed below.

Consultation questions

Do you support the proposed introduction of a late lodgement fee to increase compliance? Do you support the setting of that fee at \$14,804? Do you believe the late lodgement fees will influence the timely submission of annual re-accreditation forms?

Do you support the proposal to transition from certificate registration fees to certificate creation fees? Why? Do you believe fees at the point of certificate creation would increase compliance and improve the quality of certificate creation documentation?

Do you support the proposal to introduce a fee applicable to retailers when they lodge an energy acquisition statement? Why?

Do you have any other feedback on the proposed fees?

7. Assessment of options

This chapter summarises the methods used to evaluate and compare the options and the costs, benefits, and competition impacts of the preferred and alternative options.

7.1 Approach to assessment of options

The decision rule used in this RIS is a multi-criteria analysis (MCA) because the options are recovering approximately the same amount and it is difficult or impossible to estimate quantitatively the effects of fee structure on the criteria. An MCA by its nature subjectively judges the relative importance of the outcomes and the effectiveness of achieving those outcomes. The results of any MCA are sensitive to the choice of criteria, weightings, and scores. An MCA transparently shows the considerations involved in comparing options and how the department made judgments in relation to those consideration to arrive at the preferred option.

Four criteria were used, which were seen as equally important to the program objectives, and therefore given equal weighting (Table 17).

Table 17: Criteria in multi-criteria analysis

Criteria	Description	Weighting
Competition and innovation	The price of services should not limit access. High fixed annual fees or entry fees might discourage small operators from participating in the program, with a negative impact on industry development and employment.	25%
Horizontal equity	VEU fees should only recover the costs of administering the VEET Act. VEU fees should recover the costs of the program from participants who benefit from the program or give rise to the need for regulation while minimising the support it requires from taxpayers. Fees should aim to minimise cross-subsidies between different VEU program participants.	25%
Compliance	Participants with good compliance should face lower costs compared to those with a poor compliance history and who take more of the ESC's resources. Fees should discourage behaviour which transfers costs and risks from APs to the ESC and is economically inefficient.	25%
Simplicity	Pricing structures should be easy to understand and simple to administer. The fees should not impose a disproportionate burden to administer or be a barrier for stakeholders to understand and predict.	25%

Each option was scored against each criterion on a scale of -10 to +10. The standards for these scores are defined in Table 18. Each of these scores are assessed by comparing outcomes for each option to the 'base case' of no policy action being taken, i.e. no fees are collected from participants in the program (as discussed in section 2.4). Scores against individual criteria were then weighted and combined to give an overall score for each option.

Table 18: Criterion score standards

Criteria score	Standard
-10	A score of -10 means the option performs significantly worse than the base case.
0	A score of zero means the option achieves outcomes to the same extent as the base case.

The first two criterion (competition and innovation, and horizontal equity) were assessed based on quantitative analysis of the impacts of any given fee option and were determined by converting the total annual cost for APs to a per certificate created cost. This allowed comparison of the fee options on different sized APs based on the number of certificates traded per year. This RIS analysed the costs per certificate created for six varying sizes of APs:

- 12th percentile AP: 2,000 certificates/year
- 24th percentile AP: 5,000 certificates/year
- 38th percentile AP: 20,000 certificates/year
- 60th percentile AP: 70,000 certificates/year
- 80th percentile AP: 150,000 certificates/year
- 99th percentile AP: 500,000 certificates/year.

In addition to assessing the impacts on varying sizes of APs, this RIS also assessed the impacts on APs with different levels of services. Three service level scenarios were defined to examine these impacts on:

1. existing APs with 'basic service' (certificate fee + annual reaccreditation fee)
2. existing APs with 'full service' (certificate fee + annual reaccreditation fee + one annual product application + annual variation of accreditation condition fee + one annual project-based application fee)
3. new APs with 'basic service' (certificate fee + annual reaccreditation fee + accreditation fee).

The other two criterion (compliance and simplicity) were assessed based on qualitative analysis and through internal consultation.

In the analysis of measuring impacts of each fee type, characteristics of the VEU program from 2021 were assumed. This was due to the impacts of the COVID-19 pandemic with 2021 providing the most recent year of complete data (number of APs and the amount and distribution of certificate creations by APs).

As discussed above, the VEU program fees have not been amended since the program began in 2009, which has led to an under-recovery of fees relative to costs over time. Additionally, the ESC has new responsibilities emerging from the *Victorian Energy Efficiency Target Amendment Act 2022* that increases the costs to be recovered through fees. Subsequently, it should be noted that all APs will incur increased costs under any of the fee options compared to current fees.

7.1.1 Consideration of discount rates

The fees have been calculated in nominal terms that would recover the ESC's costs over three years, i.e., the dollar amounts of fees the ESC will collect. Presenting the data in nominal terms is key for stakeholders to understand the fees that will be paid under different options. The modelling results ensured that the fees would remain stable in nominal terms and cover the ESC's costs over the period.

See section 4.3 for detail on the total costs to be recovered across all options, discounted using a net present value calculation.

7.2 Detailed evaluation

7.2.1 Cost impacts per certificate for varying AP service levels and AP sizes

The ESC advice and feedback from internal consultation are summarised below for each level of service.

This analysis assumes certificate prices of \$73, which is approximately the average price for the current financial year.

Cost impacts for existing APs with basic service levels

For existing APs with basic service (annual reaccreditation fee and certificate fee), option 1 has higher costs per certificate for smaller APs. This arises because the new fee structure includes new or higher fees that do not vary with the number of certificates created, and small APs need to recover these costs over a smaller number of certificates. Options 2 and 3 ensure that smaller APs do not face considerably higher costs per certificate compared to larger APs, with option 2 providing slightly lower costs for smaller APs compared to option 3. The ESC has advised that this may otherwise create an incentive for some APs to reduce certificate creation to lower their per certificate costs. Overall, the analysis shows that while option 1 may be the most cost-reflective, it would impose a higher burden on smaller APs compared to options 2 and 3.

Figure C: Cost impacts per certificate for existing APs with basic service level

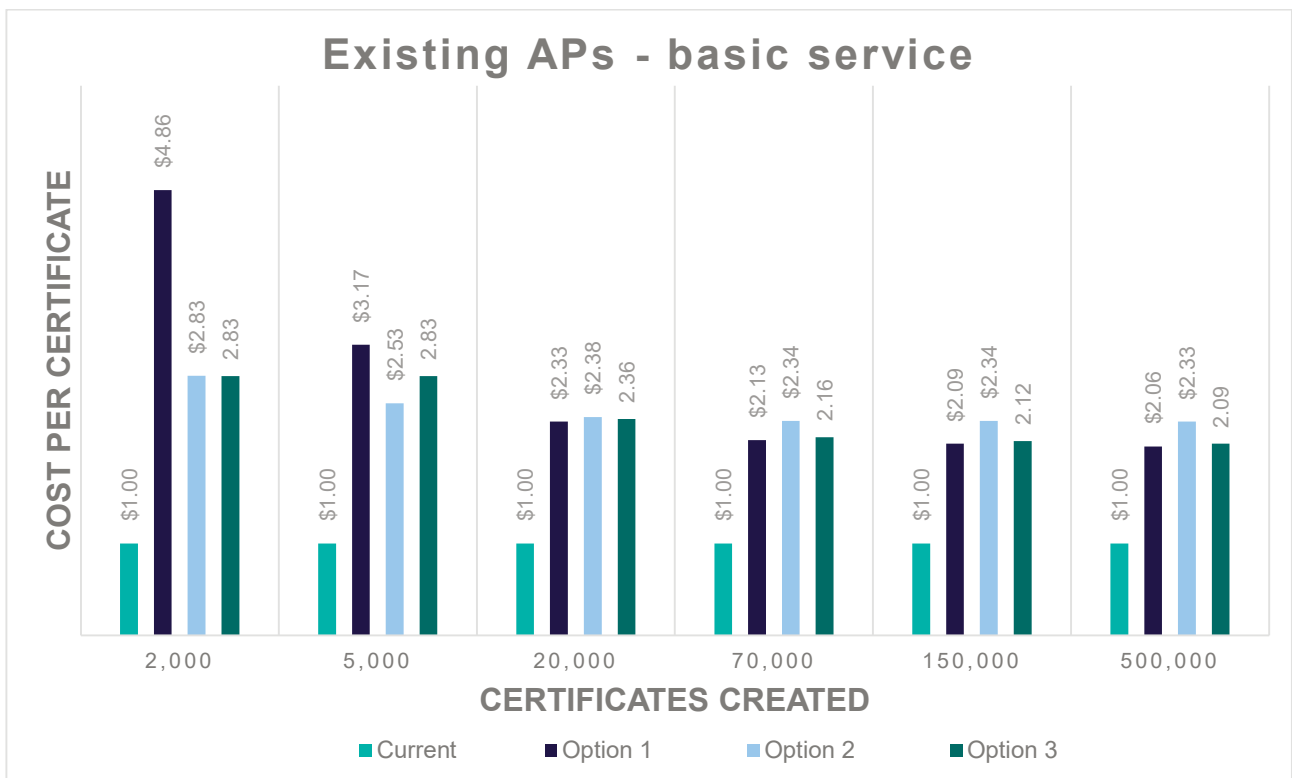


Table 19: Annual cost impacts for existing APs with basic service level

AP size in annual certificate revenue	\$146,000	\$365,000	\$1,460,000	\$5,110,000	\$10,950,000	\$36,500,000
Number of certificates created annually for this size AP ²⁷	2,000	5,000	20,000	70,000	150,000	500,000
Current estimated annual fee cost	\$2,000	\$5,000	\$20,000	\$70,000	\$150,000	\$500,000

²⁷ Assuming a VEEC price of \$73, the approximate current price.

Option 1 estimated annual fee cost	\$9,720	\$15,850	\$46,600	\$149,100	\$313,500	\$1,030,000
Option 2 estimated annual fee cost	\$5,660	\$12,650	\$47,600	\$163,800	\$351,000	\$1,165,000
Option 3 estimated annual fee cost	\$5,657	\$14,142	\$47,212	\$151,212	\$317,612	\$1,045,612

Cost impacts for existing APs with full-service level

Similar to the results of existing APs with basic service, existing APs with full service includes a broader range of fees and subsequently leads to an increasing cost per certificate for APs of all sizes. As seen in Figure D below, there are large per certificate costs for smaller APs. ESC advice has noted it is unlikely that very small APs would require a full service and thus incur the full range of fees.

Figure D: Cost impacts per certificate for existing APs with full-service level

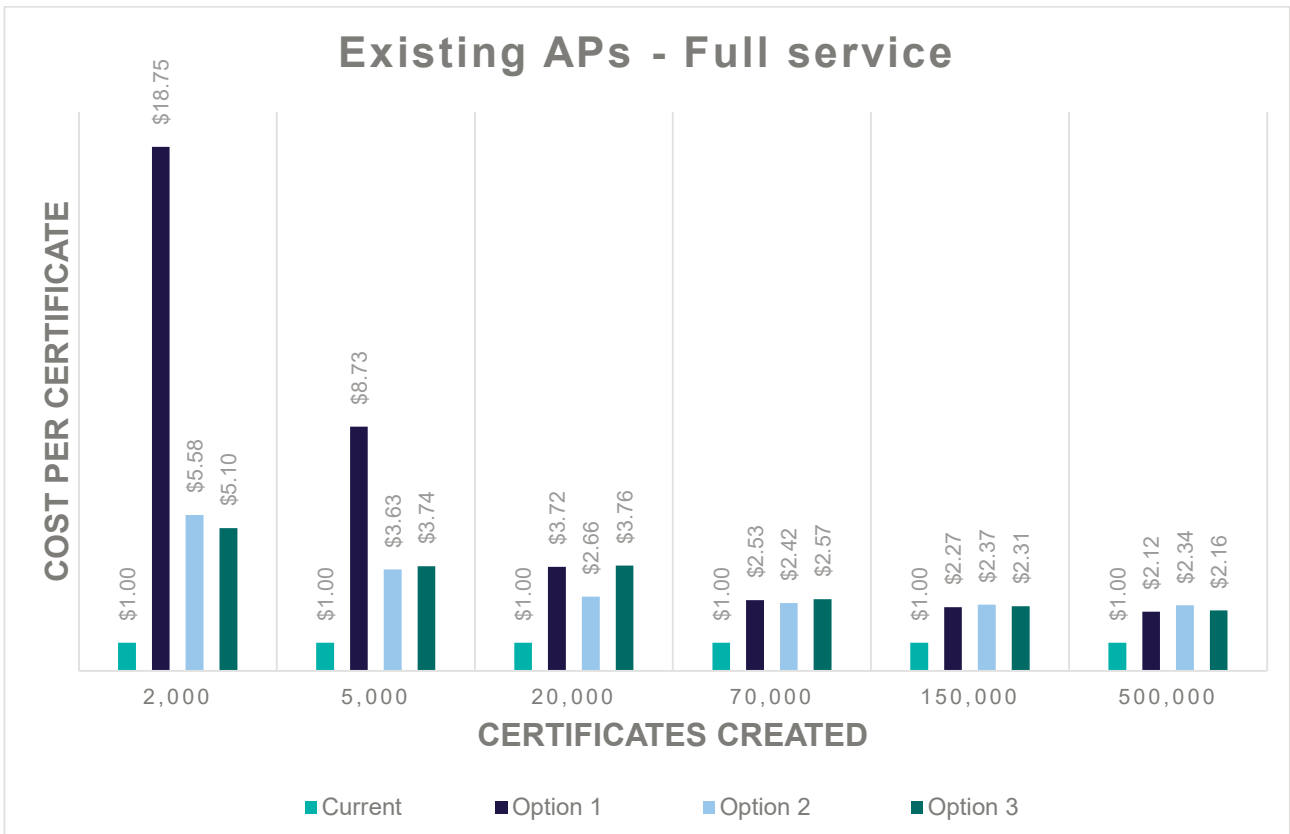


Table 20: Annual cost impacts for existing APs with full service level

AP size in annual certificate revenue	\$146,000	\$365,000	\$1,460,000	\$5,110,000	\$10,950,000	\$36,500,000
Number of certificates created annually for this size AP ²⁸	2,000	5,000	20,000	70,000	150,000	500,000
Current estimated annual fee cost	\$2,000	\$5,000	\$20,000	\$70,000	\$150,000	\$500,000
Option 1 estimated annual fee cost	\$37,500	\$43,650	\$74,400	\$176,900	\$340,900	\$1,058,400
Option 2 estimated annual fee cost	\$11,160	\$18,150	\$53,200	\$169,400	\$355,500	\$1,170,000
Option 3 estimated annual fee cost	\$10,201	\$18,686	\$75,200	\$179,700	\$346,900	\$1,078,400

Cost impacts for new APs

New APs seeking to participate in the VEU program will incur fees in relation to accreditation and certificate creation/registration. The analysis indicates that fees under option 1, result in high costs per certificate (see Figure E) and may deter smaller APs from participating or entering the VEU program. Options 2 and 3 both facilitate smaller new APs to participate in the VEU program.

²⁸ Assuming a VEEC price of \$73, the approximate current price.

Figure E: Cost impacts per certificate for new APs with basic service level

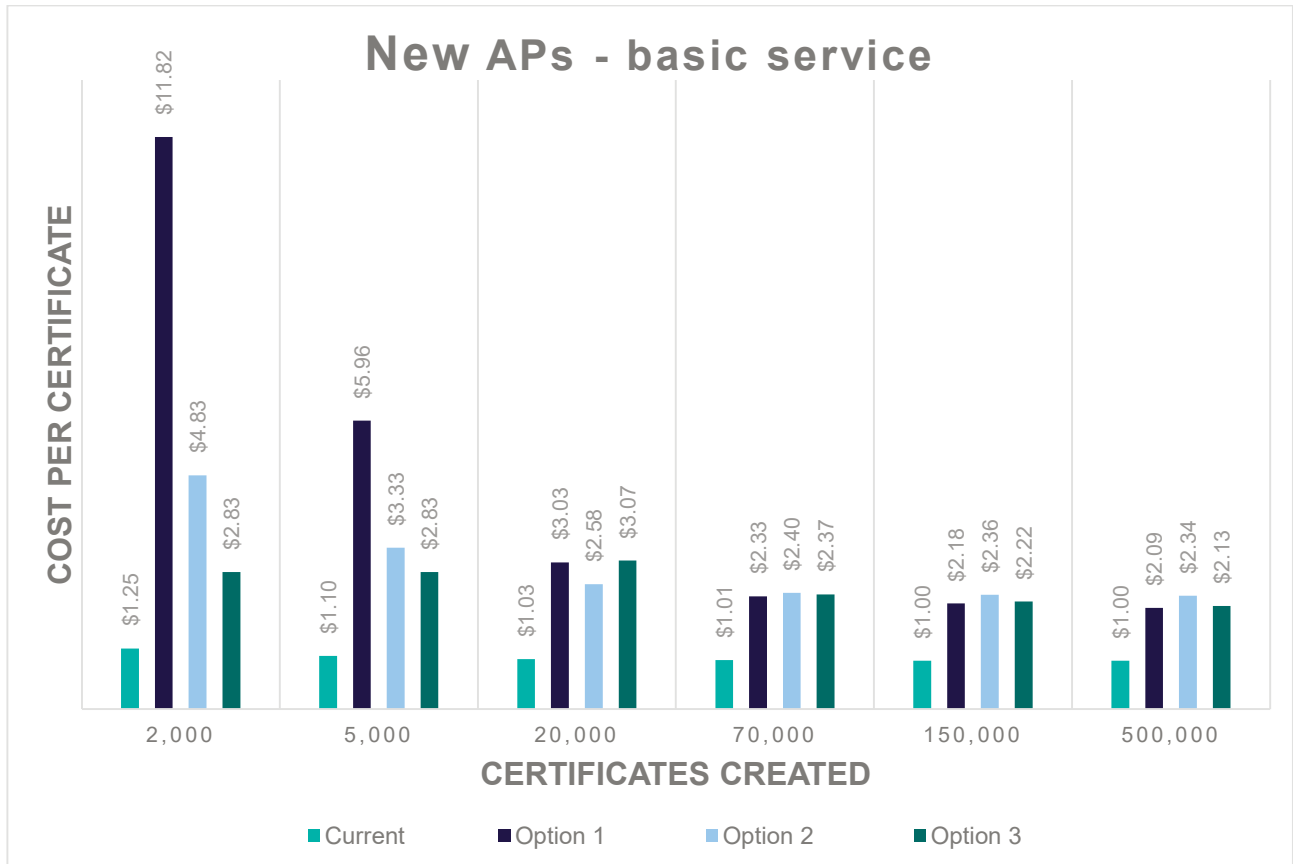


Table 21: Annual cost impacts for new APs with basic service level

AP size in annual certificate revenue	\$146,000	\$365,000	\$1,460,000	\$5,110,000	\$10,950,000	\$36,500,000
Number of certificates created annually for this size AP ²⁹	2,000	5,000	20,000	70,000	150,000	500,000
Current estimated annual fee cost	\$2,500	\$5,500	\$20,600	\$70,700	\$150,000	\$500,000
Option 1 estimated annual fee cost	\$23,640	\$29,800	\$60,600	\$163,100	\$327,000	\$1,045,000
Option 2 estimated annual fee cost	\$9,660	\$16,650	\$51,600	\$168,000	\$354,000	\$1,170,000
Option 3 estimated annual fee cost	\$5,657	\$14,142	\$61,350	\$165,850	\$333,050	\$1,064,550

²⁹ Assuming a VEEC price of \$73, the approximate current price.

7.3 Summary of multi-criteria analysis evaluation outcomes

Table 22 summarises the scores allocated to each option following the scoring criteria and methods outlined above. Each of these scores are assessed by comparing outcomes for each option to the base case of no policy action being taken, i.e., no fees are collected from participants in the program. The base case receives a score of 0 for each criterion.

Table 22: Summary of MCA evaluation of fee options

Criteria	Weighting	Option 1	Option 2	Option 3
Competition and innovation	25%	-10	-3	-4
Horizontal equity	25%	10	7	8
Compliance	25%	6	8	5
Simplicity	25%	-3	-3	-6
Total weighted score	-	0.75	2.25	0.75

7.3.1 Competition and Innovation

Option 1

Option 1 is based on activity-based costing where the fees reflect the incremental costs of providing each service and an annual fee that recovers fixed costs. The higher fee levels for accreditation related services in this option may discourage market entry and the higher fee levels for product application and project-based activities may discourage product and service innovation which will have long-term negative effects on the economic efficiency of the program. As such, option 1 was allocated a -10 against this criterion as it does not meet the competition and innovation objectives.

Option 2

Option 2 sets fees at a level to avoid excluding small APs by setting most fees between \$500 and \$3,000 (with the exception of the lodging of an energy acquisition statement which is a fee to retailers). The certificate fee is increased to achieve full cost recovery. This change means that option 2 reduces barriers to entry for APs with limited ability to pay significant up-front costs relative to option 1. Nonetheless, option 2 was allocated -3 against this criterion as it performs worse than the base case of no fees in promoting competition and innovation.

Option 3

Option 3 is an alternative way to support smaller APs, by creating an annual threshold for certificate creation, below which 'small' APs would pay zero fees for accreditation and reviews of a reviewable decision. Small APs would pay a higher certificate fee to avoid creating an incentive to reduce certificate creation to fall below the threshold. In addition, the certificate fees for other APs are higher in order to achieve full cost recovery. For this reason, option 3 was allocated a -4 the competition and innovation objective given the potential impacts or barriers to entry for larger APs subsidising the costs of smaller APs.

7.3.2 Horizontal Equity

All option seek to fully recover costs from the program through fees. This means all options have a positive score for this criterion compared to the base case of a taxpayer subsidy funding the program.

Option 1

The objective of achieving horizontal equity in the design of the fee structure seeks to minimise cross subsidisation between different VEU program participants. Option 1 was allocated a +10 for this criterion as it

fully recovers costs from program participants and is based on activity-based costing where the fees fully reflect the costs of providing each service. Cross subsidisation is minimised under this option.

Option 2

Option 2 fully recovers costs from the program. However, larger APs may subsidise smaller APs due to the greater reliance on certificate fees for cost recovery when compared to option 1, which reduces its score against the horizontal equity criterion. Furthermore, project-based activities and product application fees are set below cost recovery, so APs that engage in these activities will be subsidised by those that do not.

Option 3

Option 3 also fully recovers costs. Option 3 presents a different approach to supporting smaller APs where below a threshold level of certificate creation accreditation fees are waived for some APs, whereas larger APs pay accreditation fees. On the other hand, smaller APs are charged a higher certificate registration fee than larger APs to avoid an incentive to reduce certificate creation or split certificate creation across several legal entities; this reduces the total subsidy between larger and smaller APs. Overall, larger APs subsidise smaller APs, but to a lesser extent than option 2. Accordingly, this option was allocated a +8 against the horizontal equity as it goes some way to achieving the criterion but is not as equitable as option 1.

7.3.3 Compliance

All options are predicted to create greater levels of compliance than the base case because charging fees disincentivises incomplete or inaccurate applications, lodgements and certificate creation, and so scores for all options are positive.

Option 1

Option 1 drives compliance outcomes that are significantly better than the base case, as fees incentivise thorough and complete applications, lodgements and certificate creations. Option 1 charges a certificate fee at point of creation which is the largest factor in helping to incentivise greater compliance. However, it does not include a late lodgement fee which means this option is likely inducing poorer compliance when compared to options 2 and 3.

Option 2

Similar to option 1, option 2 drives higher compliance than the base case. It includes both a late lodgement fee and charges a certificate fee at point of creation. This combination of fees has the greatest likelihood of ensuring strong compliance from program participants with certificate creation and accreditation timelines. However, as it charges reduced fees for project-based activity impact reports and product applications, there is a weaker incentive to comply than for option 1 and 3. Similarly, since it charges reduced accreditation fees, there is a weaker incentive to comply with accreditation requirements than option 1. Overall, the largest effect comes from the certificate creation and late lodgement fees, so this option receives a higher score than option 1 and 3.

Option 3

Similar to option 1, option 3 drives higher compliance than the base case. It includes a late lodgement fee however it charges a certificate fee at the point of registration. The late lodgement fee is assessed as having a larger impact on compliance than the point of certificate fee, so this option is assessed as having greater levels of compliance than option 1. Option 3 charges no accreditation fees for small APs providing a no fee-based incentive to comply with accreditation requirements for those APs, which represented approximately a quarter of program participants. On the other hand, for larger APs, which represent 75% of participants, the fees are the same as for option 1, creating an incentive to comply than for those APs.

7.3.4 Simplicity

All options are more complex than the base case of fees lapsing and the ESC receiving funding through government appropriations. This means that scores for all three options are negative.

Option 1

Option 1 is a relatively simple fee structure, with simple categories of fees and eligibility for those fees. Therefore option 1 receives a score of -3.

Option 2

Option 2 is as simple as option 1. Whilst the fees are set at different levels, the categories and eligibility are the same as option 1. Therefore, option 2 receives the same score as option 1, i.e. -3.

Option 3

This option presents a more complex fee structure, with many fee categories having two different fee rates depending on the size of the AP. This means that option 3 is assessed as the most complex of the evaluated options and the score of -6 reflects this.

7.3.5 Conclusion

All options score more highly than the base case because they produce much better outcomes for horizontal equity and compliance than allowing the fees to lapse.

Option 1 is based on an activity-based costing, where fees reflect the incremental costs of providing each service, and an annual fee that recovers fixed costs. Although fully cost recovering each activity through the fee charged for that activity sends accurate price signals and therefore would be expected to be the most horizontally equitable and economically efficient in the short term, this does not consider the long-term effects of this fee structure. The high fees for various services in option 1 are expected to discourage market entry and product and service innovation, which would have long-term negative effects on the economic efficiency of the program. Additionally, since this option has a certificate creation fee but no fee for the late lodgement of an annual accreditation renewal application, this option receives a moderate score for compliance. Option 1 scores equal to option 3 but lower than option 2, as a result, option 1 is not recommended.

As stated previously, option 2 is intended to avoid excluding small APs by setting most fees at between \$500 and \$3,000 (except for the lodging of an energy acquisition statement which is a fee to retailers). The certificate fee is increased to achieve full cost recovery. This variation means that option 2 reduces barriers to entry for APs with limited ability to pay, thus increasing competition and innovation. However, it would mean that large APs subsidise smaller APs due to the greater reliance on certificate fees for cost recovery than option 1 which reduces its score for horizontal equity. Overall, option 2 achieves the best balance across each of the four criteria compared to the other options and receives a higher score than the other options. Therefore, option 2 is the preferred option.

Option 3 is an alternative way to support smaller APs, by creating an annual threshold for certificate creation, below which small APs would pay zero fees for accreditation and all APs would pay zero fees for reviews of a reviewable decision. Other APs are charged at full cost recovery for most fees, and slightly more than full cost recovery for certificate registration fees to ensure full cost recovery is achieved, which introduces a cross-subsidy between large and small APs. The certificate fee is also higher for smaller APs to ensure there is no incentive for APs to reduce their certificate creation to fall under the threshold. However, option 3 introduces complexities that would be very difficult for the ESC to administer and for APs to understand and comply with. Option 3 scores equal to option 1 but lower than option 2, as a result, option 3 is not recommended.

7.4 Ensuring access to review of decisions

Option 1

Option 1 recovers costs of reviewable decisions but is likely to be expensive for many program participants and may discourage them from seeking a review. Therefore, this fee may not ensure equitable access to justice.

Option 2

Option 2 balances cost recovery with equitable access to justice by setting the reviewable decision fee at a level which is not expected to present a material barrier for participants seeking a review of a decision they believe is unfair or unreasonable.

Option 3

Option 3 does ensure that all participants can seek reviews of decisions without any fee barriers, however charging no fee could potentially result in frivolous or vexatious submissions for reviews of fair decisions.

7.5 Consultation questions for this chapter

The department is seeking your feedback on the preferred option for the fees, in particular the questions listed below.

Consultation questions

Which is your preferred fees option? Why?

What do you expect the impacts of the preferred option (option 2) on participation and investment in energy efficiency to be?

8. Implementation, monitoring and evaluation

This chapter provides further detail on how the preferred option will be implemented and evaluated.

8.1 Implementation

The fees are due to take effect from 1 July 2023 and will be set for three years.

The proposed commencement date will allow time for the ESC to communicate the new arrangements to the sector and establish the required systems and processes. The ESC will advise APs of new fee categories and payment processes after they are announced by the Minister for Energy and Resources.

The new and expanded services which require increased fees will apply once the VEET Amendment Act changes come into effect. Most of these changes will come into effect when proclaimed by the Minister for Energy and Resources – this is planned for mid-2023. The implementation of these new and expanded services will be phased to accommodate APs adapting to the new requirements. These transitional timeframes are summarised below, refer to Table 5 for further detail:

- Annual re-accreditation requirements will be implemented over a 12-month transitional period after Part 2 of the VEET Amendment Act is proclaimed.
- Variations to accreditation requirements will be implemented for APs who have transitioned to annual reaccreditation.
- Opening an account to hold and trade certificates will be implemented once Part 3 of the VEET Amendment Act commences on 1 November 2023. There will be a 12-month transitional period for existing certificate holders to pay this fee. The fee will only need to be paid once.
- Fees for reviews of a reviewable decision will be implemented once Part 7 of the VEET Amendment Act is proclaimed.

8.1.1 Transitional arrangements

It is proposed that for services which are already underway or are likely to be still underway on 1 July when the new fees commence, the ESC will publish expected timelines for services to be completed before the new fees commence and arrangements for those services underway during the transition from the current fees to the new fees. The ESC will have the power to reduce or waive fees as part of these transitional arrangements.

If as proposed, fees for certificates are moved from the point of registration to creation, transitional arrangements will be established to ensure fees are not charged twice for the same certificate or not charged at all. The following transitional arrangements are proposed:

- certificates which are created but not yet registered on the date the new fees commence will have transitional arrangements to pay the old fees at the point the certificate is validated by the ESC and able to be registered
- certificates which are created before the date the new fees commence (1 July) but are then withdrawn or otherwise not validated by the ESC after the commencement date will not be charged fees
- activities which have been undertaken, but for which certificates have not yet been created on the date the new fees commence will be subject to the new fees
- applications for accreditation which are underway on the date which the new fees commence will pay the old fees at the point the application is approved by the ESC. Applications which are underway but are then not approved will need to reapply and pay the relevant fee.
- the proposed retailer energy acquisition statement fee will commence for the 2023 certificate target. This target's certificate liability surrender is due on 30 April 2024.

- product registration approvals which are underway on the date the new fees commence and are approved by the ESC will not be required to pay fees. Product registration applications which are underway but are then not approved will need to reapply and pay the new fee.

8.2 Monitoring

The ESC will implement data analytics and reporting to monitor and evaluate the fees. The ESC will be responsible for monitoring the cost recovery of the program, including by publishing its Performance Reports on the program. This will provide transparency and insights into the effectiveness of the regulatory framework and allow for emerging issues to be identified and responded to in a timely fashion. The risks of over and under recovery of costs are analysed in Appendix B, and ESC will consider this in its monitoring activities.

8.3 Evaluation

The department will work with the ESC to evaluate the fees as part of a broader review of the VEU program in 2024 to inform the setting of program target levels for 2026 through to 2030.

Specific metrics to monitor and assess the implementation and effectiveness of the proposed fees may include:

- effective fees per certificate for APs with varying levels of certificate creation and service levels
- certificate creation volumes
- AP registration and participation levels
- timely lodgements of accreditation renewals
- certificate withdrawals
- product applications
- project-based activity certificate creation levels
- number of activities
- number of registered products and certificates created for each product

In addition, the fees will be further reviewed prior to 2030 as part of considering how the VEU program will contribute to Victoria's emission reduction goals beyond 2030. Should the VEU program continue beyond 2030, the fee levels may need to be revised again.

8.4 Consultation questions for this chapter

The department is seeking your feedback on the preferred option for the fees, in particular the questions listed below.

Consultation questions

Do you agree with the proposed timeline for implementation of these proposed fees? Why? What impacts will the proposed timeline of implementing fees from 1 July 2023 have for you?

9. Consultation questions

Interested parties and stakeholders are invited to make submissions to the department on the proposed fees and regulations by **26 April 2023**.

The department will consider all submissions received in response to the proposed fees and options. Following this, a notice of decision and statement of reasons will be published.

Table 23: Consultation questions

Question number	Consultation question
1	Which is your preferred fees option? Why?
2	What do you expect the impacts of the preferred (option 2) on participation and investment in energy efficiency to be?
3	Do you agree with the proposed timeline for implementation of these proposed fees? Why? What impacts will the proposed timeline of implementing fees from 1 July 2023 have for you?
4	Do you support the proposed introduction of a late lodgement fee to increase compliance, and setting that fee at \$14,804? Why? Do you believe the late lodgement fee will influence the timely submission of annual re-accreditation forms?
5	Do you support the proposal to transition from certificate registration fees to certificate creation fees? Why? Do you believe fees at the point of certificate creation would increase compliance and improve the quality of certificate creation documentation?
6	Do you support the proposal to introduce a fee applicable to retailers when they lodge an energy acquisition statement? Why?
7	Do you have any other feedback on the proposed fees?

Appendix A: How the VEU program works

The VEU program achieves a reduction in greenhouse gas emissions by reducing the total demand for energy by residential and business consumers. This reduction in demand is achieved by improving the energy efficiency of premises, or the appliances and equipment used within the premises.

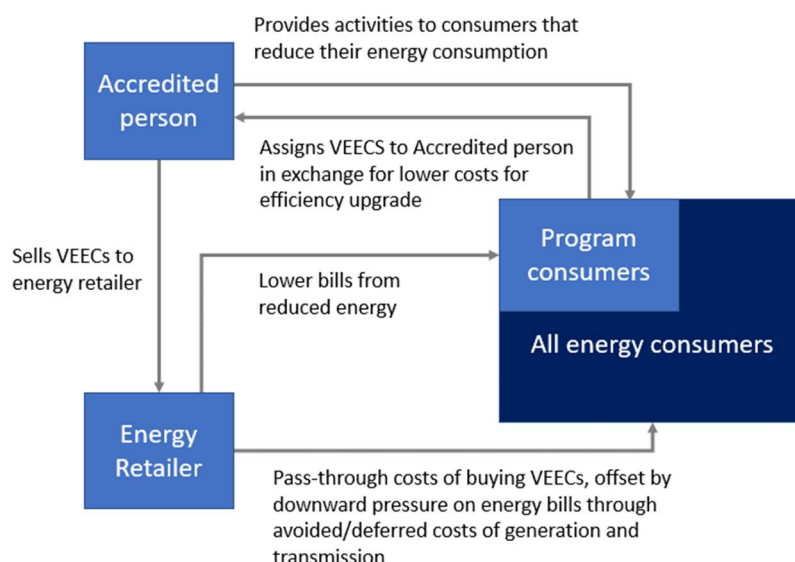
While improving energy efficiency will result in lower energy costs for those participating in the VEU program, there may be an initial investment cost to modify or replace appliances or adapt premises, which may be a barrier to energy efficiency improvements occurring.

These investment barriers have been examined in previous reviews and impact assessments have been prepared for the overarching legislation. The existence of these barriers has historically justified the need for the VEU program.

The VEU program reduces these investment barriers by creating a tradeable certificate. The value of certificates is created by requiring energy retailers to buy certificates and this value can be used to lower the costs investing in energy efficiency improvements for energy consumers.

The market for certificates operates through APs who may create certificates for energy consumers. Consumers assign the certificates to the APs in exchange for being offered a discount on an energy efficient upgrade to their premises. This reduced price, together with the shift in effort from the consumer to the APs to pursue certificate-creating activities and provide information about how to best undertake an upgrade, helps consumers overcome the barriers to investing in energy efficiency improvements. APs recover this discount and their own costs by selling the certificates to energy retailers. There are currently over 200 APs able to create certificates. Figure F shows how the VEU program works and shows how energy retailers pass through the costs of buying certificates to the energy consumer.

Figure F: How the Victorian Energy Upgrades program works



The VEU program consumer assigns certificates to an AP for lower cost energy upgrades, while the AP sells certificates to the energy retailer.

The number of certificates a retailer needs to surrender each year depends on the amount of energy they purchase from the wholesale market. Most of the energy they purchase and sell on to Victorian energy consumers is 'liable energy' for the purposes of the VEU program. For each retailer, the share of total liable energy that they purchase, and sell will correspond to the share of the annual certificate target that they are

responsible for. For instance, if they purchase and sell one third of all the liable energy, then they must deliver certificates that correspond to a third of the annual target under the VEU program. One certificate corresponds with the reduction of one tonne of GHG emissions.

Currently, certificates can be created in two ways:

- Through activities prescribed in the current regulations that use a simplified approach, whereby the GHG abatement (and the number of certificates) for each activity is 'deemed' through a standard methodology included in the current regulations.
- Through project-based activities, which are possible under the separate *Victorian Energy Efficiency Target (Project-Based Activities) Regulations 2017 (Vic)* (PBA regulations). Project-based activities are customised (and generally large-scale) discrete activities that improve energy efficiency at premises and create certificates through calculating GHG abatement by measuring the actual energy saved.

The VEU program is a market-based approach to achieving the objective of reducing GHG emissions. By creating a market in certificates, competition among APs to sell certificates to energy retailers means that certificates will tend towards activities that have the lowest cost for each tonne of GHG emissions avoided.³⁰ This also means that the market hinges on GHG abatement values prescribed for each activity, as these directly price the activity in the market. Activities included in the VEU program are expected to increase the take-up of energy efficiency improvements beyond business-as-usual levels. Analysis and calculations for these activities exclude the generation of additional certificates.

As greenhouse gas emission reductions are created by incentivising gas and electricity efficiency activities, this supports the second objective of the VEET Act, to encourage the efficient use of electricity and gas.

Participation by consumers, including businesses, is entirely voluntary. Agreeing to undertake certificate - creating activities relies on the consumer deciding as to whether they will be better off, taking account of any reduced prices, information and services provided by APs. Consumers who elect to participate in the VEU program enjoy reductions in their energy costs afterwards, for at least the period where the upgrade reflects a bring-forward of efficiency that would be achieved under a business-as-usual scenario and through reductions in wholesale energy costs.

Energy retailers are required to buy certificates but will pass some of the cost on to their customers — including those not participating in the VEU program by accessing efficiency upgrades through activities³¹. Modelling by the department shows that historically, this additional cost has been more than offset by the reduced demand for energy brought about by improved energy efficiency that places downward pressure on wholesale energy prices.

Suppliers of certificates investing in new business models to deliver low-cost upgrades at scale supports the third objective of the VEET Act — encouraging investment, employment and technology development in industries that supply goods and services which reduce the use of electricity and gas by consumers. This has led to:

- the development of new technologies
- the rapid achievement of market penetration (for example, LED lighting)
- significant employment in both the identification and delivery of installations and the manufacturing of products
- investments to generate these new activities.

30. In this context, lowest cost is the cost difference offered to consumers to take up the activity, as well as the AP's costs of complying with the VEU program (including the \$1 per certificate registration fee).

31. Thwaites, J, Faulkner, P and Mulder, T (2017) *Independent review into the electricity and gas retail markets in Victoria*, viewed 22 November 2022.

Appendix B: Forecast volume of certificates, accredited providers and services performed

Table 24: Forecast certificates, accredited providers, and services

	2023-24	2024-25	2025-26
No. of certificates created/transferred	7,200,000 ³²	7,300,000 ³³	7,300,000 ³⁴
No. of APs subject to annual reaccreditation fee	100	110	120
No. of applications of accreditation	15	15	15
No. of variations of accreditation conditions	30	30	30
No. of entities submitting energy acquisition statements	38	38	38
No. of VEET account creations	75	75	75
No. of product applications	1,231	1,231	1,231
No. of project-based activity impact reports	233	233	233

These forecasts are ESC estimates, extrapolating out trends based on existing data. Some figures are also based on assuming that annual VEET targets are met. These assumptions are listed below in Table 25.

Table 25: Assumptions made in forecasting certificates, accredited providers, and services

Forecast item	Assumption made
No. of certificates created/transferred	Assumed the legislated targets for each year are met and that the 2026 target (which has not been set) matches the legislated target in 2025.
No. of APs subject to annual reaccreditation fee	Assumed the number of APs in the program starts at 100 (based on levels from previous years), that 5 APs leave the program each year, and that 15 APs enter the program each year.
No. of applications of accreditation	Assumed that 15 new applicants apply each year to take advantage of new activities announced by the Department.
No. of extended accreditations	Assumed that 30 existing APs apply each year to add new activities to their accreditations to take advantage of new activities announced by the Department and respond to market dynamics.
No. of entities submitting energy acquisition statements	Assumed numbers are in line with data from the most recent years.
No. of VEET account creations	Relative to previous years, assumed slightly reduced trading account creations due to introduction of fee associated with the application.
No. of product applications	Assumed numbers are in line with data from the most recent years.

³² The certificates surrendered to meet the VEU target for 2024 is assumed to be created and registered in the 2023-24 financial year, as the certificate market normally runs six months ahead of the liability.

³³ As above, certificate creation and registration is assumed to meet the 2025 VEU target.

³⁴ For the purpose of this analysis, certificate creation and registration in 2025-26 is assumed to be the same at 2024-25. This is a simplifying assumption and is not intended to be indicative of the future target setting for 2026 to 2030.

Sensitivity analysis (if the cost variables change)

While all fee options were designed to be fully cost recoverable, consideration was given for scenarios where the certificates created are both lower and higher than forecast, as this would present risks to the ESC for over- or under-recovering its costs.

ESC advice shows that 83 per cent of the ESC’s costs relate to certificate creation (recovered through certificate fees). Subsequently, while the analysis could be undertaken with other variables, ESC advice has stated that variations in cost recovery would be immaterial and rather, the number of certificates created was the key consideration.

The analysis shows that when certificate creation volumes are 20 per cent lower than forecast, option 1 had the lowest risk as the ESC’s costs would reduce by roughly the same amount as its revenue (Table 26). Moreover, as options 2 and 3 involve a degree of cross-subsidy, they present a greater risk of over- or under-recovering its costs.

Table 26: Sensitivity analysis on certificate creation volumes 20% lower than forecast

	Total revenue collected	Total costs to recover	Difference	Percentage difference
Option 1	\$45,269,113	\$45,269,113	\$0	0%
Option 2	\$44,085,951	\$45,269,113	-\$1,183,162	-2.7%
Option 3	\$45,096,205	\$45,269,113	-\$172,908	-0.4%

Conversely, if certificate creation volumes were 20 per cent higher than forecasted, the ESC would over-recover under options 2 and 3, with no changes in difference for option 1 (Table 27).

Table 27: Sensitivity analysis on certificate creation volumes 20% higher than forecast

	Total revenue collected	Total costs to recover	Difference	Percentage difference
Option 1	\$63,144,825	\$63,144,825	\$0	0%
Option 2	\$64,327,987	\$63,144,825	\$1,183,162	2.7%
Option 3	\$63,317,733	\$63,144,825	\$172,908	0.3%

Appendix C: Impacts on electricity prices

Whether APs would pass on in full any cost increases into the price of a certificate, depends on competitive dynamics in the market for certificates. In perfectly competitive markets, prices will be determined by the marginal cost of the marginal supplier. The marginal supplier is defined as the supplier with highest costs that is most at risk of being outcompeted. If this marginal supplier is outcompeted, they change from being a price setter to a price taker and accept certificate prices that do not allow them to pass on all costs. This means that, if the certificate market is perfectly competitive, whether fee changes are passed through to the certificate price will depend on whether these service fees form part of the marginal cost of the marginal supplier.

The certificate fee costs would likely be passed through into retail electricity prices because this cost forms part of the AP's short run marginal cost. That is, the cost of each installation. Certificate creation, validation, and registration related costs account for 83 per cent of the ESC's costs for the VEU program. Other fees may be part of long-run marginal costs, that is, costs not associated with a particular installation. There may be periods when these costs are not reflected in the efficient market price.

In recent years, the certificate price has been highly variable, even aside from government changes to the program that have affected the types and costs of the upgrades being delivered. However, during this time the number of active APs has not changed substantially – changing only 7 per cent from 72 certificate sellers in January 2020 to 77 certificate sellers in January 2023, while the certificate price increased by approximately 150% during this three-year period. This muted response may indicate that the certificate market is not perfectly competitive due to barriers to entry and that prices are set above the marginal cost of the marginal supplier. In this case, APs are likely to be able to absorb some or all of the increased fees, on the other hand, this may suggest that APs have some price-setting power. For the purpose of this analysis, a lower-bound estimate of the pass-through costs will assume APs and energy retailers absorb the full costs and no increases are passed through to energy consumers.

To be conservative, this analysis assumed an upper-bound of 100 per cent cost recovery. To model the impact of new fee options on retail electricity prices, a range was created:

- the low end of the range is based on APs absorbing additional fees, given that these are within the existing range of certificate price fluctuations (approximately \$25 per year) that APs currently absorb
- If an assumption is made on a level of pass-through certificate costs that is equivalent to 100% cost recovery, this equates to pass-through costs \$2.65 per certificate for fee option 2.
- If a typical level of competition in the market were assumed, the electricity price impact would fall somewhere between the low and high end estimates. The department considers that this range reasonably reflects the potential impacts of the proposed new fee arrangements on retail prices.

The impact on a typical residential and commercial customer's annual bill has been determined. These calculations assumed current average annual bills of \$1,400 for households and \$5,612 for businesses. The analysis used a simple retail price model, populated with cost estimates from the ESC's most recent Victorian Default Offer (VDO) decision.

Analysis suggests the impact of the new fee arrangements would be small. These impacts range from 0 per cent up to 0.184 per cent for households, which translates into an increase of less than \$1.20 per year.

Table 28: The range of impacts on electricity bills for energy consumers from option 2

	Lowest estimated pass-through costs	Highest estimated pass-through costs
Household bill impact	\$0 per annum	\$1.20 per annum
Business bill impact	\$0 per annum	\$6.00 per annum

Note that this analysis of electricity prices does not factor in overall bill reductions that the scheme can provide to customers through energy-saving products.