

Australian Energy Market Commission
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Submitted online at www.aemc.gov.au

26th February 2014

RE: 2014 Retail Competition Review Approach Paper

AEMC Ref: RPR0002

Dear Commissioners,

Thank you for the opportunity to comment on the Approach Paper for your 2014 Retail Competition Review program.

As the peak body for the community services sector in South Australia, SACOSS has a long-standing interest in the delivery of essential services. Our research shows that the cost of basic necessities like electricity impacts greatly and disproportionately on vulnerable and disadvantaged people. Our advocacy is informed by our members; organisations and individuals who witness these impacts in our community.

The South Australian Government removed retail price regulation and adopted the National Energy Customer Framework on February 1st, 2013. South Australian households and small businesses have now experienced the first year of these significant market reforms. The Australian Bureau of Statistics Consumer Price Index for Adelaide Electricity Prices has shown that average electricity prices have reduced in calendar year 2013. However, recent reports by the AEMC¹ and the Victorian Essential Services Commission (ESCV)² also highlight that South Australia continues to have both the nation's highest electricity prices and highest rates of electricity disconnections for failing to pay bills on time.

Please find a detailed submission attached that responds to the questions posed in the Approach Paper.

We thank you in advance for your consideration of our comments. If you have any questions relating to the above, please contact SACOSS Senior Policy Officer, Jo De Silva on 8305 4211 or via jo@sacoss.org.au.

Yours sincerely,

Ross Womersley
Executive Director

¹ AEMC 2013 Residential Electricity Price Trends www.aemc.gov.au/market-reviews/completed/retail-electricity-price-trends-2013.html

² ESCV Energy retailers comparative performance report – Customer service 2012-13 Table 3.2, p31 available from www.esc.vic.gov.au/Energy/Energy-retail-performance-reports

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SACOSS Submission to:

2014 Retail Competition Review – Approach Paper

AEMC Ref: RPR0002



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Background

The Australian Energy Market Commission (AEMC) is responsible under the Australian Energy Market Agreement (AEMA) for assessing the state of competition in electricity and natural gas retail markets. The AEMC's reviews provide advice to governments to support a commitment made by all jurisdictions under the AEMA to remove retail energy price regulation where effective competition can be demonstrated.

The 2014 review will be the first AEMC review of retail energy market competition that looks at all jurisdictions in the National Electricity Market (NEM) at the same time. The Approach Paper applies solely to the 2014 review. The AEMC intend to consult in the second half of 2014 to refine the approach for future annual competition reviews.

The reviews are to principally cover energy markets in jurisdictions that are subject to retail price regulation. However the AEMC will also consider the effectiveness of competition in jurisdictions where prices have been deregulated. SACOSS attended an AEMC forum in Adelaide on 17th February 2014.

The South Australian Government removed price regulation for both electricity and gas on February 1st, 2013. The effect of this is to shift reliance from regulatory price setting to competition in the sale of energy.

The Approach Paper incorporates a series of 22 questions at Appendix A. The SACOSS response to these questions follows:

SACOSS Response

SACOSS sees a number of unique features of the South Australian electricity and gas markets that justify specific attention:

- The extent of vertical integration in both electricity and gas
- The lack of competition for gas / treatment of gas as a 'value add' to electricity sales
- Structural issues since market start (especially in electricity but also gas)

Market definition

1. Is there evidence to support alternative market definitions to those that we are proposing to use for the review? We plan to base our analysis on separate markets for electricity and gas in each NEM region (ie two markets per region), except for Queensland where South East Queensland will be treated as a separate geographic market to the rest of Queensland.

SACOSS supports the separate consideration of electricity and gas but is strongly of the view that that the extent of vertical integration in the South Australian electricity market means that consideration of 'retail' in isolation from 'generation' is problematic.

Table 1 illustrates the relationship between small customer market shares and generation ownership. The data is based on market shares published by ESCOSA at December 2012. The AER is now responsible for publishing retail statistics as part of the NECF but does not publish market shares for all retailers.

Retailer	Small Customer Base (Dec 2012)		Conventional Generation	MW	Wind Power	MW
AGL (incl Powerdirect)	455,324	55%	Torrens Island	1280	Hallett1, Hallett 2, Wattle Point, North Brown Hill, The Bluff	309
Origin	146,113	18%	Quarantine, Ladbroke Grove, Osborne	484	-	
Simply Energy	76,474	9%	GDF Suez: Pelican Point, Synergen Peaking stations	860.5	Canunda	46
Energy Australia	84,724	10%	Hallett	228.3	Waterloo, Cathedral Rocks	177
Lumo	48,891	6%	Infratil: Angaston, Pt Stanvac and Lonsdale	128	Snowtown	98.7
Alinta	9,531	1%	Pt Augusta Power Stations	770	-	
		99%		3,751		631

Table 1: Relationship between retail market shares and generation ownership in South Australia as at end December 2012. Sources: AEMO, AER, ESCOSA

The AEMC's 2008 review of competition in SA highlighted the lack of competition for gas in regional SA³:

“ ... the Commission's findings are that competition is effective for small electricity and small natural gas customers in South Australia, although competition is relatively more intense in electricity than in gas. However, in making its findings the Commission has identified some structural limitations in relation to the ability for gas retailers to access firm transmission haulage services. These limitations are affecting the ability of regional small gas customers to access the full benefits of competition

³ Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia AEMC Ref EMO0004 First Final Report 19 September 2008, p19-20

with market contract offers available to these customers being limited to those provided by Origin.”

SACOSS believes it would be appropriate for the AEMC to update its perspective on this and advise consumers as to whether this situation has changed in the 5 years since the review.

Customer activity in the market

2. Are small customers able to access energy related information that is easy to understand, relevant and up to date, that supports their decision-making process to choose an energy offer?

The adoption of the National Energy Customer Framework (NECF) from February 2013 led to the launch of Energy Made Easy for SA. While generally welcomed, this was not a significant advance on the ESCOSA price comparison service available for many years before that date.

SACOSS notes that access to comparison information relies heavily on access to the internet. We would like to draw the AEMC’s attention to the challenges this presents for lower income households, particularly the elderly. The Australian Bureau of Statistics (ABS) publishes data on household and personal Internet Access and Usage in 8146.0 – Household Use of Information Technology, 2012-13. According to the ABS, 17% of households do not have internet access. Further, Figure 1 relates households with and without internet access by equivalised household income quintile and shows that over 40% of households in the bottom quintile report not having home internet access.

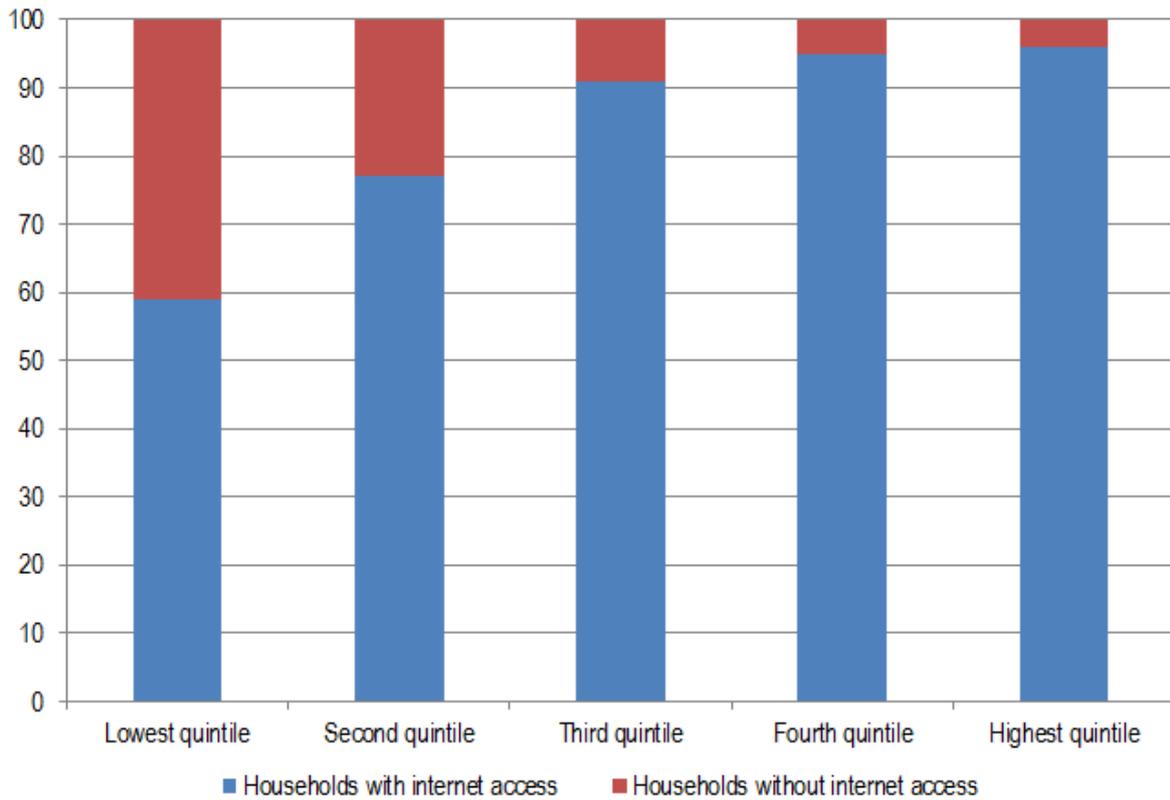


Figure 1: Household Internet Access by Equivalised household Income Quintile. Source: ABS 8146.0 2012/13

The issue seems to be more acute for older Australians (over 65) as illustrated in Figure 2. These figures indicate that a majority of older Australians do not access the internet. This is particularly the case for those without tertiary education qualifications as illustrated in Figure 3. The ABS data indicates that older Australians comprise around 3 million people (1/6th of the population of persons over 15 considered in the report).

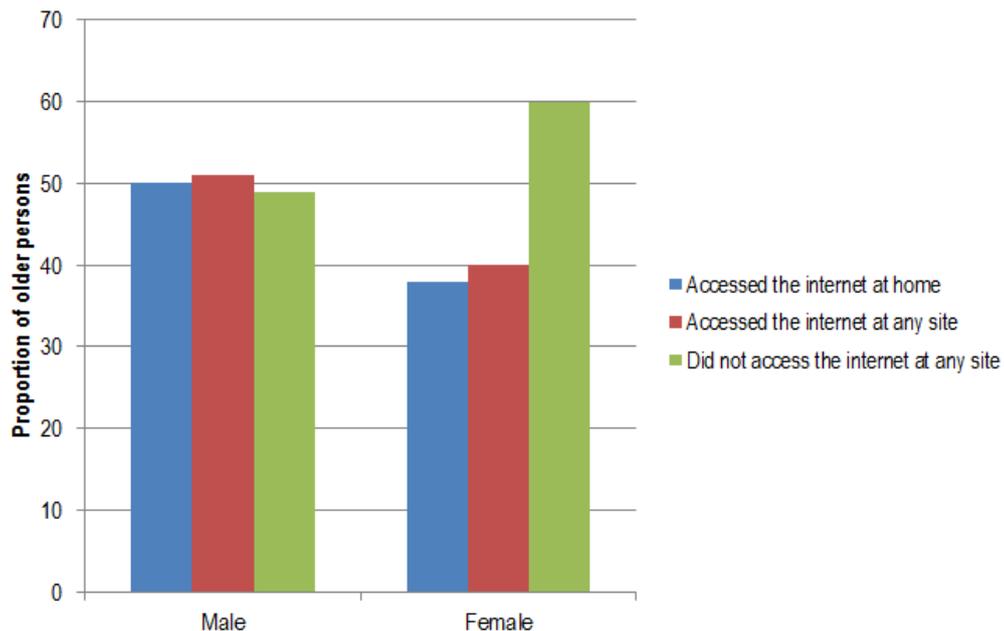


Figure 2: Internet Access by older persons. Source: ABS 8146.0 2012/13

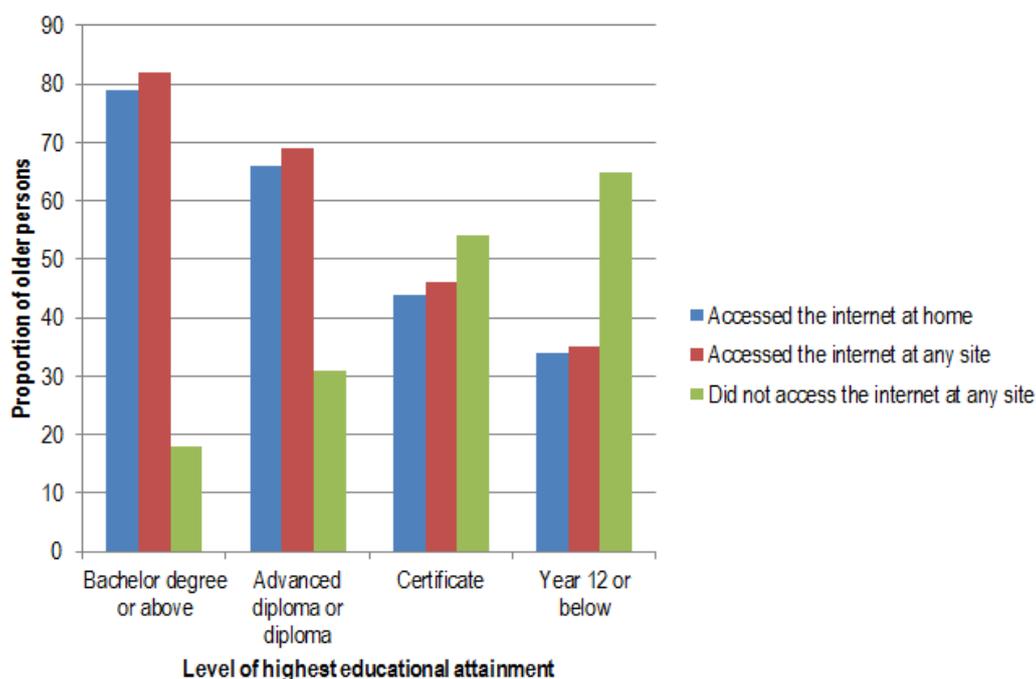


Figure 3: Internet Access by older persons in relation to level of education attainment. Source: ABS 8146.0 2012/13

Another key issue for consumers relates to the difference between the prices (and cost estimates) at the time of signing on compared to the prices/costs experienced during the contract term. This is an issue highlighted in the current rule change proposal from CUAC and CALC⁴ – the first rule change proposal received for the National Energy Retail Rules.

A further issue, and one identified by the Australian Competition and Consumer Commission (ACCC) is the apparently universal market approach of pricing by percentage discounts. The ACCC referred to this in 2013 to this as *Discounts off what?*⁵ and continues to be a priority for the watchdog as outlined by ACCC Chairman Mr Rod Sims, 21 February 2014 (Speech to CEDA Conference)⁶:

The energy sector consumer protection priorities set out in the Competition and Enforcement Policy:

In the energy sector our focus in 2013 was on addressing unlawful door-to-door sales conduct by energy retailers. AGL and APG were ordered to pay penalties greater than \$1 million, and our proceedings against Energy Australia and Origin Energy are still before the Federal Court.

Our next area of focus in the energy sector is misleading discount claims. The ACCC is increasingly concerned about possible misleading conduct by energy retailers in their promotion of energy plans. These concerns relate to the promotion of discounts and savings off energy use and/or supply charges under those plans. We refer to this new focus of our energy work as “discounts off what?”

⁴ <http://www.aemc.gov.au/retail/rule-changes/open/retailer-price-variations-in-market-retail-contracts.html>

⁵ <http://www.accc.gov.au/media-release/discount-off-what-energy-plan-promotions-a-concern>

⁶ <http://www.accc.gov.au/speech/ceda-conference-looking-forward-to-2014>

This new focus will not come as a surprise to the sector. In August 2013 the ACCC wrote to energy retailers about our concerns. In December 2013 the ACCC commenced legal action against AGL South Australia for allegedly misleading residential consumers in South Australia about electricity discounts.

There will soon be further court action.

3. What motivates small customers to switch from a standing (or regulated) offer to a market offer?

SACOSS believes that, since market contracts have been available for over a decade in South Australia, this presumably only occurs due to retailers actively recruiting these 'sticky customers' or when they move home (including into aged care accommodation).

4. What motivates small customers to switch energy retailers?

SACOSS believes that survey techniques are appropriate to answer this question.

5. What are the reasons behind some small customers remaining on a standing (or regulated) offer rather than shopping around for a market offer?

As discussed, internet access is almost a necessity to pursue an informed choice. Also, literacy, numeracy and confidence can be substantive barriers. For many though, the 'search costs' do not outweigh perceptions of the savings on offer.

6. Are there any barriers preventing customers from switching energy plans within their current retailer or offered by an alternative retailer?

Other than issues raised above, the accumulation of debt with a retailer can inhibit switching since this would trigger alternative (and more aggressive and expensive) debt collection methods by retailers.

Barriers to entry, exit or expansion

7. Are there any current or expected barriers to entry, exit or expansion that impact on the development of effective competition in small customer electricity and natural gas retailing?

SACOSS is of the view that the dominant retail market barriers actually reside in the wholesale market.

There is no evidence of substantial market share being achieved in South Australia without vertical integration – only Lumo has been seen to grow its market share since the 2008 allegations of the exercise of market power and this has been enabled by the portfolio of generators by Lumo's owners Infratil.

The Australian Energy Regulator in its 2012 *State of the Energy Market* report observed:

“AGL Energy’s strategic withholding of generation capacity contributed to average spot prices in South Australia being significantly above those in other NEM regions between 2007-08 and 2009-10.”

The behaviour of AGL was used as the basis for a rule change proposal⁷ that ultimately did not proceed. SACOSS notes however that AGL (and its wholly owned subsidiary Powerdirect) have managed to stabilise market share at around 55% since these time when these assertions were made. This is illustrated in Figure 4 (noting that since December 2012, the AER has been responsible for reporting retail statistics but does not include separate reporting of Powerdirect).

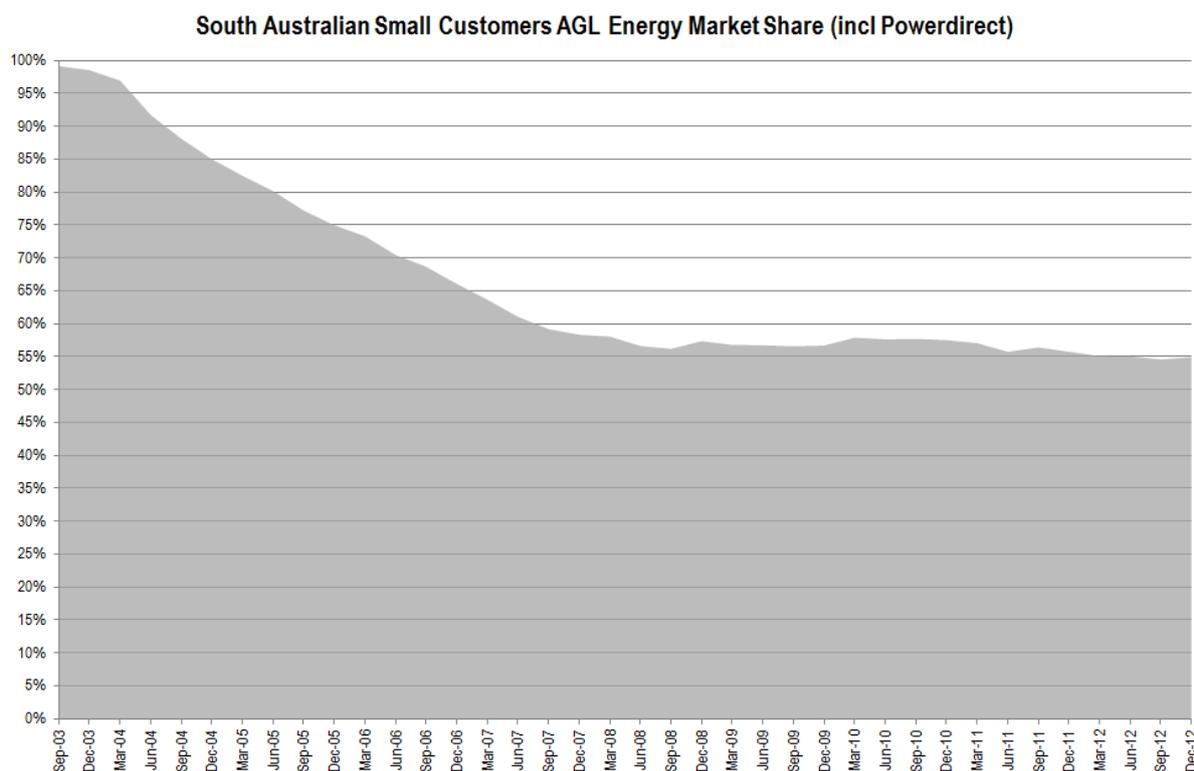


Figure 1: AGL Energy electricity small customer market share 2003-12. Source: ESCOSA

8. Have the barriers referred to above dissuaded retail businesses from entering, expanding within, or exiting the market?

SACOSS notes that the only *new entrants* of late seem to be solar businesses seeking retail licenses or exemptions related to lease-based solar energy products.

9. Are the barriers referred to above likely to persist or abate in the future?

SACOSS is of the view that the issues are structural and relate to the monopoly of AGL at market start.

⁷ <http://www.aemc.gov.au/electricity/rule-changes/completed/potential-generator-market-power-in-the-nem.html>

The South Australian privatisation of electricity assets has been (and continues to be) widely commented on. Without offering an opinion on whether or not consumers are better off with or without privatisation, SACOSS would like to draw attention to the legacy impacts of the way privatisation was handled in South Australia.

The South Australian government sold the Electricity Trust of South Australia (ETSA) businesses to Cheung Kong Infrastructure Holdings Ltd (CKI) and Hongkong Electric Holdings Ltd (HEH) via a tender process concluding in December 1999. When CKI and HEH were awarded the ETSA Utilities (the network business) & ETSA Power (the retail business) tender at A\$3.4 billion, it was agreed between the South Australian Government and CKI/HEH that should ETSA Power be sold within two years after the tender was awarded, any amount generated above A\$150 million is to belong to the South Australian government⁸. In January 2000 AGL paid CKI/HEH \$175m for the business and added approximately 734,000 customers to their books⁹.

The awarding of the entire franchise to one entity has shaped the small customer market since inception. As the South Australian regulator noted in 2002¹⁰:

“The South Australian market is unique, and this can be highlighted by the domination of the single retailer (AGL) at commencement of the competitive market in January 2003. In no other market in the UK, NSW or Victoria has there been only one dominant retailer at market commencement with 100% of the new market. This situation calls for unique measures for protecting consumers and encouraging other retailers to join AGL in supplying the domestic and small business market. The Government’s approach is unique and squarely puts the responsibility back with the retail industry to demonstrate the prices they seek to apply in South Australia are justified.”

Over a decade later, AGL Energy continues to hold contracts with over 50% of small customers in South Australia¹¹. Through needing to hedge such large demand, AGL also now owns significant generation assets in South Australia including – since July 2007 - the state’s largest, Torrens Island Power Station (TIPS) – a 1280MW gas-fired powered station in a market whose demand only occasionally exceeds 3000 MW¹².

⁸ CKI Media release January 2000 available from www.cki.com.hk/english/whatsNew/2000/20000114.htm

⁹ Refer to Australian Stock Exchange archive for AGL 24th August 2000 “Preliminary Final Report & Press Release Part A” available from: <http://www.asx.com.au/asx/statistics/displayAnnouncement.do?display=text&issuerId=40&announcementId=199820>

¹⁰ South Australian Independent Industry Regulator Reviewing and Approving Electricity Retail Prices in a Competitive Market, Initial Thoughts April 2002, page 29 www.escosa.sa.gov.au/library/020408-Review_ApprRetailPrices.pdf

¹¹ Source: ESCOSA, AER reports and AEMO Switching data indicate the AGL and subsidiary Powerdirect continued to hold around 55% of small customer contracts at the end of 2013 – 11 years after the commencement of full retail contestability in the SA electricity market

¹² Information on the AGL acquisition of TIPS is summarised in a supplementary AGL Submission to the AEMC review of the Effectiveness of Competition in the Electricity and Gas Retail Markets in South Australia September 2008 available from <http://www.aemc.gov.au/Media/docs/AGL%20Supplementary-760a4c20-1864-4bf1-adda-19a697969a7c-0.pdf>

The end result of the way privatisation was handled is a dominant player in relatively small market. SACOSS would argue that this is an important challenge for the development of competition in SA, especially in a context where Origin Energy has a similarly dominant position in the South Australian gas market.

Supporting this view, the Case Study prepared by KPMG for the AEMC to celebrate 15 years of the National Electricity Market (NEM) found that¹³:

“Getting industry structures right was key for effective competition” and that “... there is an explicit trade-off between the benefits of a competitive industry structure and maximising sales proceeds from privatisation. The gains for the economy of a competitive industry structure needs to take precedence over the fiscal impacts of privatisation. To do otherwise poses a risk to the benefits of the reform being sustained.”

SACOSS is of the view that this is particularly relevant to the way that competition is judged in the South Australian market.

Independent rivalry

10. To what extent do energy retailers compete with each other in terms of price or product/service differentiation to acquire new, and retain existing, small customers?

11. What sort of product and/or service improvements have retailers delivered to small customers in electricity and natural gas retail markets?

12. In those jurisdictions where price regulation is in place, has retail price regulation encouraged, or impeded, tariff innovation or product/service innovation in small customer electricity and natural gas retail markets?

13. In those jurisdictions where price regulation has been removed, has retail price deregulation encouraged, or impeded, tariff innovation or product/service innovation in small customer electricity and natural gas retail markets?

By and large, the prices households pay for electricity comprise a fixed component – the ‘service access charge’ or ‘supply charge’ – and a ‘rate’ based on the volume of electricity consumed over the quarter. This is generally expressed as ‘cents per kilowatt-hour’ or c/kWh. Most households are paying somewhere around 70 cents per day for the fixed component (about \$250 pa) and over 30 cents per kWh.

The various offers in the market from the 12 electricity retailers selling into South Australia are variations of this with some variations in the ‘structure’ of tariffs. When the residential electricity market was opened up to competition in 2003, AGL Energy, the incumbent

¹³ “15 Years of the National Electricity Market: the book”, AEMC 13 December 2013
<http://www.aemc.gov.au/news/whats-new/15-years-of-the-national-electricity-market-the-book.html>

retailer, set its tariffs to have higher prices in Summer (the January-March quarter). 11 years later, 7 of the 12 retailers follow this same practice. Further, 11 out of the 12 retailers structure their tariffs in what is referred to as 'inclining blocks' where prices increase as consumption increases. The only retailer that does not, Powerdirect, is a wholly owned subsidiary of AGL Energy.

14. What types of marketing practices, or business behaviours, have small customers experienced in different electricity and natural gas retail markets?

The AEMC is referred to the various ACCC actions regarding door-to-door selling and misleading claims in the energy sector. As mentioned, the Discounts Off What? Issue is to be a priority for the ACCC in 2014. SACOSS is concerned that there seems to be an ongoing list of marketing approaches in the sector that require intervention to protect the consumer interest.

Customer satisfaction

15. Are customers satisfied with the service quality they receive from their energy retailer(s) and the value for money?
16. Are customers satisfied with the level of choice available in the market?
17. Are customers satisfied with the ease and speed with which they can switch retailers?
18. Is there evidence of any long term jurisdictional or cross-jurisdictional trends in the number and nature of customer complaints to retailers or ombudsman?

The AEMC is referred to the various AER, ESCOSA and Ombudsman¹⁴ reports that show complaints are generally growing in recent years.

Retailer outcomes

19. How does the presence of price regulation affect retailer risk profiles and retailer risk management strategies?

In SA the key risk management strategy for energy retailers is that of the physical hedge – i.e. vertical integration.

20. Are energy retailers to small customers able to recover their efficient costs and an appropriate return at current standing (or regulated) offer contract tariffs or at current market offer contract tariffs?

The extent of vertical integration in South Australia makes it very difficult to distinguish the returns achieved by retail sales from those made in the wholesale market.

¹⁴ EWOSA Annual Report 2013 www.ewosa.com.au/images/publications/EWOSA_REPORT_2013.pdf

21. Is there evidence of a material divergence in the level of competitive market costs between any of the jurisdictions where market offers are available?
22. Is there any evidence to explain the underlying cause(s) of any material inter-market divergence in retailer costs (ie the costs faced by the retailer)?

These questions relate to the Victorian experience reported by the ESCV¹⁵ and the AEMC in its 2013 Residential Electricity Price Trends Report (13 Dec 2013).

Comparing the states, the combined wholesale/retail components of each show that, of the jurisdictions where retail competition exists, the highest prices are in the two jurisdictions where price regulation has been removed: SA and Victoria as shown in Figure 5.

AEMC Residential Electricity Prices (Competitive Wholesale/Retail elements) by State 2013-14

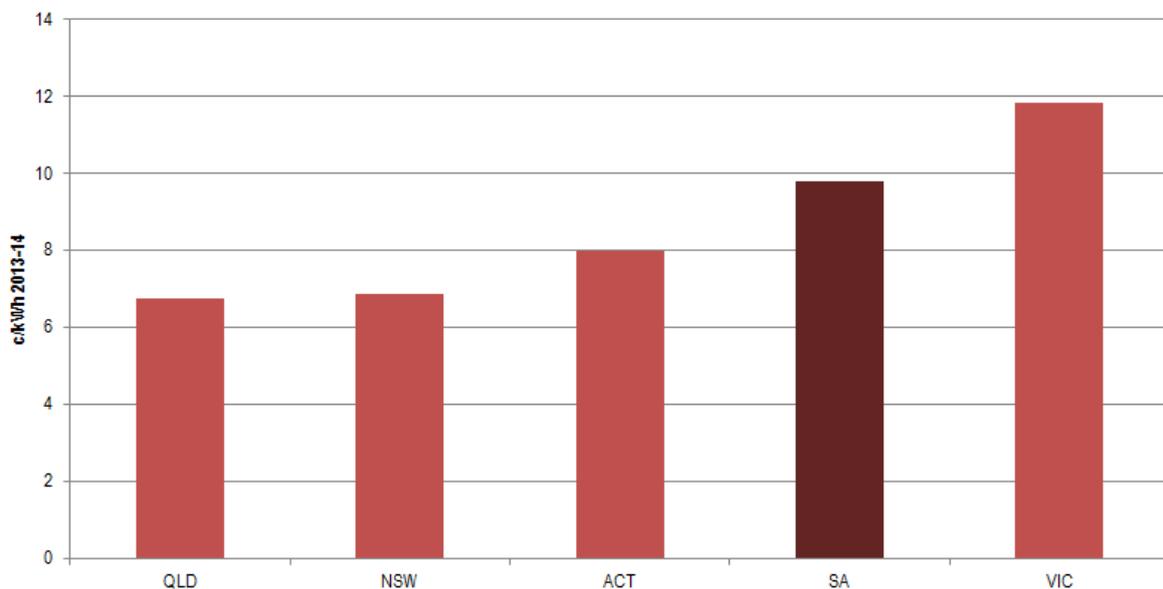


Figure 5: Estimates of Wholesale Energy Costs 2013-14. Source: AEMC¹⁶

Coincidentally, the Energy Supply Association of Australia (ESAA) National Electricity Reform Scorecard¹⁷ rates these two jurisdictions the highest for “... *progressing reforms to improve the efficiency and competitiveness* ...” of their electricity markets.

Understandably, there is a key consumer issue of who benefits from these reforms and the extent to which consumers actually benefit.

¹⁵ ESCV Analysis of Electricity Retail Prices and Retail Margins 2006-12 available from <http://www.esc.vic.gov.au/Energy/Analysis-of-Electricity-Retail-Prices-and-Retail-M>

¹⁶ AEMC 2013 Residential Electricity Price Trends www.aemc.gov.au/market-reviews/completed/retail-electricity-price-trends-2013.html

¹⁷ http://esaa.com.au/policy/electricity_reform_scorecard

Discount off what? Energy plan promotions a concern¹⁸

27 June 2013

The Australian Competition and Consumer Commission will be writing to energy retailers to put them on notice about possible misleading promotions.

In a speech to the Consumer Action Law Centre's energy workshop in Melbourne, ACCC Deputy Chair Delia Rickard said the ACCC is increasingly concerned about possible misleading conduct by energy retailers in their promotion of energy plans.

"These concerns relate to the promotion of discounts and savings off energy use and/or supply charges under those plans."

Ms Rickard said no one should be surprised that the ACCC will take a firm approach where it forms the view that misleading representations are being made to consumers about savings.

The Deputy Chair also spoke about other energy consumer issues which form part of the ACCC's compliance and enforcement priorities.

"The ACCC has taken court action and we've obtained significant penalties against energy retailers and their marketing companies for poor conduct in door-to-door sales.

"This includes misleading statements about the purpose of salesperson's visit, such as representing they were not there to sell anything, and making misleading statements about the price of products, and claims that consumers were being overcharged by their current supplier."

In opening the workshop, Ms Rickard said comparability is a dilemma facing Australian energy consumers.

"While retail competition and choice have delivered many benefits, unfortunately it is a difficult and complex process for the average consumer to compare and decide on which energy plan suits them best."

Ms Rickard discussed the Australian Energy Regulator's price comparator website, Energy Made Easy, which allows households to compare gas and electricity offers as well as consider their energy usage.

Ms Rickard also provided an update on some of the key developments which will provide consumers with a voice at the energy regulation table.

Release number:

144/13

¹⁸ <http://www.accc.gov.au/media-release/discount-off-what-energy-plan-promotions-a-concern>