

*Integral claims that unlike retail-only energy companies, Integral Energy also has over 50 years of experience in managing one of Australia’s largest energy networks. Every day we distribute electricity to over 2.1 million people in households and businesses across 24,500 square kilometres of Greater Western Sydney, the Illawarra, and the Southern Highlands of NSW. Integral’s network area covers some of the fastest growing regions of Australia, including Sydney’s Greater West, the Southern Highlands and the Illawarra.”*

## **GREENSWICH** <sup>183</sup>

**Sponsor: Global Green Plan** [www.globalgreenplan](http://www.globalgreenplan)

*This is a business unit of the not-for-profit Global green plan environmental organization.*

*The FAQs explain that the money that is paid through GreenSwitch is only “the difference between the cost of standard fossil power and Greenpower. The generator also gets a payment through the wholesale market when the power is fed into the grid. At this time renewable energy is more expensive to produce than fossil power.*

*GreenSwitch 100% GreenPower green energy*

*By selecting the GreenSwitch Neighbourhood option for your electricity supply, we guarantee that we will supply 100% government accredited GreenPower energy. All electricity generated in this way is done through renewable sources. More information, is obtainable to the GreenSwitch website at [www.greenswitch.com.au](http://www.greenswitch.com.au)*

*GreenSwitch neighbourhood is available at an extra 4.4 cents per kilowatt hour (inc GST on top of your regular electricity tariff. That’s a lot cheaper than most other electricity companies.*

*Remember we still donate 4% of your electricity spend to your nominated partner. If you would like to know more about GreenPower, our GreenSwitch neighbourhood product and Renewable Energy in general, please download our GreenPower Fact Sheet.*

## **NEIGHBOURHOOD ENERGY (previously known as Our Energy Neighbourhood**

The domain change for has been changed to Neighbourhood Energy, to show they are more about neighbourhood than about energy.

The website claims that Greenswich neighbourhood is available at an extra 4.4 cents per kilowatt hour (including GST) above the regular electricity tariff, which it claims is a lot cheaper than most other electricity companies.

They offer to donate 4% of the electricity spend into a nominated community partner which is the primary positioning theme

## **RED ENERGY**

Red Energy is a stand-alone electricity retailer with a two-year history Victorian energy market for over two years.

They provide two options to save on electricity bills through pay-on-time contractual terms for those on a 2-yearfixed term contracts and those without such contracts:

5% Pay on Time Discount <sup>TM</sup> and no fixed term contract

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<sup>183</sup> Information taken from website [www.greenswitch.com.au](http://www.greenswitch.com.au)

OR

7% Pay on Time Discount <sup>TM</sup> and a 2 year fixed term contract<sup>1</sup> (in South Australia only until withdrawn – check published terms and conditions)

Guarantees continuity during the switching period

The meter will continue to be read on a quarterly basis by the same company that reads it at the moment.

Entices customers to support renewable energy at no extra cost and the fact that they are 100% owned by Snowy Hydro.

Red Energy is wholly owned by Snowy Hydro Limited (SHL), an Australian-owned company generating renewable peak energy and provides other energy-related products. The parent company SHL have assets of \$2 billion in assets in Australia.

Red Energy only supplies electricity, however hopes to offer you gas in the future.

## **Business Models**

The Wallis Retailer Survey published in October 2007 on the AEMC site reports that:

*The 13 retailers selling to domestic and small business<sup>3</sup> (business) customers in Victoria operate a range of business models. These extend from mass market retailing with large customer bases to niche operations focusing on specific product and service offerings catering to specific market segments. Most retailers concentrate on the domestic market although two specialize in products and services for businesses.*

*Several companies do not actively market to businesses at all. All companies offer green energy and one exclusively does this.*

*The ownership of the retailers also varies from publicly listed companies, to privately owned firms to government owned enterprises. Most are owned by Australian interests (whether privately or publicly), but two are owned by overseas interests. Since the market deregulated there have been mergers and takeovers between what were then incumbent suppliers and 10 totally new entrants.*

*Most retailers operate in more than one state. The extent of operations in other jurisdictions are summarized in Table 1*

<sup>3</sup> In this Report “business customer” refers to businesses consuming up to 160MWh per annum of electricity and 5 TJ per annum of gas

*“None of the second tier retailers who are licensed to sell both electricity and gas in Victoria operates in the ACT. The niche retailers, as their name suggests, operate more widely across the country when considered as a group. Between them they are operating in every state where energy retail markets are contestable.*

*All retailers are making market offers for electricity to every part of Victoria as reference to Table 2 shows. While market contracts are on offer in every part of the state for gas, the number of retailers offering them varies from 2 in the North West, to a maximum of 5 in all areas<sup>4</sup>. <sup>4</sup> At the time of the study, one retailer licensed to sell gas in Victoria was not doing so.”*

Some retailers just won't approach apartment blocks, ostensibly because of access difficulties. Some have abandoned unhedged residential customers. These cannot be the signs of market success.

## **IMPACT OF PRICES AND PROFIT MARGINS ON ENERGY RETAIL COMPETITION IN VICTORIA**

The CRA International Price and Profit Report “*Impact of Prices and Profit Margins on Energy Retail Competition in Victoria Final Report*” commissioned by the AEMC for the current Retail Competition Review (Victoria) is briefly discussed below, mostly in terms of its limitations.

This report is dated 8 November was been published online on the eve of the deadline for responses to the First Draft. Presumably a draft report had also been made available to the AEMC but this was not made publicly available to stakeholders who should have had the same opportunity to study preliminary material as the AEMC to allow more time to digest even preliminary results, given the tight deadlines.

The public had expected additional time to provide feedback on the CRA Report – indeed the AEMC had promised this, but again time has run out and the COAG deadlines are descending.

Because of the last-minute publication of this Report it would not have been feasible for any stakeholder to make a meaningful response to this report to meet the 9 November deadline for response if anyone noticed it at all online. It would have been helpful if at least an em-mail notification had been sent to all existing registered stakeholders who had provided email details.

Best practice requires that all evaluative material recognizes its own limitations and publicly highlights the limitations of any piece of study or research.

In passing I note the strong reservations and disclaimers made in the CRA Report about the quality or completeness of the data available. This is further discussed under the section in passing Prices and Profit Margins.

Cursory observation is made here that the CRA Report was based on best estimates only in the absence of actual data from retailers and that much reliance was placed from publicly available information and on historical data dating back to 2003.

CRA International are to be congratulated for acknowledging the limitations of the data and estimates presented in this report on the basis of paucity of available actual data and other considerations. CRA has professionally and diplomatically handled the issue of the poor quality of data available.

How could this reputable firm have been expected to produce reliable and accurate results under the circumstances? Has much strategic planning went into the exercise of determining the criteria that would be needed for robust assessment of the market?

One burning question is, was CRA sufficiently assisted with data that was or should have been carefully gathered not as a snapshot exercise but as a consistent best practice approach to collected pertinent data longitudinally after receiving best advice on evaluative design in assessing the impacts of competition? Can of proper assessment of such matters possibly be effected if undertaken a matter of months before regulatory change and price deregulation is undertaken

In good faith, perhaps an interpretation can be placed that these reservations and disclaimers are so significant as to possibly have the effect of appreciably diluting any weight placed on the report as showing how successful competition has been in a financial sense from retailer perspective.

These reservations summarize real concerns:

- CRA was forced to rely on publicly available information and historical data in order to assess the revenue and cost components that determine retailer margins;
- CRA was unable to obtain actual data from retailers;
- CRA was forced to rely on broad range estimates only because of unavailability of robust data in particular actual data;
- CRA was forced to rely on historical energy retail margins, and information in the public domain to assess the revenue and cost components that determine retailer margins; in particular revisiting of the previously analysis that was undertaken to calculate a regulated price path in 2003, with substitute for CRA's best estimates only of cost outturns for the years 2004-2007.
- CRA was forced to place reliance on average consumption levels of those on standing offers in order to assess retailers' revenues from customers on standing offer contracts. The material was partly sourced in August 2007 from retailers' websites with 'some input' from retailers describing their market offers that were available at the time. Typical discounts were assumed.
- CRA conceded the likelihood that actual results are more likely to be nearer to the midpoint or at the lower end of the ranges quoted in CRA's "best estimates" CRA have specified how their estimates were formulated for the different cost item as follows:

***Energy purchasing costs:** For electricity, these costs have been estimated using historical published contract prices for a fully contracted retailer. In the case of gas they estimated that energy purchase costs had increased by CPI+2 percentage points each year over the last four years.*

***Network charges:** For both electricity and gas, CRA estimated transmission and distribution charges on the basis of the published regulated network charges*

***Fees and levies:** These arise in both electricity and gas and were estimated from public sources.*

***Retailer operating costs.** These were costs that an energy retailer incurs in the course of carrying out its business and include a wide range of items, including billing, call centre, credit management, trading and IT costs, as well as corporate overheads.*

Their **estimates of these costs** is the same for gas as for electricity, and based on an assessment of recent regulatory decisions and other information in the public domain.

Much emphasis is placed on **comparisons between electricity margins for standing offers and market offers, and the market as a whole, under varying wholesale energy cost conditions.**

It is not clear on cursory glance at the first few pages of the report what data had been relied upon in determining **wholesale energy cost conditions**, including load growth factors; infrastructure maintenance and the like.

The margins are not discussed in detail here except to comment on how wide they are and to refer again to the quality of the data made available for best estimate calculations.

The estimates were based on 60% of customers being on market contracts and this being maintained.

As pointed out by Mr. Dufty in his submission another way of putting this is that 30% of domestic and 40% of commercial customers that took up market offers indicated that these contracts did not meet their expectation

CRA acknowledged the likelihood that actual results are more likely to be nearer to the midpoint or at the lower end of the ranges estimated as “best estimates

This presumption based on the quality of the data, and the fact that retailers that adopted a less than conservative hedging strategy than assumed in the study may have experienced high wholesale electricity purchase costs. Those presumptions were consistent with the EBITDA’s reported by Origin Energy and AGL in their annual reports of the past several years.

The broad estimates provided, given the frequently acknowledged data limitations in the CAR Report must count for reasonable grounds to take a pause and make an honest assessment of whether results such as these in the absence of accurate and reliable actual data are sufficient grounds for removing standing offers and lightening regulatory burden to the extent of possibly compromising the broader goals of competition that are not by any means restricted to monetary gains and profit margins.

The indicators relied upon that there is significant competitive activity in the retail market for electricity and gas for small-volume users in Victoria have been cited as follows:

***“The Victorian retail electricity and gas markets have experienced significant levels of new entry<sup>184</sup>”***

#### **Comment**

That is true. There has been competitive activity.

There has also been significant evidence of market failure.

Jackgreen’s Chairman John Smith has commented in this second-tier niche retailer’s Annual Report<sup>185</sup>

*“The group of second tier retailers which includes, Jackgreen, are themselves becoming targets for the larger players or business consolidation. Earlier this year Ergon Energy (Qld) paid \$105M for Powerdirect, the country’s inaugural second tier retailer.”*

*“The disconnect between the National Energy Market Management Company (NEMMCO) and the national pricing saw the wholesale energy prices in June this year reach a staggering 8 times their monthly June average and 10 times the prices paid in early months of 2007. With high concern from the market, regulators and energy user groups, no-one including our Governments were willing to act!”*

This is an important consideration when assessing how quickly new entrants and more established second-tier retailers might fare when full price deregulation becomes a reality.

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<sup>184</sup> CRA Final Report “Impact of Prices and Profit Margins on Energy Retail Competition in Victoria. Competitive Trends in Victoria 8 November 2007, p 4 “Competitive Trends in Victoria.”

<sup>185</sup> Jackgreen, a greenenergy specialist retailer currently selling electricity only though with licences in NSW and South Australia to sell gas,

And further from the same annual report 2007:

*“The ACCC, the master of the new National Regulator, confirmed that they would review the performance of individual companies in the market with a view to determine if any “gaming” of wholesale prices had occurred. It’s clear to Blind Freddy that it had occurred; the question was who caused it and who benefited from it? Again the market activity is fairly transparent and somewhere north of the Murray and south of the Brisbane River will find those most active.*

*The fallout was immediate, NSW based independent Retailer Energy One handed back all its customers, took a big \$ hit and their share price dropped by 400% the same week*

*Momentum Energy sold off 15,000 unhedged residential customers to get out of that market. In one fell swoop the contestable market lauded by successive Governments had come back to bite them.”*

John Smith Chairman of Jackgreen, has made an honest assessment and appears to be only too well aware of the pitfalls of the decisions being made and premature decisions about market trends.

The recent is evidence also of market failure RoLR event where 11,000+ customers were transferred under those provisions; and again when another 15,000 unhedged residential customers were found to be unprofitable and sold off (see Jackgreen’s comment’s above

As observed by Gavin Dufty in his November 2007 Submission to the current Review, the AEMC Report appears to ail to discuss and analyze the multifaceted nature of the standing offer (such as RoLR provisions).

The estimates were based on 60% of customers being on market contracts and this being maintained.

CRA figures and AEMC’s findings (as commented on by Gavin Dufty) emphasize that

*“...of the 60% have taken market offers, 70% of domestic and 60% of commercial customers said contracts had met expectation.*

As pointed out by Mr. Dufty another way of putting this is that **30% of domestic and 40% of commercial customers that took up market offers indicated that these contracts did not meet their expectation**

On p 2 the November 2007 Submission to the AEMC Review on behalf of St Vincent de Paul Society, Mr. Dufty has pointed out that

*“When this expectation failure rate (between 18% - 24% of the total market) is considered in conjunction with those that have not actively participated in the market (40%), an overall market performance measure can be ascertained. Such a market performance measure indicates that over 50% (58-64%) of customers in the Victorian energy market believe is has either failed their expectations of there are not actively participating.”*

Further Mr. Dufty comments

*The AEMC draft review also failed to ascertain the nature of the issues that may be affecting this group. Such an analysis could reveal where potential or actual market failure exists. A key issue in ensuring all households regardless of income or location have access to affordable and appropriate energy contracts.*

*Mr. Dufty has specifically asked what evaluation was undertaken that customers were actually getting what they believed they were offered.*

Other reservations expressed by Mr. Dufty for St Vincent de Paul include failure to

*“measure the level of sophistication of customer behaviour for example the quality of decision making, an indicator of market maturity.*

He points out that

*“when such an analysis was undertaken in the UK it was found that 20% of those who switched with the specific goal of seeking a lower price, in fact, had switched to a contract that resulted in high prices. A similar analysis should be undertaken here.*

The snapshot approach has also been targeted by Mr. Dufty as a flaw in evaluative design as a “point in time” approach to evaluate what is both a very dynamic energy market and the broader changes in the community such as ageing of the population.

Mr. Dufty specifically mentions the data gathering stage as:

*“a snapshot of the market during this specific period in time (mid-2007) – a time where the full impact of volatility in the wholesale energy market was yet to be experienced, a period of time that has yet to see the impact of carbon trading regime, and a period of time prior to the introduction of smart meters.”*

He predicts that all these factors

*“will significantly change the nature of the Victorian energy market and hence the nature of competition.”*

One might ask what plans there are for proper longitudinal evaluation of post-decision dissonance by customers who made switching choices, based perhaps on incomplete understanding of the choices being made

The CRA report further observes in a brief analysis of Competitive Trends in Victoria on page 4 of their report:

*“There is virtually universal access to market offers that provide discounts to the standing offers across all the electricity networks and the major gas networks”*

## **Load Growth and Management**

There appears to be a need for taking a more robust view of the factors impacting on competition, even under the apparently narrow definition of that term embraced by the AEMC in this Retail Competition Review

As far back as June 2002, The Energy Action Group cautioned the ACCC on matters that would have significant impact on energy reform over the next few years.<sup>186</sup>

Whilst it is clear the current review aims to examine the success or otherwise of retail competition in Victoria since FRC was introduced, without examining the range of factors impacting on cost control by retailers and consumers, and considering in detail the entire marketing distribution chain, a slanted and narrow view of competition factors will be gained.

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<sup>186</sup> Energy Action Group Submission to the ACCC SP/PowerNet Revenue Cap Association

The major concerns expressed in that report were about

*“load grown as a major driver of network investment”*

*“The SPI PowerNet Revenue Cap Application shows that load growth adds \$145m of the total projected capital expenditure of \$387m”*

Below is a quote directly from that submission

*The questions that the Commission needs to resolve are how much and what control will consumers and retailers have over their costs, particularly if the NEM Rules and Codes and the Network Control Ancillary Service Payment market are complex and non transparent. Accepting the current arrangement between SPI PowerNet and VENCORP and the NECA Hybrid interconnector Code Change proposals add to market complexity and increases consumer and retailer risk.*

*This Determination needs to simplify the institutional arrangement between VENCORP and SPI PowerNet. One consideration should be the amalgamation of the two organisations and rejecting the Hybrid Interconnector Code Change proposals before the Commission.*

*One of ACCC objectives should be to decrease market complexities so as many market participants and consumers can continue to benefit from the reform process.*

*The current trend to add complexity to the NEM greatly increases arbitrage and gaming opportunities for participants.*

*At the end of the day, consumers need to continue to support the reform program.*

*Increasing the complexity of the NEM ensures that the underwriters (consumers) only get suspicious when then they see more arbitrage opportunities being added with each new ACCC Code Change and Revenue Cap determination.*

***Complex far reaching interrelated decisions.***<sup>187</sup>

*The ACCC Electricity Group is currently faced with a complex number of interrelated decisions around the future structure of the National transmission system. The failure to consider each decision in relation to the others will cause problems well into the future for the transmission asset owners and the market.*

*This Determination, coupled with the ElectraNet Determination and the NECA Hybrid Interconnector Determination, provides the opportunity to ACCC to reduce market complexity. There is a common myth held by economists that all functions of the NEM need to be subjected to competitive pressures. The SPI PowerNet application shows that there are a number of projects, particularly the introduction of several independently owned and dispatched hybrid interconnectors and dynamic capacitor banks that are argued (wrongly in our view) to enhance the NEM transmission system.*

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<sup>187</sup> Ibid EAG ref 23



## **Conclusion**

*The challenge facing the ACCC is to make the right decision. This decision has to ensure that SPI PowerNet can make a sufficient return on investment and at the same time ensure that there is capital investment to the forecast load growth over the regulatory period as well as ensuring the refurbishment of an aging asset base.”*

*SPI PowerNet owns but does not control the asset base.*

*The SPI PowerNet Determinations need to make a strategic set of decisions*

*□ ensure that minimum changes occur to the WACC equation and the methodology for determining WACC is consistent across the Commonwealth*

*□ ensure that newly discovered assets are not rolled into the asset base and that easements are excluded from the asset base.*

*□ reject any attempt by the proponent to adjust the initial RAB*

*□ minimise market complexity and possible gaming opportunities that will be created by the move to introduce hybrid interconnectors and other exotic transmission arrangements into the NEM. A single asset owner in each region simplifies the management of transmission assets.*

*□ assess the costs and benefits of integration the system planning function back into the transmission businesses.*

*□ address the problems evident in both Victoria and South Australia jurisdictions where the only viable solutions to transmission augmentation Load Management, Demand Management and embedded generation are discounted as the market based solution. Currently in both Victoria and South Australia there are minimal mechanisms that can facilitate either Demand Management or ensure that embedded generation can compete with transmission augmentation as an option for system development Load Management<sup>4</sup>, Demand Management and embedded generation need to be treated in an equal manner to transmission augmentation in meeting load growth requirements. A mechanism needs to be developed to ensure that all 4 options can compete equally. Currently the only viable option is transmission augmentation.*

*□ make provision for SPI PowerNet to develop and sustain an employee and industry skills base.*

*The Energy Action Group, as a membership based, not-for-profit incorporated association representing the interest of less than 160MWh consumers across the National Electricity Market, in its Submission on the AEMC Scoping Paper on Transmission and Pricing Rules Initial Consultation Scoping Paper (funded by an NEM Advocacy Panel Emergency Grant).*

*“The national electricity market objective is to promote efficient investment in, and efficient use of, electricity services for the long term interests of consumers of electricity with respect to price, quality, reliability and security of supply of electricity and the reliability, safety and security of the national electricity system.”*

*It is important for the AEMC to recognize that the overwhelming majority of transmission revenue comes from electricity consumers.*

*EAG has significant concerns that the AEMC, the MCE and the Reliability Panel are in the process of running a number of reviews concurrently. Further, that a number of these reviews interact with each other and that this convoluted process may lead to very poor policy and rule making.*

*It is EAG's contention that the AEMC has an extremely busy work plan: that the time frame provided for in Diagram 12 and the AEMC web site is far too ambitious to carry out this joint review. We have made a series of comments in the second part of the submission to illustrate this point.*

*There have been a number of attempts to address transmission pricing issues by both the NECA and the ACCC. To date, all the work by these bodies appears to have failed to deliver the desired outcome. It is likely that this review process will do the same if the time frame continues to be unduly compressed. The process runs the risk of following the badly flawed ACCC Regulatory Test consultation process.*

*One of the implicit objectives of this revenue/pricing review and possible Rule reset should be the minimization of regulatory uncertainty for the transmission businesses so that they can continue investing in new and replacement infrastructure with minimal dislocation to their work programs."*

Each time that I try to get into the present and look at the current agendas for reform and approaches being adopted, I slide back into a de ja vu mode looking backwards and finding how little things have changed; how valid earlier predictions were; and how much balance appears to be missing from the optimistic forecast of competition impacts and future successes.

Again, as observed by the EAG in the same paper<sup>188</sup>

*"EAG has significant concerns that the AEMC, the MCE and the Reliability Panel are in the process of running a number of reviews concurrently. Further, that a number of these reviews interact with each other and that this convoluted process may lead to very poor policy and rule making.*

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<sup>188</sup> Energy Action Group Submission to the ACCC SP/PowerNet Revenue Cap Association

## **Metering issues**

Cited below is an extract from presentation in October 2006 to the Metering International Conference in October 2006 by John Dick as President of the Energy Action Group

### ***Philosophical Overview***

*We will not get all the decisions right in the move to Advanced Metering Infrastructure (AIMRO) and we are at the start of the learning curve as to what does and doesn't work.*

*It is clear and transparent to most that the Australian regulatory environment has not delivered an avalanche of innovative ideas to date, in fact the regulators and the industry appears to be almost completely risk adverse to innovation and has to be dragged shouting and screaming to implement even small changes.*

*The current industry arrangements makes it impossible for the industry participants to capture the full \$ from value chain, but AIMRO can still easily meet the single market objective in the long term interests of consumers!*

*We appearing to be grasping at a number of straws based on estimated values in the analysis of Advanced Meter Roll Out without adequately thinking through the issues.*

*It is a risky strategy to compare the NEM with other countries given the disparate Australian climatic conditions, opportunistic generator bidding behavior, the various idiosyncrasies and massive asymmetric risks of our unique merit order dispatch gross pool energy market and Ancillary Service Payment markets, along with the very weakly interconnected transmission system and radially based distribution systems.*

### ***Risk in the NEM:***

*Most people understand that the NEM is a gross pool merit order dispatch market. The market allocated risk and cost to various parties and counter parties. One of the major objectives of a retailer is to manage the various market risks!*

*The current round of AIMRO consultation has failed to address "market risk" and the costs of risks as a significant issue.*

*"Standing offer" for less than 100 MWh residential consumers include the smeared costs of "risk as a premium" plus some head room to encourage retail competition.*

### ***User/Causer Pay an Underlying principle of the NEM***

*The under pinning of the NE Market arrangements is the user/causer pay principle! The participant who causes a problem compensated the rest of the market to ensure that the market comes back to an equilibrium. The energy only market floor is - \$ 1000 and the cap is + \$ 10,000. The average spot pool price is under \$ 60/MWh.*

*The NEM places significant asymmetric risk on consumers. Consumers underwrite a high proportion of the risk without an understanding or an ability to act to minimize that risk.*

### ***Three examples of "Risk"***

*In the first month of the Ancillary Service Payment Market (ASPM), TransGrid pulled several northern NSW inter-connectors out of service to install a communications system. The overall costs of this action under causer/user pay principle was generators \$ 80 m. consumers \$ 80 m.*

*On the 16th January 2007, the ASPM cost \$ 20 m for the day. The 6 sec raise ASP in South Australia reached prices of \$ 35,000/ MWh for a short period of time.*

*We are currently seeing the fallout of the costs to retailers in NSW, who had pool exposure in June 2007, when the market almost breached the Cumulative Price Threshold of \$ 150,000/MW/ week for the first time.*

### ***NEM Overview***

*Australia network businesses are in the process of moving to or have already moved to summer peaking systems. There is continuing deterioration of the Annual Load Duration Curves, (with the exception of Tasmania) across the market.*

*The industry structure and arrangements reward load growth and under user/causer pay principles, consumers pay significant risk premiums to cover rare events.*

*Energy costs (including the retail capped /standing offer prices) along with network prices are trending up quite rapidly across the NEM, in response to associated peak load growth and the asymmetric risk of the market!*

*Current government energy efficiency and greenhouse abatement issues along with the AEMC, AER and MCE processes will have minimal impact on current consumption patterns in part due to lead times to change those consumption patterns. The movement of the old energy inefficient household fridge to the shed beer fridge is an example of behavior that sustains high consumption levels.*

*The current drought has highlighted that generation capacity constraints in the NEM is water as well as gas. Spot gas prices reached over \$ 300/ GJ in Victoria this winter, the contract price is \$ 3.40/GJ.*

*Both transmission and distribution networks are aging as energy consumption and particularly peak load growth continues to increase*

*The NEMMCo SOO 2006 indicated that peak load (MW) is growing at 3.2% a doubling of peak consumption in 21 years.*

*NEM annual energy consumption GWh is growing at 1.7% or doubling every 41 years. However large energy intensive projects have the potential to change the energy growth projection quite rapidly, Desalination is a good example.*

*The 2004 to 2007 transmission regulatory determinations and ElectraNet revenue applications have allocated around \$ 1878 m for asset replacement and \$ 3694 m for load growth.*

*The 2004 to 2007 jurisdictional distribution determinations allocated \$ 13 b and the next regulatory round starting in NSW. The NSW businesses will be applying to the AER for something like \$ 12 b, up from the \$ 5 B awarded in the last IPART regulatory determination. Qld and South Australia seem to be following a similar pattern to NSW.*

*It appear that the NEM network capex “ask” is increasing by around 100% or 200% every 5 year round of regulatory determinations, depending on how you do the numbers, NSW and Qld are good examples.*

### ***One important side effect of “light handed regulation” is poor information***

*How can you model AIMRO without the appropriate data, analysis and information! There are a number of important deficiencies in the current MCE papers out for consultation as a result.*

*What reliable data is available on heating and cooling one of the largest component of small business and residential consumption patterns!*

*How many a/c’s and what size and star rating?*

*EAG aware of a/c units of sizes up to 50 KW are being installed in Qld., while 30 KW units are becoming common in NSW.*

### **Load and Consumption Data**

*Billions of \$ have been awarded by the regulators on inadequate load forecasts produced by the network businesses and in turn added to the Regulated Asset Base RAB.*

*Almost all of the consumption data used by the AGO, ESAA, ABS, ABARE etc and the various consultants in the energy efficiency and demand management debates for less than 100 MWh consumers across the NEM are estimates. How can you track behavioral changes and make decisions based on 1 or 3 month metering settlement data of the most volatile load!*

*What is the energy efficiency standards of new air conditioning being installed?*

*What sizes are the units being installed and what units are they replacing or are they new installations?*

*What happens to old energy inefficient units being replaced or is another unit being installed as well?*

*Enough Australians have a level of disposable income to rapidly change energy consumption patterns in very short period of time.*

*Appliance purchase information is not being effectively tracked. All Australian Governments seem to be doing is legislating without understanding what's actually happening in the market place!*

*The Incandescent light /Compact Fluorescent Light bulbs energy efficiency regulation provides a useful example, given that there are better technologies available like Light Emitting Diodes (and LED have no mercury content). Fixing the power factor problem associated with CFL's is a further issue to be resolved!*

*AIMRO data will allow retailers to more effectively manage temperature sensitive load! Currently a retailer doesn't usually know about a residential customers change in behavior until up to at least 12 weeks after an event. (one, three month settlement period on a meter reading) or a one month billed customer up to four weeks after the change.*

### **Reliability "Ancillary Services"**

*On top of the energy only market there are 8 different Ancillary Service Payment arrangements designed to ensure that the system operates with the minimum of disruption. There are 6 markets for frequency control 3 raise and 3 lower. One to cover network control NCAS and another to cover restart (Black Start).*

*NEMMCo has statutory responsibility to run a reliable and secure system. NEMMCo has the power to direct a market participant to operate. The market participant is paid operations and maintenance costs for the direction. The record to date for a direction is \$ 20 m for the day.*

*The annual Inter-regional price differentials are running at \$ 1.6 to 1.7 b\*. This figure has a relationship to generator market power and can be dependant / or is independent of peak load consumption. The flawed AER Regulatory Test has impeded the development of more robust state based transmission system along with inter-connectors. This adds to retailer risk and is paid for by consumers!*

*(Type 5 ) Interval Metering assist in the allocation of risk and costs under the user/causer pay principle. (Type 4) AIMRO has the potential to significantly reduce asymmetric risk*

### **Price Caps /X Subsidies for less than 160 MWh Consumers**

*Price caps: work when the cap is higher than the retailer energy purchase price, however it is a recipe for disaster if the caps are lower than the energy purchase price.*

*X subsidies: flat load consumers subsidize volatile load customers. A flat load average on-peak consumer in Victoria with a bill slightly over \$ 850/a is subsidizing a summer air conditioned consumer to the tune of \$ 200/a in energy terms The impacts on distribution and transmission costs DUoS and TUoS are extra! While massive intra tariff cross subsidies continue to exist, there is a strong diminution of price signals and the continuation of inequitable outcomes*

### **Further issues with the current Settlement/Billing arrangements**

*The current settlements arrangements based on type 5 meters use Net System Load Profiling (one hat fits all in a region) as the basis for settlements. It takes up to 2 meter reads to settle the market. With 3 monthly meter reads the settlement arrangements take up to 30 weeks to complete.*

*(Algorithms are uses to simplify the settlement processes and reduce financial exposure.)*

*However reconciliation between the settlements data and the distribution and retailer billing systems is an issue for some large retailers with multiple billing systems. Along with the fact that consumers are not impressed with billing errors! Utility industry ombudsman complaints are at record levels and in a number of jurisdictions the number of complaints is still rising!*

### **Retailer “Risk”**

*The use of NSLP as a basis settlements increases trading risks and un-hedged exposure to the energy market. Over contracting costs the retailer revenue.*

*Needs to know their dynamic trading position/exposure in relation to both their customers’ load and customer churn. Know their energy contract position in relation to their customers energy consumption.*

*Understand their exposure and make provision for their exposure to the Ancillary Service Payment Market.*

***There appear to be significant unstated cash flow benefits to retailers to move to AMI, these include:***

*Faster and more accurate settlements.*

*Accurate information to manage the retail hedge book. Rapid assessment of pool exposure or surplus energy/hedge contract that can be sold.*

*There are ongoing disputes between retailers about the transfer process and between the retailer and the distributor as to the amount relating to DUoS and other network charges.*

*The recent Retailer of Last Resort event raised questions as to what evidence was going to be used to accepted responsibility by the various parties involved in the resolution for the various financial obligations associated with this arrangement. The use of NSLP as a basis of allocating costs is not particularly helpful in allocating costs and obligations!*

## ***Distribution Business Behavior***

*Many distribution networks do not enforce their connection agreements so reactive power, power quality and network outage management are issues that are not well addressed across the NEM. The use by regulators of Guaranteed Service Levels doesn't inspire consumer confidence.*

*Under the Building Block Approach to Incentive Regulation a DB's can be rewarded with \$ to pay consumers for complaints, so there's little incentive for a DB to fix problems!*

*There are potential savings in using AMI data to the minimize Distribution Loss Factors.*

### ***AMI offers a path to the "Smart Grid"***

*Replacing Type 5 and 6 Meters with Type 4 Meters offers a long term vision (more than 10 years) to transform the 1930's technology of a number of the distribution networks into the smart grid of the 21st Century.*

*There are clear customer benefits from better managing uncontrolled distribution outages. In a number of regulatory determination DB's are given revenue to pay for their failure to control customer outages!*

*Sceptics believe that we are adding "cruise control" to a T Model Ford!*

### ***Some brief comments on NERA/CRAI MCE Modeling***

*Modeling is extremely difficult when you don't have reliable consumption data at the small consumer level along with behavioral data.*

*There is little market based evidence that the CRAI modeling results will reduce the Critical Peaks and increase energy consumption. Some recent research presented to the conference by Sarea Coates raises some questions about the NERA led, CRAI modeling results where the increased energy consumption after the peak load interruption fails to occur.*

### ***"Trivia"***

*I understand that the practice of swapping used meters between various parties still occurs after a new meter is installed. Hopefully in most cases the amount of energy consumed by the customer is being recorded for settlements purposes.*

*It is fortunate that the current MCE work on AIMRO is not ,unlike the Victorian Studies ignoring the provision of metering by independent third-party metering providers. Who have the potential to offer a range of competitive metering services.*

*The magnitude of the hurdles for DM, EE and renewable energy is so large that combined they will not make a significant contribution to changing load or consumption patterns in the next 5 years and it is unlikely that this position will change in the next 10 years. The 1 in 10 year temperature sensitive load compared to the 9 in 10 year load forecast varies by 1000 MW in both Victoria and NSW.*

*Changing the NEM Rules will not facilitate significant increases in DM, EE or renewable energy. A Photo Voltaic array has around a 15% Available Capacity Factor. The best Wind Farm has 42%. Fossil fuel power stations have ACF over 90%. The investment in renewable energy has to be significantly larger than the investment in fossil fuel plant. To get the same bang for the buck!*

### ***Some Conclusions***

*It is disappointing to see the lack of concrete information on the table for consultation given the resources put in to the AIMRO exercise to date.*

*The lack of long term “real time” customer load and behavioural data makes modelling difficult.*

*Cost smearing does absolutely nothing for the user/causer pay principle under pinning the market.”*

In its **6 November 2007** submission to the AEMC Rule change proposal – demand management and transmission networks made the following observations<sup>189</sup>:

*“The focus of the proposals is on correcting the major bias against demand management<sup>190</sup> (DM) in the National Electricity Market (NEM). Over many years, the Council of Australian Governments (COAG) and the Ministerial Council on Energy (MCE) have repeatedly expressed their support for DM but little has been done to address the very large incentives for inefficient investment and inefficient consumption of electricity.*

*The failure to harness an adequate level of DM is such a fundamental flaw of the NEM that broad-scale changes to the Rules are urgently required. Unnecessary pressures to build expensive new infrastructure inflate costs - decrease the efficiency and reliability of networks, destroy options for cost-effective DM and unnecessarily raise prices for consumers. These outcomes are in conflict with the long-term interests of consumers.*

*Through various forums, the Total Environment Centre (TEC) has been advocating for DM to become a primary focus for decision making about the National Electricity Market, in particular for incorporation of DM principles within the National Electricity Rules (the Rules). To counter the strong bias of networks towards inefficient augmentation, it is essential that cost-effective DM is the priority consideration for meeting energy demands before other options are considered. In this way, the market can truly serve the long-term interests of consumers through harnessing maximum efficiency.”*

As Executive Director of TEC, Jeff Angel recognizes that

*“several parallel processes are currently occurring which are relevant to these proposals.”*

Those proposals are outlined the body of the 48-page submission document where it is explained *“why the proposed changes still require urgent attention.”*

Though the proposals

*“directly address arrangements for transmission networks, the intention is that the same principles should also filter down to the Rules and future determinations for distribution networks.”*

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<sup>189</sup> Submission to AEMC Rule change proposal – demand management and transmission networks. Total Environment Centre

<sup>190</sup> TEC defines demand management (DM) as follows: *“Demand management in this proposal can be read to include ‘demand response’, ‘demand side management’, ‘demand side response’, ‘energy efficiency’ and ‘non-network solutions’. In general, DM can include both the management of peak loads and energy efficiency as a way of meeting capacity requirements with the greatest cost-efficiency. It includes a diverse array of activities that meet energy needs, including cogeneration, standby generation, fuel switching, interruptible customer contracts, and other load-shifting mechanisms.”*



At the very least, TEC believes that

*“the preferential optimization of DM should be the priority for matters to be addressed in any review of the Rules by the AEMC.”*

The introduction to this substantial submission refers to:

1. Neglect of demand management (DM) as a pervasive problem throughout the NEM, despite professed intentions that demand side options should be given ‘due and reasonable consideration.
2. Perceived lip service to DM when compared to the massive incentives for inefficient supply side approaches, with resultant “inefficient, peak-driven transmission infrastructure investments at the expense of the long-term interests of consumers.
3. An approach that is seen as resulting in “inefficient, peak-driven transmission infrastructure investments at the expense of the long-term interests of consumers, with little change since the Parer Report<sup>191</sup> which noted:

*“A key feature of competitive markets is the active participation of both the supply and demand sides. Without this, competition is blunted and the potential for the exercise of market power is enhanced. ... Many submissions to the Review contended that demand side involvement in the NEM is under-developed.”*

The TEC states that along with a range of community groups and the Clean Energy Council they will continue to advocate for the inclusion of demand management objectives in the National Electricity Law.

There are those who have believe that there is little evidence to support the assertion that

*“there is little evidence to support such an assertion”.*

Nevertheless I have included some of the TEC proposals.

I am not qualified to comment on that criticism, but do feel very concerned about the way things are going and the extent the needs of consumers are being eroded in this climate of reform especially within the energy area.

A major concern expressed in the TEC Demand-Side Proposal is included under 2 “Other NEM processes to address DM.”

## ***“2 Other NEM processes to address DM***

### ***2.1 DM as a Jurisdictional Direction***

*Once regulation of distribution becomes national, it has been proposed that “environmental issues” and consideration of demand side options be regulated according to jurisdictional requirements. Mechanisms have been proposed for dealing with these issues, the primary one being a so-called “Jurisdictional Direction”. Gilbert+Tobin and NERA Economic Consulting created the term<sup>6</sup>, and Clayton Utz is currently investigating a similar approach for the MCE’s Retail Policy Working Group<sup>7</sup>.*

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<sup>191</sup> Parer Report Commonwealth of Australia, *Towards a Truly National and Efficient Energy Market*, 2002, p 173

*“Leaving incentives for DM to the discretion of the jurisdictions is a poor substitute for responsible and truly national regulation for the efficient use of electricity. This approach continues the tradition of sidelining DM and grouping it with “environmental matters”, with the implication and practical effect that it is not something to be actively pursued within the NEM.*

*This is short-sighted at best, since DM can, and should be required, to be an integral component of an efficient and reliable electricity system, leading to reduced costs and reduced prices for electricity consumers.*

*The jurisdictional direction proposal is inadequate to meet the needs of the full and proper utilization of DM in the NEM.”*

Concerning efficiency goals, the TEC

*“Efficiency*

*Economic efficiency is central to the NEM and to achieve this there must be a renewed emphasis on DM. Transmission and distribution networks, in practice, are natural monopolies and therefore lack natural incentives to carry out their operations in the most efficient manner, since there is a lack of competition to force efficiency. This places the responsibility for efficiency on the NEM Rules and on regulators. Under the current Rules, however, it is in the interests of network businesses to increase their revenue through the expansion of their asset bases, driven by inefficient consumption of electricity.*

*The NEM is focused on the inefficient expansion, rather than the avoidance of new infrastructure. At the very least, the issue of balance results from the fact that in the vast majority of cases, the process of evaluating alternatives is only raised once infrastructure proposals are under way, and are usually in an advanced stage of development. It is only then, if at all, that more cost-effective DM solutions are contemplated. The time allowed for adequate investigation of alternatives is then limited by the networks’ pre-determined timeframe, which may not be sufficient to allow for the planning and advancement of beneficial non-network solutions.*

*Despite the huge efficiency potential offered by DM, efficiency gains within the DM provider market itself are also hampered by artificially low requests for DM services. This reduces competition within that market and its ability to compete with supply side alternatives, resulting in reduced overall efficiency.*

*The AEMC has previously acknowledged<sup>8</sup> potential benefits arising from the development of demand management and other energy sources, that is, that by utilizing these sources:”*

<sup>8</sup> Australian Energy Market Commission, Review of the Electricity Transmission Revenue and Pricing Rules – Transmission Pricing: Issues Paper, November 2005, p 32.

*“... transmission can avoid the need for, or can itself be avoided by, the development of local generation, DSM and non-electricity options. Therefore, transmission regulation and pricing should ensure transmission does not “crowd out” alternatives. The Commission considers it important for transmission regulatory arrangements to be structured in a way that ensures that there is an appropriate opportunity for alternatives.*

<sup>192</sup> ***“Long-term interest of consumers***

*The long-term interest of consumers would be served by greater efficiency, which would result in lower costs and prices, and increased reliability, leading to improved supply and fewer system failures.*

*Although the AEMC currently considers the reduction of greenhouse emissions immaterial to the long-term interests of consumers as defined by a narrow economic interpretation of the NEM Objective, and therefore outside its regulatory scope, TEC regards this position as untenable and subject to re-evaluation. Despite the current regulatory disconnect between the long-term interests of consumers as seen in a narrow economic sense and the broader long-term interests of consumers, DM contributes to the long-term interests of consumers in the context of climate change by:*

- reducing future carbon costs;*
- avoiding wide-scale economic devastation, and;*
- facilitating protection of the environment.*

*These are integral to meeting community needs. TEC is pursuing the issue, however, in other arenas and this proposal does not hinge on this argument.”*

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<sup>192</sup> Total Environment Centre’s submission to AEMC Rule Change Proposal Demand Management and Transmission networks 6 November 2007

## THE INTERNAL ENERGY MARKET – some theory models

### IMPLEMENTATION AND REVIEW

The Ministerial Council on Energy (MCE) will be amending the NEL towards the end of 2007 to implement commitments in the Australian Energy Market Agreement (AEMA) relating to the completion of the transfer of economic distribution functions to the national framework.<sup>193</sup>

The separation of generation/transmission provisions will not be implemented as part of the economic package. The NEL provisions could be inserted as part of the non-economic distribution and retail package or as a separate NEL amendment bill.

The MCE has policy oversight for the electricity review schemes and will consider whether the amendment to the NEL adequately reflects the in principle COAG decision.

I have noted comments such as those of Adjunct Professor Alan Pears<sup>194</sup> in his submission: National Frameworks for Distribution Networks Network Planning and Connection Arrangements.

Though these comments were addressed in another context the insights are relevant to all consultative processes:

*“Given the urgency, driven by climate change policy and the need to aggressively respond to growing peak electricity demand, it is critical that this process delivers real outcomes quickly. Good intentions are no longer sufficient. Fines and incentives should be applied to ensure action.*

*The outcomes of this process are critical to overcoming the barriers to demand-side action and distributed generation that have marred the energy market since its inception. Indeed, the fact that it has taken this long to address these issues indicates a serious failure of public policy process.”*

I quote directly from EAG’s 2005 Submission to the AEMC Scoping Paper and Pricing Rules Initial Consultation Scoping Paper, as below:

*“This submission makes some broad policy recommendations, then reviews the recommendations of the ACG/NERA report of August 2007. “*

*“EAG has further concerns relating to the emphasis of the process on strictly economic outcomes. Electricity is pivotal to the workings of our society with the power industry relying on a highly trained technical skills base to develop the system to its current level of complexity. Prior to market start, the interconnected transmission system was designed for reinforcement i.e. supplementation of energy supply between jurisdictions in times of shortage.*

*The move to the NEM has converted the purpose of the transmission system to carrying energy flows for market trading and in a manner not originally intended. That is not to say that inter-regional energy flows shouldn’t occur. However, in this review process the AEMC must accept the needs for a vision for NEM transmission. Further, this vision should incorporate a long term view of market development. In theory, the vision is currently provided by the Annual National Transmission Statement (ANTS).”*

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<sup>193</sup> Release of a Regulatory Impact Statement on the Separation of Generation and Transmission found at [http://www.mce.gov.au/assets/documents/mceinternet/Regulatory\\_Impact\\_Statement20071015121839.pdf](http://www.mce.gov.au/assets/documents/mceinternet/Regulatory_Impact_Statement20071015121839.pdf)

<sup>194</sup> Submission National Frameworks for Distribution Networks Network Planning and Connection Arrangements. Alan Pears is an engineer and educator who has worked in the energy efficiency field for twenty years. He is Senior Lecturer in Environment and Planning School / Work Unit, Global Studies, Social Science and Planning

Many pertinent reports are not included or cross-referenced at all in the material shown on the AEMC's Retail Competition Review website. Yet they need to be taken into account, even if not commissioned for the Retail Competition Review.

A thorough scoping exercise should involve looking backwards over at least the last five years to pre-full retail competition days. Collecting robust comparative data is a first essential step and being prepared to undertake a professional analysis based on best practice evaluative process.

It is surprising that the starting point for assessing energy market competition impacts over the last three years has focused on the mid-point of the market distribution chain.

In 2003, in discussing infrastructure projects, emerging economies and Government renegeing, author Ravi Ramamurti, of the Department of Business Administration, Northeastern University, Boston, USA summarizes his paper as follows<sup>195</sup>:

*“Despite deregulation and privatization, governments in emerging economies continue to play important roles in private infrastructure projects, thereby exposing private investors to the risk of government renegeing. The government's role as deal maker—and deal breaker—in infrastructure investments stems from its role as financier, customer, supplier, competitor, and/or regulator. (The only role governments have shed as a result of recent economic reforms is that of producer.)*

*Based on the literature, I propose three explanations for government renegeing: (1) economic uncertainty, which necessitates contract renegotiation; (2) the logic of the “obsolescing bargain,” which makes deals less attractive to governments ex post than they were ex ante; and (3) political change, which puts new leaders in charge with incentives to renege on old promises.*

*I assert that these risks can be contained, respectively, through contract design, investment strategy, and institutional design. Using this framework, I conclude that Enron's strategy in the controversial Dabhol project in India was sensitive to first of the three factors and relatively less mindful of the other two.*

*The policy implication for MNCs is that they should be attentive to all three factors that cause government renegeing rather than just one or two.*

**Jamison (2005)** summarized the Internal Energy Market as follows:

*“The Internal Energy Market provides new opportunities to energy consumers and to energy undertakings. It has the potential to increase economic and technical efficiency, as well as security of supply, thus improving European welfare and the competitiveness of European industry. It can also be an important tool to reinforce political and economic links with Eastern European and South Mediterranean countries, thus contributing for stability and development in these areas.*

*“If the Internal Energy Market is not properly organized, and if the increasing interaction between national political, economic and institutional decisions is not duly taken into account, it may engender inefficiencies, leading to high energy prices and poor quality of service and even endangering security of supply.*

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<sup>195</sup> Ramamurti, R “Can governments make credible promises?” Journal of International Management 9(3) 2003, pp253-269 Insights from infrastructure projects in emerging economies Institutions and International Business. Journal of International Management 9(3) 2003 pp 253-269 ages 253-269 Institutions and International Business

*“Completion of the Internal Energy Market is a complex and relatively slow process. It is strongly influenced by the different speeds of national legal, institutional and industry developments. The present stage of the Internal Energy Market is a critical one.*

*It is the duty of energy regulators to point out the present difficulties and to suggest appropriate solutions leading to fair, efficient, secure and integrated energy markets in the European Union.”*

*“Should consumer policy be administered separately from competition policy or should institutional arrangements reflect the synergies between the two?”*

**The Internal Market in Electricity Directive** is the Directive 2003/54/EC of the European Parliament and the Council of 2003-06-26 concerning common rules for the internal market in electricity. This Directive repeats the earlier Directive 96/92/EC. The new directive is based in the Treaty establishing the European Community, and in particular Article 47(2), Article 55, and Article 95 thereof.

A recent brief analysis of the **internal energy market’s missing steps** undertaken by the Council of European Energy Regulators included the following observations under points quoted verbatim<sup>196</sup> I hope the CEER will forgive me quoting so extensively, with the pure goal of sharing valuable data in this submission.

## **COMPLETING THE INTERNAL ENERGY MARKET: THE MISSING STEPS**

*In the old days of national monopolies, energy utilities were under Government’s “command and control”. The benefits and costs of this approach were supported by consumers and utilities according to national criteria. Cross-border energy trade was limited to wholesale transactions among incumbent utilities, cross-subsidies between different groups of national consumers were tolerated, some utilities were subsidised while others were not sufficiently remunerated. Since there was no competition among utilities and no choice for consumers, national decisions had no direct impact upon utilities or consumers in other countries.*

*Directives 96/92/EC (electricity) and 98/30/EC (natural gas) established the legal basis for the Internal Energy Market. Millions of eligible consumers are already free to choose their electricity or natural gas supplier in any Member State of the European Union. Energy undertakings are free to trade and to invest in all Member States. This means that national energy systems are now open. Political, legislative or regulatory decisions concerning energy investment and trading frameworks in one Member State have a potential impact upon all Member States. Acquisition, investment or trading decisions by one energy undertaking have a potential impact upon all EU energy markets. However, the Internal Energy Market is still far from being a reality.*

*The Internal Energy Market provides new opportunities to energy consumers and to energy undertakings. It has the potential to increase economic and technical efficiency, as well as security of supply, thus improving European welfare and the competitiveness of European industry.*

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<sup>196</sup> Council of European Energy Regulators found at [http://www.ceer.eu/portal/page/portal/CEER\\_HOME/CEER\\_PUBLICATIONS/PRESS\\_RELEASES/CEER\\_PRES\\_2003-10-06.PDF](http://www.ceer.eu/portal/page/portal/CEER_HOME/CEER_PUBLICATIONS/PRESS_RELEASES/CEER_PRES_2003-10-06.PDF)

*It can also be an important tool to reinforce political and economic links with Eastern European and South Mediterranean countries, thus contributing for stability and development in these areas.*

*If the Internal Energy Market is not properly organized, and if the increasing interaction between national political, economic and institutional decisions is not duly taken into account, it may engender inefficiencies, leading to high energy prices and poor quality of service and even endangering security of supply.*

*Completion of the Internal Energy Market is a complex and relatively slow process. It is strongly influenced by the different speeds of national legal, institutional and industry developments. The present stage of the Internal Energy Market is a critical one. It is the duty of energy regulators to point out the present difficulties and to suggest appropriate solutions leading to fair, efficient, secure and integrated energy markets in the European Union.*

- a) The five major factors hindering the fast development of a single energy market may be grouped into the following categories:*
- b) Lack of transmission capacity (in particular, cross-border interconnection capacity).*
- c) Lack of transparency in network access conditions (including network access tariffs and congestion management).*
- d) Lack of transparency in the technical operation of interconnected systems.*
- e) Lack of robust, deep and liquid organized energy markets in most geographical areas.*
- f) Lack of transparency and predictability concerning rules applied to the approval or refusal of mergers and acquisitions in the energy field.*

*Transmission capacity, in particular cross-border interconnection capacity, is essential for the development of efficient energy trade and for increasing security of supply. While a few new interconnectors are under construction and the European Council requested electricity interconnection capacity to be substantially increased by 2005 (up to, at least, 10% of the installed production capacity in each Member State), five main problems remain:*

- g) Administrative procedures are too lengthy and sometimes prone to political interference, leading to unreasonable delays and even, in some cases, to project cancellation.*
- h) The allocation of interconnection capacity to long-term contracts between utilities reduces the available commercial capacity in some areas.*
- i) Vertically integrated utilities usually have no interest in developing new interconnectors.*
- j) Special regimes applied to the construction, operation and use of merchant lines may reduce the commercial capacity available to network users in general and discourage the expansion of public networks.*
- k) Some degree of coordination among those responsible for transmission network planning and construction is necessary if “patchwork” solutions are to be avoided.*

*Recent initiatives from the European Commission related to energy infrastructure recognize some of these difficulties and will lead to suitable solutions.*

*A clear and integrated map of transmission capacities available and under construction in Europe is urgently needed, both for electricity and for natural gas.*

*Transmission networks were not developed in order to support efficient trade. Distribution networks were not developed in order to support the efficient integration of decentralized generation into the electricity system. Therefore, network planning – and not only interconnection planning – must be adapted to the new requirements, in order to ensure quality and security of supply under new market and environmental conditions.*

*Transparency in network access conditions must be improved in order to ensure fair treatment of all network users, independently of their size, nationality, contractual arrangements or ownership.*

*Trust in the independence and non-discriminatory behaviour of Transmission Systems Operators (TSOs) is strengthened by their full separation from any other interest in generation, trading or supply. Ownership unbundling, although introduced in an increasing number of Member States, is not yet fully applied.*

*This situation is particularly worrying in those countries where independent energy regulators have not yet been appointed (Germany and even more Switzerland).*

*In order to ensure non-discrimination, network access tariffs must be fully cost-reflective. Cross-subsidies between different activities (e.g. transmission and generation in vertically integrated undertakings) or between different groups of consumers (e.g. low-voltage and high-voltage) result in harmful distortions of competition.*

*The recent Regulation (EC) n 1228/2003 of the European Parliament and of the Council on conditions for access to the network for cross-border exchanges in electricity lays down basic principles with regard to tariffication and capacity allocation. Regulatory authorities and the European Commission will co-operate in order to ensure appropriate compliance with the Regulation and full transparency.*

*As a consequence, from 2004 on, access to electricity networks will be more transparent throughout Europe. A similar Regulation for natural gas is needed.*

*Transparency of network access and efficiency of network operations is better ensured when the TSO is also the owner of all relevant transmission assets.*

*Technical coordination among TSOs is essential for the proper operation of the interconnected electricity and natural gas systems. Lack of coordination has two major inconvenients- it may:*

- jeopardize reliability and security of the interconnected systems;*
- limit the commercial freedom of network users beyond strictly necessary levels.*

*The technical rules, procedures and criteria governing operation of the large interconnected EU energy systems have to be adapted and rewritten, taking into account the complexity resulting from the increasing number and diversity of commercial transactions taking place nowadays. They shall be prepared by TSOs, approved by regulators (since they may have impact upon costs and competition) after extensive consultation of all stakeholders and made public; review procedures shall be transparent and known in advance.*

*Following the CEER's request at the Electricity Regulatory Forum in February 2002, European TSO associations are working towards the definition of a comprehensive set of common security and reliability standards. Similar efforts should be developed by natural gas TSOs.*



*The step-by-step completion of the Internal Energy Market requires the increasing convergence of regional markets. However, in some regions organized energy markets still do not exist and in other regions the existing markets are not robust, deep and liquid enough. The design and implementation of efficient energy markets (electricity and gas) in Europe should be a high priority. Well functioning market must also provided appropriate risk management instruments: in a market environment, vertical integration is not necessarily the most efficient mechanism.*

*Moving from national monopolies to EU electricity and gas markets requires important adjustments to the present energy industry structure. EU energy markets cannot function properly without a reasonable number of energy undertakings selling their products and services in several Member States.*

*Restructuring of the energy industry will bring more innovation and more efficiency to energy markets. Therefore, it is important that national governments and competition authorities co-operate among themselves and with the European Commission in order to implement a coherent policy regarding the approval of merges and acquisitions, as well as the assessment of market power.*

*Energy regulators have signalled their will to co-operate towards this common goal.*

*The recent Directives 2003/54/EC (electricity) and 2003/55/EC (natural gas) provide a clear framework for completing the Internal Energy Market. The way forward was jointly defined by the European Parliament and by the Council.*

*The CEER will work with the European Commission, in close co-operation with all relevant stakeholders, in order to ensure that the Internal Energy Market, through appropriate regulation, will fulfill consumer expectations in terms of price, quality and security of supply.*

*Recent – unrelated – incidents that affected many electricity consumers in Europe may be the consequence of some factors described above which hinder the development of a single energy market. They are not a consequence of liberalisation and integration of European electricity market. These problems have been identified, as well as their respective solutions.*

*Some people believe that the Internal Energy Markets magnifies the risks and reduces opportunities. The CEER thinks the opposite is true. Therefore, we will endeavour to complete the Internal Energy Market as soon as possible, according to the mandate which was given to us by the Member States, by the European Parliament and by the Council. The CEER are working towards the completion of the Internal Energy Market to ensure that European consumers obtain the full benefits of liberalised markets as well as secure supplies of energy.*

*Rome, October 6, 2003”*

Political, legislative or regulatory decisions concerning energy investment and trading frameworks in one Member State have a potential impact upon all member states

This is a climate of compromised confidence in consumer protection. It is also a policy climate of proposed change, so it may be opportunistic to learn from the experience of or research of others by applying relevant principles in a different context.

Many weaknesses have been identified in current regulatory instruments, compliance enforcement, affiliations, efficacy of complaints schemes and compromised consumer protection. There is general consensus on these issues across the board. The suggestions may therefore be helpful despite the context in which they are made.

This paper provides a framework of some of the strategies governments can use to mitigate regulatory and political risk to private companies investing in infrastructure projects in developing countries.

One section of the paper focuses on strategies that can improve **transparency, independence, competence, and credibility of the regulator**, but other aspects of government, as they affect regulatory and political risk, are also discussed.

*Jamison et al* have drawn attention to the paper by *Kaufman et al (2004)*<sup>197</sup> examining six dimensions of government for 199 countries and territories in four time intervals between 1996 and 2002 using an unobserved components model, using 250 individual measures taken from 25 different sources, including international organizations, political and business risk-taking organizations, think tanks and nongovernmental agencies.

The governance indicators examined are:

1. voice and accountability (political process, civil liberties, and political rights)
2. political stability and absence of violence
3. government effectiveness
4. regulatory quality
5. rule of the law, and
6. control of corruption

The limitations of margins of error were acknowledged by the authors because of reliance on subjective perceptions and for certain dimensions given the context were unaccompanied by reliable objective data – those of corruption, confidence and property protection.

Despite the context, many of the issues examined may be relevant in examining current parameters *Jamison's (2004)* choice of *Kurtzman et al's 2004* paper<sup>198</sup> may be helpful were it examines five indicators:

1. corruption
2. efficacy of the legal system
3. deleterious economic policy
4. inadequate accounting and governance practices, and
5. detrimental regulatory structures

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<sup>197</sup> Kaufmann, Daniel, Aart Kraay, Massimo Mastruzzi. Revised 2004. "Governance Matters III: Governance Indicators for 1996-2002," World Bank c/f Jamison (2005)

<sup>198</sup> Kurtzman, Joel, Glenn Yago and Triphon Phumiwasana. 2004. "The Global Costs of Opacity." *MIT Sloan Management Review* 46(1): 3844. c/f Jamison (2005)

## COMMENT ON REGULATORY BURDEN ISSUES

Turning now to a more dedicated examination of infrastructure policy reform with energy at the top of the list, this limited submission refers to recent findings in the literature that may be worth considering.

The purpose of providing the detail included below is to illustrate how difficult it is to come up with a magical and swift solution to infrastructure regulatory change and benchmarking.

The community at large has expressed ongoing concerns about the speed with which proposed change is occurring.

The literature review undertaken by Jameson et al in 2005 is discussed in some detail below. Mark Jamison is Director Public Utility Research Centre, Warrington College of Business Administration University of Florida.

His research interests are focused on the nexus between business strategy and government policies, primarily for network and information industries in an international context. He is inspired by new breaking ground, conventional wisdom or points of view conflicts. His current interests include network ownership and entrepreneurship, strategic choices in network connectivity, and effects of public and private ownership, best practices in regulatory policy and leadership in public policy. Along with co-authors Lynne Holt and Sanford V Berg, he summarizes his concerns as follows”

*“There remain important gaps in our understanding of the various instruments that can be used to mitigate regulatory risk. Tradeoffs between predictability and flexibility and between independence and accountability raise issues. Arguably, there exist situations where policy flexibility is needed to lower risk or increase expected returns on investment, both of which would encourage long-term investment.”*

This literature review<sup>199</sup> discusses

*“.....well-conceived regulatory frameworks, including independent regulators, sound price-setting regimes and transparent regulatory processes that invite stakeholder participation, can improve the investment climate by increasing predictability and reducing political risk”*

These authors have taken the care to identify gaps in the literature on risk mitigation in infrastructure. Notable gaps are *“an understanding tradeoffs between instruments that have conflicting effects, the dynamic process of policy development, sustainability of infrastructure policies, leadership, and the effects of multilateral institutions. We also find a lack of synergy in some areas of research and recommend approaches for increasing awareness and collaboration.”*

### **Section V – Conclusion**

In this literature review the authors identify and summarize key elements of the literature on risk mitigation in infrastructure. We focus on two elements of this literature, namely how regulation affects investment risk and the financial instruments that investors can use for mitigating risk. They also identify gaps in the research in understanding tradeoffs. Some of the numerous papers, books, etc., that are useful background on regulation and risk but that we did not review are listed below.

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<sup>199</sup> Jamison, MA, Holt, L, Ber, SV, (2005) Mechanisms to Mitigate Regulatory Risk in Private Infrastructure Investment: A Survey of the Literature for the World Bank. The Electricity Journal Vol 18(6) July 2005 pp 36-35

With full credit to the authors for their thorough literature review and their arrangement of logical parameters through which ideal regulatory frameworks can be considered, the discussion and references below are intended to stimulate consideration of any issues that may have been missed to date in terms of determining best practice regulatory framework for the utility area in particular.

The authors include the terms energy, telecommunications, water and transport in defining infrastructure.

Whilst predominantly focused on examining new regulators in developing countries, and the complex structural, legal and financial barriers to achieving best practice outcomes the article also discusses certain “basic principles that are at play at all governmental systems, so that knowledge of those principles can be usefully applied to match any country’s institutional endowment.

The authors believe that there is independency between the effectiveness of the regulatory system and the regulatory entity with the overall manner in which policymakers can answer the following questions:

1. How does the country’s overall regulatory framework affect capital market development for infrastructure projects?
2. How robust is the relationship between that country’s framework and capital market development?
3. Are there strategies for increasing regulatory discretion in contracts commensurate with gained regulatory expertise over multiple years, and do these strategies actually work?

The literature review is neatly divided and examines controllable factors that are addressable by the regulator and the broader macro-regulatory system – meaning the institutional environment in which the regulator operates and does not directly control.

The second dimension along which the authors believe the literature can be usefully be categorized and for the purposes of our review, these categories are:

1. **Regulatory Framework** – *How the institutional design of the regulatory entity, the design of the government’s overall regulatory system (including courts, checks and balances within the government, etc.), and a country’s relationships with other countries and multilateral institutions relate to opportunism.*
2. **Corruption** – *The relationship between corruption and risk, and methods for mitigating risk resulting from corruption.*
3. **Sustainability** – *Approaches for increasing the political sustainability of policies and institutional mechanisms, including the application of pro-poor policies.*
4. **Renegotiation and Bailout** – *Approaches for dealing with unforeseen events or failures in institutional design, corruption prevention measures, or sustainability approaches that may trigger contract renegotiations or bailouts, including strategies for avoiding such situations.*
5. **Financial Instruments** – *Instruments, such as risk mitigation insurance, guarantees, and other risk reallocation products that decrease investor risk, given the set of institutional instruments.*

The authors purport that

*“Opportunism is said to occur when the government changes the rules affecting cost recovery after the utility has made irreversible investments.”*

The authors believe that corruption levels and pro-poor mechanisms are frequently considered features of the regulatory design, the literature addresses them separately.

## **Regulatory Framework**

### **1. Regulatory Entity**

*Jamison (2005)* suggests the following as crucial factors in determining appropriate regulatory frameworks that reduce political risk and improve investment climate by increasing predictability:

- Independent regulators
- Sound price-setting regimes
- *Transparent regulatory processes with meaningful stakeholder participation*

*Jamison et al* observe that regulators do not operate in a vacuum. Their effectiveness can be dramatically altered by the *“country’s governmental checks and balances (including the judicial and legal systems) for regulating the financial sector, environmental policies, and the country’s conflict resolution mechanisms, political system, and relationships with other countries and with multilateral institutions.”* There is no one-size-fits-all regulatory option since such factors are different for each country.<sup>200</sup>

Regardless of country, *Jamison et al (2005)* purport that certain design principles must be taken into account by all those committed to reducing risk and maximizes the effect of regulation. These questions are posed.<sup>201</sup>

1. *How does the country’s overall regulatory framework affect capital market development for infrastructure projects?*
2. *How robust is the relationship between that country’s framework and capital market development?*
3. *Are there strategies for increasing regulatory discretion in contracts commensurate with gained regulatory expertise over multiple years, and do these strategies actually work?*
4. *How does the country’s overall regulatory framework affect capital market development for infrastructure projects?*
5. *How robust is the relationship between that country’s framework and capital market development?*
6. *Are there strategies for increasing regulatory discretion in contracts commensurate with gained regulatory expertise over multiple years, and do these strategies actually work?*

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<sup>200</sup> Sunita Kikeri and John Nellis, 2004, “An Assessment of Privatization,” *The World Bank Research Observer*, Vol. 19, No. 1: 87118; at p. 111. They note that regulatory frameworks need to take into account each country’s unique political, legal, and institutional context, an observation attributed to World Bank, 2004, “Reforming Infrastructure: Privatization, Regulation, and Competition.” Washington D.C.: The World Bank. c/f Jameson et al (2005) *ibid*

<sup>201</sup> *Ibid* Jamison et al (2005) Mechanisms to Mitigate Regulatory Risk in Private Infrastructure Investment:

*Jamison (2005)* refers to the collective findings of three major banks, including the World Bank in a paper discussing the regulatory framework and processes used to manage risk. This paper discusses the importance of the following:<sup>202</sup>

- 1. Transparent regulatory processes**
- 2. The need for community and citizen involvement**
- 3. Effects of subsidizing service providers**
- 4. Effects of subsidies on competition**

These authors hold that unless accountability and risk mitigation measures are incorporated by policymakers into contracts with private companies, the risks of privatization may exact a high price for all stakeholders.

## **Transparency, Independence, Governance Issues**

*Jamison et al* refer to the paper by *Brown and Ashley (2002)* for the World Bank<sup>203</sup> by emphasizing the importance of transparency

One important finding of that paper is that “having the government itself hear appeals of regulatory decisions removes any benefit from having an independent “*regulatory agency.*”

*Brown and de Paula (2002)* strongly uphold transparency principles including that all evidence, whether fact, opinion or argument presented by decision-makers must be publicly exposed. This should include all oral and material relied upon, which must be readily available.

No substantive opinion should be rendered without full explanation. The paper explains that having the government itself hear appeals of regulatory decisions removes any benefit from having an “independent” regulatory agency.

In discussing the appeal process *Brown and Ashley (2002)* mention that in many jurisdictions “*parties can appeal government decisions to the courts. For example, special or preexisting tribunals hear regulatory appeals in England, India, and Bolivia. The paper argues that unless the special tribunal is judicial, its decisions could be subject to judicial review. Direct appeals to the courts have the benefit of fulfilling constitutional or other legal rights available to citizens; however, where independent regulation is a new concept the judiciary is often unprepared to deal with such matters.*

*Jamison (2005)* includes reference to *Stern and Cubb’s (2003)*<sup>204</sup> London paper of regulatory effectiveness and governance with particular emphasis on the electricity industry.

The shortcomings of regulatory governance in developing and transition economies are discussed, but many of the issues can be applied to other arenas.

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<sup>202</sup> Asian Development Bank, Japan Bank for International Cooperation, World Bank. 2005. “Accountability and Risk Management.” In *Connecting East Asia: A New Framework for Infrastructure c/f Jamison (2005)*

<sup>203</sup> Brown, Ashley C., and Ericson De Paula. 2002. “*Strengthening of the Institutional and Regulatory Structure of the Brazilian Power Sector.*” World Bank Report on the PPIAF Project for Brazil Power Sector, Task 4, Washington, D.C., The World Bank c/f Jamison et al (2005)

<sup>204</sup> Stern, Jon and John Cubbin. 2003. “*Regulatory Effectiveness: The Impact of Regulation and Regulatory Governance Arrangements on Electricity Industry Outcomes: A Review Paper,*” Preliminary Draft. Department of Economics Discussion Paper Series, City University of London, No. 04/01 c/f Jameson et al 2005)

The use of econometric studies in gauging the quality and effectiveness of regulatory agencies on electricity and telecommunications utility outcomes and on research review conducted in the area form the focus of the paper, also identifying those areas of research that may enhance evaluation of performance and impact of regulatory agencies.

**Comment:**

It is unclear how much the issue of governance and accountability has been considered.

From cursory glance at the status of consultation papers being reviewed by the retail Policy Working Group (Energy) it would seem that a model that includes proposed approaches in relation to specific legislation rather than under the umbrella of an overall national consumer policy independently administered, the latter being recommended by CHOICE (ACA) and other community agencies as the preferred model for consumer protection.

On the issue of evaluation, please refer to separate documentation on some best practice evaluative processes, which in the short available time may not have been considered at all in the evaluative design the subject of current Government Inquiries and Reviews.

In my opinion, these principles should be embraced in overall regulatory design across the board. No attempt should be made to bargain away the right of any aggrieved individual or other stakeholder to be stripped of the right of appeal at the highest level. However, in the case of private individuals their access to resources is extremely limited.

The current generic process are deficient for a host of reasons discussed elsewhere specifically under Consumer Protection deficiencies.

Also highlighted by Jamison is the paper by *Burns and Riechman's (2004)*<sup>205</sup> is a conceptual study examining the key drivers of investment behaviour of regulated infrastructure companies under performance-based regulation.

A particular case study from the UK is used by the authors to illustration how in the early stages of privatization incentives to improve quality are weak, with incentives to cut costs and distribute profits to shareholders stronger.

*Burns and Riechman's (2004)* conceptual study examines key drivers of investment behavior of regulated infrastructure companies under performance-based regulation. It uses a case study of Railtrack in the U.K. to illustrate a situation where in the early stages of privatization, the incentives to improve quality were extremely weak and the incentives to cut costs and distribute profits to shareholders were stronger.

This would indicate that if benchmarking principles are not included transparently and robustly in the design stage market failure may result with band aid solutions developing in much the same haphazard manner in which regulation has developed to date.

Getting the conceptual framework right takes time and effort. It cannot be rushed. Decisions need to be balanced and take into account all stakeholder input, with appropriate time-lines allowed, and opportunities for regular review and rule change that fair, equitable, transparent and accessible.

The authors acknowledge that the cost:benefit ratio for establishing quality indicators can be difficult to determine for both current and expected future output performance. Negotiations should not be left to the end of a price review period.

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<sup>205</sup> Burns, Phil and Christopher Riechman. 2004. *Regulatory Instruments and their Effects on Investment Behavior*. "World Bank Policy Research Working Paper 3292, Washington, D.C.: The World Bank. c/f Jamison et al (2005) ibid c/f Jameson et al (2005)

*Jamison et al (2005)* recommend this paper as one that offers a number of practical suggestions regarding benchmarking under performance-based regulatory principles.

*Jamison* refers to another World Bank Argentinian study of regulatory design for infrastructure<sup>206</sup> using a local case study in analyzing the mutually related concepts of independence and economic autonomy

If independence is to be achieved and seen to be independent, the paper argues for adoption of the following broad concepts:

1. *Regulators should operate independently from political pressures—from ministries and from the regulated enterprises, private or public;*
2. *Regulators should be appointed on the basis of professional rather than political criteria and should have formal protection from arbitrary removal during their term;*
3. *The appointment process should involve both the executive and the legislature, to ensure proper checks and balances; and (4) regulatory agencies must first have their own resources.*

Sustainability issues are also addressed in Estache's (1997) paper, holding that accountability requires transparency in the regulatory agency's decision-making process and clear simple procedural rules.

*Warrick Smith's 1997* analysis for the World Bank<sup>207</sup> concerning the regulatory independence debate is another paper including in *Jamison's (2005)* literature review. The controversial but important concepts examined include the relationship between independence and accountability.

Issues explored include:

1. Regulatory independence when there is a distinct legal mandate independent of ministerial control;
2. Professional criteria prescribed for board appointment;
3. Executive and legislative branches involved in the process
4. Fixed term appointments and protection from arbitrary removal
5. Staggered terms
6. Autonomous budget and
7. Reliable sources of funding

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<sup>206</sup> Estache, Antonio. 1997. "Designing Regulatory Institutions for Infrastructure – Lessons from Argentina." Note No. 114 in *Public Policy for the Private Sector*. Washington, D.C.: The World Bank. c/f Jamison (2005) ibid c/f Jamison et al (2005)

<sup>207</sup> Smith, Warrick. 1997. "Utility Regulators: The Independence Debate." Note No. 127 in *Public Policy for the Private Sector*. Washington, D.C.: The World Bank. c/f Jameson et al (2005)



## Comment:

It has been argued that in the Australian energy regulatory framework (and perhaps elsewhere) current regulations and the deliberative processes leading to decisions are not always transparent and often far from clear and simple expressed in unambiguous.

Best practice requires that all stakeholders have proper opportunity to express their views in public hearings and to appeal decisions, with proper timelines and flexibility in submission parameters, as an ongoing process that does not end when the deadlines have expired. Responding to competition and community needs is a journey that does not end with the introduction of regulations that may no longer keep up with dynamic environments.

Of course this is the theoretical rationale behind current reviews, but there are concerns about the extent to which decisions may be rushed without full and robust research and community participation. In addition there are also concerns about too broad a conceptual framework that leaves it open to state regulators to fall into the same perceived trap as before by introducing ad hoc band-aid type responses to market failure that lead to further inconsistency, ambiguity and complaints about regulatory burden.

*Jamison et al (2005)* highlight the work of *Kelly and Tenenbaum (2004)*<sup>208</sup> on behalf of the World Bank that develops a conceptual paper recommending practices for funding of energy regulatory commissions, including levels, sources of funding, approval of budgets and fees, authorization of commission and penalty treatments against regulated companies. In examining eight regulatory commissions by way of example, the paper deals also with accountability for commission use of expenditure and performance.

Each of these recommendations may be worth considering in determining a proper regulatory framework and accountability principles

## 2. Regulatory System

In discussing regulatory systems Jamison et al direct attention to *Baldwin and Cave's (1999)*<sup>209</sup> overview of legislative bodies, courts, central government departments and local authorities.

Another pertinent choice by Jamison is *Henisz Witold and Zelner's (2004)* paper<sup>210</sup> of political economy of private electricity provision in Southeast area.

## Comment.

Though focused on ASEAN countries, the value of this paper in the current regulatory review may be examination on how difference in policy credibility affected government opportunism and investor's choices of strategic safeguards.

Of equal importance may be the examination of how strong political ties between government agencies weaken formal checks and balances. Another Jamison choice is that of the same authors<sup>211</sup> in 2005 regarding political risk in infrastructure investment.

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<sup>208</sup> Kelley, Elizabeth and Bernard Tenenbaum. 2004. "Funding of Energy Regulatory Commissions." Energy Working Notes, No. 1, Washington, D.C.: The World Bank. c/f Jameson et al (2005)

<sup>209</sup> Baldwin, R., and M. Cave. 1999. *Understanding Regulation: Theory, Strategy, and Practice*, Oxford: Oxford University Press, Chapter 5 c/f Jameson et al (2005)

<sup>210</sup> Henisz, Witold, and Bennet Zelner. 2004. "The Political Economy of Private Electricity: Provision in Southeast Asia," Reginald H. Jones Center for Management Policy, Strategy and Organization, University of Pennsylvania.

<sup>211</sup> Henisz, Witold, and Bennet Zelner. 2005. "Managing Political Risk in Infrastructure Investment," Reginald H. Jones Center for Management Policy, Strategy and Organization, University of Pennsylvania. c/f Jamison et al (2005)

### **Comment:**

For current Australian-based purposes and although not related in infrastructure risk in developing countries the cautions about checks and balances are applicable in any framework. These are four basic principles:

On the basis of research and interviews with managers, regulators, lawyers, and consultants, the authors identify four basic principles that private infrastructure investors should apply to reduce political risk:

1. Develop business models that are appropriate for the country's normal business practices in the national context and that avoid special treatment;
2. Shape public opinion in favor of the investment;
3. Develop relationships with policymakers and key domestic businesses; and
4. Avoid doing business with governments that lack political checks and balances, have unclear authority, and weak regulatory institutions.

Another preliminary draft paper cited by *Jameson et al (2005)* was the one present in Rome, Italy by *Jadresic and Fuentes in 1999*<sup>212</sup> again on reduction of political and regulatory risk in the infrastructure sector.

### **Comment:**

The value of this in the current Australian enquiries may be the focus on strategies to improve transparency, independence, competence and credibility of the regulator. Other aspects of government as they affect regulatory and political risk are also discussed.

This is a climate of compromised confidence in consumer protection. It is also a policy climate of proposed change, so it may be opportunistic to learn from the experience of or research of others by applying relevant principles in a different context.

Many weaknesses have been identified in current regulatory instruments, compliance enforcement, affiliations, efficacy of complaints schemes and compromised consumer protection. There is general consensus on these issues across the board. The suggestions may therefore be helpful despite the context in which they are made.

This paper provides a framework of some of the strategies governments can use to mitigate regulatory and political risk to private companies investing in infrastructure projects in developing countries. One section of the paper focuses on strategies that can improve **transparency, independence, competence, and credibility of the regulator**, but other aspects of government, as they affect regulatory and political risk, are also discussed.

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<sup>212</sup> Jadresic, Alejandro, and Fernando Fuentes. 1999. "Government Strategies to Reduce Political and Regulatory Risks in the Infrastructure Sector." Preliminary draft presentation for conference, Private Infrastructure for Development: Confronting Political and Regulatory Risks; September 8-10, Rome, Italy c/f Jamison et al (2005)

*Jamison et al* have drawn attention to the paper by *Kaufman et al (2004)*<sup>213</sup> examining six dimensions of government for 199 countries and territories in four time intervals between 1996 and 2002 using an unobserved components model, using 250 individuals measures taken from 25 different sources, including international organizations, political and business risk-taking organizations, think tanks and nongovernmental agencies.

The governance indicators examined are:

1. voice and accountability (political process, civil liberties, and political rights);
2. political stability and absence of violence;
3. government effectiveness;
4. regulatory quality;
5. rule of the law, and
6. control of corruption.

The limitations of margins of error were acknowledged by the authors because of reliance on subjective perceptions and for certain dimensions given the context were unaccompanied by reliable objective data – those of corruption, confidence and property protection.

**Comment:**

Despite the context, many of the issues examined may be relevant in examining current parameters *Jamison's (2005)* choice of *Kurtzman et al's 2004* paper<sup>214</sup> may be helpful were it examines five indicators:

1. corruption
2. efficacy of the legal system
3. deleterious economic policy
4. inadequate accounting and governance practices, and
5. detrimental regulatory structures

**Comment:**

The relevance of another study by *Sirtaine et al*<sup>215</sup> of the profitability of Latin America Infrastructure Concessions highlighted by *Jamison et al* to current Australian parameters may be examination of whether the quality of regulation during privatization helps to bring into alignment a company's rate of return and its cost of capital.

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<sup>213</sup> Kaufmann, Daniel, Aart Kraay, Massimo Mastruzzi. Revised 2004. "Governance Matters III: Governance Indicators for 1996-2002," World Bank c/f Jamison (2005)

<sup>214</sup> Kurtzman, Joel, Glenn Yago and Triphon Phumiwasana. 2004. "The Global Costs of Opacity." *MIT Sloan Management Review* 46(1): 3844. c/f Jamison (2005)

<sup>215</sup> Sirtaine, Sophie, Maria Elena Pinglo, J. Luis Guasch, and Vivien Foster. 2004. "How Profitable are Infrastructure Concessions in Latin America? Empirical Evidence and Regulatory Implications," Washington, D.C.: The World Bank. c/f Jamison (2005)

Since the study may have applicability to the current goals – unless time and effort is made to get regulatory quality right, Australia may look forward to another decade of imperfections perpetuated. None of this can be achieved at the high speed expected. The study

*“.....shows that the quality of regulation makes a difference and explains at least in part the variance of returns across concessions.”*

The community continues to express concerns over the speed at which the whole regulatory process in the energy industry is being revamped.

This study estimates the returns on investments of private investors in 34 Latin American infrastructure concessions. It also examines whether the quality of regulation during privatization helps to bring into alignment a company’s rate of return and its cost of capital. This study shows that the quality of regulation makes a difference and explains at least in part the variance of returns across concessions.

Jamison’s choice of *Van der Walt’s (1999)*<sup>216</sup> preliminary draft presentation at the Rome conference on Private Infrastructure for Development: Confronting Political and regulatory Risks may be particularly pertinent for the Australian parameters.

The proposals for metering changes and for energy efficiency measures may have an enormous impact on private property owners. They may seek compensation for loss caused by the exercise of proposed regulatory powers. If constitutional provisions are used to mitigate such losses, the concerns of investors may be addressed.

There are risks associated with making exemptions for private property where the rest of the community faces upgrades and retrofits to suit metering policy changes as well as energy efficiency proposals,. With regard to the latter, health risks, contractual issues, quality of provision, trade measurement and utility practices are discussed in considerable detail in a separate submission to the National Framework on Energy Efficiency (NFEE2) submitted on 25 September.

The concerns are not trivial. Current maintenance attention to of hot water services, especially in older multi-tenanted dwellings and impacted on embedded or ‘inset’ end-consumers, represents a potential health hazard and prospective governmental liabilities, so say nothing of the economic cost of meeting health-related issues and hospitalization if Legionnaire’s disease, for example became a serious issue. Since these issues are quite extensively discussed and referenced in a separate submission as mentioned, I will refrain from repeating the arguments here.

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<sup>216</sup> Van der Walt, A.J. 1999. “Reducing Regulatory Risk in Infrastructure by Requiring Compensation for Regulatory Takings: A Comparative Perspective.” University of South Africa. Preliminary draft presentation for conference, Private Infrastructure for Development: Confronting Political and Regulatory Risks; September 8-10, Rome, Italy c/f Jamison (2005)

**Comment:**

Finally regarding regulatory entity, *Jamison et al (2005)* refers to the *World Resources Institute Paper with others (2005)*<sup>217</sup> on benchmarking best practices and accountability in the electricity sector.

Given that the Australian enquires and reviews have a commitment to achieving some degree of benchmarking this may be a useful resource. It includes 60 indicators assessing questions of good governance in the electricity sector

Baseline indicators include:

1. Policy Processes
2. Regulation
3. Environmental and
4. Social aspects

The framework is recommended by Jamison et al as an “assessment tool across countries to help public-minded organizations promote good governance in the electricity sector.

***Corruption (broadly defined)***

**Comment:**

*Jamison et al* discuss corruption in their literature review as broadly defined. Whilst this can seem a loaded term, it is used in this discussion more broadly to include misleading conduct or unethical, policy or terminology, intentional or otherwise that can lead to consumer detriment, and not intended to offend any individual or agency.

Corruption is a matter of degree and whilst in the context of developing countries may imply a certain meaning in terms of illegal corruption (bribery), it is used here in a broader sense where

*“legal corruption as a result of legal political financing or undue influence of political firms on policymakers.”*

It is my contention as an observer that there are levels of conduct, often driven by existing policy that fall into a grey area where social justice issues have been compromised and re-balancing has become overdue. If it were not the case, the current Inquiry would be redundant.

Misleading conduct is also a matter of degree and policies in place can either deliberately or inadvertently condone such conduct by allowing loopholes and interpretations to creep into regulatory instruments, including codes and guidelines that overtly, almost unashamedly, appear to exploit consumer rights, entitlements and interests.

Refer, for example, the VESC<sup>218</sup> *Bulk Hot Water Guideline 20(1) 2005* that allow for magical algorithm formulae through which water meters posing as either gas or electricity meters are used to calculate water volume and then by conversion factor converted into deemed gas or electricity usage, and charges expressed in cents per litre.

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<sup>217</sup> World Resources Institute, National Institute of Public Finance and Policy, and PrayasPrune. 2005. *Electricity Governance Toolkit: Benchmarking Best Practices and Promoting Accountability in the Electricity Sector* (Pilot version) c/f Jamison et al (2005)

<sup>218</sup> Victorian Essential Services Commission, the current regulator

This is despite the fact that energy suppliers are licenced to sell gas or energy not value-added commodities such as *“hot water services”* and that gas is measured in either cubic meters or megajoules, and electricity measured in Kw/h. these arrangements are discussed in considerably further detail elsewhere.

Another example could be the perception that in seeking to secure competitive market contracts it may be permissible to omit to mention any front-end or back-end penalty to consumer detriment that switching choices may herald. This was one issue discussed at the recent Public Meeting auspices by the AEMC Retail Competition Review on 4 September 2007 chaired by John Tamblyn.

At both the Melbourne Public Meeting on 4 September and the parallel meeting in Bendigo the following day, John Tamblyn mentioned that full retail competition would not necessarily mean lower prices but could mean that

*“competition is sufficient to keep the marketplace in balance.”*<sup>219</sup>

At the Bendigo meeting on 5 September Mr. Tamblyn said:

*“competition is sufficient to keep the marketplace in balance, even if every customer is not necessarily well-informed.”*<sup>220</sup>

### **B. Corruption.**

*Jamison et al (2005)* consider corruption to be of particular concern on the basis that it

1. Decreases service output by increasing, costs,
2. Diverts capital from productive uses
3. Takes wealth from its legitimate owners

The authors<sup>221</sup> cite ongoing corruption is a concern listed by respondents in World Bank investment climate surveys, who also expressed concerns about the effects of corruption on investment.<sup>222</sup>

As noted by *Jamison et al (2005)* where transparent processes are lacking, corruption is often an indicator in governance indices.

Private participation contracts that lack transparency are particularly vulnerable to various manifestations of corruption or unethical behaviour, with the potential for such behaviour to occur at different stages in a contractual infrastructure project cycle:

1. Project identification
2. Contract Award
3. Negotiation
4. Project Finance
5. Implementation

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<sup>219</sup> CUAC Quarterly Newsletter AEMC review of effectiveness of FRC,” p. 4.

<sup>220</sup> CUAC September Quarterly “AEMC Review of Effectiveness of FRC

<sup>221</sup> Ibid Jamison et al (2005) Mechanisms to Mitigate Regulatory Risk in Private Infrastructure Investment:

<sup>222</sup> Mary Hallward Driemeier and David Stewart, 2004, “How Do Investment Climate Conditions Vary Across Countries, Regions, and Types of Firms?” Background paper prepared for the *World Development Report 2005: A Better Investment Climate for Everyone*. c/f Jamison et al (2005) ibid

*Jamison et al (2005)* examine

1. The various conditions in which such conduct is likely to occur in infrastructure sectors;
2. The extent to which competition of service providers, the transparency of the regulatory process, budget oversight, performance audit capability and other governance oversight
3. Whether corruption can be adequately addressed if strategies are applied only in the public sector, aim to identify the strategies that could be used to reduce the incidence of corruption (used broadly)

The authors attempt to answer those questions by referring to the literature review the subject of their comprehensive paper

### **Comment**

The issues raised should form part of the overall framework not only in considering consumer protection, but also in term of how these gaps can affect competition and productivity overall.

In referring to bribes paid to electricity and telecommunications utilities, authors *Clarke, George and Xu (2004)*<sup>223</sup>, as referred to by *Jamison et al (2005)* concede that denovo private firms are more likely to be the bribe payers where this occurs and utilities are less likely to receive bribes in countries with greater capacity in terms of better-developed telecommunications systems, more competition in the telecommunications sector and utility privatization.

Of more interest to the current Australian reforms is the empirical data analysis by *Daniel Kaufmann, 2004*<sup>224</sup> from the 2004 Executive Opinion Survey of the World Economic Forum cited by *Jamison et al (2004)*.

The paper shows evidence of improved governance resulting in high incomes per capita and suggests that of the fifteen obstacles to global competitiveness

*“the eradication of corruption would have the greatest benefit for a country’s ability to compete globally (as measured by its ranking on the World Economic Forum’s Growth Competitiveness Index.)”*

Further the study claims that though

*“poorer countries have higher levels of illegal corruption (bribery) than their richer counterparts. However, there is great variability among richer countries in the OECD and elsewhere in the level of corruption that could be described as “legal” (legal political financing or undue influence of political firms on policymakers).”*

These considerations are crucial to any overall framework parameters.

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<sup>223</sup> Clarke, George R.G., and Lixin Colin Xu. 2004. “Privatization, Competition, and Corruption: How Characteristics of Bribe Takers and Payers Affect Bribes to Utilities.” *Journal of Public Economics* 88: 2067-2097  
c/f *Jamison et al (2005)* *ibid*

<sup>224</sup> Kaufmann, Daniel. 2004. “Corruption, Governance and Security: Challenges for the Rich Countries and the World.” In *Corruption, Governance and Security*.

## ***Sustainability***

*Jamison et al (2005)*, after a thorough literature review, and given their standing within a world-class Public Utility Research Centre in Florida comment on the political, popular and legal support for selected features of sustainability of government institutional structure and anticorruption (broadly defined) as they affect investment risk by improving the predictability of outcomes.

There is a risk where governance of these issues is limited to regulators and policymakers too close connected with the consumer policy framework. There are possible conflicts of interests associated with such issues and also with industry-specific complaints schemes, as discussed in more detail under discussion of the consumer policy framework.

*Jamison et al (2005)* discuss the concept of sustainability in their preamble to examination of this category of literature on the topic.

They refer in particular to the sustainability of government institutional structure and anticorruption policies as affecting investment risk by improving the predictability of outcomes.

*Jamison (2005)* offers the following viewpoint<sup>225</sup>:

*“A regulatory agency’s ability to function is determined not just by its own technical capacity to perform its duties, but by legal rules that define its formal authority, the willingness of the courts and other governmental entities to recognize and follow these legal rules, and the belief and acceptance of operators, customers, foreign governments, and multilateral organizations (such as The World Bank) that the regulatory agency is legitimate and capable.”*<sup>226</sup>

The authors discuss political pressures on governments to renegotiate or terminate private contracts as infrastructure projects fail to deliver affordable services to the poor.

In Australia, if subsidies such as may be currently contemplated by shifting social justice responsibility for guaranteed service from private companies to charity agencies and government services, and focusing entirely on those who meet the defined criteria of financial hardship alone, not only do agencies and the government absorb all additional costs of delivering a partial solution to justice and equity principles, but private companies are absolved altogether from meeting social justice obligations.

Refer for example to *Gavin Dufty’s*<sup>227</sup> VCOSS Congress Paper (2004) discussing the current and past philosophies of the Victorian Essential Services Commission as identified at the World Forum on Energy Regulation, Rome 2-7 October 2003.

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<sup>225</sup> Ibid ref 8 Jameson et al (2005) Mechanisms to reduce regulatory risk

<sup>226</sup> Mark A. Jamison, 2005, “Leadership and the Independent Regulator,” Public Utility Research Center, University of Florida, Gainesville, Florida.

<sup>227</sup> Dufty, G, Who makes social policy? – The rising influence of economic regulators and the decline of elected Governments. Policy and Research Unit, St Vincent de Paul VCOSS Congress Paper 2004; and John Tamblyn’s Paper presented to the World Forum on Energy Regulation, Rome, Italy 5 – 9 October 2003, Concurrent Overview Session 5 “Are Universal Service Obligations Compatible with Effective Energy Retail Market. Victoria’s Experience to Date.



As countries become more democratic, infrastructure projects that fail to deliver affordable services to the poor can result in political pressure on governments to renegotiate or terminate private contracts. For example, subsidies are often part of pro-poor strategies. If they are not effectively targeted or services are under-priced, revenue streams needed to meet contractual performance outcomes may be jeopardized. Therefore, risk mitigation policies need to consider pro-poor strategies.

*Jamison's* challenging questions need to be carefully considered in this climate of policy change:

1. *What leadership and other skills do utility regulators need to succeed in their roles?*
2. *To what extent can changes in government institutions and policies affect behavior and at what pace can behavior change?*
3. *How can regulators and others exercise leadership for the capacity and stability of government institutions?*

**Comment:**

*Dr Charles Albano (2007)*<sup>228</sup> uses a chameleon for his logo to symbolize adaptive leadership. He describes adaptation as “a dynamic process of mutual influence. All creatures act on their environments and their environments, in turn, act on them.” He claims that organizations are capable of intelligent, purposeful, collective action, those taken to influence their environments in desired directions.

If regulators need to have adaptive leadership styles then they should be chosen carefully, bearing in mind that “relationships between living entities are circular and interactive.”

*Mark Jamison* as lead author of the majority of the studies cited here followed the 2004 literature review with a concept paper written the following year on Leadership and the Independent Regulator.<sup>229</sup>

*Jamison (2005)* claims that

*“regulators are sometimes scapegoats for unpopular policies and unavoidably become involved in shaping the policies that they are supposed to implement. As a result of such frictions, regulators are sometimes removed from office or marginalized in some way.”*

He recommends strategies by which adaptive leadership can be used to help constitutes to adapt to new policies and changing situations, whilst still staying in the game.

The foremost leadership skill recommended is the ability to

*“get on the balcony and see what is really going with operations, politicians, consumers and others - a meaningful engagement with all stakeholders.”*

Current strategies in heralding reform measures are thought by many to be lacking in the department of meaningful dialogue. Not that the dialogue is not occurring, but there are queries about how meaningful that dialogue is; how well the consumer voice and other voices are being heard; the extent to which airing and meaningful reciprocal dialogue is occurring with stakeholders in time to make a difference before new regulations are put in place.

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<sup>228</sup>Albano, C (Dr.) Leadership Skills – What is Adaptive Leadership? 22 April 2007 found at <http://www.selfgrowth.com/articles/calbano.html>

<sup>229</sup> Jamison, Mark A. 2005. “Leadership and the Independent Regulator,” Public Utility Research Center, University of Florida, Gainesville, Florida.

In a climate of rushed policy change such as is envisaged, and in the light of the tensions and apprehensions apparent on both sides of the fence, all stakeholders are begging for more certainty and stability that they perceive to be offered, improved meaningful dialogue and longer timelines to give effect to the theory of stakeholder consultation.

The public at large is also looking for improved transparency, such as publishing of all external reports relied upon, whether or not specifically commission for this current Retail Review, but as long as they give a more complete picture of the market and its performance. Other examples are poor accessible to deliberative documents and all of the thinking, evidence and material that guides government decisions

<b>COMPARING MECHANICAL AND ADAPTIVE VIEWS</b>	
Mechanical	Adaptive
Attention is focused on activities.	Attention is focused on value-added outcomes
Job descriptions are long, detailed and constraining	Job descriptions are intentionally broad-based to allow for flexibility
Role expectations are narrow and rigid.	Roles are fluid. Within limits, people are expected to substitute for one another.
Contacts are confined and communication is channeled by higher management.	Contacts are open and networks are encouraged to form.
Policies are mostly oriented toward control, what people can't do.	Policies encourage people to take a "can do" mindset to find solutions
The organizational structure is bureaucratic and fragmented into many departments	The structures are more fluid and of shorter duration. Changes in design are aimed at enhancing flexibility and responsiveness
Authority is based on rank, and it is expected that influence will equate with formal authority.	Authority is accorded a place, but reliance on it is played down. Greater influence is accorded people who demonstrate ability to add value.

Efficiency and predictability are sought and reinforced.	Achievement, innovation and change are sought and rewarded.
Cooperation among departments is subject to a lot of formalization and clearances. Turf guarding prevails.	Cooperation is a highly regarded value in the organization and is far more easily gained.
Information is kept close hold	Information is widely available to facilitate work accomplishment and permit more opportunities for more people to add value to operations.
Traditional values are fostered such as unit loyalty and obedience to the effect that they stifle initiative and hamper teamwork across departments.	Newer values such as cooperation, and responsiveness along with treating other units as internal "customers."
Source: Albano, C (Dr.) Leadership Skills – What is Adaptive Leadership? 22 April 2007 found at <a href="http://www.selfgrowth.com/articles/calbano.html">http://www.selfgrowth.com/articles/calbano.html</a>	

*How do political party, personal, and informal relationships affect the effectiveness of formal policies on regulatory systems, regulatory agencies, and corruption?*

These considerations should be paramount in the minds of those formulating reforms and consumer policy frameworks, more especially in the essential services arena

*To what extent have past infrastructure reforms in developing countries improved access of the poor to utility services?*

The concepts are still applicable to countries like Australia that are not termed “developing”

*Jamison et al* cite a selection of authors who have written on the relationship between the urban poor to private infrastructure.

These include *Cowan and Tynan (1999)* whose conceptual paper recommends that:

*“policymakers consider the market structure and potential for entry before entering into privatization contracts.”*

Though not the focus of this submission, there are many concerns about the current marketplace, in a climate of vertical and horizontal integration with market dominance perceived on many grounds by a select few whose power and vertical structures may make it exceedingly difficult for new entrants to survive in an open fully deregulated market.

*Cowan and Tynan (1999)*<sup>230</sup> as cited by *Jamison et al (2005)* that contracts need to achieve the following:

- 1) *“Ensure that the privatization agreement does not cut off service options for the poor or reduce choices.”*
- 2) *“Contractual provisions should focus more on output standards (quality of service) and less on input standards, such as standards based on an international company’s technology.”*
- 3) *“Other items to consider include: alternative interconnection arrangements for the poor, subsidies that are targeted and not tied to one supplier, and changes in the regulatory process to improve service for the poor and gauge willingness to pay.”*
- 4) *“Policy decisions made during the transition to a concession will likely need to be made sequentially.”*
- 5) *“Once a contract is finalized, it is difficult to change entry and competition rules, provide for alternative supplies, and stipulate lower technical standards.”*

Another paper cited by *Jamison et al (2005)* covering the area of making allowances for the poor is that of *Antonio, Foster and Woden (2002)*<sup>231</sup>

The paper examines and explains the following:

1. *Macroeconomic and microeconomic linkages between infrastructure reform and the poor and discusses setting priorities*
2. *Describes reforms’ impacts on access and affordability for the poor;*
3. *Discusses approaches for improving access for the poor, including operator obligations, connection targets, low cost technologies, subsidies and cross-subsidies, and open entry;*
4. *Describes approaches for improving affordability, including lifeline subsidies, means-tested subsidies, vouchers, balancing connection and usage charges, billing options, and prepaid service.*

The issue of prepaid services has become one causing tension and concern within the community with many submissions focusing on this and on the proposal to roll out interval meters. There is a general consensus that community concerns have been ignored.

*Jamison et al* discuss the paper by *Foster and Araujo (2004)*<sup>232</sup> discussing infrastructure reform in relation to the poor.

Though focused on the impoverished Guetamalan community, many of the issues discussed are still relevant when considering the plight of those on lower fixed incomes.

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<sup>230</sup> Brook Cowen B, Tynan P & N . 1999. “Reaching the Urban Poor with Private Infrastructure, Finance, Private Sector, and Infrastructure Network”, Note No. 188, Washington, D.C.: The World Bank.

<sup>231</sup> Estache, Antonio, Vivien Foster, and Quentin Wodon. 2002. Accounting for Poverty in Infrastructure Reform: Learning from Latin America’s Experience, Washington, D.C.: The World Bank.

<sup>232</sup> Foster, Vivien and Maria Caridad Araujo. 2004. “Does Infrastructure Reform Work for the Poor? A Case Study from Guatemala.” Policy Research Working Paper 3185, Washington, D.C.: The World Bank.

The paper explains how utility sector policies have affected the poorer households including

1. Barriers to universal access of services
2. Impacts of tariff reforms
3. Impacts of subsidy policies on service affordability

Endeavouring to sell the concept of full deregulation by referring to customer choice without a proper understanding of behavioural economics, and especially how consumer choices can be distorted and regretted for a number of reasons.

Comprehensive expert submissions to the Productivity Commission have covered this point and are briefly discussed under “vulnerable consumers”

The term “*empowerment*” can often be a cover-up for failing to adopt pro-active and carefully considered strategies.

Gavin Dufty, Social Scientist, St Vincent de Paul has eloquently refused principles that expect to shift responsibility to charities and government agencies for those who are vulnerable and disadvantaged, including those with financial hardship.<sup>233</sup>

Respected agencies such as CUAC have made many submissions on the same topic

David Tennant, Director Care n Financial Counselling Service has spoken about the dangers of taking the consumer out of consumer advocacy and has criticized certain interpretations of the advocacy role and delivery<sup>234</sup>

These inputs are further discussed under vulnerable and disadvantaged consumers.

*What are the most effective pro-poor strategies used in developing country infrastructure concessions to date and why have these strategies been effective?*

Though the Australian situation is not one of a developing country, pro-poor strategies are still indicated in dealing with the financial hardship of vulnerable and disadvantaged consumers

*How do direct subsidies granted by government ministries for an infrastructure concession dovetail with pro-poor subsidies used in ratemaking and what are the ramifications?*

*As summarized by Jamison et al (2005), the 2000 paper by Loveo, Gurenko, Haney, O’Keefe and Shkaratan<sup>235</sup> discuss subsidies and their performance in relation to the poor, with the venues studied being central and Eastern Europe and the former Soviet Union.*

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<sup>233</sup> Dufty, G, (2004) VCOSS Congress Paper Who makes social policy? – The rising influence of economic regulators and the decline of elected Governments. (Policy and Research Unit Society of St Vincent de Paul Victoria). Should be read in tandem with Essential Services Commission, regulatory framework, [www.reggen.vic.gov.au/electricity136.html](http://www.reggen.vic.gov.au/electricity136.html); Tamblyn J chairperson Essential Services Commission, World forum on energy regulation, Are Universal service obligation compatible with Effective energy retail market competition, Victorian experience to date, Rome Italy October 5-9 2003

<sup>234</sup> Tennant, D (2006) Speech delivered to 3<sup>rd</sup> National Consumer Congress hosted by Consumer Affairs Victoria 16 March 2006 The dangers of taking the consumer out of consumer advocacy:

<sup>235</sup> Lovei, Laszlo, Eugene Gurenko, Michael Haney, Philip O’Keefe, and Maria Shkaratan. 2000. “Scorecard for Subsidies: How Utility Subsidies Perform in Transition Economies,” Note No. 218 in *Public Policy for the Private Sector*. Washington, D.C.: The World Bank.

The criteria for evaluating various subsidy schemes are discussed including:

1. *The share of the subsidy that goes to the poor*
2. *The predictability of the benefit for the poor*
3. *The extent and significance of unintended side effects*
4. *Administrative cost and difficulty*

Whilst these broad issues are worthy of scrutiny they need to be examined in the light of an unstable environment with major regulatory change in the Australian environment and the nature of market dominance shared between three major vertically or horizontally integrated retailer/gentailer players and overseas ownership

Finally under Sustainability, *Jamison et al (2005)* highlight the study of the Public Private Infrastructure Advisory Facility Washington DC<sup>236</sup>

That study of urban poverty in developing countries focuses on

1. The concerns of the poor in responding to water sector reform proposals;
2. Elements of water sector reform;
3. Legal frameworks that can affect the poor in privatized arrangements;
4. Contractual incentives for providing water services to the poor, tariff and subsidy mechanisms that help and hurt the poor and;
5. The types of information that should be collected as part of the transaction preparation phase

In the Australian context there are specific areas of concern with the proposed water efficiency measures as well as in the context of current provisions, notably for embedded consumers.

These issues are more thoroughly discussed in a dedicated submission to the national Framework on Energy Efficiency dated 25 September 2007 (individual submission); and one from CUAC dated 26 September.

Some issues include:

How the specific needs of **embedded consumers** will be addressed in the planning and implementation of water reform measures?

Though some thought has been given in the proposed NFEES Stage 2 Measures 8.2.5 National Water Heater Strategy to mandates for new buildings and retrofits for privately owned property, the particular needs of those who are embedded or inset consumers have not been considered

The Consumer Utilities Advocacy Centre (CUAC) is an independent consumer advocacy organization which ensures the interests of Victorian electricity, gas and water consumers—especially low income, disadvantaged, rural and regional, and Indigenous consumers—are effectively represented in the policy and regulatory debate.<sup>237</sup>

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<sup>236</sup> Public Private Infrastructure Advisory Facility. 2002. *New Designs for Water and Sanitation Transactions: Making Private Sector Participation Work for the Poor*. Washington, D.C.: The World Bank.

<sup>237</sup> CUAC Quarterly September 2007 p 1

CUAC believes all Victorians have a right to:

1. ♦ affordable and sustainable electricity, gas and water
2. ♦ have their interests heard in policy and regulatory decisions on electricity, gas and water
3. ♦ not be disconnected from electricity, gas and/or water due solely to an inability to pay

This body is respected for the expertise it has gained in researching and advocating for improved utility policies.

The CUAC's September quarterly<sup>238</sup> reported discussions at the recent forum organized by CUAC for consumer advocates and policymakers to discuss pricing in the light of the rapid energy market developments, Gavin Dufty from St Vincent de Paul

*“Gavin Dufty from St. Vincent de Paul Society proposed pricing principles which would allow a fixed price for a minimum level of consumption or ‘lifeline’ per household, with tariffs increasing in blocks after the minimum. This would, he argued, protect low income earners, reward reduction in energy consumption, and work well with the introduction of interval meters.*

*Jim Gallagher, a consultant, discussed network pricing options from the Network Business perspective. Brad Shone from the Alternative Technology Association looked at how proposed developments such as interval meters, cost reflective prices and emissions prices would impact on consumers.*

*Robert Wiles, an independent adviser on energy market regulation and reform, discussed how more complex pricing structures would increase the need for organisations to provide independent advice on a regulatory and individual basis.*

The same article reported the input of Catherine Waddams, an expert on privatization, regulation and competition in energy in Britain and Europe in analyzing the deregulation experiences in other countries, particularly the UK. CUAC reports that Catherine Waddams “startling research showed that of those switching retailers, only one-fifth achieved the best possible outcome and more than a fifth ended up worse off,” even allowing for those who switched to green power.

Other issues discussed at that forum and reported by CUAC were how the proposed developments such as interval meters, cost-reflective prices and emissions prices would impact on consumers (Brad Shone, Alternative Technology Association).

### **C. Sustainability**

*Sustainability of government institutional structure and anticorruption policies affect investment risk by improving the predictability of outcomes. The political, popular, and legal support of these features of government and culture determine sustainability.*

*For example, a regulatory agency's ability to function is determined not just by its own technical capacity to perform its duties, but by legal rules that define its formal authority, the willingness of the courts and other governmental entities to recognize and follow these legal rules, and the belief and acceptance of operators, customers, foreign governments, and multilateral organizations (such as The World Bank) that the regulatory agency is legitimate and capable.<sup>239</sup>*

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<sup>238</sup> CUAC September Quarterly “Minister Batchelor Guarantee Safety Net at CUAC Pricing Forum, p2

<sup>239</sup> Mark A. Jamison, 2005, “Leadership and the Independent Regulator,” Public Utility Research Center, University of Florida, Gainesville, Florida.

*As countries become more democratic, infrastructure projects that fail to deliver affordable services to the poor can result in political pressure on governments to renegotiate or terminate private contracts. For example, subsidies are often part of pro-poor strategies. If they are not effectively targeted or services are under-priced, revenue streams needed to meet contractual performance outcomes may be jeopardized. Therefore, risk mitigation policies need to consider pro-poor strategies.*

*Sustainability of the institutional and anticorruption policies raises several questions. What leadership and other skills do utility regulators need to succeed in their roles? To what extent can changes in government institutions and policies affect behavior and at what pace can behavior change? How can regulators and others exercise leadership for the capacity and stability of government institutions? How do political party, personal, and informal relationships affect the effectiveness of formal policies on regulatory systems, regulatory agencies, and corruption? To what extent have past infrastructure reforms in developing countries improved access of the poor to utility services? What are the most effective pro-poor strategies used in developing country infrastructure concessions to date and why have these strategies been effective? How do direct subsidies granted by government ministries for an infrastructure concession dovetail with pro-poor subsidies used in ratemaking and what are the ramifications?*

Jamison, Mark A. 2005. "Leadership and the Independent Regulator," Public Utility Research Center, University of Florida, Gainesville, Florida.

*In this concept paper, the author argues that being a utility regulator is dangerous because the independence of the regulator necessarily removes power from politicians, operators, and others. Furthermore, regulators are sometimes scapegoats for unpopular policies and unavoidably become involved in shaping the policies that they are supposed to implement. As a result of such frictions, regulators are sometimes removed from office or marginalized in some way.*

*How can regulators not only survive in such an environment, but also thrive?*

*"This paper describes a leadership concept called adaptive leadership that regulators can use to help their countries adapt to new policies and changing situations, while allowing the regulator stay in the game. The first leadership skill discussed is the ability to get on the balcony to see what is really going with operators, politicians, consumers, and others.*

*Once this perspective is obtained, then the regulator can engage stakeholders in an adaptive process in which people make necessary changes to traditions and expectations, while hanging on to the things that are truly important.*

*Regulators can do this by bringing attention to problems that people want to ignore because they involve difficult tradeoffs, by providing certainty and stability when tensions become too high for work to be done, and by keeping attention focused on the work and the issues."*

Lovei, Laszlo, Eugene Gurenko, Michael Haney, Philip O'Keefe, and Maria Shkaratan. 2000. "Scorecard for Subsidies: How Utility Subsidies Perform in Transition Economies," Note No. 218 in Public Policy for the Private Sector. Washington, D.C.: The World Bank.

*This paper describes criteria for evaluating various subsidy schemes, including how well the poor are reached, the share of the subsidy that goes to the poor, the predictability of the benefit for the poor, the extent and significance of unintended side effects, and administrative cost and difficulty. It analyzes the main types of utility subsidies in Central and Eastern Europe and the former Soviet Union."*



*This report examines the extent of urban poverty in developing countries, concerns of the poor in responding to water sector reform proposals, elements of water sector reform, legal frameworks that can affect the poor in privatized arrangements, contractual incentives for providing water services to the poor, tariff and subsidy mechanisms that help and hurt the poor, and the types of information that should be collected as part of the transaction preparation phase.*

#### **D. Renegotiation and Bailout**

*What happens if an unforeseen shock makes existing utility policies ineffective, counterproductive, or even unsustainable? What if the regulatory system or agency proves to be unsustainable? Such breakdowns often result in contract renegotiation and bailouts, and governments address these possibilities in several ways.<sup>240</sup> Sometimes contracts or concession agreements provide specific provisions for renegotiation, arbitration, or bailouts. Breakdowns involving foreign investors may also be the subject of trade agreements between countries. Governments may also provide sovereign guarantees of loans involving multilateral institutions, such as The World Bank or International Monetary Fund.*

*Formal provisions for renegotiation and bailouts can reduce investment risk by providing certainty for how unusual circumstances will be dealt with. However, once renegotiation and bailout become formal options, they can also become strategic variables for operators interested in behaving opportunistically.*

*Governments can restrict such opportunistic behavior on the part of operators by formally limiting renegotiation and bailout options, but the enforcement of these formal restrictions is in part dependent on the stability and legitimacy of the government institutions that are being stressed by the unforeseen shock or institutional breakdown. One strategy for addressing this problem is to use international institutions and other countries to enforce renegotiation and bailout policies.*

*These tensions between the need for adaptability and the need for certainty, the dependence during times of crises on government institutions that are themselves either involved in or the source of the crisis, and the need for national sovereignty and the need for international support make risk mitigation and risk allocation difficult. In risk allocations between the public and private sectors, the general consensus is that risk should be borne by the party most equipped to manage it, generally through diversification of risk. For certain situations, at least in practice, the determination of the appropriate party to manage the risk might not be obvious.*

*The topics of renegotiation and bailout raise several questions: For the host country and its regulator, what is the impact of contract renegotiations on private investment in future infrastructure projects? Are such renegotiations always bad? How could the incidence of renegotiations be reduced and what is the role of the regulator to that end?*

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<sup>240</sup> Approximately 50% of all concession contracts signed since the mid-1980s were ultimately renegotiated either by government or provider initiative. See Antonio Estache, 2005, "PPI Partnerships Versus PPI Divorces in LDCs." World Bank Policy Research Working Paper 3470, Washington, D.C.: The World Bank, at p. 1.

*Regulators and host countries also must contend with the prospect of bankruptcy or of failure of private infrastructure providers in concessions to deliver on contractual obligations. What strategies could be taken to respond to those possibilities and minimize the risk of such occurrences in the first place? What elements and principles should be considered for inclusion in effective regulatory contracts?*

[Bakovic, Tonci, Bernard Tenenbaum, and Fiona Woolf. 2003. "Regulation by Contract: A New Way to Privatize Electricity Distribution?" World Bank Working Paper No. 14, Washington, D.C.: The World Bank.](#)

*"This concept paper explains what regulation by contract is, sets out the key characteristics of such contracts, explains the reasons why private investors like power purchase agreements but also identifies what their limitations are, and outlines reasons why regulatory contracts differ from commercial contracts. The balancing act of the two competing objectives addressed in regulatory contracts is neatly captured by the authors: "The idea is to limit the discretion of the regulator in areas that are known to deter investment while at the same time using independent regulation to avoid uncertainties for investors created by political micromanagement and changes of government or governmental policy."*

*The authors also address the question of whether regulatory contracts should be a transitional mechanism in developing countries. They conclude that the underlying principles of regulatory contracts – performance-based, multiyear tariff setting systems – have been adopted successfully in developed countries.*

*Therefore, they are applicable to the regulation of private distribution systems in developing countries.*

[Basanes, Federico C., Eduardo Saavedra, and Raimundo Soto. 1999. Post-Privatization Renegotiation and Disputes in Chile. IFM116, Washington, D.C.: Inter-American Development Bank.](#)

*"Using Chile as a case study, this paper explains that disputes leading to renegotiation most often occur where regulation is incomplete, information asymmetry is high and regulatory institutions are less able to monitor the private operators. Conflict stemmed mostly from: (a) the existence of vertical integration, (b) the lack of definition of certain areas in regulation; and (c) the institutional weaknesses of regulatory bodies."*

[Ehrhardt, David, and Timothy Irwin. 2004. "Avoiding Customer and Taxpayer Bailouts in Private Infrastructure Projects: Policy Toward Leverage, Risk Allocation, and Bankruptcy," World Bank Policy Research Working Paper No. 3274, Washington, D.C.: The World Bank.](#)

*Using case studies and an empirical study, this paper examines how governments and regulators respond to the prospect of bankruptcy through analysis of the capital structure and risks involved in five infrastructure projects. The paper also presents an empirical framework for analyzing the effect of leverage and regulation so as to estimate the probability of bankruptcy given different degrees of leverage and risk. The final section of the paper identifies several options governments can use to increase the operator's financial capacity to assume risk, including: on balance sheet financing, parent company guarantees, minimum equity levels in the company undertaking the project, performance bonds, and third party guarantees. Alternatively, contracts could explicitly include risk-sharing mechanisms, such as rate-of-return bands and profit-sharing, trigger point resets, cost pass through mechanisms, and so-called "shipwreck clauses."*

Estache, Antonio. 2005. "PPI Partnerships versus PPI Divorces in LDCs." World Bank Policy Research Working Paper 3470, Washington, D.C.: The World Bank.

*"This paper examines the distributional effects and the historical context of PPI partnerships to explain why so many partnerships have failed while others continue to occur. Latin America with its richer developing countries has been the most successful region in attracting private investment. The next most successful are East Asian countries for electricity generation and distribution and Eastern Europe for telecommunications. For transportation, high-traffic road systems seem to be most successful in attracting private investment. Only 25 percent of rail system projects in 131 countries reported PPI arrangements for operations or management in 2003. The water sector has fared worst with these arrangements. The poorest countries have been least successful in entering into PPI arrangements.*

*Although short-run effects of PPI have been positive, the longer run situation is more complex because many countries eventually returned to subsidization for sectors other than transport, where inter-modal competition exists. With respect to the water sector, cream skimming has been fairly typical.*

*Reforms have increased access in most sectors in most regions, with greater access being realized in the telecommunications sector and the least in the water and sanitation sector. In terms of improved affordability, few countries paid much attention to tariff design and progressively targeted subsidies.*

*The establishment of autonomous regulators varies across country and sector; while not a sufficient condition for attracting PPI, the presence of such agencies might help. Reforms appear to improve efficiency, quality, and access but at higher fiscal and distributional costs than anticipated.*

*Finally, the paper examines the distributional effects of PPI by region and sector, as well as the user groups most supportive of PPI (bankers, some operators, mostly nonresidential users) and groups most likely to abandon PPI (politicians, NGOs, unions, taxpayers, residential users, and operators with bad PPI experiences). The author concludes that reforms have generally realized efficiency gains but have failed to improve the lot of the poorest. Politicians and the international community need to support developing tools of regulators to provide service efficiently and fairly. Opportunities for the private sector to assume more responsibility for minimizing operation and maintenance costs also needs more emphasis. Additional reform needs to take into consideration weaknesses of the capital markets. Greater transparency governing PPI transactions is needed. The new international accounting standards scheduled for 2006 should improve transparency, but strict enforcement will be required.*

Guasch, J. Luis, JeanJacques Laffont, and Stephane Straub. 2003. "Renegotiation of Concession Contracts in Latin America," Policy Research Working Paper No. 3011, Washington, D.C.: The World Bank.

*This paper takes an empirical approach to determining factors that contribute to the increased probability of concession contract renegotiations initiated by firms.*

*The existence of a regulator at the time the concession is awarded reduces the probability of renegotiation, but price cap regulation increases that probability.*

*Contracts exclusively financed by private money increase the probability, and minimum income guarantees do not appear to offer protection against shocks (contrary to expectations). Finally, the probability of renegotiation increases significantly in the years after a national election, which suggests that political cycles matter.*

Harris, Clive, John Hodges, Michael Schur, and Padmesh Shukla. 2003. "A Review of Canceled Private Projects." Note No. 252, Washington, D.C.: The World Bank.

*This paper reviews infrastructure projects that were canceled if one or more of the following events occurred before the end of the project's expected life, as determined in a contract or license: 1) the private company sold or transferred its economic interests in the project to the public sector, 2) the private company physically abandoned the project (such as withdrawing all staff from the project), and 3) the private company ceased to provide services to all customers or halted construction of the project for around 20 percent or more of the project's expected life following the revocation of a license or repudiation by the relevant contracting or licensing authorities.*

*The authors found that only 48 private infrastructure projects were canceled in 1990-2001, 1.9 percent of nearly 2,500 infrastructure projects that reached financial closure during that period. More than a third of the projects were from the Mexican toll road program.*

*The water sector had the second highest rate of cancellation (3.5 percent of projects canceled) followed by electricity distribution projects. Most water and sewerage and electricity sector projects were canceled because of problems with and controversies over price increases and payment collections from consumers.*

*In contrast, projects in the telecommunications sector were usually canceled because they failed to attract a sufficient customer base or the government decided to change the market structure.*

*Some of the projects encountered problems in the bidding phase, and more than half of the 48 projects encountered political and social opposition attributable to lack of transparency in the contract award or to alleged corruption and propriety. The authors recommend ensuring transparency in the award process, building public consensus for the reform, phasing in tariff increases, making judicious use of transitional subsidies, and being realistic in the user fee structure.*

The International Bank for Reconstruction and Development/the World Bank. 2005. *Doing Business in 2005: Removing Obstacles to Growth*, Oxford: Oxford University Press.

*"This report analyzes data from a large cross-section of countries to identify limits to economic development. The study finds that extensive regulation of business is a key limiting factor in economic growth. For example, if the government requires numerous approvals for a business to enter a market or to change in response to changing demand, beneficial business activity is limited, and both investors and consumers suffer. The report provides indices that represent the extent of economic regulation in a country."*

Tremolet, Sophie, Padmesh Shukla, and Courtenay Venton. 2004. "Contracting Out Utility Regulatory Functions, Environmental Resources Management."

*"Through use of a survey instrument, the authors gather information on regulators' reasons for contracting out, their experiences with it, and the critical decisions they had to make once the decision to contract out was made. The survey results indicate that the functions most contracted out are tariff reviews and output measures, although the supply of consultants is not considered abundant. Facing resource limitations, regulators are often forced in their contracting decisions to make choices between independence in decision-making, developing in-house competence, and improving agency legitimacy.*

*From an analysis of survey findings, the authors developed a conceptual framework to guide policymakers and regulators in their decision making ability. The survey instrument and case studies are included in this paper.”*

Wells, Louis T. 1999. “Private Foreign Investment in Infrastructure: Managing Non-Commercial Risk.” Harvard University. Preliminary draft presentation for conference, Private Infrastructure for Development: Confronting Political and Regulatory Risks; September 8-10, Rome, Italy.

*“This concept paper notes that contract instability is especially likely to occur if the host government or political opposition group receives information (however incomplete) about deals struck elsewhere that appear to be more favorable than the existing agreement. This paper explains the motivations for countries to seek contract renegotiations and for contract managers to resist them, and identifies renegotiations.”*

## COMMENT ON ENERY-SPECIFIC REGULATORY CONTROL

*Dr Charles Albano*<sup>241</sup> uses a chameleon for his logo to symbolize adaptive leadership. He describes adaptation as “*a dynamic process of mutual influence. All creatures act on their environments and their environments, in turn, act on them.*” He claims that organizations are capable of intelligent, purposeful, collective action, those taken to influence their environments in desired directions.

If regulators need to have adaptive leadership styles then they should be chosen carefully, bearing in mind that “*relationships between living entities are circular and interactive.*”

*Mark Jamison* as lead author of the majority of the studies cited here followed the 2004 literature review with a concept paper written the following year on Leadership and the Independent Regulator.<sup>242</sup>

*Jamison (2005)* claims that:

*“Regulators are sometimes scapegoats for unpopular policies and unavoidably become involved in shaping the policies that they are supposed to implement. As a result of such frictions, regulators are sometimes removed from office or marginalized in some way.”*

He recommends strategies by which adaptive leadership can be used to help constitutes to adapt to new policies and changing situations, whilst still staying in the game.

The foremost leadership skill recommended is the ability to:

*“...get on the balcony and see what is really going with operations, politicians, consumers and others - a meaningful engagement with all stakeholders.”*

I refer again to the work of the Energy Action Group (EAG) as a 27-year old non-profit organization focused in the main on energy issues relating to small consumers (less than 160 MWh per annum and 10 TJ/a. Members determine EAG policies and directions with activities covering both national and sub-national issues for the social action component of their work EAG has a policy of trying to work collaboratively with market participants and other consumer groups (like EUAA) on issues of common interest.

In its 2005 submission to the Ministerial Council on Energy on national electrically law and electricity rules<sup>243</sup> EAG expressed its particular disappointment.

*“.....with the MCE process to date as there has been little effective analysis of the strengths and weaknesses of the current NEM arrangements.”* Illustrating the point with the opening comment shown below:

*“Currently some \$17 B worth of network capital investment has either been approved or is in the process of being approved by the ACCC and the jurisdictional regulators to replace aging assets, to provide new investment for increased per capita consumption and new connections to the year 2009. At least \$6 to 7 B of the \$17B will be spent to meet summer peak load growth and continue the process of lowering the asset utilization curve!*

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<sup>241</sup>Albano, C (Dr.) Leadership Skills – What is Adaptive Leadership? 22 April 2007 found at <http://www.selfgrowth.com/articles/calbano.html>

<sup>242</sup> Jamison, Mark A. 2005. “Leadership and the Independent Regulator,” Public Utility Research Center, University of Florida, Gainesville, Florida.

<sup>243</sup> EAG Submission to Ministerial Council on Energy National Electricity Law and National Electricity Rules 2005

*There has been a noticeable deterioration across the NEM in the networks annual load duration curve due to the increase in temperature dependant summer peak loads. This outcome also requires new generation investment particularly gas peaking plant. (The only exception to this outcome appears to be Tasmania.) This is not an economically efficient market outcome!*

*The current market arrangements fail to effectively allocate the summer peak load costs to the source of the demand.*

*Almost all market participants obtain significant rewards from summer peak load growth, even host (1<sup>st</sup> tier) retailers.*

*This is one of the most significant outcomes to come from the old NEC.*

*The new NEL/NER fails to address the issue rewarding inefficient summer peak load growth providing a policy setting to address this issue!*

*It is EAG contention that the NEL/NER acts as a behavioural driver on market participants and one of objective of this new package should be to address some of the deficiencies of the Code.*

I again urge the Commission to examine the critical input by Gavin Dufty, Social Scientist, St Vincent de Paul in his 2004 VCOSS Paper examining government policy and attitude in relation to Universal Service Obligations<sup>244</sup>

There is so much that remains unaddressed. I am only too well aware of poor funding and staffing levels and poor support generally. Until or unless strong leadership, independence, adequate funding and active consumer participation, including end-user participation, consistent with grounding theories as embraced by David Tennant, Director of Care Financial Inc. NSW, are included the consumer policy framework agenda. An outcomes based consumer policy agenda is what is required. This has been lacking to date. Therefore the current Productivity Commission enquiry is crucial with recommendations awaited with bated breath.

However, much more than consumer involvement is required. As observed by Energy Action Group, “*numbers, expenditure and price and behaviour drivers*” are crucial factors in the equation. There seems to be little evidence that these complex factors have been carefully considered in the rush to effect energy reform with full price deregulation to complete the FRC cycle. In particular behavioural economics and best practice evaluative processes have been sadly neglected in the rush to uphold apparently pre-determined decisions with less than optimal commitment to or value placed on

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<sup>244</sup> Refer for example to G Dufty “Who Makes Social Policy?– The rising influence of economic regulators and the decline of elected Governments. VCOSS Congress Paper 2004<sup>244</sup> and Tamblyn, J. Powerpoint presentation at World Forum on Energy Regulation, Rome September 2003 “*Are Universal Service Obligations Compatible with Effective Energy Retail Market Competition?*” John Tamblyn was the Chairperson Essential Services Commission Victoria. He is now Chairperson of the AEMC.

## COMPLIANCE ISSUES

The ACCC has already formally expressed increasing concern “with merger parties” attitude towards undertakings.<sup>245</sup>

Of public concern is the issue that if, despite formal undertakings by energy providers, either upstream or downstream or more narrowly within the retail market component, are being breached, what is likely to happen if and when deregulation becomes a reality.

In 2004 a consortium comprising Alinta, DUET and Alcoa had secured approval from the ACCC for its proposal to acquire the DBNPG after agreeing to court enforceable undertakings. Those undertakings became the subject of Federal Court rulings against Alinta 200 Ltd for breach of the undertakings with costs awarded to the ACCC.

On 12 October 2006, Freehills had reported as follows:<sup>246</sup>

*The Australian Competition and Consumer Commission (ACCC) instituted proceedings in the Federal Court, on 14 September 2006, against Alinta Ltd for breach of undertakings provided to the ACCC in 2004. Alinta made the alleged undertakings as part of a consortium which obtained ACCC approval for the acquisition of the Dampier to Bunbury natural gas pipeline (DBNGP). The ACCC alleges that in breach of the undertakings, an Alinta employee was involved in negotiations between DBNGP Holdings and other shippers. These proceedings have been brought at a time when the ACCC is emphasising the importance of compliance with the ‘spirit’ of undertakings, as well as technical compliance with the terms.*

*Alinta’s conduct comes at a time when the ACCC is becoming increasingly concerned with merger parties’ attitude towards undertakings. Many merger parties have engaged in conduct, which while technically compliant with undertakings, is inconsistent with their spirit. To address such conduct the ACCC has indicated that it will include a good faith clause in all future undertakings and possible inclusion of a preamble setting out the concerns that the undertaking is addressed to concern.*

The ACCC reports that<sup>247</sup><sup>248</sup> the outcomes of the action taken by the ACCC against Alinta in *Australian Competition and Consumer Commission and Alinta 2000 Ltd* produced a positive outcome for the ACCC and for competition in Australia in relation to breach of Section 87B undertakings. In reporting the outcomes, these words were used on behalf of the ACCC in their Media Release on 29 August MR 235/07

*“The Federal Court has made orders settling the litigation between the Australian Competition and Consumer Commission and Alinta 2000 Ltd by consent of the parties.*

*The Federal Court has made orders settling the litigation between the Australian Competition and Consumer Commission and Alinta 2000 Ltd by consent of the parties.*

*The orders include a declaration that Alinta breached section 87B undertakings and an order that Alinta pay the ACCC's costs.”*

*“In September 2006, the ACCC filed proceedings against Alinta Ltd (now known as Alinta 2000 Ltd) in the Federal Court for breach of the undertakings under section 87B of the Trade*

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<sup>245</sup> Freehills online report 12 October 2006, “ACCC accuses Alinta of breaching undertakings” found at [http://www.freehills.com.au/print/publications\\_6178.html](http://www.freehills.com.au/print/publications_6178.html)

<sup>246</sup> Ibid Freehills Report 12 October 2006

<sup>247</sup> ACCC 29 August 2007 Media release MR 235/07 Federal Court declares Alinta breached s87B undertakings” <http://www.accc.gov.au/content/index.phtml/itemId/797046/fromItemId/2332>

<sup>248</sup> See Also Sydney Morning Herald 29 August 2007 Alinta breached pipeline undertakings



*Practices Act 1974 that Alinta gave to the ACCC at the time of its part acquisition of the Dampier to Bunbury Natural Gas Pipeline in Western Australia.”*

*“The Federal Court has ordered the following:*

- *a declaration that at all material times from 23 January 2006 until 6 October 2006, a member of Alinta staff was in a position in which she was involved in commercial negotiations between DBNGP Holdings Pty Limited and gas shippers*
- *a declaration that Alinta's conduct in transferring the member of staff into the above position, and permitting her to remain there in circumstances where Alinta Ltd knew that she was involved in commercial negotiations with gas shippers, constituted a breach by Alinta of the undertakings, and*
- *an order that Alinta pay the ACCC's costs.*

*"This is a positive outcome for the ACCC and for competition in Australia," ACCC Chairman, Mr Graeme Samuel said today. "The undertakings were put in place to ensure that Alinta's competitors were not negotiating with Alinta staff about their use of the pipeline.”*

*Alinta breached pipeline undertakings*

*"The situation that arose was unacceptable and constituted a real risk to competition. The ACCC takes 87B undertakings extremely seriously and will pursue breaches of these undertakings to the full extent of the law."*

The background to this matter as reported by the ACCC on 29 August 2007 is as follows:

*Alinta purchased a 20 per cent interest in the pipeline in October 2004 and its subsidiary, Alinta Asset Management was appointed to assist in managing the pipeline. In order to address potential competition issues arising from that fact that Alinta would become an owner and manager of the pipeline, as well as a shipper on the pipeline, the ACCC required Alinta to give undertakings to the ACCC to address its competition concerns.*

*The undertakings sought to prevent Alinta from using its part ownership of the pipeline and management role, to discriminate against other gas shippers that used the pipeline. In particular, the undertakings provided that no member of staff of Alinta was to engage in commercial negotiations between the company charged with operating the pipeline and other shippers on the pipeline.*

There has been recent Federal and Supreme Court action<sup>249</sup> concerning clarification as to the proper interpretation of the Gas Industry Act and the National Gas Access Code. The Essential Services Commission believed that an **asset management group**, even an “agent” capacity, such as that contracted to Alinta (Alinta Asset Management, AMM), to Envestra (AAP, previously Origin Energy Asset Management). This is part of seeking clarification of the current framework for the economic regulation of gas pipelines in Australia. On 15 June 2007 there were three matters upon which special leave applications were sought for hearings before the Supreme Court in Sydney as appeals from the Federal Court. Two applications for hearings were granted, and the third referred to the full court. Details are shown below.

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<sup>249</sup> Federal Court declares Alinta breached s87B undertakings Federal Court declares Alinta breached s87B undertakings Statement re Court Action by Alinta Asset Management 13 September 2006 Essential Services Commission

**LIST OF BUSINESS FOR SITTINGS AT  
SYDNEY FRIDAY, 15 JUNE 2007 SPECIAL LEAVE APPLICATIONS TO BE  
HEARD IN SYDNEY**

<i>No.</i>	<i>Applicant</i>	<i>Respondent</i>	<i>Court appealed from</i>	<i>Results</i>
1.	Attorney-General of the Commonwealth	Alinta Limited & Ors (S207/2007)	Federal Court of Australia (Full Court) [2007] FCAFC 55	<b>Granted</b>
2.	Australian Pipeline Limited	Alinta Limited & Ors (S226/2007)	Federal Court of Australia (Full Court) [2007] FCAFC 55	<b>Granted</b>
3.	Alinta Limited & Ors	Australian Pipeline Limited (in its capacity as responsible entity of Australian Pipeline Trust) & Anor (S245/2007)	Federal Court of Australia (Full Court) [2007] FCAFC 55	<b>Referred to Full Court</b>

In its most recent Competition and Market Report Freehills conveyed the outcome of the Supreme Court appeal by Alinta Asset Management (AAM) against Essential Services Commission. On 22 August 2007 the Supreme Court ruled that AAM must hold a gas distribution licence in order to operate the Multinet Gas distribution network, and must comply with the requirements of the national Third Party Access Code for Natural Gas Pipelines systems.

**High Court of Australia** \_\_\_\_\_

**LIST OF BUSINESS FOR SITTINGS AT CANBERRA BEFORE THE FULL COURT COMMENCING ON TUESDAY, 25 SEPTEMBER 2007**

6.	Attorney-General of the Commonwealth	Alinta Limited & Ors (S331/2007)	Federal Court of Australia (Full Court)
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## **THE PUBLIC INTEREST TEST AND SOCIAL IMPACTS ASSOCIATED WITH COMPETITION POLICY – IN THIS CASE ENERGY REFORM – some broad reflections**

*“Market forces are global, but the social fallout that policy makers have to manage are local”<sup>250</sup>*

That was the opening line of Chapter 5 of the Senate Select Committee’s SSC Report on the Socio-Economic Consequences of Competition Policy.<sup>251</sup>

The first observation made by the SSC in this chapter was the impact of specific infrastructure investment (e.g. the Snowy Mountains Scheme) on urban concentration and the impacts on rural and regional Australia in response to wider economic and social currents.

Whilst the Senate Committee did not seek to duplicate the work done by the Productivity Commission, and the Committee confirmed that there were overall benefits to the community of national competition policy, it found that those benefits had not been distributed equitably across the country. Whilst larger business and many residents in metropolitan areas or larger provincial areas made gains, residents from smaller towns did not benefit from NCP.

The Productivity Commission’s findings had produced estimates that were subject to variation. What the Committee had been concerned to ensure, was that the impacts of the policy are monitored in a rigorous fashion and the results of such monitoring are reported to policy-making authorities

Social commentators had found that

*Structural change (had) also left a growing group of so-called ‘battlers’ in comparatively low-paid jobs, poorly organized and reliant on a relatively stagnant minimum award wage structure. As these people slip behind the rest of the population (including fellow workers able to benefit from enterprise bargaining), they feel insecure and as bitter and resentful of people of people on welfare as they are of the ‘tall poppies’*

Social services were not shown to improve during NCP

The SSC took seriously the suggestions in many submissions that some aspects of NCP and its administration would appear to be in conflict with the principles of good health, community and social welfare service provision.

Whilst not negative changes were found to be

*“.....as a result of NCP or indeed micro-economic reform generally,” the Committee found that there was “potential there for the NCP to worsen the impact of rural downturn, industrial changes, globalization etc...”*

The Committee acknowledged the right of the Australian community to “be informed of the costs of the policy, particularly through clear identification of social change, hardship and environmental costs.”

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<sup>250</sup> Western Australian Parliamentary Standing Committee on Uniform Legislation and Intergovernmental Agreements, Competition Policy and Reforms in the Public Utility Sector, Twenty-Fourth Report, Legislative Assembly, Perth, 1999, p xvii

<sup>251</sup>“Riding the Waves of Change” A Report of the Senate Select Committee Ch 5 the Socio-economic consequences of national competition policy. 2000 found at [http://www.aph.gov.au/Senate/Committee/ncp\\_ctte/report/c05.doc](http://www.aph.gov.au/Senate/Committee/ncp_ctte/report/c05.doc)

The Productivity Commission had “identified job losses by infrastructure providers in its latest report, and justified these losses in terms of improvements in efficiency. The adverse impacts of these employment losses can be compared to the impacts of the early tariff reductions on the manufacturing industries.”

A significant finding of the Senate Committee Report was that:

*“To improve efficiency, State governments have sought to address overstaffing in their electricity utilities. This saw total employment in the electricity supply industry decline from slightly more than 80,000 in 1985 to around 37,000 in 1997....much of this decline occurred prior to implementation of the NCP in 1995. However reductions in employment have continued since then...”<sup>252</sup>*

*“The Committee doubt(ed) that the benefits of NCP will ever be able to be satisfactorily measured. The Commissions’ attempts are praiseworthy but they are estimates subject to variation. What the Committee is concerned to ensure, is that the impacts of the policy are monitored in a rigorous fashion and the results of such monitoring are reported to policy-making authorities.”*

The impact of NCP on social welfare was discussed extensively in the Senate Committee’s Report

In particular the Committee examined:

1. Whether or not the supply provision of social welfare services health and related services had been adversely affected by the introduction of NCP; and
2. Secondly whether there was a need for structural adjustment assistance or transitional assistance for those adversely affected by NCP

The Committee noted how many social, welfare and medication organizations had supported the view that *some aspects of NSP and its administration would appear to be in conflict with the principles of good health, community and social welfare service provision*

It has been suggested that some aspects of NCP and its administration would appear to be in conflict with the principles of good health, community and social welfare service provision.

In commenting on the impact of the provision of social welfare services, health and related services the Report continued

*“.....the local area seems to be where the problems surface first and, in the old structure, we were able to try and jump on that very quickly. I am not saying that is the answer to everything-there are a lot of bloody awful services out there that should have been defunded-but I do feel that the move to competition as the answer to that is actually causing much more fragmentation. Also, from the ground, it is the most incredible waste of money I have ever seen in my life. “*

*“Many people feel that this marketplace stuff has got out of hand. To some extent, in my mind, national competition policy is seen as this marketplace ideology writ large. We want to see a benefit that has more social value for people in their lives.”*

The concern is how the Productivity Commission intends to meet the gap when the Commonwealth is required to meet the needs of the low fixed-income vulnerable and disadvantaged groups (not simply on financial hardship grounds), when price deregulation becomes a reality as is predicted.

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<sup>252</sup> Productivity Commission, Impact of Competition Policy Reforms on Rural and Regional Australia, Inquiry Report, No 8, September 1999, p 108.

Will the compensatory services following price deregulation and removal of the safety net be contracted services of a similar standard to what has been bluntly deemed by the Select Senate Committee as “bloody awful services that should have been defunded.....”?

The SSC predicted

*“An unintended consequence of changes to the way social welfare services are funded, would appear to be these additional administrative costs. Further, it is evident that narrow cost/benefit analysis is not capable of examining many of the social factors involved the application of NCP in the social welfare sector.”*

There were problems recognized with project commencement requirements; funding issues; systems parameters; best practice recruitment parameters; continuity of funding

There were recommendations that data collection should be qualitative and not merely quantitative.

The SSC recognized the need for robust assessment of impacts of various policies adopted.

It is not enough to rush enthusiastically into reform of the magnitude envisaged and imminent for energy infrastructure regulatory and economic change.

These cautions are included here as they have already been identified upon robust enquiry to by problem areas. The whole community shares concerns about writing off standing offer arrangements not only in terms of how these will negatively impact on social welfare factors, but also in terms of how these offers or “*price to beat*” arrangements may actually detract from competition and inform consumer choice<sup>253</sup>

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<sup>253</sup> As noted by Gavin Dufty for St Vincent de Paul Society in the November 2007 submission to the AEMC Retail Competition First Draft, page 4

The Select Senate Committee had made these recommendations in Ch 5 of their 1999 Report<sup>254</sup>:

“Recommendations

14. *That all reviews of legislation and changes to competitive arrangements in the social welfare sector adhere to the broad principles of the public interest and take account of the difficult to measure social factors rather than relying on narrow, more easily measurable, economic factors. That all contracting out arrangements and competitive tendering processes and documentation in the social welfare sector be public and transparent. There should be a presumption that all documents will be public and any claims of commercial confidentiality should be kept to a minimum and where essential.*
15. *That Governments critically examine competitive tendering processes for social welfare services with a view to ensuring that a sophisticated and flexible approach is taken to the provision of service. The process should consider as part of the public interest test: quality, consistency and continuity of service; the value of local co-operative arrangements and the personal nature of such service.*
16. *That, where appropriate, the Commonwealth Departments of Health and Aged Care and Community Services, examine competitive tendering programs and determine which services are properly and efficiently competitively tendered and which may be contracted out on a benchmark of service basis. Particular attention should be paid to rural and remote communities where locally provided co-operative services may be integral to the success of service delivery. “*

Another important recommendation of the SSC was in relation to impacts on urban, rural and regional communities expressed as follows:

*“For rural development policies to be successful there needs to be a greater focus on people. Perhaps the best way to achieve this is by emphasizing the value of social obligations rather than the 'rights' of self-interested individualism. Conventional wisdom stresses the importance of competition rather than community. While the current approach to rural development, at the very least, recognizes the importance of rural Australia, successful achievement of its objectives requires a more critical consideration of the dominant neo-liberal approach to policy-making.”*

*However, only under very special circumstances will the process of adjustment generated by unfettered market forces be socially optimal. Processes of economic contraction are likely to proceed excessively rapidly as the loss of one area of economic activity imposes external costs on others.*

Finally, because of time constraints here I quote from the same chapter of the SSC Report on the impacts of micro reform

*“.... (the) “impact of micro reform is becoming more and more severe in terms of its effects. And it is becoming harder, for fiscal and other reasons, to smooth the social effects.”*

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<sup>254</sup> A Report of the Senate Select Committee on the Socio-economic consequences of national competition policy, Ch 5 found at [http://www.aph.gov.au/Senate/Committee/ncp\\_ctte/report/c05.doc](http://www.aph.gov.au/Senate/Committee/ncp_ctte/report/c05.doc) Found at [http://www.aph.gov.au/Senate/Committee/ncp\\_ctte/report/c05.doc](http://www.aph.gov.au/Senate/Committee/ncp_ctte/report/c05.doc)

It was recognized that

*“In the small rural centres of Australia, the circumstances befitting perfect competition are most unlikely.”*

Deregulation of professions and centralization of policies of government departments were considered amongst other factors to have a detrimental social impact on rural populations.

As far back as 1999 in discussions about National Competition Policy generally it was recognized that anger in the many rural populations had metamorphosed into fatalism and the feeling that the government had left the negotiating table.

It can only be hoped that the energy reforms will not lead to outcomes like that for the vulnerable groups and populations, and that the remainder of the Australian population does not become even more disillusioned than they are about the general and specific impacts of the proposals envisaged in terms of the social and welfare prices that will undoubtedly be paid.

Besides that there is the question of the smaller energy companies, the second-tier retailers simply trying to retain liquidity and a small share of the market. They too must be given every support since in some ways they will potentially share the same position of facing power imbalance detriments, fear of uncertainty and worse than that fear of being swallowed up by the giants. Powerdirect has already seen that happen as the inaugural second-tier retailer.

Dr. S. Dovers of the Australian National University is quoted by the SSC as saying:

*“Anyone who has played junior football can impart the invaluable lesson that a level playing field, set rules and fixed goal posts - the stuff of healthy competition - matter little when someone twice your size charges at you. Just as big firms can (and do) run over and flatten small firms in a "fair and competitive" market, so it is that weakly institutionalized policy considerations can be easily outweighed by strongly institutionalized ones. Thus it is for ESD, and the lack of institutionalization is evidenced in comparison to other public policy fields. Even official sustainability policy states that environmental, social and economic policy should be balanced and integrated, and this means that there should be some degree of parity in policy processes.”*

With those reservations in mind it is important that sufficient lead time is allowed to plan for the price and social impacts that will leave possibly half the population at risk of shell-shock and disadvantage when price deregulation becomes a reality.

The SSC had received many submissions and other evidence on these issues in particular:

The inadequacy of the NCP legislation and agreements;

- The inadequacy of State legislative review processes;
- Pricing, subsidy or regulatory distortions having adverse environmental impacts;
- Fundamental issues of private versus public ownership of natural resources;
- Adverse social impacts of water pricing reforms: and
- The inadequacy of the application of the public interest test.

In Chapter 4<sup>255</sup> of its Senate Select Committee Report “Riding the Wave of Change” reference was made to a recurring theme identified in the interim report. These related to difficulties in the way in which National Competition Policy had been implemented. Prominent amongst those difficulties were problems with interpreting and understanding the Public Interest/Public Benefit Test, including these factors:

- a lack of understanding of the policy;
- a predominance of narrow economic interpretation of the policy rather than wider consideration of the externalities;
- a lack of certainty between States and Territories as differing interpretations of the policy and public interest test, result in different applications of the same conduct;
- lack of transparency of reviews; and
- lack of appeal mechanisms.

The Committee’s reservations were confirmed by the responses received to the Interim Report. The SSC formed the view that failure to properly explain the NCP had contributed to these serious problems. Policy and rule-makers need to make sure that the policies proposed are not only well understood by stakeholders but by themselves, with a thorough understanding guaranteed for those directly affected, or the broader public. This cannot be achieved without effective communication, timely provision of all protocols and documentation relied upon, and meaningful and timely stakeholder dialogue. That dialogue should be ongoing, and open. It should not be restricted to chance availability to respond to numerous consultation initiatives with overlapping deadlines.

The mechanism should exist for informal dialogue and proactively sought inputs from all stakeholders. This should apply to every avenue of public policy with the principles of transparency and accountability being paramount.

Chapter 6 of the SSR of 2000 referred to the essence of the Interim Report in which the Committee had canvassed the difference between the public interest test of the NCP and the public benefit test of the ACCC as follows:

*“The need for public debate and understanding has not diminished.*

*Public benefit has been and is given wide ambit by the Tribunal as, in the language of QCMA (at 17,242), ‘anything of value to the community generally, any contribution to the aims of society including as one, of its principal elements (in the context of trade practices legislation) the achievement of the economic goals of efficiency and progress’. Plainly the assessment of efficiency and progress must be from the perspective of society as a whole: the best use of society’s resources. We bear in mind that (in the language of economics today) efficiency is a concept that is taken to encompass ‘progress’ and that commonly efficiency is said to encompass allocate efficiency, production efficiency and dynamic efficiency.”<sup>256</sup>*

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<sup>255</sup> Chapter 4, The Public Interest Test in “Riding the Wave of Change, Report of the Senate Select Committee 2000

<sup>256</sup> Victorian Newsagency Decision, ATPR 41-357 at 42,677.



Clause 1(3) of the Competition Principles Agreement provides that Governments are able to assess the net benefits of different ways of achieving particular social objectives.

Quoting directly again from Ch 6 of the SSR Report of 2000

Without limiting the matters that may be taken into account, where this Agreement calls:

- a) *for the benefits of a particular policy or course of action to be balanced against the costs of the policy or course of action; or*
  - b) *for the merits or appropriateness of a particular policy or course of action to be determined; or*
  - c) *for an assessment of the most effective means of achieving a policy objective;*
- the following matters shall, where relevant, be taken into account:*
- d) *government legislation and policies relating to ecologically sustainable development;*
  - e) *social welfare and equity considerations, including community service obligations;*
  - f) *government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;*
  - g) *economic and regional development, including employment and investment growth;*
  - h) *the interests of consumers generally or of a class of consumers;*
  - i) *the competitiveness of Australian businesses; and*
  - j) *the efficient allocation of resources.*

The Committee continues to be concerned about the application of ‘public interest’ given the confusion that exists over what the term means or allows under NCP. The confusion, when

*“...combined with the administrative ease of simply seeking to measure outcomes in terms of price changes, encourages the application of a narrow, restrictive, definition. The Committee considers that it is important to devise a method of assessment of the policy which attributes a numerical weighting to environmental and social factors to avoid the over-emphasis on dollars merely because they are easy to measure. Mr. Waller advised the Committee that:*

*“In summary, it is a difficult area. There are problems of methodology, there are problems about the practical application of the policy. Underlying all this, I would say that I think that, in net benefit terms, the national competition policy arrangements are of major value to Australia in meeting the problems it faces globally.”<sup>257</sup>*

*“The Committee recognizes the argument that the NCP has contributed to Australia’s success in meeting the problems it faces globally, particularly, the economic shocks that came out of the “Asian melt down”. However, even if it is accepted that that is the case, the country’s overall ability to cope internationally is not always fully appreciated in the face of lost jobs, reduced pay and conditions, failing or lost social infrastructure, or the other adverse consequences of structural change that are perceived to be attributed to NCP.”*

*One of the most significant statements made in this chapter is of direct relevance to the proposed infrastructure reforms.*

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<sup>257</sup> Mr M Waller, Committee Hansard, 1 November 1999, p 841

I quote directly from the statements made by Mr. Ritchie National Farmers Federation in his dialogue with Senator McGauran:

*Mr RITCHIE—My assumption is that obviously we support some of the initial gains that have been made under national competition policy, but in areas such as infrastructure, NFF is starting to have some real, serious concerns. The picture that Rod Nettle painted about what is going to happen to rural and regional Australia is not a difficult picture for us to extrapolate to, either. If you apply a strict principle of user pays to the provision of infrastructure, then you are not going to have a rural and regional Australia to worry about in 25 to 50 years because nobody out there can afford to pay.*

*This is the whole principle of externalities under which economic theory had been working for 100 years until we decided to throw it out in 1994. Let us go back and see if that was a sensible decision to throw out the principle of externalities and external benefits.*

At 9.30 AM on 1 November 1999 a group of most distinguished participants comprising the Select Committee on the Socio-Economic Consequences of the National Competition Policy met to discuss a range of issues associated with competition impacts on the community at large, and on social and welfare parameters in particular applying the public interest test.

The Chairman opened the proceedings with an outline of the enormous number of issues that needed to be discussed in examining the operation and administration of the national competition policy on the community and environment and to receive feedback on the issues raised in the committees interim report and in the reports from other inquires, and to look for possible solutions.

The Committee was given the impossible task of not only discussing the issues on the table, but also of presenting its report within the last sitting day in December 1999, which a guess would have been within a five week period.

That was eight years ago almost to the day. The witnesses were asked to give evidence and were offered indemnity under parliamentary privilege to encourage frank discussion

I have not had the time to study that report or to glean insights as to the findings. I chanced upon the report and before filing it away for future more leisured reading, I grasped the opening lines

Looking as if he were “*champing at the bit.*” Graeme Samuel, President National Competition Council, was invited to make opening comments. He chose to focus on the definition of the term public interest – which he said defies all attempts at further definition, because “the public interest is as broad as it is long, but it endeavours to encompass what the two words suggest—that is, the public and the interests of the public.”

The best I can manage is to direct readers to the reservations that have been expressed my multiple community organizations and consumer policy advocates many times over, and especially in the lead-up to full retail competition in 2003.

As a newcomer, I needed a starting pint for examining what has been happening in the market. I wanted to know what people had thought about the original proposal to implement FRC in the energy industry; whether there had been any well-considered evaluations undertaken; what detriments had been discovered.

The more I searched the less time I had to read solely what had been put forward as justification for the decision that appears to be so imminent to substantially lift the regulatory burden before even the completion of the Inquiry into Australia's Consumer Policy Framework or its initial Draft Report, and without any informed prediction about the impact of the proposals on the community, their "*switching behaviour*" that has been put forward as upholding the decision soon to be made. I was also mindful of the some of the pitfalls of starting to consider price deregulation.

The more exposed I became to the phenomenal range of issues that needed to be addressed, the more I realised that even if events and other pressures had not overtaken me,

I had no chance of grasping the range of issues that needed to be taken into account, given the huge volume of documentation to be sourced and studied, not only on the basis of what the AEMC had commissioned and published, or what stakeholders had submitted to date, but also because I felt it would be entirely unrealistic to make an informed input without casting a wider net in endeavouring to make a lay assessment of the huge impact that the proposed energy reforms will have on this community

From the outset I had felt that endeavours to "*scope*" for the issues at hand had not begun to scratch the surface. I was concerned about the quality of the evaluative process and will briefly comment on this later.

Others have already published concerns about the quality and interpretation of the data relied upon in AEMC deliberations to date to support perspectives that retail competition has been successful; that switching behaviour as described in the Retail Policy Draft Report dated 5 October 2007 supports this view and that Australia is ready for the next step in completing the deregulation cycle – that of price deregulation and considerable lightening of the regulatory burden.

Graeme Samuels in 1999 during the dialogue about the socio-economic impacts of competition policy referred to above began his musings with observations of the more sinister aspects of the public interest – what he had previously described as attempts by those "having a vested interest to claim the retention of their vested interest

He suggested that:

*"one of the objectives of competition policy is to subject those claims to a rigorous, independent, transparent test to see whether, in fact, vested interests are being protected or whether public interests are genuinely being served by the restrictions on competition that are the subject of reviews under the Competition Principles Agreement.*

He then went on to discuss the level of guidance should be provided to agencies involved and various tiers of government at national state and local level, so that they could gain a "better understanding of the way that the public interest issue should be considered.": He was not satisfied that this had been achieved with the best success levels.

The first measure is then is for governments to determine guidelines as to the application of the public interest test to offer the best level of assistance to those that are applying the test in its application.

He identified three areas of public interest that needed as a first-line to be taken into account – that any reviews of legislation is undertaken independently, rigorously and transparently, in order to ensure that enough material was received from stakeholders

*"that presents the genuine public interest as distinct from material being received from vested interests that are purporting to represent the public interest."*

His recommendations went beyond recognition of public interest parameters, the rigorous application of the public interest test and the principles of transparency and accountability. He felt that “the public interest should have been applied right throughout the process of competition policy.

Mr. Samuel saw a place for reexamining why and whether state legislation and regulation should have been exempted from s51 of the Trade Practices Act. This had been achieved by lobbying governments, not by being subjected to rigorous public interest test.

The cynics have suggested that the reason they secured exemption by transparent public interest assessment.

Following Alan Fells’ explanation of the examples in the wine growers and medical fields.

Senator Murray sought some clarification as to how switching gas water electricity and so on to more competitive practices were differentiated in the public interest analysis and the perceived consequences, baring in mind the social issues and the essential nature of these services. He referred to the industrial relations Commission philosophies regarding safety net considerations, and compared this philosophical approach to that of the ACCC and ASIC..

*“The process of those reviews is, as we have said on many occasions, to be conducted independently, transparently, objectively and rigorously. Those reviews have the capacity to examine all the options and to examine all the issues of public benefit that have been established in case law, in practice and in commission decisions through authorization processes over the past 25 years. You have got all the capacity to do that and you should, in fact, do it. They involve considerations, not only of economic issues, but also of social issues. Indeed, the Competition Principles Agreement in clause 1(3) lists only one economic issue, that of economic efficiency, amongst the seven, eight or nine—I forget the exact number—issues that need to be considered where relevant and where appropriate in the area of public benefit assessment.”*

*The others, as you will know, relate to employment issues, ecological issues, environmental sustainability, occupational health and safety, social welfare, equity considerations, regional employment and regional development. There are a whole lot of issues there that are listed and they are not exclusive. They are inclusive. Social issues and social relevance is very much a part of competition policy and ought to be applied with all the wealth of experience that has been developed over the past 25 years in the administration of the authorization of public benefit and public interest tests.”*

There are cautions about the tactical shift by industry groups, home and abroad and pertinent questions as to whether such a shift is motivated by a confluence of self-interest. In the area of goods, it is easy to say that growing competition from inexpensive imports that do not meet voluntary standards and a desire to head off liability lawsuits and pre-empt tough state laws or legal actions that may have resulted from a laissez-faire response to policies in place.

One interesting US example is the case of the Altria group, owner of the cigarette manufacturing firm Phillip Morris. The unexpected proposal was made by that group to allow the F.D.A. to regulate the manufacture and marketing of tobacco products. Such legislation is pending in the US. Critics are saying that this is a bid by Phillip Morris to weaken opposition to cigarettes by working with the government, and could help the company maintain its market share.

Reducing regulatory burden is a long-time goal of the Productivity Commission in Australia as well as of other bodies. It is commendable if the outcomes for all concerned are equitable. The energy industry in Australia appears to be super-enthusiastic about the changes proposed putting forward well-structured and plausible arguments in the interest of least burdensome regulatory control. What will be the consequences for consumers?

Rosario Palmieri, a regulatory lobbyist at the US National Association of Manufacturers, a body that has often opposed government regulations, is reported as observing the change with equanimity.

The Director of Regulatory Policy OMB Watch (Office of Management and Budget) of the Washington group that tracks regulatory actions has never seen so many industries joining the push for regulation. He poses a pertinent question: will this achieve a real increase in standards and public protections or simply serve corporate interests?

Of the US situation Sarah Klein, a lawyer at the Centre for Science in the Public Interest is seeking to examine the problems created by a failed voluntary system in the grocery store and produce grower segment.

Ms Klein sees the situation as a strange bedfellow one where community organizations and watchdogs are putting into place national regulatory frameworks for quite different reasons to those of industry players. Says Klein:

*“.....industry officials, consumer groups and regulatory experts all agree there has been a recent surge of requests for new regulations, and one reason they give is the Bush administration’s willingness to include provisions that would block consumer lawsuits in state and federal courts.”<sup>258</sup>*

It is more than interesting that some of this thinking is reflected in the conceptual model proposed by Arthur Allens Robinson in the Consultation Framework recommendations.

Some are saying that it is like Christmas in particular industries. However, many clauses are being challenged in the US courts where they block the inherent right of individuals to seek seamless redress through the courts and are not theoretically expected to rely on advocacy and alternative dispute models alone.

In the New York Times Opinion article dated **16 September 2007**<sup>259</sup>, still on the subject of uniform regulation and in the case of toys, for example, mandatory testing is believed to be a good idea in principle. However, it is observed that “unless the rules are backed up with vigorous enforcement, the government’s imprimatur could give parents a mistaken sense of security. For any set of government standards to work (in this case safety, but applicable to other matters) the Consumer Product (or in the case of Australia Goods and Services) must be able to enforce companies’ compliance with spot checking of compliance and policing.

For such policing to occur in the energy industry in Australia resources are required. Will the state or the federal government have those resources to ensure enforcement, and in the case of those who find a way to shift the goal posts and escape or ignore enforcement strategies, even when generic provisions are relied upon, that may provide a challenge?

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<sup>258</sup>New York Times September 16, 2007 In Turnaround Industry seeks US legislation <http://www.nytimes.com/2007/09/16/washington/16regulate.html?pagewanted=2&th&emc=th>

<sup>259</sup>New York Times September 16 2007 Editorial Opinion. The Need for Regulation

Without meaning to be unnecessary skeptical, but influenced by the US experience that has recently received press coverage, perhaps all responsible parties will see fit to carefully examine each proposal to lighten the regulatory burden that comes from industry and seek

*“to understand the full consequences of regulations on all citizens.”*

At present, within the energy industry benchmarks of best practice consumer-focused service deliveries and protections may have become a blurred and inaccessible partly because of under-funding and resourcing, but also perhaps because of policies that are weighted from the outset in favour of industry<sup>260</sup>.

There is also the question of procedural inertia. Without a dedicated research and policy body such as has been suggested by CHOICE (ACA) and other community organizations these gaps will continue to compromise proper protection.

The public has never felt less confidence that their rights will be upheld or that justice will be readily accessible. Theory and practice gaps have become more noticeable despite myriads of guidelines in place. Enhanced education of key energy regulatory staff and complaints scheme staff may not go astray.

Current strategies in heralding reform measures are thought by many to be lacking in the department of meaningful dialogue. Not that the dialogue is not occurring, but there are queries about how meaningful that dialogue is; how well the consumer voice and other voices are being heard; the extent to which airing and meaningful reciprocal dialogue is occurring with stakeholders in time to make a difference before new regulations are put in place.

In a climate of rushed policy change such as is envisaged, and in the light of the tensions and apprehensions apparent on both sides of the fence, all stakeholders are begging for more certainty and stability that they perceive to be offered, improved meaningful dialogue and longer timelines to give effect to the theory of stakeholder consultation.

The public at large is also looking for improved transparency, such as publishing of all external reports relied upon (one example may be the AEMC contracted survey to Wallis Consulting – perhaps the public can have full access to the entire report with conclusions rather than a raw data summary as presented at two recent Victorian public forums during September).

The community continues to express concerns over the speed at which the whole regulatory process in the energy industry is being revamped.

The Victorian **Department of Justice** recognizes the need to ensure that civil procedures better support the focus of modernizing justice, protecting rights and addressing disadvantage. In addition, effective processes need to be available to support prompt and fair resolution of commercial dispute.

Turning now to a more detailed examination of infrastructure policy reform with energy at the top of the list, this limited submission refers to recent findings in the literature that may be worth considering.

The community at large has expressed ongoing concerns about the speed with which proposed change is occurring.

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<sup>260</sup> Dufty, G, Who makes social policy? – The rising influence of economic regulators and the decline of elected Governments. Policy and Research Unit, St Vincent de Paul VCOSS Congress Paper 2004; and John Tamblyn’s Paper presented to the World Forum on Energy Regulation, Rome, Italy 5 – 9 October 2003, Concurrent Overview Session 5 “Are Universal Service Obligations Compatible with Effective Energy Retail Market. Victoria’s Experience to Date.

A study published in the CUAC quarterly July 2007 examined models of consumer consultation. Through a public grant the paper Consumer Consultation: International Best Practice Models was produced by the Monish Centre for regulatory studies and funded through a CUAC public grant.

CUAC the study identified that effective consumer consultation needed to draw from different models. Key concepts identified were:

1. A clear, genuine commitment to consult, beyond either manipulation or tokenism
2. Use of a wide range of consultation mechanisms rather than a single method
3. Commitment of appropriate resources
4. A mix of formal and less formal arrangements; and
5. Public accountability and transparency.

These principles are upheld in numerous quarters.

A literature review<sup>261</sup> recently undertaken by *Jamison, Holt and Berg* of the Public Utility Research Centre, University of Florida discussed.

*“Well-conceived regulatory frameworks, including independent regulators, sound price-setting regimes and transparent regulatory processes that invite stakeholder participation, can improve the investment climate by increasing predictability and reducing political risk”*

These authors have taken the care to identify gaps in the literature on risk mitigation in infrastructure. Notable gaps are:

*“...an understanding tradeoffs between instruments that have conflicting effects, the dynamic process of policy development, sustainability of infrastructure policies, leadership, and the effects of multilateral institutions. We also find a lack of synergy in some areas of research and recommend approaches for increasing awareness and collaboration.”*

Whilst efforts are made by community organizations to support the socioeconomic rationale for customer protections in energy markets<sup>262</sup>, and whilst there are widespread concerns about the tokenism of community consultation in the major regulatory and consumer policy changes that are being envisaged, the public appear to be at ongoing of detriment on account of alleged exploitation of policy provisions in place that either inadvertently or deliberately facilitate questionable conduct that leave the public at risk.

In a policy climate such as the current one it may be a good time for some of these issues to be re-examined. I note that Richard Bolt, now Secretary Department of Primary Industries, had some years ago expressed many concerns about the whole issue of bulk hot water arrangements.

The incremental way in which the current framework has been evolving in response to changes in the market landscape confronting consumers has resulted in a retrospective band-aid approach that has led to complexity, duplication and even confusion for all stakeholders.

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<sup>261</sup> Jamison, MA, Holt, L, Ber, SV, (2005) Mechanisms to Mitigate Regulatory Risk in Private Infrastructure Investment: A Survey of the Literature for the World Bank. Found at <http://bear.cba.ufl.edu/centers/purc/primary/documents/RiskMitigationLiteratureReview.pdf>

<sup>262</sup> Refer to funded project CUAC Partnership Grant produced by PeopleFirst

The opportunity now exists for these deficiencies to be addressed with a forwarding thinking approach. This cannot be achieved without adequate leadership, responsiveness to a dynamic environment and changing needs; complete independence from the control of line agencies more closely involved in developing regulations and potentially with a vested interest in protecting decisions made; a strong consumer voice (*with proactive involvement not only of consumer agencies but interested individual grass-roots end-consumers*).

Another example is poor accessible to deliberative documents and all of the thinking, evidence and material that guides government decisions.

As far back as 2004, , Social Scientist of Policy and Research Unit, St Vincent de Paul Society VCOSS Congress Paper 2004<sup>263</sup> addressed flaws Victorian regulatory policy and the views of John Tamblyn expressed at the World Forum on Energy Regulation, Rome in September 2003 entitled

*“Are Universal Service Obligations Compatible with Effective Energy Retail Market Competition? John Tamblyn is now Chair of AEMC’s Review into Retail Competition Policy.”*

At that time John Tamblyn was Chairperson of the Essential Services Commission and is now Chairperson of AEMC’s Retail Policy Competition Review.<sup>264</sup>

With the permission of Gavin Dufty, Manager Social Policy and Research I quote more than liberally from his 2004 VCOSS Congress Paper. Though written four years ago around the twelve month mark following the introduction of full retail competition in some states, Dufty’s is not only just as relevant today in looking forwards to the next step in completing the energy deregulation cycle but a milestone starting point to promote public debate about the imminent decision that could irreversible detriments not only to competition goals as described in AEMC’s proposals but in terms of the social consequences for the community that were so eloquently discussed by the Senate Committee.

In raising significant social policy issues that have arisen during the review of effectiveness of retail competition in the Victorian energy market and review of the Victorian gas and electricity code, Gavin Dufty paper<sup>265</sup> explores:

*“The potential and real impact economic regulators have on shaping and redirecting elected governments’ social policy objectives.”*

Mr. Dufty notes that:

*“There is lack of awareness of and respect for the role and mandate of the State Government in setting and delivering social and other objectives within the democratic process.”*

Through case study of the Victorian energy market this paper powerfully illustrates significant social policy issues that have arisen during the review of the effectiveness of retail competition in the Victorian energy market and the review of the Victorian gas and electricity retail code.

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<sup>263</sup> Dufty, G (2004). Who Makes Social Policy? – The rising influence of economic regulators and the decline of elected Governments. VCOSS Congress Paper 2004

<sup>264</sup> Powerpoint presentation World Forum on Energy regulation, Rome September 2003 “Are Universal Service Obligations Compatible with Effective Energy Retail Market Competition? John Tamblyn (then) Chairperson Essential services Commission Victoria.

<sup>265</sup> IBID Dufty G



Since the issues impact on the role of safety net arrangements; eligibility for government assistance and the potential for universal service obligations for essential services, these issues are as pertinent today in the light of imminent price deregulation in the energy industry, substantial lightening of the regulatory burden to the extent that may occasion detriment to the low-income groups and others with a range of vulnerable and disadvantaged conditions.

This paper<sup>266</sup> highlights inequality issues, questions how the needs of the vulnerable and disadvantaged can be addressed within energy policy and suggests that there may be an enhanced role of universal service obligations for essential services.

Those issues have become topical once again in the light of proposals by the Government to allow price deregulation in the entire Australian energy market, barring Western Australia, as part of the current Review of the Impact of Competition in the Gas and Electricity Retail Markets.

Time constraints do not permit proper examination of the First Draft Report and accompanying documents. Instead this submission is focused almost exclusively on the social implications of the proposals made by highlighting the respected views of those who have watched closely full retail competition impacts.

Mr. Dufty's VCOSS paper also analyses the hidden agenda in policies adopted by the Essential Services Commission, resulting in withdrawal from the traditional basic protections delivered via universal service.

The scheme adopted was to fall back on "*residual markets*" through retailer of last resort arrangements {RoLR} whereby a retailer opts to inherit vulnerable consumers where no one else would, or in the event of market failure. The RoLR would be financially compensated in such circumstances but the universal safety net protections would become obsolete and inaccessible.

Many concerns have been expressed about the most recent RoLR event during this year and what it says about market failure and inadequate protections for both new entrants into the market and for the public at large.

Mr. Dufty eloquently attacks a conceptualized approach by the Essential Services Commission that is used merely to address market failure instead of maintaining overall consumer protections for Victorian consumers. The risks to consumers of such a strategy are enormous and encourage retailers to abandon all but the "*most profitable customers.*"

Explains Mr. Dufty:

*"In effect the ESC is proposing to increase costs for many who are already disadvantaged purely to stimulate competition with little to no regard for the social impacts."*

The idea was for the regulator to increase default prices (the safety net) to stimulate competition and address the needs of the vulnerable and disadvantaged especially those with financial hardship by shifting responsibility to charity organisations or government agencies, leaving the retailers to make high profit margins in the interests of competition.

Such an imbalance cannot be in the interests of achieving equity or to meet minimal social justice goals.

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<sup>266</sup> Dufty, G (2004). Who Makes Social Policy? – The rising influence of economic regulators and the decline of elected Governments. VCOSS Congress Paper 2004

<sup>266</sup> Powerpoint presentation World Forum on Energy regulation, Rome September 2003 "Are Universal Service Obligations Compatible with Effective Energy Retail Market Competition? John Tamblyn (then) Chairperson Essential services Commission Victoria.

This approach was supported by John Tamblyn, then Chairperson of the ESC, and now chairing the Australian Energy Market Commission's Review of the Impact of Competition on Retail Gas and Electricity Markets.

Further, Mr. Dufty's paper exposes the rationale behind Mr. Tambyln's powerpoint presentation at the World Forum on Energy Regulation in Rome in 2003 as referenced above.

Consumer protection has never been as compromised as at this crucial time of policy and regulatory change within the energy industry. It may be timely for these considerations to be aggressively addressed before another decade of poor protection is heralded. Compromised consumer confidence of compromised consumer protection.

As mentioned in my preliminary submission dated 9 October, I have attended two recent public meetings associated with energy reform initiatives, one under the auspices of the Retail Competition Review and the other as the Public Consultation Forum associated with the initiatives of the National Framework on Energy Reform (NFEE2).

At two recent public meeting in Melbourne on 4 September 2007 to explain the AEMC's approach to that current AEMC Chairperson for the Review John Tamblyn mentioned that price deregulation and full retail competition would not necessarily mean lower prices but could mean that

*"competition is sufficient to keep the marketplace in balance."*

At the Melbourne meeting, there followed a discussion about how much disclosure was really necessary when upholding competitive goals. Misleading conduct is a matter of degree and cannot be condoned in any context by policy-makers or regulators in the name of aiming to promote maximal market competition.

Apparently a similar comment was made at the Bendigo forum on 5 September, with the addendum that effective competition could mean that

*"competition is sufficient to keep the marketplace in balance, even if every customer is not necessarily well-informed."*<sup>267</sup>

It would appear then that Mr. Tamblyn's ideas have altered little since he was Chairman of the ESCV.

Recommendations will be made by the Australian Energy Market Commission (AEMC) to the Ministerial Council on Energy (MCE). The Draft Recommendations are to be published on 28 September.

The AEMC's Retail Competition Draft Report is awaited but we note that the raw data only has been published online as presented at the recent Public Forum and not the full report commission by Wallis Consulting so that the public can make their own evaluation of the conclusions drawn.

As Eyler (1979) said

*"What are figures worth if they do no good to men's bodies or souls?"*<sup>268</sup>

I have concerns about both economic and non-economic regulatory provisions within existing and proposed energy reforms. The decision has apparently already been made.

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<sup>267</sup> CUAC September Quarterly "AEMC Review of Effectiveness of FRC

<sup>268</sup> c/f Ovreitveit (1997) Evaluating Health Interventions. Open University Press. McGraw-Hill (reprinted 2005), Ch

There is one thing that stands out. In this climate of proposed change and increasing leanings towards the “*light-handed*” and “*lighter-handed*” regulatory approach, unless the first-line conceptual framework and implementation architecture is equipped to address these, however belatedly, community protections will continue to be eroded. It would appear that the decision is a fait accompli, but if all band-aid teams are not on deck reforms may lock in another decade of loosely-worded provisions that will continue to vex and disadvantage end-consumers and make inaccessible their rights.

There are downsides also to black letter law. The main reservations made here about the extraordinary speed with which things are happening.

The purpose of the Retail Competition Reviews by the AEMC is to provide advice to each jurisdiction on the appropriateness of retaining, removing or reintroducing retail energy price controls in the electricity and gas retail markets in that jurisdiction.

At the National Framework on Energy Efficiency (NFEE2) Public Consultation held in Melbourne on 25 September, Terry Collins, Manager, Products Energy Efficiency and Conservation Authority provided inspiring insights about the New Zealand conservation experience. Mr. Collins’ background is in quality management, regulatory compliance, standards development and policy and of your extensive career in legal metrology.

These issues have occupied my attention recently in endeavouring to lend a lone but not so timid consumer voice to the respected opinions and suggestions of those with standing.

Kate Noble of the Australian Conservation Foundation (ACF) presented an informed and enthusiastic plea to capitalize on the current policy climate and to harness a more aggressive approach to addressing the threats to Australia's energy future.

The presentations from representatives from ACOSS and CUAC and other community organizations were powerful and raised many consumer-focused issues – my area of interest.

All the industry presentations were well-considered and provided new insights and suggestions in the interests of best practice and concerted community consultation. Industry has put in a plea for better and more advance consultation. Consumers and their representatives feel the same way. The same applies to the current Retail Competition Review.

Despite the plethora of apparently ineffective provisions ostensibly adopted to protect consumers, and those who are vulnerable and disadvantaged in particular, the noticeable gaps are precisely in these areas.

For example the Wrongful Disconnection provisions are entirely focused on those with financial disadvantage. Insufficient attention has been given to a broader definition of disadvantage and vulnerability, which includes those who have language or perceptual or processing barriers; those who have over-brimming plates with other pressures such as accommodation or legal issues; those who have intellectual, psychiatric or social impairment and cannot find their way around the system or are reluctant to seek help for a range of reasons.

A simple process of issuing two warnings, or three, because of unpaid bills, and the methodologies used are bordering on unconscionable, given that this is an essential services.

In some cases, the issue is not about overdue bills at all but rather about disagreement about whether or not a contract exists in the first place.

This is especially so for embedded or inset end consumers in private residential property; potentially public housing, and those in transitory accommodation like caravans, boarding houses or rooming houses.

Besides these issues there is the issue of what constitutes a public service and the obligation to sustain supply.

Wikipedia describes public services<sup>269</sup> as those

*“Considered to be so essential to modern life that for moral reasons their universal provision should be guaranteed and they may be associated with fundamental human rights (such as the right to water).”*

Extended that means that in a modern society hot water at least for the purposes of showering is an essential component of tenancy agreements. Threatening to disconnect that essential service (or for that matter gas or electricity for cooking, lighting or heating) is tantamount to withdrawing a public or essential service. Making those threats as a coercive attempt to secure an explicit contract is entirely unacceptable conduct.

Though Product Disclosure regulations are in place, these are primarily designed to cover market contracts.

Those on **“default or deemed contract”** as defined within the regulations and those who are unilaterally placed in that category because they are embedded or ‘inset’ end consumers who have no separate energy meters, and should not be considered contractually bound in any sense.

These are the soft targets for the more ruthless predators. They are easier to bully and threaten than Body Corporate entities. Despite changes to residential tenancy and body corporate provisions, and despite other specific and general consumer protections, or even the fundamentals of proper trade measurement and utility practice, none of the existing provisions appears to work in practice.

The public has become concerned about policies that allowed conversion factor algorithms to be used through which water volume consumption by **embedded end-consumers** were relied upon to calculate gas or electricity consumption where no separate water meters existed.

Any measurement that allows for **water volume** calculations or some other bizarre equivalent, to be part of the equation that calculates energy consumption is fundamentally flawed and must be squashed in the public interest and in the interest of **best practice standards**, to say nothing on upholding the **spirit and intent of existing provisions**.

Energy retailers are licenced to sell either gas or electricity, but not value-added goods or services such as hot water services.

Even if by some agreement with Body Corporate entities or other parties, or through sub-contracted services energy retailers obtained some impression that there were in the business of selling heated water instead of merely the energy used to heat that water, such an arrangement would be at their direction to subsidiaries, agents servants or contractors would be under their control and their legal and other obligations could not be escaped by third party arrangements such as postulated.

Allowing water meters to pose as gas or electricity meters has staggering implications for fair trading, trade practice, trade and utility measurement best practice or intent, and has many other implications for end-consumers whose energy supplies are not individually metered for the energy they receive.

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<sup>269</sup> Wikipedia, found at [http://en.wikipedia.org/wiki/Public\\_services](http://en.wikipedia.org/wiki/Public_services)

These consumers are “*embedded end-consumers*” who have for years been exploited by deficient policies, poor commitment to compliance enforcement and ruthless retailers seeking to capitalize on any possible regulatory loopholes in singling out “*soft targets*” upon whom they can by unconscionable and improper threat of disconnection of essential services endeavour to impose “*default contracts*” and hold them improperly responsible not only for payment of energy charges more properly the responsibility of body corporate entities (Owners Corporation).

The spirit and intent of existing national and state trade measurement and utility legislation prohibits the use of inappropriate trade measure instruments. Indeed, once utility exemptions are lifted such practices will become not only invalid but illegal. This was recognized at the time of adoption of bulk hot water pricing and charging guidelines currently relied upon in more than one state. These issues are further discussed in an accompanying attachment.

Embedded end consumers (though improperly deemed to have contracts instead of Body Corporate entities) have no choices. They receive bulk energy and appear to be stuck with whatever quality of water temperature, water pressure, or maintenance is delivered. They are not properly informed of maintenance liability and most are not made overtly aware unless a problem arises that water meters are being substituted for gas or electricity meters in the calculation of costs and liabilities.

These embedded end-consumers are misleadingly led to believe that the energy suppliers are licenced to sell a “*hot water service*”; that they are entitled legally to sell heated water or the hot water service as a value-added commodity, and despite not owing the water or licenced to sell the water, can charge for energy on a cents per litre basis. Mentioning how a conversion factor can magically convert this to megajoules is hardly proper disclosure and hardly adequate trade measurement practice.

As mentioned above, the suppliers are licenced only to sell gas or electricity. Nothing else. Any sub-contractual arrangement they may make with contracted “*asset management teams,*” often part of the business structure, to organize and deliver hot water services to end-consumers is an internal servant/agent/contractor one unachievable without Body Corporate cooperation especially if the meters posing under a false identify are in fact water meters living in a locked boiler room.

The ramifications for misleading conduct, breach of contractual provisions, unfair trading practices are numerous.

Currently there are no protections for these anomalies and existing provisions both overtly and implicitly appear to condone them. So much for benchmarking.

How and when will consumer protection be restored?

The Body Corporate invites the supplier onto the premises to install a metering installation, accepts supply at the distribution supply point, in the case of case at the point at which the gas leaves the distribution system and enters the outlet of the meter.

They don't have market contract options. They have no say over the quality of service offered to them, for example water quality, pressure control of ambience temperature at start point; courtesy or ethical standards of the default bulk service provider for energy used to heat communal hot water services.

If things go wrong, they cannot rectify the matter by seeking a contract elsewhere. They have no contract to begin with yet are deemed to be contractually obligated and also deemed to be liable to provide access to meters to which they have no keys or means of accessing themselves. These conditions highlight power imbalances that are crucial to determining unfair contracts, if the contract is valid at all.

Once threat of disconnection has been issued by a provider, confidence in security of supply and of a host of rights is diminished. For vulnerable and disadvantaged consumers this is not only frightening, but they are caught in a trap from which there is no escape.

Their needs are not even identified let alone addressed. The untenable position and rights of this sub-set have for decades been swept under the carpet altogether.

Energy regulators and complaints schemes have worked out “*in consultation with industry*” what is best whether that matches best practice, benchmarked consumer protection standards, best practice trade measurement and utility practice, or worse still, direct infringement of laws and consumer protections in other legislation.

Even when a practice is recognized as being sub-standard and inappropriate or in contravention of the spirit and intent at least of existing provisions, it is adopted for pragmatic reasons and everyone turns a blind eye to infringements and improper practice.

When consumers attempt to gain access to policy documentation to better inform their decisions, supplications, advocacy or complaints plans they are denied access to those documents, at least as long as it is practical. The ideals of transparency and accountability have been clouded, if they ever existed.

Even when the policy-makers have qualms about regulations proposed and express them openly enough, the culprit regulation is put in place regardless, occasioning unacceptable consumer detriment as a rule.

Unless the overall design contains sufficient detail to cover such eventualities the problem will be perpetuated without redress. This is unacceptable.

Another example of market failure is “*dumping*” of financially unattractive customers, even where a contract does exist is not uncommon. Though there are provisions for Retailer of Last Resort (RoLR), these are indications of market failure that could have been avoided with stronger policies in place. The recent and first Victorian RoRL event is evidence of that.

Specialist advocacy groups have cautioned that the market is far too immature for price deregulation, but it appears to be a fait accompli anyway.

That being so, what will the Government do to adequately protect consumers? Will there continue to be a theory and practice gap? It is crucial to establish how market failure will be addressed and how secure consumer protection across the board will be established, not just for those who are vulnerable.

Internal Market in Electricity Directive is the Director 2003/54/EC of the European Parliament and the Council of 26 June 2003 concerning common rules for the internal market in electricity. This Directive repeals the earlier Director 96/92/EC. The new directive is based in the Treaty establishing the European Community and in particular Article 47(2), Article 55, and Article 95 thereof. A recent brief analysis of the internal energy market’s missing steps undertaken by the Council of European Energy Regulators included the following observations under points 3, 4 and 5, quoted verbatim.

## Role and impact of retail price regulation

I particularly refer and uphold to the conclusions drawn by Dr. Tenzin Bathgate as Senior Research Assistant Griffith Law School Centre for Credit and Consumer Law quoted verbatim below:

*“Finally we are not convinced that price regulation is a necessary outcome of effective competition. In Queensland the retention of the uniform tariffs vital for those in non-contestable regions and for those customers in contestable areas who will not be offered market contracts. Research is not conclusion on “.....accurate scenarios associated with the removal of price caps and deregulated FRC and on this basis we urge a holistic and careful approach to any jurisdictional reviews the AEMC will be undertaking in respect of the impact on consumers. As Allen Asher<sup>270</sup> has summed up in relation to the UK experience of deregulation: ‘The UK energy market is a good example of what happens when markets are deregulated with insufficient understanding of or interest in the impact on consumers.’”*

Dr. Bathgate has referred to a selection of pertinent articles to support her view, as shown in footnotes below.<sup>271 272</sup>

CALC made sound assessments were made of information asymmetries in the energy market which “do not only relate to tariff structures and contract terms and conditions, but also in relation to demand management and energy efficiency.”

Thus CALC recommended that

*“Any decision about the ongoing need for price regulation must be made with these factors in mind, and with a view to creating a robustly competitive market that will be in the interests of consumers” in order to make sure that competition will “not only be enhanced within an economic framework, but also within a socially and environmentally sustainable framework.”<sup>273</sup>*

As a concerned Victorian end-user with negative experiences also I applaud the stance that these organizations have taken.

I took I am extremely concerned about market structure, conduct issues and aspects of existing provisions that appear to be negatively impacting on consumer interests, without full enforcement and compliance being addressed through lack of funds or some other reason.

Poor understanding of market parameters, power imbalance, existing complexities with certain tariffs notably 10 and 11 Tariffs, and further more complex tariffs with the projected roll-out of interval meters, will complicate consumer perception of their rights and make it extremely difficult for them to monitor their own consumption, as observed by CUAC and others.

As to the consideration of pre-paid meters down the track, this would be an entirely unacceptable move from consumer standpoint, more particularly for those with any degree of vulnerability or disadvantage, not simply limited to financial disadvantage.

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<sup>270</sup> Asher Allan (2006) Consumer experience in the UK Energy Market in OECD ‘Roundtable on Demand-Side Economics for Consumer Policy, p 28

<sup>271</sup> Bowman, D., Coghill, D., and Hodge, G (2004) Protecting Utility Consumers from market failure, Centre for the Study of Privatisation and Public Accountability, Monash University.

<sup>272</sup> Wellmore (2005) “Everyone’s a Winner? Price protection in retail energy competition’ in Dr. Jane Bathgate (Ed) Electricity Issues: Interstate perspective on full retail competition for residential consumers, Centre for Credit and Consumer Law, Griffith University, pp 7-14

<sup>273</sup> AEMC Victorian Retail Review – Response to Issues Paper Consumer Action Law Centre (Gerard Brody, Senior Policy Officer)

Customer vulnerability is not limited to those with physical disability or even financial disadvantage. Other examples include those with mental or intellectual impairment; those with perceptual or cognitive impairment, those with language barriers, cultural adjustment issues, or simply an overloaded plate with other demands. The same issues were recognized by the **Tenants Union of Victoria** (TUV) in their July submission to AEMC's current Review.<sup>274</sup>

As observed by CUAC, Consumer Affairs Victoria developed a good working definition of a vulnerable consumer as *'a person who is capable of readily or quickly suffering detriment in the process of consumption.'*

The TUV has urged the AEMC to consider whether all classes of consumers and especially tenants will benefit from any proposed energy efficient measures that may purport to "ameliorate the effect of price rises occurring after the removal of price caps.

The needs of these various groups of consumers, and residential tenants in particular are poorly met by any existing or projected provisions. This imbalance needs to be redressed.

Meanwhile I would like to make some more general comments. Dr. Field has acknowledged the wide agreement that

*"consumer voices are significantly under-represented in Australian and overseas political and regulatory processes, resulting in an imbalance in the presentation of interests to those who develop public policy and make decisions."*

I am here to endorse the view that advocacy, complaints processes, appropriate redress and affordable recourses for consumers receiving less than they deserve and are entitled to precisely because of those power imbalances. Dr. Field has argued in favour of a national consumer advocacy body, citing the precedent of a national consumer advocacy body in the UK which is government-created and funded.

I believe that all industry-specific "ombudsmen" schemes should be removed altogether from their direct accountability to industry-specific statutory bodies and also from composition of constitutions that allow excessive market participant involvement. It is not the purpose of this particular submission to pursue this line of thinking at present, though I plan to return to the topic.

## **GAS INDUSTRY ACT 2001 - SECT 36**

### **Customer dispute resolution**

#### 36. Customer dispute resolution

(1) A licence to-

(a) provide services by means of a distribution pipeline; or

(b) sell gas by retail-

must be issued subject to a condition requiring the licensee to enter into a customer dispute resolution scheme approved by the Commission.

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<sup>274</sup> AEMC Review of Retail Competition – Tenant's Union Response



- (2) In approving a customer dispute resolution scheme, the Commission must have regard to-
- (a) the objectives of the Commission under this Act and under the [Essential Services Commission Act 2001](#); and
  - (b) the need to ensure that the scheme is accessible to the licensee's customers and that there are no cost barriers to those customers using the scheme; and
  - (c) the need to ensure that the scheme is independent of the members of the scheme; and
  - (d) the need for the scheme to be fair and be seen to be fair; and
  - (e) the need to ensure that the scheme will publish decisions and information about complaints received by the scheme so as to be accountable to the members of the scheme and the customers of the scheme members; and
  - (f) the need for the scheme to undertake regular reviews of its performance to ensure that its operation is efficient and effective.
- (3) The Commission may, in accordance with this Part, vary any existing licence to-
- (a) provide services by means of a distribution pipeline; or
  - (b) sell gas by retail-
- to include a condition of a kind referred to in subsection (1).
- (4) The Commission may in its discretion exempt a licence to sell gas by retail held by a significant producer from the requirements of subsection (1).

**EWOV** is a company limited by guarantee without share portfolio with an unusually close relationship with the current Victorian **Energy Regulator, Essential Services Commission (ESC)**, with very limited jurisdictional powers.

As mentioned elsewhere, apparently, the existing Victorian energy-specific industry-based complaints scheme **EWOV** is debarred under its charter from undertaking any of the following tasks:

- The setting of prices and tariffs
- Commercial activities outside of an energy or water provider's licence or core business
- The content of Government policies, legislation, licences and codes
- Complaints which are being or have been considered by a court or tribunal
- Any matter specifically required by legislation
- Customer contributions to the cost of capital works bearing in mind current law and reasonable and relevant industry practice
- Actions taken by an energy or water provider and their consequence
- Actions taken at the direction of a person or entity having regulatory or administrative power

This means very limited powers of investigation and recommendation, with uncertain enforcement powers. In fact on studying the above list it is extremely difficult to determine just what **EWOV** can achieve beyond clear-cut wrongful disconnection cases where financial hardship exists or there are simple billing enquiries.

Besides these issues within Victoria at least I believe there is considerable room for enhanced education of complaints scheme and regulatory staff to reinforce consumer protection principles that extend far beyond energy-specific regulations.

The Victorian **Department of Justice** recognizes the need to ensure that civil procedures better support the focus of modernizing justice, protecting rights and addressing disadvantage. In addition, effective processes need to be available to support prompt and fair resolution of commercial dispute.

At present, within the energy industry benchmarks of best practice consumer-focused service deliveries and protections may have become a blurred and inaccessible. The public has never felt less confidence that their rights will be upheld or that justice will be readily accessible. Theory and practice gaps have become more noticeable despite myriads of guidelines in place. Enhanced education of key energy regulatory staff and complaints scheme staff may not go astray.

Perhaps the Victorian **Department of Justice** can address this comfortably within their portfolio for raising awareness, especially in relation to best practice policies and consumer protections. The public fully expects the Department of Justice to ensure that the common law rights and other rights of the public do not become inaccessible or eroded by statutory policy across the board.

The bulk hot water pricing and billing arrangements endorsed by public policy is a classic example of where things have gone wrong with consumer rights and has remained unaddressed for years. For the policy-makers and regulators to suggest that the arrangements were made to shield end-users from price shock is to altogether forget that in these instances the consumers are not contractually bound under their fundamental common law rights. And other entitlements.

The core values expressed by the **Victorian Attorney-General** in his **2004 Justice Statement** are as follows:

*“Based on the rule of law, a number of core values underpin the justice system and are promoted by the Justice Statement:*

***Equality*** – *all citizens should be equal before the law. This is promoted by the independence of the judiciary from the other arms of government, accessible justice and respect for human rights.*

***Fairness*** – *the processes of justice should be fair, incorporating principles of natural justice and proportionate sanctions and remedies.*

***Accessibility*** – *the justice system should provide appropriate access to all people regardless of their means, and a range of processes which are appropriate to the issue to be resolved.*

***Effectiveness*** – *the justice system should be responsive, and able to efficiently deliver the outcomes expected of it by the community.”*

Meanwhile, I enthusiastically endorse Chris Field’s view that a national consumer body if created should be strictly independent and strictly bipartisan, with a focus on creating consumer advantage through economic reform.

I believe that bodies such as Consumer Affairs Victoria should assume funding and governance of all ombudsmen schemes and have a more visible presence in consumer protections, especially within the energy industry – an essential service.

In my personal perception, consumers should be able to continue to rely on unfair contractual law terms as recently introduced within Victoria, EU, UK and Scotland, and should have more accessible access to the upholding of those laws.

Within the energy industry advocacy and consumer protection is grossly under-serviced. CUAC is under-funded and barely has time or funding for their research activities, let alone advocacy, and the same applies to the Consumer Law Action Centre.

I have many reservations about the composition, jurisdictional limitations, scope, perceived independence and knowledge-base of the current energy-specific complaints scheme, whilst composition exclusively comprises either voluntary members of the scheme or else market participants, creating a potential conflict of interest, at least in the minds of the public, and despite the provisions of s36 of the Gas Industry Act 2001.

I strongly believe that detachment from industry-specific statutory authorities and more independent accountability and governance as suggested above would serve public interest better.

The Victorian Department of Justice already has a brief to support and educate business sector and other government departments in upholding the fundamental principles of consumer protection. That role should be enhanced and better funded.

I do not agree that regulation should be removed, or that industry-specific regulation should be replaced by more expensive generic recourses. In practice, these are not as readily accessible as they should be to consumers.

It is **inappropriate** and **improper** and in some cases **unconscionable** to **threaten disconnection** of essential services because of failure or refusal to disclose personal data by an end-user of bulk utility services whether gas, electricity or water that are not separately metered for each component of utility provided remembering that Gas and Electricity Licencees are not normally also licencees for water; and that measuring gas consumption of those receiving bulk gas or electricity services by measuring water volume in litres rather than gas in cubic meters is not an appropriate trade measurement practice).

The *Code of Conduct for Marketing Retail Energy* has apparently been designed to:

*“Protect consumers (which term is broadly defined and not exclusive to end-users turning on the tap or natural persons alone), promote the effective transition to full retail competition and ensure uniform marketing standards. Its objectives specifically provide that the Code of Conduct for Energy Marketing Retail<sup>275</sup> WILL:*

- *Protect consumers and promote consumer confidence in the retail energy industry by identifying high standards of behaviour for marketing energy*
- *Promote honesty, fairness and disclosure of information to consumers<sup>276</sup>*

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<sup>275</sup> Code of Conduct for Energy Marketing Retail 2004 (effective 2005)  
[http://www.esc.vic.gov.au/NR/rdonlyres/AD9FD08D-4DBB-431D-9726-8BCB3A8297DF/0/MCC\\_FinalOct04.pdf](http://www.esc.vic.gov.au/NR/rdonlyres/AD9FD08D-4DBB-431D-9726-8BCB3A8297DF/0/MCC_FinalOct04.pdf)

<sup>276</sup> Does this mean honesty about the nature of the meters, location, access, justification for imposition of deemed contract, numbers of estimates, why access to hidden meters (water) has not been sought and why in any event water meters need to be accessed to determine the amount of gas passing through them, the possible way to assess actual gas usage? What about quality of water expectations.

- *Enhance efficient retail market operation by clarifying standards and promoting certainty.*<sup>277</sup>
- *Promote ongoing cooperation between the retail energy industry, regulatory authorities, EWOV and consumer representatives*<sup>278</sup>

CUAC has been able to verify that the protections contained in the Victorian Energy Retail Code and Marketing Code of Conduct<sup>279</sup> have assisted consumers address their lack of bargaining power, including in ensuring that retailers are required to seek consumers' explicit informed consent in entering into a marketing contract, and providing redress and protection from misleading conduct."<sup>280</sup> Removal of such protections in the interests of improving competitiveness cannot be a fair and reasonable step to take.

This observation is consistent with that to CUAC's that retailers apparently

*"do not provide assistance to consumers to address information asymmetries or unequal bargaining power.*<sup>281</sup>

Such information has only been driven by government or regulatory intervention.

To rely on retailer voluntary self-regulatory measures as replacement measures for some of the current theoretical protections against perceived misuse of power or unequal bargaining power, more particularly for those consumers who are unilaterally imposed with a "**deemed contract**" status.

I can provide direct evidence to that effect as an end-consumer, including unwarranted threats of disconnection to essential services, not on the basis of overdue bills, but on the basis of a dispute over the existence at all of a "**deemed contract**" that should not exist in the first place, but more properly belongs to the Body Corporate.

Beyond that, and on behalf of the particular sub-group of end-consumers who receive bulk energy supplies – in Victoria some **26,000 of gas bulk energy**, and some **200+** using electric bulk energy, used for the heating communal, centrally heated water services of varying quality and temperature, though generally referred to as "hot water services."

Statutory policies authorized by the current Victorian Energy Regulator Essential Services Commission that may be considered by all consumers of bulk energy and many consumer organizations and advocates to be detrimentally impacting on consumer rights and entitlements.

I would like the opportunity of providing written end-consumer insights on this particular topic, despite all deadlines and regardless of any decision to publish. This material is in preparation and will be separately addressed.

The primary issues of concerns that I wish to raise in more detail than within this submission impacts on a particular sub-set of end-consumers, mostly residential tenants at the lower end of the income market, and many with vulnerability and disadvantage.

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<sup>277</sup> Should it not be reasonable expectation that regulatory authorities, industry-specific complaints schemes such as EWOV, and energy retailers volunteer to provide, or at any rate promptly respond to direct requests for clarification of policies and entitlements or providers or deemed liabilities of end-consumers of bulk energy

<sup>278</sup> Should it not be a reasonable expectation that regulatory authorities, industry specific complaints schemes such as EWOV, and energy retailers volunteer to provide, and at any rte promptly respond to direct requests for clarification of policies and entitlements of providers or deemed liabilities o end-consumers of bulk energy

<sup>279</sup> Submission AEMC Retail Competition Review – CUAC Response to Issues Paper" 10 July 2007, p4

<sup>280</sup> Submission "AEMC Retail Competition Review – CUAC Response to Issues Paper" 10 July 2007, p4

<sup>281</sup> Submission "AEMC Retail Competition Review – CUAC Response", ibid p4

These individuals are the soft targets whose needs remain unmet because of systemic deficiency and market conduct. This client group is not amongst those who are entitled to safety net provisions because of previous contracts with franchised retailers in former catchment areas. They are in a class of their own.

The needs of this and similar groups have been neglected for years. When will their individual, collective and peculiar needs be addressed, if at all and by which authority(ies), instruments, protections?

Existing wrongful disconnection processes and procedures, and enhanced **product disclosure parameters**, as well as **compliance enforcement** issues are compromised in that they do not address the needs of this subset.

Likewise, protections contained in the Victorian Energy Retail Code and Marketing Code of Conduct may have assisted various segments of consumers address their lack of bargaining power, but this certainly does not apply to those receiving bulk energy, since the ESC provisions for this special sub-set of Victorian consumers (and presumably those in other states) appear to be not only unaddressed by existing provisions, but actually compromised by them.

Specialised research to address the needs of such target groups is warranted. Many of them automatically fall into the category of vulnerable and/or disadvantaged when the term is broadly applied as for the most part those living in residential accommodation not provided with separate meters for any component of energy consumption are generally living in relatively sub-standard accommodation. Besides financial hardship those in this group may have a range of other vulnerabilities.

These factors are not considered at all when allegedly unconscionable conduct associated with threatened disconnection of essential services.

Consumer protection cannot be eroded by failure to also take into account fair trading and trade practice considerations, including provisions that focus on unconscionable conduct, misleading conduct, unfair contract terms. It is impossible to exclude the provisions of the [Residential Tenancies Act 1997 \(RTA 1997\)](#) and its corollary guidelines.

Whilst energy providers may not recognize the jurisdiction of this Act, and whilst the [RTA](#) was not designed to identify liabilities between energy providers and end-consumers, the actions of suppliers of goods and services quite simply cannot have the effect of stripping consumers of their rights under existing protections that form part of their enshrined legal and moral entitlements, general and specific.

**Fair Trading** provisions (*including unfair contract terms, without conceding the existence of any contract*); and **Trade Practice** considerations also apply, in addition to any applicable state or national utility trade measurement provisions.

Other consumer protection provisions are under **common law rights**, the **rules of natural justice**, and the **specific and peculiar rights of vulnerable, disadvantaged and low income end-users** including but not limited to those with psychiatric illness or intellectual impairment; those with perceptual or cognitive impairment, however, slight; those who simply do not understand the complexities of legalized jargon that is not translated into lay terms comprehensively and unambiguously; those who are experiencing cultural adjustment or otherwise are ignorant of their rights for some other reason.

It is this group that experience an unwarranted imbalance of power – since they have no choice at all in terms of either utility type or utility provider who may have formed a direct explicit or implicit contract with the Body Corporate (Owners Corporation) entity to supply bulk energy (gas or electricity) to residential tenancies living in multi-tenanted dwellings.

Jim Wellsmore had also mentioned the “*re-sale*” price of electricity by owners of the residential properties mentioned. Many of the same arguments apply to renting tenants in apartment blocks though the rules may be different for some tenants in certain properties, including those living in public housing. The following is an extract from his 7 February submission.

**“Inset networks”**

*We believe it is critical that the Rules include provisions relating to the operation of inset or exempt networks and the rights and obligations of the owners of these networks and their customers.*

*This is an important issue affecting the extent to which the new arrangements will protect many small customers. These primarily would be customers of exempt networks operated by, for example, caravan park owners or boarding houses where these customers are long-term residential tenants.*

*It is important that the RPWG consider the scope of rights and obligations that need to be addressed. As an example, in the case of electricity in NSW there are obligations imposed on owners of these networks with respect to the ‘re-sale’ price of electricity. On the other hand, there is no regulation of the quality of supply that can be made available to the customers of these networks in NSW. The monopoly supply situation of these end-users and the fact that most could be classified as ‘vulnerable’ makes inset networks an important consumer protection issue.*

*7 February, 2007 Signed Jim Wellsmore Acting Principal Policy Officer.”*

## **CONSUMER PROTECTION ISSUES**

Dr. Caroll O’Donnell refers in her two substantial and well-reasoned submissions to the Productivity Commission to the “*potential effects of dominating power of any kind (including unequal knowledge, or money or choice) in any market relationship.*”

As an end-consumer of energy acting on behalf of a particularly vulnerable and disadvantaged embedded end-consumer of energy, I would particularly like to endorse Dr. O’Connell’s perceptions that

*“industry-based management perspectives would be more helpful because matters which are actually linked in normal life could be recognised and dealt with better when in dispute.”*

It is indeed the case that a large number of energy-specific codes and guidelines exist. There is certainly room for many existing code and guideline provisions to be incorporated into the National Framework under consideration whilst consideration is being given to what can be retained by the State and what needs to be nationalized. The concerns I have about this process generally and also in relation to the energy market, is that the enthusiastic embracement by market participants and their professional associations of light-handed regulation is not by way of heralding an era where proper controls disappear, compliance and enforcement become relegated and less accessible, and one loophole after another is sought to free the industry from proper accountability, regardless of the theory models that may be implemented to counteract such risks.

Though the Consultation Paper that does not yet represent a fixed position by the RPWG, MCO SCO, I have particular concerns about aspects of the following:

- **Default Supply Contracts** generally
- **Unilaterally perceived default supply contacts** as they specifically affect embedded end-consumers where the contract more properly lies with the Body Corporate where the end-consumers live in multi-tenanted dwellings without separate meters to measure gas or electricity consumption. The same applies to those technically using embedded networks which the distribution network is crossed over to another network in the middleman custody change-over. This often applies to those in caravan parks, rooming houses, boarding houses and nursing homes, high rise blocks, but can occur for smaller apartment blocks. Inflated costs on utility charges without controls can signal exploitive practices without accountability since some such distributors can be exempted from energy regulations.
- **Credit Management**
- **Sales and Marketing**
- **Disconnection processes**, generally and specifically for vulnerable and disadvantaged consumers, with that definition being broad and not limited to those with financial disadvantage

**Information Disclosure** specifically on bills and general price and other terms and conditions

#### **General Disclosure parameters**

“In a version of his presentation to the National Consumer Roundtable, Nagarajan’s submission to the Productivity Commission, in the context of recognising the importance of regulating cartels, quotes Graeme Samuel, the current Chairman of the ACCC as saying “To see the link more clearly, imagine the impact on consumers if businesses did not need to compete with each other for custom.

More recently the importance of regulating cartels has been explained in terms of consumer protection and Graeme Samuel, the current Chairman of the ACCC has stated

*“To see the link more clearly, imagine the impact on consumers if businesses did not need to compete with each other for customers and were allowed to agree on what price they thought would be appropriate to charge”*

Dealing first with the broad principle of how consumer protections can be maintained, there is a class of rights formed by those rights deriving from the common constitutional traditions and granted without fail refer to example to the texts of all European national constitutions and in the European Convention.<sup>282</sup>

There is an expectation that particular and broader rights of consumers enshrined either in constitutional jurisdictions or in specific enactments will be upheld, regardless of industry specific legislation, codes and guidelines.

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<sup>282</sup> New York School of Law Constitutional jurisdiction and fundamental rights. . Jean Monet Centre

These rights are not cross-referenced or referred to in passing in industry-specific provisions, so it is left potentially open for debate whether, for example an enshrined right in provisions such as residential tenancies enactments (in Victoria *Residential Tenancies Act 1997*, see especially s53, 54, 69 and any relevant trade measurement and water industry provisions; common law contractual rights) need to be recognized at all by market participants when unilaterally determining whether or not an embedded end-consumer of energy can be considered at all a “**deemed contractual customer**” rather than the Body Corporate. This concept is elaborated on further in the body of the response to the AAR Consultation paper to follow.

Under the principles of natural justice, justice should be seen to be done. If the community is satisfied that justice has been done, they will continue to place their faith in the courts, assuming in the first place that access to the courts is affordable and accessible.

At present, existing energy provisions are not cross-referenced to such protections. In addition the energy-specific complaints scheme funded by and also managed by market participants (see composition of Board of EWOV, comprising exclusively market participants (many of whose names and identifies have changes, for example Eastern Energy now owned by TRUenergy, the trading name for China Lighting and Power, CLP) appears to have a compromised concept, if any concept at all, of the requirement to recognize general and specific consumer protections enshrined outside of energy-specific regulations.

This may be fixable with education of policy makers and complaints scheme staff that it is not acceptable to have policies in place that effectively strip end-consumers of their particular rights whether general or specific, statutory or common law. In addition rights of natural and social justice, whilst less tangible, do exist and should be honoured.

If consumers feel that their rights are being eroded by policies, ultimately the cost of complaints investigation redress will become a huge burden for the government. For those reasons there should be better checks and balances in place when regulations are conceptualized and designed.

Perhaps it could be argued that failure of energy market participants; or alternatively, industry-specific or other complaints schemes; or alternatively, state or federal policy-makers and/or regulators; or indeed any other relevant entities to recognize such general and specific rights, overtly and implicitly, such failure represents “highjacking of constitutional values.”

At the Opening Address to the National Consumer Congress<sup>283</sup> in Melbourne on 14 March 2007 The Hon Chris Pearce as Parliamentary Secretary to the treasurer explained the rationale for developing mandatory standards and regulation impact standards that could be addressed in a unified national platform to save on time and expensive and achieve consistency.

By the same token the notion of a single regulator makes sense. If stakeholder consultation is carried out in a transparent, timely and consistent manner this will be reassuring to the public.

Previous approaches to structuring a consumer policy framework have been undertaken existing consumer policy framework “have largely been introduced in an incremental and often reactive fashion.” The community welcomes a more coordinated approach. The concept of consumer empowerment should not be restricted to those with vulnerability or disadvantage as broadly defined.

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<sup>283</sup>National Consumer Congress Opening Address RACV Club Melbourne 14 March 2007 <http://www.treasurer.gov.au/cjp/content/speeches/2007/004.asp>



## **Definition of customer and applications; deemed supply arrangements – energy-specific**

Take for example a situation where residential, body corporate, trade measurement, and other provisions as referred to above, deemed landlord to be liable for all charges associated with the provision of utilities that are not individually metered for each component of energy supplied (other than bottled gas) (refer to s. 53, 54, 69 *Residential Tenancies Act 1997* (Victoria) s53, 54, 69 and other related provisions).

Simply because energy providers may not recognize the jurisdiction of this Act, and whilst the RTA was not designed to identify liabilities between energy providers and end-consumers, the actions of suppliers of goods and service quite simply cannot have the effect of stripping consumers of their rights under existing protections that form part of their enshrined legal and moral entitlements, general and specific.

Fair trading provisions (including unfair contract terms, without conceding the existence of any contract), and trade practice also apply, as well as any applicable state or national utility trade measurements.

Then there are other consumer protection provisions under common law rights, the rules of natural justice and the specific and peculiar rights of vulnerable, disadvantaged and low income end-users, including but not limited to those with psychiatric illness or intellectual impairment, those with perceptual, cognitive impairment, in whichever degree, those simply who do not understand the complexities of legalized jargon that is not translated into lay terms, comprehensively and unambiguously, those who are experiencing cultural adjustment or otherwise are ignorant of their rights for some other reason.

TRUenergy has put forward the view that

*“In a highly competitive retail sector, where costs and operational efficiency are significantly impacted by regulation, it is imperative that the consumer protection regimes do not act as a ‘road block’ to effective and responsive competition.”*

Of course one does not want to block productivity goals. But to suggest that consumer protection can be sacrificed for *“effective and responsive competition”* is to go too far.

As to whether true competition exists in this climate of mergers, acquisitions, horizontal and vertical integration, sub-contracted asset management arrangements and the like, that is a topic for dedicated discussion elsewhere – and perhaps of more interest to the current Review of Retail Competition, which incidentally cannot be taken in isolation from examination of the broader macro- and micro-environments through dedicated and ongoing SWOT analysis of the market place.

Meanwhile, returning to consumer protection, it would seem that even with a huge range of existing codes and guidelines governing conduct, consumer protection is not merely compromised but almost non-existent.

Allegedly ruthless actions, even unconscionable, are part of the norm. Access to proper protection under existing generic protections is extremely difficult to access and prohibitively costly. Others have commented on this gap eloquently, including Michelle Sharpe, Laurie Malone and Carroll O’Donnell, and in a more restrained way, Lyndon Griggs.

Further detail is provided under the heading **dealing with vulnerable customers** with specific reference to the energy industry, though some of the broad principles would apply to other industries also. I can also supply direct hard evidence of such conduct, including threats of disconnection, in some cases unconscionable and unwarranted and no always related to overdue bills or current provisions for wrongful disconnection.

### **Deemed supply arrangements:**

This topic deserves more dedicated input and protracted discussion that time constraints preclude within this submission, but will be raised in other arenas.

**Energy-only contracts and embedded network arrangements** are crucial in considering the extent to which fundamental consumer rights such as under contractual law in common law provisions, social justice and rules of natural justice provisions, and in other arenas such as residential tenancies provisions may be eroded by existing (ESC) and proposed (NEM) arrangements.

It is of great concern that the ESC has seen fit and proper to licence billing specialists using creative embedded network and energy-only arrangements by which gas meters pose as water meters, and energy charges are calculated in cents per litre, all without the benefit of site-specific readings, though innocent end-consumers are held contractually responsible for providing safe, convenient and unhindered access to water meters in order to fulfill a unilaterally perceived contract with either an energy supplier, a licenced billing agent, or other licenced or unlicenced energy-only provider.

If the pitfalls of supporting such arrangements through policy provisions is not arrested and re-examined in terms of consumer right erosion, the government may well face expensive litigious action.

The Consumer Utilities Advocacy Centre (CUAC) is an independent consumer advocacy organization which ensures the interests of Victorian electricity, gas and water consumers—especially low income, disadvantaged, rural and regional, and Indigenous consumers—are effectively represented in the policy and regulatory debate.<sup>284</sup>

CUAC believes all Victorians have a right to:

- ◆ affordable and sustainable electricity, gas and water
- ◆ have their interests heard in policy and regulatory decisions on electricity, gas and water
- ◆ not be disconnected from electricity, gas and/or water due solely to an inability to pay

This body is respected for the expertise it has gained in researching and advocating for improved utility policies.

The CUAC's September quarterly<sup>285</sup> reported discussions at the recent forum organized by CUAC for consumer advocates and policymakers to discuss pricing in the light of the rapid energy market developments, Gavin Dufty from St Vincent de Paul

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<sup>284</sup> CUAC Quarterly September 2007 p 1

<sup>285</sup> CUAC September Quarterly "Minister Batchelor Guarantee Safety Net" at CUAC Pricing Forum, p2

*“Gavin Dufty from St. Vincent de Paul proposed pricing principles which would allow a fixed price for a minimum level of consumption or ‘lifeline’ per household, with tariffs increasing in blocks after the minimum. This would, he argued, protect low income earners, reward reduction in energy consumption, and work well with the introduction of interval meters.”*

*“Jim Gallagher, a consultant, discussed network pricing options from the Network Business perspective. Brad Shone from the Alternative Technology Association looked at how proposed developments such as interval meters, cost reflective prices and emissions prices would impact on consumers.*

*Robert Wiles, an independent adviser on energy market regulation and reform, discussed how more complex pricing structures would increase the need for organizations to provide independent advice on a regulatory and individual basis.”*

The same article reported the input of Catherine Waddams, an expert on privatization, regulation and competition in energy in Britain and Europe in analyzing the deregulation experiences in other countries, particularly the UK.

CUAC reports that Catherine Waddams:

*“startling research showed that of those switching retailers, only one-fifth achieved the best possible outcome and more than a fifth ended up worse off,”* even allowing for those who switched to green power.

Other issues discussed at that forum and reported by CUAC were how the proposed developments such as interval meters, cost-reflective prices and emissions prices would impact on consumers (Brad Shone, Alternative Technology Association).

The legal firm Allens Arthur Robinson as solicitors acting for the MCE have submitted their recommendations that have now been incorporated in the Composite Consultation Paper under current consideration.

I expect to prepare a detailed response to the Composite Recommendations adopted so far with a view to suggesting refinement in consumer interests. I note that the intent was to incorporate conceptual thinking rather than recommend precise drafting language.

It is of some comfort to know that whist:

*“The various Working Papers have been discussed with the RPWG and those discussions have been taken into account in preparing the Consultation Paper, the conclusions and recommendations in the paper do not represent agreed outcomes by the RPWG.”*

The paper has been prepared by Allens Arthur Robinson for consultation,” and has

*“not yet been endorsed by the RPWG, the SCO or the MCE.”*

The principle of deregulation has been on the table for a while. As an individual from the community committed to best practice policies and consumer protection, I am not only a latecomer individual stakeholder with deliberations and input, but for a number of reasons have been either unaware of, or unable to respond to submission deadlines to Issues Papers and other consultations before now.

However, I have some genuine concerns on behalf of the community and in the interests of industry best practice and I would submit, whether belatedly or in other aspects premature to submit for considerations selected concerns, both for the perusal of the RPWG and the Productivity Commission. To save duplication time and effort, I am preparing this with the aim of targeting both arenas.

There are some concerns about whether such decisions should be made in relation to specific legislation rather than under the umbrella of an overall national consumer policy independently administered.

I would like to create a separate opportunity to target in a topical and more immediate way the deliberations of the RPWG, and to provide that Group with a preview of what I would like to see published by the AEMC and Productivity Commission at a later stage in formal response to the awaited Draft Reports. Neither of those measures will address adequately a series of narrowly and more detailed concerns focused on the neglected protections of **embedded end-consumers**.

CUAC's October 2007 Quarterly Report reported on the Retail Policy Working Group update. This is the subcommittee "charged with developing the national consumer protection framework for energy retail and distribution, reporting to the Standing Committee of Officials (SC)) and advising the Ministerial Council on Energy (MCE) on the final framework

The CUAC intends to make a submission to the Retail Competition Review First Draft Report.

Meanwhile, the CUAC paraphrasing from the September Quarterly Report reflects the views of the community that:

*"All obligations pertaining to access – in particular the obligation to offer supply and conditions under which supply can be disconnection – be contained in legislation with explicit articulation that disconnection should only be a last resort; that conditions precedent to supply be removed; that social and environmental policy objectives be added to the NEL and National Gas Law objectives.*

*Other recommendations from CUAC include effective consumer protection; deemed distribution provisions and extended life of consumer protections (such as they are and are effective) to at least the end of 2008.*

May I add my lone voice to those recommendations and the recommendations of countless others most concerned about current proposals for an imminent free-for-all, anything goes market climate?

CHOICE has highlighted certain particular areas for special consideration within a broad range of consumer markets that is including telecommunications, energy, therapeutic goods, food, intellectual property and many more, not merely in relation to particular legislation.

This respected body also believes that the existing framework under the Competition and Consumer Group in the Markets Division of Treasury has a limited role in developing consumer policy, and has strongly recommended not only a radical change to the existing framework but far more independence.

I vigorously support such a perspective and all of the observations and recommendations made.

As repeated in the consumer policy section, the incremental way in which the current consumer framework has been evolving in response to changes in the market landscape confronting consumers has resulted in a retrospective band-aid approach that has led to complexity, duplication and even confusion for all stakeholders.

I read with great interest the speech that delivered by David Tennant<sup>286</sup>, Director Care Inc Financial Counselling Service, ACT on **16 March 2006** at the 3<sup>rd</sup> National Consumer Congress hosted by Consumer Affairs Victoria entitled “*The dangers of taking the consumer out of consumer advocacy*” presented at the 3<sup>rd</sup> National Consumer Congress, hosted by Consumer Affairs Victoria.

That presentation represented a response to Professor Chris Field’s Discussion Paper (relying on a confidential draft, some of the philosophies of which seems to have been submitted to the Productivity Commission as submission 102. David Tennant is Director, Care Inc. Financial Counselling Service. David Tenant makes no apology for being direct and largely critical of Chris Field’s publicly expressed views about advocacy.

It is generally acknowledged that regulatory burden has scope for rationalizing, harmonizing. However, much more than that is required especially with regard to structuring a strong, functional consumer policy framework that, under the strongest independent leadership is capable of regular review and restructuring to respond to dynamic market needs.

There have been articulate and informed criticisms made of both these provisions in many of the submissions already made to the Productivity Commission during this inquiry to date. I will refrain from repeating these but call particular attention to the following submissions:

- Caroll O’Donnell Sub001 and Sub020
- Laurie Malone, FIAM, Sub004
- Dr. Michelle Sharpe Sub005
- Dr Leslie Cannold, Ethicist, Reproductive Choice Sub006
- John Firbank Sub013
- Lyndon GriggsSub018
- Hank Speir, Sub019
- Deborah Cope, PIRAC Economics Sub106
- CHOICE (joint submission with several community organizations) Sub108

There is one thing that stands out. In this climate of proposed change and increasing leanings towards the “*light-handed*” and “*lighter-handed*” regulatory approach, unless the first-line conceptual framework and implementation architecture is equipped to address these, however belatedly, community protections will continue to be eroded.

I have glanced at some of the submissions already made to the Productivity Commission and particularly wish to call attention to the respected views of the following with my personal endorsement of the views expressed, rather than repeat what has already been so eloquently presented.

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<sup>286</sup> Tennant, F “The dangers of taking the consumer out of consumer advocacy” Speech delivered by David Tennant as Director, Care Inc. Financial Counselling Service at the 3<sup>rd</sup> national Consumer Congress, hosted by Consumer Affairs Victoria Melbourne 16 March 2006

As pointed out by Lyndon Griggs, these factors underpin some of the problems in securing equitable consumer protection

- A marked contrast between the bargaining position of vendor and purchaser;
- Information asymmetry; and
- An imbalance in the available resources for enforcement between the two parties.

Lyndon Griggs says:

*“Despite this extensive legislative scheme, or perhaps because of its complexity and ad hoc transmutation, consumer law has failed to adapt to many situations within the contemporary environment. Consumer law seems to have responded by establishing processes which should support consumers in the role as purchaser and which should improve the quality of the outcomes (e.g. improved disclosure should lead to better decision making), but which in many cases doesn’t seem to have improved the consumers decision making (i.e. Consumers are consumer or overwhelmed by disclosure, or choice).”*

Griggs has recommended a number of measures through which *“consumer policy can meet the challenges of this century and not merely respond to the last.”*

As Lyndon Griggs, Michelle Sharpe and others have observed access to justice issues remains a pivotal factor in consumer protection.

Section 51AB prohibits corporations from engaging in conduct *“that is, in all the circumstances, unconscionable”* in the supply or possible supply of goods or services to a consumer. The provision provides a non-exhaustive list of four matters which a court may have regard to in determining whether a corporation’s conduct is unconscionable.

These matters include the following:

- the relative strengths of the bargaining positions of the corporation and the consumer;
- whether, as a result of conduct engaged in by the corporation, the consumer was required to comply with conditions that were not reasonably necessary for the protection of the legitimate interests of the corporation;
- whether, the consumer was able to understand any documents relating to the supply or possible supply of the goods or services; and
- whether any undue influence or pressure was exerted on, or any unfair tactics were used against, the consumer in relation to the supply or possible supply of the goods or services.

Dr. Sharpe has observed that:

*“Section 51AB can be enforced by consumers against unscrupulous corporations through the institution of legal proceedings.”<sup>287</sup>*

*However, the provision is of little assistance if the consumer is ignorant of the existence of section 51AB and/or lacks the resources to engage in litigation. It is, therefore, the role of the ACCC to administer the TPA by educating the public about their rights and obligations under the TPA and taking enforcement actions”.*<sup>288</sup>

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<sup>287</sup> Under the TPA consumers may obtain an injunction or damages or any other order the court considers appropriate to enforce the TPA under sections 80, 82 and 87.

<sup>288</sup> TPA, Part II.

*Dr. Sharpe has summarised the outcomes of the Working Paper of November 2006, as part of the ACCC Enforcement and Compliance Project,<sup>289</sup> a working paper was delivered to the ACCC assessing the impact of the ACCC's enforcement of Part IVA of the TPA ("the Working Paper").<sup>290</sup>*

### **Dr. Sharpe's Recommendations:**

In conclusion the Working Paper suggested that ACCC enforcement of section 51AB, and consequently the protection of consumers, could improved by:

- *adopting a different, harder approach when dealing with corporations who are deliberately breaching the TPA and that this may mean parliament may have to empower the ACCC with a greater range of civil and criminal penalties for such conduct;*
- *adopting a clear coherent case theory when commencing proceedings against a corporation and that this might involve seeking the advice or assistance of lawyers or counsel external to the ACCC;*
- *developing best practice guidelines or codes of conduct which offer greater clarity to businesses as to the type of conduct expected of them;*
- *development of some kind of policy with the ACCC as to when, and to what extent, it may be appropriate to negotiate or mediate with corporations alleged to have contravened the TPA."*

Dr. Sharpe has identified enforcement problems under Section 51AB

- *"When dealing with a corporation that was deliberately and consciously in breach. While the ACCC was initially effective in stopping these kinds of corporations from engaging in the offending conduct the corporation did not benefit from programs or schemes designed to improve the corporation's future compliance with the TPA.*
- *Instead, such corporations would frequently be subsumed by new a corporation and would relocate its activities to a different Australian address or, more often, a New Zealand one."*

Consumers need to be provided with inexpensive and accessible means of redress, especially where systemic issues exist not only within the policies of market participants (in this case the energy industry), but also where internal government policies and procedures, at any level is a significant factor in creating consumer detriment. It is one of those instances that drives the more narrowly focused context of this submission.

Griggs has recommended that an organization like CHOICE, and the approval of the ACCC, perhaps classes of consumers can be represented in proceedings by such a body, rather than piecemeal approaches to individual cases, especially where systemic deficiencies are identified. He has embraced the concept of remedial flexibility.

If timely inexpensive solutions could be found that do not place unnecessary burdens on government agencies under generic provisions, but achieve effective deterrent outcomes, this is clearly a preferred choice.

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<sup>289</sup> Further information about the project can be obtained at <http://www.cccp.anu.edu.au/projects/project1.html> (10 August 2006.)

<sup>290</sup> Sharpe and Parker, *The ACCC Compliance and Enforcement Project: Assessment of the Impact of ACCC Regulatory Enforcement Action in Unconscionable Conduct Cases*, November 2006.

Dr. Caroll O'Donnell School of Behavioural and Community Health Sciences and Faculty of Health Sciences, The University of Sydney has made some bold and worthy suggestions in her submissions to the Productivity Commission. she has referred to the Hilmer Report which stated that:

*“Competition policy is not about the pursuit of competition per se. Rather it seeks to facilitate effective competition to promote efficiency and economic growth while accommodating situations where competition does not achieve efficiency or conflicts with other social objectives. These accommodations are reflected in the content and breadth of application of pro-competitive policies, as well as the sanctioning of anti-competitive arrangements on public benefit grounds (1993, p. xvi).”*

One of the key considerations for the Productivity Commission is the:

*“Shared responsibility of consumers, businesses and governments for responding to consumer issues and the recognized need for a well-functioning ‘demand-side’” wherein “policy settings that facilitate effective participation in markets by consumers are an integral complement to competition among suppliers.”*

As suggested by CHOICE (ACA) and multiple co-authors (Submission 108 Productivity Commission September 2007), without the strongest possible consumer voice, but independent strong leadership at the highest level with direct Ministerial access, in tandem with other measures, policy setting will not only be failing the general consuming public and vulnerable and disadvantaged consumers in particular, but will be failing industry competition goals.

CHOICE (ACA) with multiple co-authors and endorsement from numerous other community agencies

Whilst some of the thinking appears to have been made, it is comforting to know that the Retail Policy Working Group (RPWG) has not yet reached a settled position on these matters, and one can only hope that the constructive criticisms that have already been made to the Productivity Commission and to Ministerial groups such as the RPWG and the Market Reform Team will be fully taken into account before any settled position is adopted and implemented.

I quote from that submission:

*“But in seeking to improve the operation of markets, the role of consumers in their own right cannot be ignored. That is, there is a need for a well functioning ‘demand side’. Thus policy settings that facilitate effective participation in markets by consumers are an integral complement to competition among suppliers.”*

*“To this end, Australia has in place a broad ranging and multi-faceted consumer policy framework. Generic provisions in the Trade Practices Act 1974 (TPA) and State and Territory Fair Trading Acts are key overarching measures. In addition, there are various industry-specific regulations, and non-regulatory measures such as voluntary industry codes of conduct and arrangements for providing information to consumers to assist their purchasing decisions.”*

*“This framework has been evolving in response to various changes in the market landscape confronting consumers. For example, notwithstanding the more competitive market environment, greater product complexity and new forms of transacting have led to pressure for increased government involvement.”*



I wholeheartedly endorse the views and suggestions already expressed to the Productivity Commission so eloquently by community organizations, notably the CHOICE submission 108 co-authored and endorsed by numbers of others is that to date consumer protections that have been offered by state regulations, notably in Victoria, are fundamentally unsound; largely inaccessible, with poor commitment to compliance enforcement and with complex underlying agendas to either tacitly or explicitly favour industry and competition goals rather than a genuine commitment to upholding consumer protection.

Despite the existence of generic provisions under TPA and FT, these recourses are expensive and far less accessible than they should be as well as possibly hampered by cross-jurisdictional barriers. It is no wonder that industry participants would prefer lighter self-regulatory control and reliance almost exclusively on generic provisions.

The industry-specific complaints schemes are often excessively linked to industry participants as well as to regulators with exceptionally limited powers of jurisdiction, and many are not seen to be objective because of these barriers.

Overall, the framework requires radical change not simply fine-tuning.

**CHOICE (ACA)** has made a joint community submission with endorsement from many others suggesting radical changes to enhance national consumer policy, recognizing that the current framework suffers from impoverishment from a combination of low priority diffusion of responsibility and weak national leadership. These issues are discussed here briefly and at length in the CHOICE submission 108 to the Productivity Commission.

In its 2005 submission to the Ministerial Council on Energy, the EAG discussed merits review and judicial review processes as follows:<sup>291</sup>

*“Merits review can form a significant part of such checks, balances and the reversability of poor decision making which is particularly important in an industry with significant natural monopolies and hence the need for economic regulation. A merits review process acts as an important discipline for regulators in ensuring they undertake an objective, robust and transparent evaluation.*

*However, it is also important to develop a ‘sound’ and ‘fair access’ merits review process (see, for example, issues of standing and funding as discussed in this submission).*

*The EAG is of the opinion that a merits review process given appropriate resourcing being made available to consumers, coupled rules about vexatious and frivolous appeals will lead to better decision making by the market operator and the various regulatory bodies (AEMC, AER, NEMMCo and ACCC) involved in the NEM..*

*The provision of Judicial Review in the NEL/NER provides for a expensive and hopeless outcome where at best “a decision is set aside” and is then sent back to the body that made the poor determination/decision in the first place. It is clear that an independent merits review should give a better outcome and provide scrutiny on poor regulatory decisions. The issue then becomes how to resource consumers in a merits review process so they can effectively participate.”*

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<sup>291</sup> EAG Initial Submission to the Ministerial Council on Energy on National Electricity Law and National Electricity Rules 2005

I wonder whether the AEMC, Productivity Commission and Market Reform Team have yet accessed a disturbing September 2004 Report by Energy Action Group entitled:

*“Report on the Essential Services Commission Energy and Water Ombudsman Victoria Response to Retailer Non-Compliance with Capacity to Pay Requirements of the Retail Code”* September 2004. It deals with serious concerns about consumer protection, systemic deficiency, disclosure, transparency and accountability parameters. It is a must read despite being three years old. The concerns are just as valid now.

This is the link

<http://www.chronicillness.org.au/utilitease/downloads/Energy%20Action%20Group%20report%20re%20retailer%20non-compliance%20and%20the%20ESC.doc>

With the author’s consent I cite the discussion in that document:

***Discussion (by EAR in their report cited above September 2004)***

*The EWOV can make Binding Decisions and could have exercised this power to send a very sharp signal to retailers that non-compliance would not be tolerated. Instead only one such decision has been made, and FCRC (Sharam 2004) reports that taking complaints to the EWOV frequently leaves the customer in the position of having an unaffordable instalment plan.*

*The EWOV also has a MOU (see [http://www.esc.vic.gov.au/apps/page/user/pdf/MOU\\_EWOV\\_Nov03.pdf](http://www.esc.vic.gov.au/apps/page/user/pdf/MOU_EWOV_Nov03.pdf)) with the ESC that it could have used to prompt the ESC into addressing the issue appropriately. It has not used the dispute resolution mechanism available in the MOU.*

*It is also worth commenting that despite EWOV’s efforts to bring this systemic issue to the attention of the ESC, EWOV has not been consistent in its reporting. A more robust identification of the issue as ‘systemic’ and linkage to retailer non-compliance with the Retail Codes may have assisted in prompting the ESC to act. The EWOV also may have bought the regulators lack of action more pointedly to the attention of the public and the Victorian government. A regulatory failure of this scale and duration clearly requires action.*

References (cited in report from EAG)

1. ASIC (1999) *Approval of external complaints resolution schemes*, ASCI Policy Statements [PS 139] [http://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/ps139.pdf/\\$file/ps139.pdf](http://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/ps139.pdf/$file/ps139.pdf)
2. Kliger B (1998) *Unfair Deal*, Financial and Consumer Rights Council, Melbourne
3. [http://avoca.vicnet.net.au/~fcrc/research/utility/unfair\\_deal/index.htm](http://avoca.vicnet.net.au/~fcrc/research/utility/unfair_deal/index.htm)
4. Sharam A (2004) *Power, Markets & Exclusion*, Financial and Consumer Rights Council, Melbourne <http://www.vcross.org.au/images/reports/Full%20Report.pdf>

I have many concerns about the limitations of the current complaints scheme jurisdictions, constitution, funding parameters and excessively close relationship with both the regulators and the market participants. I will not deal with this issue in detail here, but suffice it to say that I was further shaken by the report and the hard data cited. I have just accessed and have grave concerns about consumer protection issues.

In addition, I came across the submission that CUAC made in 2006 to the MCE SCO concerning the poor attitude to consumer consultation and refusal to extend deadlines.

In further support of the concerns that I have already expressed about the consultative process and issues of accountability, transparency I refer to the very same concerns raised by CUAC in their submission to the MCE SCO in January 2006<sup>292</sup>

The Submission was made by CUAC as a comment on the paper *Public Consultation on a National Framework for electricity and gas distribution and retail regulation* (the Paper), prepared by Gilbert + Tobin and NERA Consulting for the Ministerial Council on Energy (MCE) Standing Committee of Officials (SCO). In the opening comments CUAC has mentioned that this body was established

*“to ensure the interests of the interests of Victorian electricity, gas and water consumers, particularly low-income, disadvantaged and rural consumers, are effectively represented in the policy and regulatory debate.”*

Apparently CUAC had sought an extension of a mere

*“two additional weeks to the 24 community and consumer groups representing the main consumer organizations working on NEM issues on behalf of residential and low-income consumers – a key group of stakeholders.”*

It is my understanding CUAC that interpreted refusal of a simple reasonable request as evidence to support concerns about

*“the value that the SCO accords to consumer input, as well as displaying a poor understanding of the resources available to consumer organizations.”*

Finally, I note that CUAC raised concerns about the lack of any research or data to justify a result that would significantly weaken the Victorian regulatory framework.

It was CUAC’s view that the Paper should have stated that

*“the intention behind a regulatory structure is to ensure that consumers benefit from competition and that their interests are protected in the long run.”*

The paper includes valid comments about accountability and the need to achieve proper consultation and

*“the need for jurisdictions to retain jurisdictions must retain the capacity to achieve social and environmental policy objectives.”*

I had not read the submission at the time of completing and forwarding my revised submission dated 9 October also touching upon consultation, accountability and transparency issues, besides issues of evaluative process and balanced assessment of facts in determining Australia’s readiness for completion of FRC by including price deregulation and lightening of the regulatory burden to such an extent as to represent significant consumer detriment.

I have written to numbers of organizations state-wide as listed on the cover letter to AEMC – 28 listed though some still to hear from me as an end-consumer sharing the concerns of many organizations. I have had quite positive feedback from some of these, including Care Financial Inc NSW.

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<sup>292</sup> Consumer Utilities Advocacy Centre Ltd to the Ministerial Council on Energy Standing Committee of Officials Public Consultation on a National Framework for Energy Distribution and Retail Regulation dated January 2006 found at <http://www.mce.gov.au/assets/documents/mceinternet/ConsumerUtilitiesAdvocacyCentre20060116121912.pdf>

I refer to [Andrew Nance's \(2004\)](#) personal submission to the MCE<sup>293</sup> on retail regulation issues is hard-hitting, direct and uncompromising in its evaluation of consumer impacts as a result of FRC and “*competition*” goals as implemented. This too is further discussed in the same section with direct quotes from that submission as a public domain document.

Now the community faces price deregulation also. I quote verbatim from that submission below and suggest that the same concerns should apply to all states, now some three years later, even though it must be recognized that prices are higher for residential electricity in South Australia than in other states.

There is nothing in place yet for proper protections for the vulnerable groups. the position of “**inset customers**” “**embedded network consumers**” and those receiving bulk hot water under arrangements that are well overdue for reconsideration in the public interest and in the interests of restoring fundamental common law, statutory, social justice and natural justices entitlements.

As mentioned elsewhere and repeated here for emphasis, the rights of the entire community are also issues of public interest. It cannot possibly be acceptable to strip these rights away by incorporating into energy-specific provisions anything that will have the effect of making less accessible or altogether unreachable the entitlements that are in place within other protections under Acts of Parliament or other provisions.

Andrew Nance: (2004) submission to MCE

*“SA with the highest residential electricity prices in the NEM (25% increase upon the introduction of FRC) is witnessing a dramatic increase in numbers of group of households referred to in this submission as ‘vulnerable.’ By vulnerable, we mean vulnerable to losing access to the ‘essential service’ of energy (i.e. disconnection from electricity or gas) or vulnerable to having to forego other essentials (such as food, health care etc) as a result of allocating limited financial resources to meeting rising energy costs. Often these households will have low levels of literacy and numeracy, cultural and other factors.”*

*“While reforms continue to ignore the existence of this group of consumers and target the ‘average’ consumer, these vulnerable households will continue to be failed by the ‘market’ and many families will continue to suffer unnecessarily. As the Issues Paper acknowledges, then seems to forget, Electricity and Gas are essential services.”*

*“We have such little information on what is happening to residential consumers (and vulnerable consumers in particular), it is impossible to offer any support to shifting control outside of the state (to what appears to be an unelected, unaccountable bureaucracy).”*

*“It is recommended that the SCO inquire into residential disconnection rates in SA since the introduction of Full Retail Contestability (FRC) on January 1<sup>st</sup> 2003. Further it is suggested that the SCO inquire into why, over 18 months alter, no meaningful data has been released into the public domain. Further it is suggested that the SCO inquire into how many fatal house fires have occurred in SA in homes disconnected from electricity for inability to pay since FRC – and then maybe ask why there have been no inquiries or actions in response.”*

*“The issues paper offers nothing for ‘vulnerable consumers.’ It is asserted that without a more detailed analysis of the potential impacts and complementary measures that would compensate for the impact on vulnerable households, further action on the EMR process is potentially negligent.*

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<sup>293</sup> Personal Submission to MCE SCO National Framework for Electricity and Gas Distribution and Retail Regulation – Issues Paper October 2004

Found at <http://www.mce.gov.au/assets/documents/mceinternet/AndrewNance20041124123357.pdf>

*The fervent pursuit of ‘competition’ and ‘economic efficiency’ while a growing number of households are simply ‘falling off the edges’ can not be justified at this or any other time.”*

*“To assert that the overarching objective of the EM process and the resultant new institutions is the long term interest of consumers’ yet not allow the likes of the AER to consider social and environmental objects (as it represents a distraction from its core business of ‘economic regulation’) is a pretty sad indictment of the forecast capabilities of the organization.”*

*“...The dysfunctional nature of the current advocacy arrangements (and subsequent capacity in the jurisdictions) is widely acknowledged by EMR Officials yet, to add insult to injury, submissions on this issues paper are due before even the earliest discussions on improving consumer advocacy.*

*“There has been no convincing argument presented that this latest attempt to rearrange the deckchairs on the Titanic will actually provide any tangible benefit to consumers. This industry has an impressive ability to capture and retain any efficiency gains and manufacture new elements of risk for which consumers must reward them for managing. Where’s the cost-benefit analysis? The Exec Summary of the Issues Paper (p12) states:*

*“The benefits arising from these reforms are expected to flow to end users and the community as a whole” Why has it been so difficult to attempt to quantify and assure some figures? Why are we being asked to tinker with details when there is no guarantee of benefits to anyone other than simplifying the compliance effort of the industry? This market is supposed to be for consumers is it not?*

Please refer to the Wesley Voice publication Spring Quarterly 2004<sup>294</sup> published with the view of examining what had happened since the application of competition policy

Though relating to competition issues dating back to earlier FRC days, the issues raised and the hard data published serve as eye openers into issues relating to consumer protection and the absence of evidence that large sub-sets of energy end-consumers have benefited from FRC.

That important article was published to examine the impact of competition policy introduced in the 1990s to open up the Australian energy market to competitive forces, in the expectation that competition would achieve cheaper prices for consumers and reduce risks to Government.

Wesley Voice reported as follows cited verbatim:

*“Regulation was seen to be crucial to minimize distortions in the market, encourage competition, set rules and act as an independent voice between competing interests.*

*In South Australia there are two key regulatory bodies associated with the provision of electricity and gas.*

*Firstly there is an Office of the Technical Regulator.*

*This Regulator is responsible for ensuring safety, accuracy of metering within appropriate tolerances especially for gas, making sure that the correct mix of gases is transported through the pipe system.*

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<sup>294</sup> Wesley Voice Spring Quarterly 2004 pgs 1-8 Low income people and energy choices – background to SA Energy Market; and Characteristics of Economic Goods/Services and ‘Essential services’ p 9 found at <http://www.unitingcarewesley-sa.org.au/Portals/0/WesleyVoice%20Issue%201%20--%20Spring%202004.pdf>

*The major burden of economic regulation falls to ESCOSA, the Essential Services Commission of South Australia which has responsibility for regulating price levels, industry standards, codes of practice, etc.*

*Since the introduction of FRC, there has been a paucity of information, particularly about impact on vulnerable and lower income households.*

*Recent research by Professor Richardson and Peter Travers from National Institute of Labour Studies (NILS) shows that 58.7% of the bottom half of South Australian's income distribution are households spending 4% or more of their disposable income on power. About 4.7% of all SA households spend 9% or more of their disposable income on energy, this includes the poorest households in this State, the rate in South Australia is higher than that for the rest of Australia.*

*Five per cent of the lowest quintile of households report being unable to heat their home due to financial stress, this is double the rate for the rest of Australia and is taken for the General Social Survey 2002 (an ABS survey).*

*A Carer's Association survey in 2003/04 found that consumption was on average, 15% higher for carer households."*

*"These recent surveys reinforce observations from welfare and community service organisations that rising energy costs, in particular, and rising utility charges in general are having a significant impact on low income and vulnerable households.*

*UnitingCare Wesley believes that before further moves are made to change energy markets, there needs to be much better understanding of the impacts of the significant recent changes that have been made to the structure of energy markets. For example policy makers and the broader community need a much better understanding of fuel driven poverty.*

*A clear understanding is needed as to what comprises an essential service and what legislative and regulatory arrangements need to be established in order to protect consumers and to ensure appropriate access to essential services. (A short discussion on this topic follows this story).*

*An industry levy should be applied to all sectors of the electricity market that can then be applied to services that assist low income and vulnerable households. In particular this levy should be used to support financial counsellors, given that significant amounts of their work involves utilities problems. The funds would be managed by an independent group drawing membership from energy industry stakeholders.*

*Then the funds could also be utilised for 'retrofit' and other energy efficient measures for vulnerable households, to obtain the best value from a limited energy budget.*

*There is a clear need for community service organisations to work with energy retailers to develop and implement appropriate hardship policies. Similarly there is a clear need for a better understanding of Community Service Obligations as applied to energy markets. For example, on equity grounds, there is a strong argument for a guaranteed minimum supply of electricity for all households - maybe enough to operate a refrigerator, maintain hot water and run a couple of lights.*

*One of the consequences of application of competition policy to the electricity industry has been the loss of data, particularly related to stresses for vulnerable consumers. It is imperative that ESCoSA collect and publish data on disconnections, energy used by household type and in particular develop fuel driven poverty indicators that are published annually, to inform public policy.*

*Before any further moves are undertaken to establish an Australian Energy Regulator, a national fuel driven poverty research project needs to be undertaken. These impacts need to be considered in developing the legislative, regulatory, or programmatic changes.*

*UnitingCare Wesley believes that there is a sound case for State Governments regulating to cap prices if the market is unable to effectively moderate energy prices, as has been the experience in South Australia since application of competition policy to the electricity market.*

- *There is also a view that it is appropriate for State Government to consider re-entering the electricity generation market.*

*Another very useful idea is the notion of socially responsible tariffs (SRT). “In basic form, an SRT has low or no fixed charges and an ‘allowance’ of energy that reflects a quantity that can sustain a basic standard of living at an affordable rate.*

*The cost per unit then increases in ‘bands’ of increasing consumption. Provided a targeted concession regime exists to allow for instances of significant consumption demanded by health needs, such a tariff structure better reflects this ‘essential service’ nature of domestic energy consumption.*

*Such a tariff arrangement is also consistent with, what should be, the environmental objectives of energy markets: maximum energy efficiency and minimum greenhouse emissions. Households that have ‘small’ consumption due to economic circumstance as well as households that choose to limit consumption through active management of demand (or through operating a solar electricity system for example) are equally rewarded for the minimal ‘drain’ they place on the network.”*

*Reproduced from a SACOSS discussion paper written by Andrew Nance.*

## **Summary**

*The application of competition policy to energy markets in South Australia has led to significant increases in electricity prices for residential consumers with particular hardship being caused for low income and vulnerable households.*

*There is a need for concerted action at all levels of the South Australian community including:*

- *It is appropriate that the broader community take active steps to reduce their demand for electricity.*
- *State Government needs to ensure that fuel driven poverty is understood before making further changes to the States energy market.*
- *State Government also needs to review concession policies in the light of growing in energy related hardship.*
- *ESCoSA, the Regulator has a role in requiring transparency of the market through readily available data.*
- *ESCoSA must ensure that hardship provisions are established and applied, recognising that electricity is an essential service and so is different from other standard market goods.*

- *ESCoSA needs to require effective hardship policies from retailers and explore socially responsible tariffs.*
- *GST should be removed from residential electricity bills.*
- *State Government should return to the market as a generator, using renewable energy technologies.*
- *An industry levy is needed to assist with funding financial counselling, in the first instance and other vulnerable household assistance.*
- *The whole community is urged to embrace “Solar Adelaide”, increasing our use of solar energy and reducing the need for new infrastructure.*



## COMMENT ON ENERGY-SPECIFIC REGULATORY CONTROL

Dr Charles Albano<sup>295</sup> uses a chameleon for his logo to symbolize adaptive leadership. He describes adaptation as *“a dynamic process of mutual influence. All creatures act on their environments and their environments, in turn, act on them.”* He claims that organizations are capable of intelligent, purposeful, collective action, those taken to influence their environments in desired directions.

If regulators need to have adaptive leadership styles then they should be chosen carefully, bearing in mind that *“relationships between living entities are circular and interactive.”*

Mark Jamison as lead author of the majority of the studies cited here followed the 2004 literature review with a concept paper written the following year on Leadership and the Independent Regulator.<sup>296</sup>

*Jamison (2005)* claims that:

*“Regulators are sometimes scapegoats for unpopular policies and unavoidably become involved in shaping the policies that they are supposed to implement. As a result of such frictions, regulators are sometimes removed from office or marginalized in some way.”*

He recommends strategies by which adaptive leadership can be used to help constitutes to adapt to new policies and changing situations, whilst still staying in the game.

The foremost leadership skill recommended is the ability to:

*“...get on the balcony and see what is really going with operations, politicians, consumers and others - a meaningful engagement with all stakeholders.”*

Against that backdrop and with limited time to explore other valuable philosophies, I would like to run attention to the social issues and social relevance competition of the deregulation proposals.

I also examine briefly how the effects of competition were evaluated at the outset of FRC in one particularly state where the findings of UnitingCare Wesley were published and are as valid now as they were when written.

With the permission of **Gavin Dufty, Manager Social Policy and Research St Vincent de Paul Society**, I quote more than liberally from his 2004 VCOSS Congress Paper.

Though written four years ago around the twelve month mark following the introduction of full retail competition in some states, it is not only just as relevant today in looking forwards to the next step in completing the energy deregulation cycle but a milestone starting point to promote public debate about the imminent decision that could irreversible detriments not only to competition goals as described in AEMC’s proposals but in terms of the social consequences for the community that were so eloquently discussed by the Select Senate Committee of the Socio-Economic Consequences of the National Competition Policy.

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<sup>295</sup>Albano, C (Dr.) Leadership Skills – What is Adaptive Leadership? 22 April 2007 found at <http://www.selfgrowth.com/articles/calbano.html>

<sup>296</sup>Jamison, Mark A. 2005. “Leadership and the Independent Regulator,” Public Utility Research Center, University of Florida, Gainesville, Florida.

Gavin Dufty's (2004) VCOSS Congress Paper<sup>297</sup> explores

*“the potential and real impact economic regulation has on shaping and redirecting elected governments' social policy objectives.”*

Through case study of the Victorian energy market this paper powerfully illustrates significant social policy issues that have arisen during the review of the effectiveness of retail competition in the Victorian energy market and the review of the Victorian gas and electricity retail code.

Since the issues impact on the role of safety net arrangements; eligibility for government assistance and the potential for universal service obligations for essential services, these issues are as pertinent today in the light of imminent price deregulation in the energy industry, substantial lightening of the regulatory burden to the extent that may occasion detriment to the low-income groups and others with a range of vulnerable and disadvantaged conditions.

The views of Gavin Dufty, Social Scientist at the Victorian Council for Social Service raise:

*“.....significant issues for elected governments, the community and other individuals and organizations involved in the development and delivery of social policy and associated programs. This paper will conclude that governments must legislate to ensure that regulators and other instruments act within the social and environmental framework mandated through the democratic process.”*

As noted by Mr. Dufty, it is of substantial community concern that regulators can

*“propose and implement programs that are contrary to elected governments' policy statements and the ability of regulators to involve third parties, such as the not for profit sector, in being responsible for assessing utility customers' entitlements for waivers of penalties or eligibility for assistance.*

As far back as 2004 Mr. Dufty summed up the beliefs of the Essential Services Commission as follows:

*“Competition will not only deliver the best outcomes for domestic energy consumer but it will also serve to protect them from abuse by companies operating within this market*

*There is a need to strip away Universal Service Obligations (the safety net) as they undermine the benefits of competition.”*

That is now exactly what is about to happen.

Quoting directly from Mr. Dufty's VCOSS Congress Paper:

### *1.0 Background*

*In the mid 1990s gas and electricity industries in Victoria were privatised. As a part of privatization the Kennett Government established the Office of the Regulator General, which was later to become the Essential Services Commission (ESC).*

*The primary objective of the Essential Services Commission is to;*

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<sup>297</sup> Dufty, G (2004). Who Makes Social Policy? – The rising influence of economic regulators and the decline of elected Governments. VCOSS Congress Paper 2004

<sup>297</sup> Powerpoint presentation World Forum on Energy regulation, Rome September 2003 “Are Universal Service Obligations Compatible with Effective Energy Retail Market Competition? John Tamblyn (then) Chairperson Essential Services Commission Victoria.

*Protect the long-term interests of Victorian consumers with regard to the price, quality and reliability of essential services.*

*The Commission's objectives also include a requirement to*

*Promote a more certain and stable regulatory framework that is conducive to longer-term infrastructure investment and to maintain the financial viability of regulated utility industries.*

*In seeking to achieve its primary objective, the Commission must have regard to the following:*

- (a) to facilitate efficiency in regulated industries and the incentive for efficient long-term investment;*
- (b) to facilitate the financial viability of regulated industries;*
- (c) to ensure that the misuse of monopoly or nontransitory market power is prevented;*
- (d) to facilitate effective competition and promote competitive market conduct;*
- (e) to ensure that regulatory decision making has regard to the relevant health, safety, environmental and social legislation applying to the regulated industry;*
- (f) to ensure that users and consumers (including low-income or vulnerable customers) benefit from the gains from competition and efficiency; and*
- (g) to promote consistency in regulation between States and on a national basis.*

*The Commission also has objectives under the Electricity Industry Act 2000, which are:*

- (a) to the extent that it is efficient and practicable to do so, to promote a consistent regulatory approach between the electricity industry and the gas industry; and*
- (b) to promote the development of full retail competition.<sup>298</sup>*

*There are also numerous regulatory instruments that the ESC has at its disposal; these include licenses, codes, guidelines and determinations. It is via these regulatory instruments that the ESC can determine how the providers of these essential energy services operate within Victoria. This includes not only pricing and service quality but also practices and procedures that are to be adopted by the companies when dealing with customers.*

*It is important to note when reading through the objectives of the ESC that the major focus is the promotion of a competitive energy market. The ESC position on such matters can be summed up as follows “as in any industry competition is designed to bring consumers long-term benefits as a result of retailers competing to provide the best combination of products, service and price.”<sup>299</sup> The ESC also believes that competition will serve to protect small energy users from detrimental activities undertaken by companies: “Effective energy retail competition can protect the interests of most consumers”<sup>300</sup>.*

*The ESC even goes as far as believing that “Market-wide USOs (Universal Service Obligations<sup>301</sup>) can inhibit development of competition & limit public & consumer benefits.”<sup>302</sup>”*

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<sup>298</sup> Essential Services Commission, regulatory framework, [www.reggen.vic.gov.au/electricity136.html](http://www.reggen.vic.gov.au/electricity136.html)

<sup>299</sup> Essential Services Commission, power of choice, All about your new power a step-by-step guide, page 4

<sup>300</sup> Tamblin J Chairperson Essential Services Commission, World forum on energy regulation, Are Universal service obligation compatible with Effective energy retail market competition, Victorian experience to date, Rome Italy October 5-9 2003 (now Chairperson AEMC)

<sup>301</sup> Universal service obligations are defined minimum service standards (including price) that are available to all customers, regardless of whether they are on a contract or not.

*In short the ESC believes that:*

*Competition will not only deliver the best outcomes for domestic energy consumer but it will also serve to protect them from abuse by companies operating within this market*

*There is a need to strip away Universal Service Obligations (the safety net) as they undermine the benefits of competition.*

## **2.0 Regulation and social policy**

*During the past twelve months the ESC has undertaken two reviews that have resulted in their entry into the arena of social policy making; in both cases the proposals by the ESC have the potential to detrimentally impact upon low income and disadvantaged Victorians and directly contradict the policy direction and programs of the elected State Government.*

### **2.1 Review of the effectiveness of retail competition and the consumer safety net for electricity and gas.**

*The ESC from time to time undertakes reviews into various matters. In late 2003 it undertook a review into the effectiveness of retail competition. In this review the commission identified that there were some areas where competition was not effective and was failing particular households. In particular the ESC concluded that low volume energy consumption households (with bills of under approximately \$980 per annum) and households that take electricity on an off peak tariff were effectively being excluded from market offers by energy retailers<sup>303</sup>.*

*In response to this, the ESC proposed that the state concession framework be reconceptualised to address these issues of market failure<sup>304</sup>. John Tamblyn, Chairperson of the Essential Services Commission, proposed the question in a world energy forum on regulation: Are universal service obligations compatible with effective energy retail market competition?*

*In this paper Mr Tamblyn proposed three options for reconciling the perceived dichotomy of universal service obligations and competition.*

*Firstly, “raise default price level/restrict price rebalancing/target CSOs to vulnerable users.*

- Increase default margins above supply costs*
- Price headroom<sup>305</sup> as incentive for market offers*
- Higher default price as incentive to seek market offers*
- Support with strengthened information disclosure*
- Restrict extent/pace of price rebalancing*

*Target budget-funded CSOs to unprofitable, low income and remote customers*

*Support with retailer programs to assist vulnerable/low income consumers”*

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<sup>302</sup> Tamblyn J, World forum on energy regulation, Rome Italy October 5 – 9, Are Universal Service obligation compatible with Effective Energy retail Market Competition. (now Chairperson AEMC)

<sup>303</sup> Energy retailers are private companies that sell energy to households.

<sup>304</sup> Tamblyn J, World forum on energy regulation, Rome Italy October 5 – 9, Are Universal Service obligation compatible with Effective Energy retail Market Competition.

<sup>305</sup> Headroom refers to the profit margin that exists for various customers; as such the regulator is suggesting that the profit margin within the default prices should be increased as a means to stimulate competition.

***In this option the Regulator proposes to increase default prices (the safety net) to stimulate competition, give people more information about the market and target government funded CSO, (concessions) to unprofitable customers to compensate for market failure.***

*Secondly “Market prices for majority of users/target default prices/CSOs to vulnerable users.*

*–Most consumers on market contracts/no default option*

*–Minimum retail contract requirements*

*–Supported by strong information disclosure obligations*

*Default contract/price obligations and budget-funded CSOs targeted to low income, remote and welfare supported consumers*

*Supplement with retailer programs for vulnerable users”*

***In this option the Regulator proposes that customers, who accept a market offer, should not be eligible for the full safety net protections. Market offers will have basic protections (e.g. under existing contract protections such as those offered by the Trade Practices Act), more information provision would be provided and retargeted CSO’s (concessions) to act as a subsidy provided to those that the market is failing (in lieu of market contracts.)***

*Thirdly: “Improve Retailer of Last Resort (RoLR) arrangements.*

*Concerns about credit risk/retailer failure can undermine retail competition & consumer benefits*

*–Confidence in operation of wholesale & retail markets*

*–Adverse impacts on affected customers*

*Key issues for an effective RoLR scheme*

*–Clarity on how customers will be reallocated*

*–Clarity on prices and T & C of RoLR service*

*–Recognise financial exposure of RoLR provider*

*–Ensure reasonable terms/treatment of customers*

*Objective of moving customers onto market contracts ASAP”*

***In this option the ESC is proposing the establishments of clear guidelines for a retailer of last resort (i.e. a retailer that will provide energy retail functions where no other will). This retailer would then be responsible for unprofitable customers. They would be financially compensated for the cost of these customers.***

*The ESC goes as far as suggesting that*

*“In considering the causes of vulnerability that contribute to the difficulty that some customers have in participating in the competitive retail market, consideration will also have to be given to whether the most appropriate way for addressing them will involve changes to the energy policy and regulation framework and/or the broader welfare, health and regional policy frameworks.”<sup>306</sup>*

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<sup>306</sup> Essential Services Commission, Review of the effectiveness of retail competition and the consumer safety net for electricity and gas, Issues paper, December 2003,p18

*In all of these models the ESC is proposing to withdraw from the traditional basic protections delivered via universal service. In lieu of a universal safety net offered via universal service obligations, the ESC proposes to protect customers where the market is failing through the establishment of “residual markets”<sup>307</sup>. This residual market would be subsidised by the Government, supposedly using monies currently allocated to fund energy concessions designed to increase affordability of energy services for low income households.*

*There are a number of issues that the ESC’s proposals raise:*

- *There is lack of awareness of and respect for the role and mandate of the State Government in setting and delivering social and other objectives within the democratic process.*
- *It shows that the ESC seeks to reconceptualise the role, scope and purpose of the state energy concessions framework, from one designed to increase access to and affordability of energy services, to one that should be used to address market failures. This not only shifts the target groups for the concessions, but also serves to reduce minimum protections to all Victorians.*
- *It seeks to erode the current framework of regulated price caps and defined minimum service standards.*
- *That targeting concessions to issues of market failure would result in some very wealthy families receiving subsidies from the State, in effect creating a situation whereby the poor within our community would provide a subsidy to the wealthy.*
- *It fails to recognize that due to the dynamic nature of markets over time the market will change, as such those who are excluded now may be included in the future of visa versa. As such there is likely to be a need for the targeting to be reviewed frequently.*
- *It creates the opportunity for private companies to ‘game’<sup>308</sup> the subsidies created to address market failure. This could occur through company’s retreating from providing services to all but the most profitable customers.*
- *It also fails to address the issue of what is an acceptable amount of subsidy that should be provided to those being excluded by the companies.*

### **3.0 Retail code review**

*The ESC has also reviewed the Victorian gas and electricity retail codes; these are the codes that specify the terms and conditions associated with the provision of gas and electricity services.*

*During this review the issue of late payment fees was put on the agenda. Late payment fees for gas and electricity account have not been a feature of the Victorian energy market, although they have started to be implemented in other states (NSW and SA).*

*The State Government has a specific policy that, “(the minister) does not support the introduction of late payment fees on low income and vulnerable customers and do not support their introduction for consumers on deemed and standing contracts”<sup>309</sup>.*

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<sup>307</sup> Residual markets occur when various customers who are directly excluded from mainstream market offers are provided a residual service; this is usually a minimalist type service.

<sup>308</sup> Gaming refers to the ability of companies to increase profit by shifting additional costs or low profitability/high risk customers onto third parties, such as government.

*In the review of the retail code, Energy Policy Unit of The Department of Infrastructure made submission to the review restating it's concerns regarding the introduction of late payment fees and reiterating the Government's policy position on this matter.*

*During this time a number of community organizations including the Salvation Army, Society of St Vincent de Paul, Victorian Council of Social Service, Financial and Consumer Rights Council, all strongly opposed the introduction of late payment fee. In addition to opposing them on equity grounds, these organizations provided various information and data sets that detailed the profile of people paying late and the impact that this would have on Victorian households.*

*Despite the views held by the State Government, members of the community and not for profit sector, and without any reference to the information provided to them and contrary to the information in the data sets, the ESC concluded that late payment fees were to be introduced.*

*The ESC proposed that companies would only be able to introduce late payment fees if they had a defined "hardship policy" that would be annually audited.*

*Furthermore the ESC proposed that people seeking assistance from welfare bodies, the Energy and Water Ombudsman Scheme and communities identified within the Victorian Government's Neighborhood Renewal Program, would be exempted from the levying of late payment fees.<sup>310</sup>*

*In response to the final decision of the retail code the Society of St Vincent de Paul and others raised numerous issue about the consultation process and robustness of the decision, in particular:*

- *The Society expressed a lack of confidence in the transparency and balance of the commission in reaching this decision. Specifically regarding the ESC failure to consider the data that was provided.*
- *In addition to strongly opposing the introduction of regressive late payment charges, the Society suggested that the ESC's proposed 'safety net' to ameliorate the impact is impractical, inadequate and in itself regressive towards low-income/disadvantaged households.*
- *In developing this "safety net" the ESC has 'hard wired' welfare agencies into the energy code, which includes Society of St Vincent de Paul, without any formal or informal consultation. This is a significant concern as this decision has the potential to increase our demand significantly and, in effect, shift cost and risk (in the form of cash flow and debt) from the gas and electricity retail companies to the charitable and not for profit sector. That is, the not for profit sector is to subsidise the for profit sector.*
- *Furthermore the ESC had failed to consider the capacity of the sector to act robustly to deliver the desired outcome. Such capacity issues that have not been considered include coverage of services (are these services available across the whole of the State) and availability of resources (monetary, human and infrastructure).*

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<sup>309</sup> Theo Theophanous, Minister for Energy Industry and Resources, Letter to Gavin Dufty 13/08/2003

<sup>310</sup> Essential Services Commission, Review of Electricity and Gas retail codes – Energy Retail Code, May 2004 Final decision Appendix 2, page 36

- *Introducing a welfare model as a safety net to ameliorate the impact of regressive late fees will in fact act to further stigmatize low income and disadvantaged households. This will occur as such a model fails to recognise that seeking support from a welfare agency can be extremely demeaning. This not only occurs when approaching an agency for assistance, but also and as importantly, when relaying this experience to a third party such as a gas/electricity retailer. The process proposed by the ESC only acts to further disempower low income and vulnerable groups, and hence disadvantage an already disadvantaged group.*

*In short, late payment fees proposed by the ESC are in direct opposition to the policy position of an elected State Government.*

*The process proposed by the ESC to ameliorate the impact of late payment fees fails to consider the capacity of welfare agencies to be an active participant in the proposed safety net, fails to understand the potential of such a process to compound people's disadvantage as it demeans them and finally, it fails to consider that many will self-select out of the process, as they do not wish to be demeaned. This the society concluded has resulted in the ESC being derelict in acting in accordance with section 8(2) of the Essential Services Commission Act 2001, in particular (f) (to) ensure that users and consumers (particularly low income and vulnerable consumers) benefit from competition and efficiency<sup>311</sup>.*

#### **4.0 Implication for social policy**

*These two case studies highlight significant issues for social policymaking and elected governments. Some of the issues include -*

*ESC proposes that an increase in energy prices would create more 'headroom' thus stimulate competition, which will turn drive down prices. This strategy is based on many assumptions, but significantly it fails to consider the likely impact that this may have on many within the community regarding both access to and maintenance of essential energy services. By increasing safety net prices many households that are unattractive to energy retailers will be stranded at this higher price effectively creating a two-tiered energy market. In effect the ESC is proposing to increase costs for many who are already disadvantaged purely to stimulate competition with little to no regard for the social impacts.*

*The ESC directly seeks to challenge and reconceptualise State Governments policy and program commitments of offering Universal Service Obligations with guaranteed minimum terms and conditions as a form of social protection The ESC proposes to offer protection this via the introduction of 'residual markets'. That is the safety net should only be offered to those that are not profitable to private companies or others groups that are excluded from participation in the competition market. This could include low volume households, all electric households with off peak or tenanted households.*

*The ESC proposes that such safety nets that are targeted to address competition failures should be directly funded via reconfiguring the current energy concession framework which are designed to increase energy affordability not mitigate against access to market offers. This has significant implications for Victorians as not all people where the market fails will be low income as such the concession become a subsidy for market failure rather than a for of energy supplement based on income and asset assessments.*

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<sup>311</sup> Dufty G, Letter to J Tabmlyn regarding retail code, 31 March 2004



*In short it becomes a market subsidy provided to private companies rather than an energy subsidy provided to disadvantaged Victorian households.*

*The ESC in allowing the introduction of late payment fees directly contradicts government policy directives, but in conjunction with the 'welfare model' safety net actually further demeans and disadvantages a group that is already disadvantaged. In short the office of the regulator is making changes to industry practices, with significant social implications for the community.*

*The ESC actions highlight the that the current regulatory framework allows for an unelected economic regulatory authority to both directly change companies' practices, or promote various policy solutions that are contrary to the state governments policy and program objectives including the provision of universal safety nets, guaranteed terms and conditions, state concessions, health and regional policy frameworks in the form of a targeted subsidy to address energy market failure.*

*Such actions by the ESC significantly change the nature and the scope of the democratic process with regards to essential energy services. This highlights that public servants can make and implement policy that is directly contrary to the wishes and commitments of Governments.*

*The ability of the ESC to institute or propose these changes has significant impacts for the state regarding the cost of and the robustness of the current energy concessions framework and down stream impacts on other social institutions such as the welfare and not for profit sector.*

*These case studies highlight the need for changes to the Essential Services Commission Act these changes should require the commission to make decision and proposals consistent with and supportive of the policy and program objectives currently being delivered. This should extend to consider Federal, State and Local Governments objectives.*

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- 4. Essential Services Commission, Review of the effectiveness of retail competition and the consumer safety net for electricity and gas, Issues paper, December 2003*
- 5. Tamblyn J, World forum on energy regulation, Rome Italy October 5 – 9, Are Universal Service obligation compatible with Effective Energy retail Market Competition.*
- 6. Theo Theophanous, Minister for Energy Industry and Resources, Letter to Gavin Dufty 13/08/2003.*

I vigorously support such a perspective and all of the observations and recommendations made.

As repeated in the consumer policy section, the incremental way in which the current consumer framework has been evolving in response to changes in the market landscape confronting consumers has resulted in a retrospective band-aid approach that has led to complexity, duplication and even confusion for all stakeholders.

It is generally acknowledged that regulatory burden has scope for rationalizing, harmonizing. However, much more than that is required especially with regard to structuring a strong, functional consumer policy framework that, under the strongest independent leadership is capable of regular review and restructuring to respond to dynamic market needs.

In relation to community service obligations in sharp contrast to the views analyzed above and those expressed by John Tamblyn during his Powerpoint Presentation in Rome in 2003<sup>312</sup> questioning the value of Universal Service Obligations, the National Competition Policy as restated in the Senate Select Committee Report 2000 categorically embraces the CSO (otherwise known as USO) as follows:

### ***Community Service Obligations***

*“An important aspect of NCP is the ability of Governments to recognize and address Community Service Obligations (CSOs).Historically, many goods and services have been supplied to people in Australia on a cross-subsidized basis rather than a full cost recovery or cost reflective basis. These include water, sewerage, electricity, gas, roads etc.*

*The system of cross-subsidization in each industry has arisen through some governments’ commitment to equality of access and commitment to development. The high costs of the construction of infrastructure to support these industries has necessitated government pricing and supply policies which support these objectives.*

*Cross-subsidization has taken a number of forms, including, from commercial or industrial users to domestic users; from wealthy to disadvantaged consumers; between population generations, (viz from the working age population to pensioners), from cities to rural, regional and remote areas. The ‘public interest test’ raises the issue of broad social goals and the concept of Community Service Obligations. The Productivity Commission (Industry Commission) estimated Australia’s expenditure on community service obligations to be in excess of \$3 billion.<sup>313</sup>*

*The Competition Principles Agreement obligates governments to address the issue of community service obligations but does not define them. While it encourages ‘transparency’ of operation, NCP leaves the responsibility to each individual government to determine definitions and construct. Consequently, each State and Territory has different models of operation and implementation of CSOs.*

*One of the problems with CSOs is the need for exhaustive definition of them to be undertaken to facilitate a seamless transition to corporate or private supply. This is difficult to achieve where these services have not been previously provided as part of a distinct program. Further, the service may be intermeshed with other services, and the removal or downgrading of one may collapse others.*

*For example, the post office or local chemist is often a focal point for small rural towns. The closure of these often causes a flow-on of closures of other businesses as people are forced to other centres for the original services.*

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<sup>312</sup> Tamblyn J, World forum on energy regulation, Rome Italy October 5 – 9, Are Universal Service obligation compatible with Effective Energy retail Market Competition. (now Chairperson AEMC)

<sup>312</sup> Energy retailers are private companies that sell energy to households.

See also Gavin Duffy’s rebuttal “Who Makes Social Policy – The rise of economic regulators and the decline of elected governments.

<sup>313</sup> Industry Commission, February 1997, Community Service Obligations: Policies and Practices of Australian Governments, Information paper, Canberra, AGPS, p20.

*There is concern that community service obligations are at risk when governments commercialize, privatize or contract-out such services. This need not be so, as Mr Samuel commented:*

*National competition policy does not prohibit community service obligations. Indeed, in our various annual reports and documents we have encouraged, urged and exhorted governments to address issues of community service obligations. It does not prohibit universal service obligations. It does not prohibit the provision of proper services of health, education, telecommunications, water, power, transport or housing to all sections of the community such as they may be entitled to in a properly constructed, fair Australia. The failure of governments to address those issues is not an issue of national competition policy; it is a failure or dereliction of national social policy.<sup>314</sup>*

*In the Committee's view recognition of the ability of NCP to coexist with CSOs provides the response to the concerns expressed by Mr Ritchie of the NFF:*

*We at NFF are saying: why are we throwing out the principle of beneficiary pays and making it user pays? Another example is what is going to happen to the cost of electricity distribution to any inland town at the moment. The new system dictates that they pay the full cost of the transmission of electricity along those wires. So almost immediately we are going to add a new cost onto rural and regional Australia that will not be apparent for anybody in metropolitan Australia. These are the dangers we see in user pays pricing principles. Only two consequences can come from it: underprovision of infrastructure or an increase in the price of infrastructure. Logically, nothing else can happen.<sup>315</sup>*

*The Committee sees value in CSOs being kept under review to monitor their continued need and ensure the most effective method of delivery is being used."*

**Recommendation**

9. *That CSO commitments be publicly acknowledged, monitored, and regularly reported on.*

*In reviewing the overall structure of the application of NCP, the Committee noted the lack of any formal appeal mechanism against the findings of a legislative review where public interest is claimed. There are a number of ways of addressing this shortcoming in the administration of the policy and the Committee would see this as a matter for consideration by CoAG.*

***Inconsistent interpretation of public interest test between the States and Territories***

*The Committee is concerned that the disparate administration of NCP may lead to different interpretations of the policy and differing applications of the public interest test. The Committee accepts that the NCC has sought to educate the widely dispersed administrators of NCP but, clearly, the education has not worked as well as intended. The NCC itself recognises this and is taking further steps to correct it.*

<sup>314</sup> Mr G Samuel, President, NCC, Committee Hansard, 1 November 1999, p 879

<sup>315</sup> Mr T Ritchie, Director Economic Policy, National Farmers Federation Committee Hansard, 1 November 1999, p 917

The Executive Summary of the Senate Select Committee Report of 2000<sup>316</sup> contained recognition of particular problems on infrastructure-related issues. Including road and rail with mention as well of issues with the regulatory practices for utilities, particularly following privatization.

Since these issues were related to infrastructure were seen to be central to the future equitable development of the Australian economy and society, the Committee recommended that the special attention by CoAG was warranted.

Two of the recommendations were that:

*That a public consultation process be mandatory in relation to applications for access to major public infrastructure facilities. (Chapter 6, Recommendation 30)*

*That issues relating to the regulation of infrastructure services are of serious concern and should be a matter for priority discussion by CoAG. (Chapter 6, Recommendation 33)*

Chapter 6 concluded with these statements.

## **Conclusion**

The Committee has concluded that the community is demanding greater government attention to the finer application of the policy and its impact on the social fabric of communities.

The community wants greater attention given to the intangible costs of policy changes, and the methods by which such costs can be alleviated such as transitional arrangements, employment programs, and community service obligations.

I quote below verbatim an extract from an online dialogue between evaluators that struck me as having extraordinary relevance to the task of current Inquiries and reviews associated with regulatory reform.

### **Bill Harris Facilitated Systems.com:**

*“The lesson seems simple: it's management's job to ensure the proper system / structure is in place in an organization to get the desired results. If that's been done, it doesn't much matter whether management "holds people accountable" (punishes transgressions with vigor) or not; the results should be good. If that hasn't been done, management is better served by being rather less heavy-handed in pushing for accountability.*

*Since any of us, including management, can and do make mistakes from time to time, it makes sense for management to assume a low-pressure stance just in case their organizational design isn't the one they need.*

*“This is, I think, a setting in which a systems approach to evaluation can help. The model showed how direct management action (pressure) might get good results quite rapidly, results that would be followed by significantly worse results soon thereafter, while structural changes would get consistently good results.*

*Does that make any sense? Have others seen similar situations? What do you see as the limits of this lesson (assuming you agree it has validity over some range)?”*

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<sup>316</sup> “Riding the Waves of Change” A Report of the Senate Select Committee on the Socio-economic consequences of national competition policy, Executive Summary found at [http://www.apf.gov.au/Senate/Committee/ncp\\_ctte/report/b01.doc](http://www.apf.gov.au/Senate/Committee/ncp_ctte/report/b01.doc)

If you're curious, you can read more on that model at <http://facilitatedsystems.com/expmngmnt.pdf>; it also contains a pointer to the project in which we implemented these changes and reduced variances by 95%.

In its submission to the Ministerial Council on energy in July<sup>317</sup>, the ACT Council of Social Services, as a peak representative body for not-for-profit community organizations, people with disadvantage and low income citizens of the Territory, with membership of the COSS network, made the following observations

### ***Broader Objectives for the National Electricity Law***

*As currently drafted, the objectives of the NEL are very narrow and reflect a dogmatic belief that "efficient investment" and "efficient operation and use of electricity services" necessarily will contribute to the long-term interests of consumers. ACTCOSS contends that the objectives must be stated in broader terms, must exclude belief systems about the effects of market competition, and, in particular, must make specific reference to social impacts and long-term (generational) sustainability.*

#### *Regulation of Smart Meters*

*ACTCOSS has very grave concerns about the social impact of pre-paid meters on low income consumers. In our opinion, it should be open to jurisdictions to ban PPMs outright (as is the case in Victoria). Where the technology is permitted, it should be strongly regulated along the lines of the current SA regulations. The current ACT regulation of PPMs is adequate but lacks some important features of the SA scheme.*

*Regulation of PPMs must be finalized before the commencement of the NEL and Rules as the new smart meter technology has an inherent PPM capacity.*

### **The Need for Effective Hardship Programs**

All retailers should be obliged to have and apply hardship policies and hardship programs which address inability to pay issues.

ACTCOSS strongly supports the existing ACT hardship arrangements which are delivered through a statutory body, the ACT Essential Services Consumer

Council, in conjunction with an obligation on retailers to have in place internal arrangements for identification and management of hardship cases.

ACTCOSS considers that the Composite Paper's Recommendation in relation to "Payment difficulties" is inadequate and that assessment of "capacity to pay" is an integral part of any hardship program. The mechanism for identifying and managing hardship may vary between jurisdictions but it must be founded on a requirement to protect vulnerable consumers as is the case in both of the current ACT and the Victorian arrangements.

*"No analysis of social impact is complete without mention of the regional public interest test. It is well accepted that at a regional level often a national level public interest test is just not relevant."*

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<sup>317</sup> ACTCOSS Comment on the MCE National Framework on Non-Economic Distribution and Retail regulation by the Retail Policy Working Group Found at <http://www.mce.gov.au/assets/documents/mceinternet/ACTCOSS20070723094513.pdf>

**Mr. Ritchie** National Farmers Federation.

*“Finally, I note that I was surprised that regional considerations were not on Brent’s list.*

*If we are going to have a public interest test we have to make sure it is done at a regional level because sometimes a national level public interest test is just not relevant.”*

Having examined very briefly some of the social issues and reform impacts to date, I would like briefly to look at the way in which this review has been undertaken.

I had been quite concerned that the analysis was limited to starting at the middle of the distribution chain and predominantly limiting information gathered relied upon and published to the retail arm of the marketing chain

The retailers have to manage the risk, but unless a most robust analysis is undertaken of the entire marketing chain,

Ritchie, from the National Farmers Federation.

*“The other aspect I would like to add to any public interest test is that there should be an analysis of the marketing chain through which the variety of products that are under discussion exist. I will keep these remarks short. We only really need to look at dairy deregulation and the impact of that on the final price paid by consumers. It would seem to me that we did not have a reasonable enough analysis of the various marketing chains through which the product went from its raw form to process form.”*

*“Social issues and social relevance is very much a part of competition policy and ought to be applied with all the wealth of experience that has been developed over the past 25 years in the administration of the authorization of public benefit and public interest tests.”*

I urge the Retail Energy Policy Working Group, AMEC, the SCO, MSO, and the Productivity and each other segment of Government involved in examination of revised policies and regulation will heed these cautions – in the public interest.

Should Australians be taking heed of the cautions expressed by Edmund Mierzwinski, consumer program director at the US Public Interest Research Group in Washington. In his words

*“I am worried about industry lobbyists bearing gifts. I don’t trust them. Their ultimate goal is regulation that protects them, not the public.”*

As reported in the New York Times<sup>318</sup>, in quoting Jenny Scott, vice president for good safety programs of the Grocery Manufacturers’ Association:

*“It’s a little unique when both consumer groups and industry associations are out there saying that we need new regulations, and the government doesn’t agree,”*

Robert Shull, deputy director for auto safety and regulatory policy at Public Citizen a consumer advocacy group based in Washington, said his organization and other consumer watchdogs would be keeping close tabs to see if these different proposals amounted to more than simply “opportunistic attempts to avoid real regulation.”

Should Australians be asking the same questions and be wary of industry motives?

I note the eloquent and credible submission to the Productivity Commission dated 11 May 2007 made by TRUenergy’s Head of Regulation and Government Relations. By way of background

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<sup>318</sup> Ibid, p 2 NYT 16 Sept07 In Turnaround Industry seeks US legislation

TRUenergy is the trading name for China Lighting and Power, a wholly owned company registered on the Hong Kong Stock exchange, with substantial interests in various thriving infrastructure entities at home (in China) and abroad. TRUenergy (CVP) had purchased TXU Australia, and EasternEnergy.

At that time the generator and retailer arm stayed with TRUenergy, whilst following part demerger the distributor arm SP Ausnet was purchased by Singapore Power. The latter, with investment partner consortium Babcock and Brown (Group) purchased Alinta recently, who had also acquired Mutlinet, GasNet, AGL (followed by demerger with AGL Energy). Also as an aside, Origin Energy Networks whose assets comprised Origin Energy Management (OEAM).

(OEAM), comprising Origin Energy, TRUenergy and AGL were the assets management team contrasted to Envestra, Australia's largest gas distributor. Those assets were sold to APA (Australian Pipeline Assets) in July 2007, with APA replacing OEAM as the management and operations services to Envestra Ltd as Australia's largest gas and transmission company. APA has a 17 percent stake in Envestra, and one-third interest in the SEA Gas pipeline. OEAM, now owned by APA also included a range of smaller complementary assets including NGV stations, cogeneration facilities and an interest in services provider to the water industry.

In a climate of mergers and acquisitions, predominantly vertical or horizontal in nature, many such acquisitions being by powerful overseas companies increasingly commandeering the infrastructure market in many quarters of the world, including Australia, will the moves to shed regulatory burdens actually result in enhanced, if any, substantial consumer protection, given that under strict regulation these protections are already compromised.

I have already digressed too far into competition issues, but these are not insignificant considerations when endeavouring to determine whether current regulatory proposals will actually have the desired effect of removing barriers to competition in a climate where the larger powers are consolidating and expending at a rate that may hurt smaller competition more than they enhance competitive activity. Other competition considerations will be separately addressed to AEMC's Retail Competition Review in response to their Draft Report.

Meanwhile further discussion of the current consumer policy framework in the energy retail sector is addressed in relation to selected provisions, and with reference also to TRUenergy's submission to the Productivity Commission in May this year (Sub034).

Getting back to the energy industry and current Inquiries and Reviews, and beyond that to the hard work that is undertaken on an ongoing basis by the Retail Policy Working Group and the Retail Market Policy Group as well as the Productivity Commission.

The concept of civil penalties has already apparently been accepted in principle by the RPWG as recommended by Lyndon Griggs and others.

There are some areas that appear not to have been considered at all, and indeed appear to have been altogether swept under the carpet. I would like to highlight one in particular – the protections for those who are embedded end-consumers of energy receiving bulk energy not separately metered for energy, and whose contractual position deserves clarification as a first principle before any other considerations are entertained.

The range of considerations encompass provisions under unfair trading practices, particularly within the Victorian legislation; body corporate (owner's corporation) considerations and provisions; trade measurement provisions; trade practice considerations; common law provisions; rules of natural justice and of social justice. These issues are discussed in great detail in the specific response to the ARR Consultation Paper dated June 2007.

What about the general and specific rights of consumers at large? Should their enshrined rights become even more inaccessible than they are within the energy industry in particular?

Existing protections appear to be compromised even under apparent strict state regulation. These may be pertinent questions:

1. Will any national energy framework improve matters unless due care is taken to ensure that in an eagerness to reduce regulatory burden, consumer protections become even more inaccessible?
2. Why should only vulnerable and disadvantaged consumers be targeted through various means?
3. What about the general and specific rights of consumers at large. Should their enshrined rights become even more inaccessible than they are within the energy industry in particular?
4. Will the proposed changes address the associated health issues and maintenance liabilities, particularly with regard to the proposed national water heater strategy?
5. What of the existing sub-standard apartment buildings and public housing dwellings? How will upgrading be addressed to bring these into line with proposed changes and standards?
6. How can low fixed income residents afford a rent hike that is associated with landlord outlay to retrofit to keep up with the new measures proposed by E2WG?
7. What will the Government do to meet capital costs of retrofit undertakings? If no action is taken, what liabilities will be faced in public health terms and the cost of treating serious, often fatal illness?
8. How seriously will compliance enforcement be undertaken as expected by dedicated manufacturers wishing to embrace national policy and regulatory consistency?
9. How will the complex contractual and liability issues be addressed collaboratively?
10. What interim measures will be put in place to address consumer protections, advocacy needs, enforcement issues and overall coordination of issues that fall under several jurisdictional umbrellas?
11. How will ongoing community consultation be effected, bearing in mind not only consumer issues, but the needs and expectations of the industry responsible for research and development plans conceptualized a long way ahead?
12. What follow-up measures will be undertaken?
13. How will accountability needs be met?
14. Will expert evaluative design inputs be sought when relying on data gathered to inform public policy?

The Retail Policy Working Group, Ministerial Council on Energy; The National Framework on Energy Reform Working Group, MCE, and the Australian Energy Market Commission (AEMC) may wish to refer to the quality submissions that have been made to them, to the Productivity Commission and to other arena before making final determinations, and whilst awaiting the Productivity Commission's deliberations and recommendations.



Perhaps the Productivity Commissions impending Inquiry into Australia's Consumer Policy Framework will assist to achieve some level of balance and objectivity. The public eagerly awaits the Commission's draft and final reports and further public consultation forums as well as ongoing consultation and input that is both meaningful and timely.

### **Conclusion**

In conclusion, responsible energy reform is welcomed in Australia.

Amongst the factors that may impact on compromised consumer protection and on best practice formulation and implementation of standards may include the speed with which decisions are being made and concerns about public accountability, transparency and genuine commitment to consult beyond either manipulation of tokenism in seeking community input.

The public seeks improved and timely access to deliberative decisions of the import envisaged.

*Madeleine Kingston*

**Madeleine Kingston**  
**Private citizen**

**Enquiries about this submission may be directed to Madeleine Kingston**  
**[mk2711@bigpond.net.au](mailto:mk2711@bigpond.net.au) or (03) 9017-3127**