



Harcourt Business Park  
Unit 16, 809 - 821 Botany Road  
Rosebery NSW Australia 2018  
(entrance off Harcourt Parade)

T: +61 (2) 8335 3333  
F: +61 (2) 8335 3300  
E: info@gridxpower.com

29 June 2007

John Tamblyn  
Chairman  
Australian Energy Market Commission  
Level 16, 1 Margaret Street  
Sydney NSW 2000

Dear Mr Tamblyn,

**Re: Review of the effectiveness of competition in the retail gas and electricity markets in Victoria**

The following is the GridX Power Pty Ltd (GridX) submission to the review of the effectiveness of competition in the retail gas and electricity markets in Victoria. GridX welcomes this review, and has structured its response around the criteria for competition that has been established by the Ministerial Council on Energy.

GridX is a distributed generation provider that uses natural gas to produce electricity and thermal energy services – distributed power, chilled water for air conditioning and hot water to homes and businesses – commonly called district supply schemes and we operate such a scheme at Glenfield, NSW.

The benefits of the technology are that it improves energy efficiency, it reduces emissions of greenhouse gases, and provides a demand management solution for electricity networks. Typically these are also “islanded” in that energy can be exported to the grid but need not be imported. GridX Power has recently applied to IPART for an islanded Retail Licence (already have a normal Retail Licence) and this is currently the subject of an IPART Consultation Paper. In short the GridX projects provide alternatives for developers and customers to waiting for or paying in total the augmentation and reticulation of existing distribution networks by incumbents and the economics hinge on full service delivery.

One of the key differences of the GridX system is that the customers are in the end tied to gas prices rather than NEM prices which is currently a very attractive proposition and highlights the issues associated with capped retail prices and that competition can come from innovative solutions if the market is allowed to deliver these to customers and is not overly regulated.

It should also be well argued that should the retail market prices drift up after removing price caps this is actually the market at work – it is signaling the need for capacity and there will be a range of responses to this signal which will include for example some reduction in demand and uptake of energy efficiency and of course development of solutions like GridX systems and projects.



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It can equally be argued that price caps that do not continually reflect the flux in the market costs or allow structuring to pass price signals through more cost reflectively will lead to an over use of power (dead weight loss).

Therefore, GridX is of the view that innovation and choice in the Victorian retail energy market will be improved by the removal of regulated retail prices. Further, the Victorian electricity industry contributes a significant proportion to the States total greenhouse gas emissions and this could also potentially benefit from removal of retail price caps as it excites innovation and exercises demand elasticity. In order to create alternative energy products and services for consumers, the retail sector needs to be able to structure its offerings without price regulation by Government.

GridX would also point out that there is a significant difference between price caps and consumer protection. If the market is indeed competitive (and GridX believes it is as outlined below) then price pressure will prevail and prices will tend to reflect real underlying costs and associated market risks with monopoly type rents forced out of the market. In short market economics will prevail.

This does not however mean that consumer protection is not required and we would submit that the National Trade Practices Act and Competition Law, and Consumer Provisions in place in Victoria do provide that protection. Our only suggestion is that if price caps are removed (as they should be) then for a period of time some form of retail price discovery mechanism be implemented to assist with consumer choice and market information – and to comfort policy makers that the market is operating competitively. Market share we do not believe is an issue related to price caps but more to the key aspects of Competition Law - and again we believe that the ACCC may be well placed to deal with those matters should they arise – particularly if there is price discovery in place for some time.

On this basis we have responded to the MCE criteria for competition as follows:

### Customer Switching & Market Shares

GridX believes that customer switching is the clearest indication for the success or otherwise of competition in a market. It shows that customers are aware of other providers and have accepted alternative offers from these retailers.

Victorian customer switching rates are as high as those in the United Kingdom. GridX has reviewed monthly switching numbers for small electricity customers in Victoria and the UK. In the 15 months to March 2006 approximately 28% of Victorian small electricity customers<sup>1</sup> changed retailer, while only 21% of UK domestic electricity meter points switched (Appendix A). The UK energy regulator removed price caps on small energy customers in 2002.

<sup>1</sup> Assumes one NMI is one customer



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While we recognise that Market Share is another criteria identified by the MCE, we believe that shares in customer numbers amongst market competitors are a direct outcome of successful customer switching but do not in themselves constitute a marker for competition – the issue is more related to market power and its possible abuse and this is currently better dealt with under Competition Law.

### Entry and Exit of Suppliers & Barriers to Entry

GridX is of the view that the existing price regulation in the Victorian electricity market over the longer term will both discourage the entry of new retailers and drive small existing suppliers from the market. While wholesale prices have been reasonably low new entrant activity has been active. However over time as price volatility and price shocks occur price regulation provides a clear barrier to entry as new entrants are unlikely to be able to purchase wholesale electricity contracts at rates that enable them to operate a viable business. These capped prices lag the market – as in fact they always will.

Wholesale electricity prices have now achieved unprecedented highs in Victoria and other States. If these levels are maintained for extended periods, GridX believes that small retailers will be forced to exit the market if they can not procure cost effective hedges that fit within the capped price regime or the regime fails to respond in a timely way (which GridX believes is not really viable). GridX understands that this has recently occurred in NSW for example with the departure of Energy One from the retail electricity market<sup>2</sup>.

The key here is the ability for the regulated system to respond quickly to the NEM volatility and this will never be the case – market interventions such as price regulated caps will always struggle in volatile markets and unfortunately the groups most susceptible are actually new entrants – not existing market players and this really is counter to developing competitive markets. It is clear that lifting market caps at this time would assist competition in our view. If the issue is the regulated regime having to continually adapt for market changes then the answer would be to remove these caps.

### Price and non-price offers

GridX has no doubt that the range of price and service offers available to customers will be improved if regulated price caps are removed. Competitors will be able to afford to make new and inventive service offerings and to test their suitability in the market, and to move to more cost reflective tariff options. This will promote innovation in the market and consumers will subsequently have more choice available to them. This is to be contrasted to a situation where price controls exist, margins are slim and the smaller market participants find it difficult to maintain a viable business.

<sup>2</sup> Australian Financial Review June 23-24, 2007, page 7



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## Customer Experiences

GridX believes that an energy market providing customers with innovative products and services will give the most positive customer experiences. This type of energy market is best facilitated by deregulated energy prices and the promotion of competition. Consumer protection should not include Regulated Prices in a competitive market – it should include the types of protections already available under Competition Law, Ombudsman Schemes, State base consumer protection, etc. and in our view a period of market monitoring and price discovery.

There is little doubt that the supply of electricity and gas is an essential service that does require the involvement of Government to monitor the activities of retailers and to establish a supplier of last resort scheme. Community organisations in the past have raised concerns that a competitive energy market will be to the detriment of consumer protection. However the average household currently spends only 2.7% of its income<sup>3</sup> on electricity and gas, and Australian energy prices are currently among the lowest in the world<sup>4</sup>. Regulated pricing cannot be sustained where the upstream wholesale market is fully competitive. If price caps are removed in Victoria, low income households could be subsidised with an energy rebate scheme by way of Government policy.

The customer experience of consuming energy is now inextricably linked to the emissions of greenhouse gases and global warming. It is likely that a national emissions trading scheme will be introduced from 2012<sup>5</sup>. Deregulated prices that include the price of carbon can provide clear price signals to consumers that will enable them to manage energy consumption more efficiently.

We hope that the information provided in this submission assists the AEMC with its review of competition in the Victorian retail energy market.

Yours sincerely,

**Colin Chambers**  
Chief Executive Officer

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<sup>3</sup> Australian Bureau of Statistics

<sup>4</sup> Electricity Supply Association of Australia

<sup>5</sup> Prime Ministerial Task Group on Emissions Trading - Final Report June 2007



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## Appendix A

Table 1: Electricity meter transfers for small customers

	Victoria small customer transfers <sup>6</sup>	UK domestic meter transfers <sup>7</sup>
Jan-05	32,414	242,589
Feb-05	33,855	359,311
Mar-05	32,879	389,804
Apr-05	37,949	390,523
May-05	42,309	368,951
Jun-05	39,293	364,951
Jul-05	44,592	329,983
Aug-05	40,502	374,575
Sep-05	38,152	348,119
Oct-05	43,828	416,099
Nov-05	38,833	385,182
Dec-05	39,012	352,808
Jan-06	37,890	281,311
Feb-06	41,142	344,026
Mar-06	46,444	535,759
<b>TOTAL</b>	<b>589,094</b>	<b>5,483,991</b>

Table 2

Approximate number of small Victorian electricity customers at June 2004	UK domestic meter points at March 2006
2,100,000	26,695,229

Table 3

	Victoria	United Kingdom
Estimated % of small customers that transferred during the 15 months to March 2006	28%	21%

<sup>6</sup> NEMMCO retail transfer statistical data. A small electricity customer uses less than 160 MWh per year.

<sup>7</sup> Ofgem Domestic Retail Market Report, March 2006