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Australian Energy Market Commission
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Review of the Effectiveness of Competition in the Electricity Retail Market in the Australian Capital Territory: Stage 2 Draft Report

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Australian Energy Market Commission's (AEMC) Stage 2 Draft Report for its review of the effectiveness of competition in the Australian Capital Territory (ACT) electricity retail market.

esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of over 40 electricity and downstream natural gas businesses. These businesses own and operate some \$120 billion in assets, employ over 52,000 people and contribute \$16 billion dollars directly to the nation's Gross Domestic Product.

Overall, esaa commends the AEMC for the reform approach set out in the Stage 2 draft report. It provides a broadly sensible way to advance competition in the ACT retail electricity market. Further, it will provide impetus for the wider program of energy market reform in the National Electricity Market (NEM).

The Stage 1 final report

The Commission's Stage 1 final report reaffirmed the findings of the Stage 1 draft report that competition in the small use retail electricity market in the ACT is not effective.

While this finding is unwelcome, it is not unexpected. As the Association has consistently argued retail price regulation is a barrier to competition and an obstacle to the further development of Australia's electricity markets. The Association's submission to the draft report and the research report attached to that submission entitled *Unfinished Business: Retail Electricity Price Deregulation in Australia* outlined in detail the adverse impact of price controls on retail competition and other parts of the supply chain, as well as the importance of deregulating prices to achieve other policy objectives, such as greenhouse gas mitigation.

The Stage 2 draft report

Under the Australia Energy Market Agreement (AEMA) retail reform process, the AEMC is required to provide advice on ways to promote the growth of effective competition for those users that do not enjoy effective competition.

The question confronting the AEMC in developing its advice for Stage 2 of its review was therefore what is the most effective way to promote the growth of competition in the ACT?

esaa's submission to the Stage 1 draft report firmly contended that, despite the finding of a lack of competition, the most effective way to promote competition was to abolish the regulated retail price for electricity. This view is based on the logic that given that price regulation is the key barrier to competition, the appropriate response is to remove price regulation. The Association argued that failure to remove regulation risked locking the ACT in the circular policy trap where insufficient competition is used to justify continuing price regulation, which further entrenches lack of competition through being a barrier to entry.

The Commission's Stage 2 draft report considered a range of pricing and non-pricing options to promote competition. Its draft recommendation is a two phase process involving a mixture of both.

Phase one involves a package of measures to foster customer awareness and reduce the 'stickiness' of customers:

- instigating a consumer education program for small electricity users (through the relevant department) that provides information on the electricity market;
- setting up a marketing campaign to inform customers of an internet and telephone facility for consumers to investigate and compare all current electricity supply products available to them as customer awareness improves;
- review the framework governing the customer protection and switching process, such that it is easy to understand and progresses smoothly. Informing customers of options for redress should problems arise;
- implementing nationally consistent frameworks, such as the NECF, as soon as practicable, to improve the harmonisation of regulatory requirements between the ACT and other jurisdictions; and
- possible merit in reviewing the guidelines for costs allocation relevant to ActewAGL.

The AEMC recommends that six months after the implementation of the phase one package of measures the ACT Government should implement phase two. Phase two consists of:

- the removal of retail price regulation for small consumers of electricity;

- establishing a monitoring program on all prices and products (and other relevant matters) relating to the supply of electricity to small customers in the ACT; and
- establishing the monitoring program for a three year period with a review at the conclusion of this initial period to assess whether the program should continue for a second period.

Overall, esaa commends the AEMC for this proposed reform approach, in particular the recommendation to remove retail price regulation in phase two. The Association considers that removing price regulation directly targets the source of the barrier to competition in the ACT and hence will be more effective in promoting competition than the other pricing options that sought to preserve the regulated price framework.

The Association also considers that the proposed time to lift the regulation – at the expiration of the current Transitional Franchise Tariff path on 30 June 2012 – is appropriate and strikes a balance between stability for industry and consumers and the imperative of reform.

In regards to the proposed price monitoring program for the ACT, esaa notes that this is consistent with the Commission's recommendation for both Victoria and South Australia following the reviews of competition in those jurisdictions.

While esaa appreciates that a price monitoring regime could provide government and consumers comfort during the initial transition to market determined prices, it is imperative that price monitoring arrangements are designed carefully to be transparent and provide regulatory certainty for industry. In particular, the regime must not be a de facto instrument of price regulation. For instance, it is possible that in the period following 1 July 2012 when the Transitional Franchise Tariff is proposed to be lifted that a carbon price is introduced to the energy sector. This can be expected to increase retail electricity prices. It is important that the design of any price monitoring regime would not result in such cost-based price increases being construed as a failure of price deregulation and an impetus for re-regulation. Similar issue arises with the pass through of network charges and the cost of government policies.

The Association considers that the proposed non-pricing options that aim to make electricity consumers less 'sticky', including the consumer education program and the marketing campaign, could play a role in facilitating competition by educating consumers about the choices they have. However, the design and implementation of measures to inform consumers of their ability to participate in the market must take care to avoid providing a competitive edge or disadvantage to businesses by inadvertently favouring new entrant retailers over incumbents or vice versa.

Further, it is critical that the implementation of the phase two measures are kept separate from the outcomes of phase one. In particular, the removal of the regulated price should not be made conditional on some measure of the 'success' of phase one in improving consumer awareness. The Association considers that while the proposed government measures to improve awareness have a role to play, in the longer term the dynamics of competitive behaviour by retailers will be the most

effective method of informing consumers of their opportunities in the market and it is these that should be relied upon to facilitate competition.

The wider context: retail price deregulation in the ACT as part of a broader reform effort

While the AEMC's recommendation for price deregulation in the ACT is a positive step forward for the development of that particular market, there are also implications for the wider NEM. Indeed, the ACT retail market's relatively small size – around 150,000 customers – belies the considerable importance of this review to the broader energy market reform effort.

For instance, unlike the AEMC's previous competition reviews of Victoria and South Australia, which found competition to be effective and hence made the recommendations to remove price controls straightforward, the finding of a lack of effective competition in the ACT posed greater challenges in designing policy responses. However, the AEMC's interpretation of the AEMA requirements and their application to the ACT situation in this review i.e. that the best policy response is nonetheless the removal of regulation, sets an important precedent and may be relevant in the AEMC's subsequent reviews of competition in other jurisdictions.

The AEMC's recommendation to remove retail price controls in the ACT will also build momentum towards a single NEM-wide retail market to complement the competitive NEM-wide wholesale market. This is relevant as twelve years after the inception of the NEM and more than two decades into Australia's electricity market reform program, the retail side of the NEM remains fragmented, mainly along jurisdictional lines.

There are a number of reasons why a single NEM retail market remains unrealised. However, in essence, esaa considers that the delineation between different customers in the NEM by virtue of state is artificial and is mainly a by-product of government policies; the most salient of which is continued retail price controls.¹

Retail price regulation, administered by all states and territories except Victoria, is a palpable barrier that divides Australia's small use electricity consumers into sub-markets. It means that retailers looking to acquire customers in different jurisdictions must incur the costs of understanding and complying with jurisdiction-specific price regulatory regimes, and importantly, must bear the risks of regulatory error by multiple regulators.

On the other hand, the removal of retail price controls would reduce costs and risks for retailers and significantly facilitate the decision to market retail electricity to any small use customer in the NEM, irrespective of location. A NEM-wide retail electricity market would promote vibrant competition, efficiency and lead to greater choice and innovation for consumers.

¹ Another reason is jurisdiction specific factors that retailers have to accommodate, such as the requirement to implement premium feed-in tariff regimes that differ across jurisdictions.

Conclusion

Retail price deregulation is the key outstanding reform in the NEM and a priority area for the Association. Successful price deregulation in the Territory would build momentum for a similar outcome in the other, larger states in the NEM that remain regulated and are scheduled for competition review by the AEMC in the years ahead.

Once again, esaa commends the AEMC for the reform approach set out in the Stage 2 draft report. The Association encourages the Commission to reaffirm its recommendation for the removal of price deregulation in its stage 2 final report and consider the issues identified in this submission regarding the phase one package of options.

Any questions in respect of our submission should be addressed in the first instance to Kieran Donoghue, by email to kieran.donoghue@esaa.com.au or by telephone on (03) 9670 0188.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Brad Page', with a stylized flourish at the end.

Brad Page
Chief Executive Officer