

The competitive market has delivered mixed outcomes elsewhere. Evidence from Britain confirms that households are not very good at making choices in a competitive energy market, often under-estimating exit fees and being hindered by high search costs. Low-income households tend to end up with the most expensive electricity rates based largely on the contracts that are marketed to them. It suggests that market power of the incumbent suppliers, coupled with customer inertia, leads to excess profits.

Evidence from Victoria suggests rural households and tenants have not been receiving the price benefits of competition.

In NSW, the level of competitive activity has increased. But this is not all good news for consumers; the NSW Energy and Water Ombudsman reported a 254% increase in complaints relating to the marketing behaviour of energy retailers in the past year. In many cases households are being misled about the highly complex products offered by energy retailers.

On 1 July 2007 the new electricity prices come into force. Alongside this will be increased marketing activity. If you thought mobile phone contracts were difficult to assess, wait until a salesperson knocks on your door to tell you how many cents per kilowatt hour at different times of the day they can offer you. You might be better convinced by the free DVD package that will be thrown into the deal.

That DVD package will be coming to you courtesy of government policy that puts profitability before efficiency and accessibility.

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PRICE PROTECTIONS FOR RESIDENTIAL GAS CUSTOMERS

Shortly after releasing its electricity price determination, IPART released its determination for regulated retail gas prices. This release was a much more low-key event: there was no press release, no explanatory note nor public discussion scheduled.

NSW gas consumers have traditionally been less worried by gas pricing due largely to the smaller coverage of gas consumers and the fewer cost concerns involved. Indeed, for these reasons, PIAC has in the past endorsed a light-handed approach to regulation of gas prices.

However, in this instance, PIAC was concerned about the lack of transparency in the IPART process and set about getting more information into the public sphere about the reasons for IPART's determination.

PIAC was successful in its demand that IPART put on the public record the reasons for its determination. PIAC was also successful in seeking an open discussion of the issues with the Tribunal members.

The draft gas price determination released by IPART last month signalled yet another shift in the direction of the regulation of essential services. It removed long-standing price protections that have until now formed a bridge between the interests of the regulated entities and the interests of consumers.

In his Second Reading Speech to the Gas Supply Amendment (Retail Competition) Bill 2001, the (then) Minister for Energy, Kim Yeadon pledged that '[t]he Government will ensure that customer protection is not compromised in the pursuit of competition reforms'.

PIAC is holding the Government to this commitment. While PIAC welcomes the benefits that competition brings to the marketplace, it also recognises the ongoing need for price protections.

If IPART continues to remove protections without any regard for the actual outcomes for consumers in the marketplace, PIAC is concerned that customers will be misled, manipulated and over-charged.

The final determination is due to be released in June and will be effective from 1 July 2007 until 30 June 2010.

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LESSONS FROM BRITAIN

On 4 May, PIAC held a seminar, 'Consumer Issues in the Competitive Energy Market', hosted generously by private law firm member of the Public Interest Law Clearing House, Allens Arthur Robinson. Regulators, government officials, retailers, consumer advocates and others who attended heard Allan Asher, Chief Executive Officer of Great Britain's Energywatch¹, deliver the keynote address, concentrating on consumer issues that currently face the British energy market.

Mr Asher described how a number of companies entered the market when competition was introduced back in 2002. However, over time competitors have merged or have been bought out so that now there are six companies controlling 99% of the market. The British experience demonstrates the natural monopoly (or oligopoly) aspect of the energy market, even in a country that doesn't have the same geographical and population challenges to competition that face Australia.

Mr Asher reported that the way in which companies were competing for a consumer's business had created many problems for consumers. For example, he reported a large number of complaints from consumers are about the sales techniques of energy companies, particularly those of door-to-door salespeople. Mr Asher said that salespeople often engaged in deceptive or unconscionable conduct, making false claims about the product. Energywatch's solution to this problem was to introduce door-to-door marketing 'no go' zones in certain municipalities to protect particularly vulnerable populations.

Interestingly, the nature of the complaints was echoed later in the seminar by Clare Petre, the NSW Energy and Water Ombudsman (EWON), who stated that last financial year saw a 254% increase in the number of complaints registered with her office.

Mr Asher reported that in Britain more than a third of those who switched energy suppliers had moved to contracts where they actually paid

more. Whilst he acknowledged that quality of service and not just the price are relevant factors in consumer switching levels, he attributed the phenomenon to the aggressive marketing techniques he described, and by the fact that consumers generally have a poor understanding of the intricacies of the energy market and which products will deliver benefits to them.

According to Mr Asher, a major contributing factor to poor consumer awareness of the energy market was a lack of comprehensive or quality information being provided to consumers by retailers. He argued that this retailer practice had led to a reduction in effective competition because informed consumer consent is an integral aspect of promoting vigorous competitive markets.

Mr Asher announced that he is a proponent of competition in the energy market, arguing that it is the most efficient way to deliver benefits to consumers. However, he was concerned that competition was being pursued for competition's sake and not, as he considers paramount, to ensure effective and responsible markets.

Responsible markets are essential in ensuring fair outcomes for all consumers of an essential service. Ignoring responsible market practice caused market failures to occur because, for example, not all consumers are contestable. Mr Asher reminded us of the frightening reality that, without a responsible energy market, market failures can lead to consumers having to make the choice between heating or eating.



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Footnotes

- ¹ Energywatch is a British agency that has a statutory responsibility to represent all residential consumers of energy in Britain, in particular, vulnerable and disadvantaged consumers.

ROLL OUT ROLLS ON

The push to roll out interval meters continues to escalate. In April the Council of Australian Governments (COAG) endorsed a staged approach for the roll out of interval meters in areas where benefits for consumers outweighed costs. The Ministerial Council on Energy (MCE) has released draft Terms of Reference in order to conduct a cost-benefit analysis and has set a deadline of September 2007 to agree on national minimum functionality for interval meters.

Despite the fact that the meter roll out will affect every Australian household and require vast capital outlays, an extremely brief time frame has been set for the completion of its cost-benefit analysis. Further, a critical public consultation period has been scheduled to coincide with the Christmas break.

Distributors remain interested in interval meters as a way to reduce the stress on demand management by facilitating peak shaving, that is, a consumer's self-management of usage to limit usage during

high demand periods. Retailers find interval meters attractive because of their potential to reduce billing errors and to take advantage of the energy customer's consumption habits through time-of-day pricing.

Whilst benefits may be derived by energy companies, the cost of installing the new meters, including the labour, parts and infrastructure costs, will be enormous. It is no secret that consumers will foot the bill for the installation.

There is no clear provision for how social impacts will be measured as part of the cost benefit analysis.

PIAC maintains its concern that the capacity of interval meters to deliver benefits, such as reduced consumption and load shifting, has been overstated.

Whilst meters will provide a wider range of energy price choices tailored to consumer usage patterns, those consumers who cannot take advantage of more favourable pricing periods will be hit with higher rates for the energy they consume.

An additional challenge is that some of the technology required to deliver metering functions currently does not exist, whilst some technological improvements may generate new problems. For instance, who will own the rights or have access to the immense amount of data that will be produced by interval meters? Remote connection also allows remote disconnection, which may facilitate an increase in disconnection rates because it can be done at the flick of a switch.

The solution to many of the problems posed by interval meters is a policy that is created with consumers being considered not just the passive recipients of a product, but as part of the answer to many of the challenges facing the energy industry.

Therefore, the push for 'Smart' meters should really be about smarter metering, where the focus is not on the technology but how people can interact with the new technology. A roll out of interval meters requires not merely a cost-benefit analysis but a considered policy that identifies the social needs of consumers to ensure that benefits are delivered to consumers as well as industry participants.

PROFITABILITY PUSHES UP ELECTRICITY PRICES

When the Independent Pricing and Regulatory Tribunal endorsed a 26 percent rise in electricity prices last month, a quick lament was that the State Government's promise of low prices had been formally dumped.

Many reasons have been given for the rise in regulated electricity prices over the next three years. Some say it is the result of climate change policies and others claim it is to ensure the lights stay on. In reality, the key driver of the forthcoming increase is the increased profitability of industry participants.

Prices are being forced up to make the energy business more attractive, perhaps to any potential buyer of NSW state-owned energy businesses, and to make it easier to lure households off the regulated tariff and onto a market contract.

At the end of the 1990s electricity users were promised lower energy bills if the power retail and generation monopolies were exposed to market forces. Yet customers now face higher power prices for the privilege of greater competition.

Full retail competition in electricity and gas was introduced in 2002, enabling households to choose their energy supplier. Importantly, the State Government retained a fully regulated tariff for households that could not secure a better deal in the market or that did not want to enter the

competitive marketplace. Since then, fewer than one in three households have elected to move off the regulated contract to have electricity and gas prices set in the competitive market.

Until now, regulation has been successful on three counts: it created effective incentives to improve productivity; it limited price increases to efficient levels; and it allowed the regulated businesses to deliver healthy dividends to the owner, the NSW Government. Everyone was winning, except for the electricity businesses looking to enter the potentially profitable marketplace.

The Tribunal's recently delivered draft determination signals a change in direction. The terms of reference issued by the Minister for Energy fail to consider the effect of the determination on consumers. Rather, the terms of reference asked the tribunal to assess costs based on a new entrants cost profile instead of the costs incurred by the regulated entities.

The determination introduces headroom, that is, inflated costs to stimulate competition. About half of the price increase is attributable to raising the profitability of the industry.

The Tribunal justified its decision based on a flawed assumption that competition is effective. The regulator expects that any 'excess' profits will be competed away. Yet there has been no analysis of the outcomes for customers who have signed contracts with new retailers, nor the effect of customer inertia and the market power of incumbent suppliers.

ENERGY IN NSW: OWEN INQUIRY COMMENCES

THE NSW Premier has recently announced a review into base-load generation in NSW to be undertaken by Professor Anthony Owen. The review ostensibly considers the technology, timing and conditions necessary for the next investment in electricity generation.

In considering whether or not to invest in generating capacity, PIAC notes an uncomfortable reality: customers will be paying for base-load generation investment now and well into the future. Yet, the cost of failing to invest will also be borne by customers through either compromised reliability or a greater reliance on more expensive peaking capacity.

The review has sparked yet another round of speculation about

ownership of electricity assets in NSW public hands. It also sparked speculation on the future of retail price regulation.

In 2004, the NSW Government released its Green Paper on the Future Directions for Energy in NSW. A great deal of taxpayer dollars was spent on consultation and analysis of the issues it addressed, which included privatisation, regulation and the conditions necessary for investment.

Since that time, stakeholders have largely given up on ever seeing a White Paper for NSW's energy policy.

While PIAC supports the intent of the recently announced review, it is a great source of frustration that NSW failed in its attempt to make its policy intentions clear before now. NSW does not need piecemeal reviews. It needs a broad-ranging, holistic and transparent process for deciding the future of energy in our state.