



Owen Inquiry into Electricity Supply in NSW

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1. Introduction

The Public Interest Advocacy Centre (PIAC) seeks to promote a just and democratic society by making strategic interventions on public interest issues.

PIAC is an independent, non-profit law and policy organisation that identifies public interest issues and works co-operatively with other organisations to advocate for individuals and groups affected.

In making strategic interventions on public interest issues PIAC seeks to:

- expose unjust or unsafe practices, deficient laws or policies;
- promote accountable, transparent and responsive government;
- encourage, influence and inform public debate;
- promote the development of law—both statutory and common—that reflects the public interest; and
- develop community organisations to pursue the interests of the communities they represent.

Established in July 1982 as an initiative of the Law Foundation of New South Wales, with support from the NSW Legal Aid Commission, PIAC was the first, and remains the only, broadly based public interest legal centre in Australia. Financial support for PIAC comes primarily from the NSW Public Purpose Fund and the Commonwealth and State Community Legal Centre Funding Program. PIAC generates approximately forty per cent of its income from project and case grants, seminars, consultancy fees, donations and recovery of costs in legal actions.

1.1 Utility Consumers' Advocacy Program

The Utility Consumers' Advocacy Program (UCAP) was established in 1998 by PIAC, funded by the NSW Government, to develop policy and advocate in the interests of residential consumers, particularly low-income consumers, in the NSW energy and water industries. The project is based at PIAC and UCAP staff receive broad policy direction from a community based Reference Group, who's members include:

- Council of Social Service of NSW (NCOSS);
- Tenants Union;
- Combined Pensioners and Superannuants Association of NSW (CPSA);
- Park and Village Service;
- Western Sydney Community Forum;
- Rural and remote consumers; and
- Institute of Sustainable Futures, University of Technology.

1.2 Owens Inquiry Terms of Reference

This submission addresses the Inquiry's Terms of Reference as a whole. Comment concentrates on the following issues:

- how consumption patterns of residential energy customers influence the need for new generation;
- the effect the proposed desalination plant has on investment in new energy generation;
- the role of retail price regulation in the energy market;
- investor interests versus consumer interests;
- the effect that changes to the current industry structure and competition policy would have on residential energy customers.

2. Demand for Electricity

The Owen Inquiry into Electricity Supply in NSW is a response to the growing rate of electricity consumption in New South Wales. The terms of reference ask that the Inquiry consider the need for new base load generation. It is PIAC's view that this analysis must be based on a careful examination of current and future energy consumption patterns, as emerging electricity generating needs are directly related to emerging consumption demands. An inquiry that looks solely from the perspective of electricity supply fails, in our view, to fully understand the drivers of the electricity market.

PIAC calls on the Owen Inquiry to analyse changing consumption patterns across New South Wales. In particular, it calls on the Inquiry to investigate the effectiveness of energy efficiency and demand management programs, funded by NSW citizens and energy customers, to reduce peak and base load consumption.

2.1 Household Demand for Electricity

The residential sector continues to substantially contribute to energy consumption levels in NSW, accounting for around 30% of total energy use.¹ Further, the amount of energy consumed by the residential sector is increasing.

The Independent Pricing and Regulatory Tribunal (IPART) recently released results of its 2006 survey of residential energy use in Sydney, the Blue Mountains and the Illawarra.² Upon comparison with the same IPART survey results of 2003, it is apparent that energy use across the entire residential sector, including income groups, dwelling types, geographic regions and occupancy sizes, has risen over the three-year period.

This increase in energy consumption has taken place at the same time that energy customers have been paying a record amount to deliver energy efficiency programs via the Energy Savings Fund, the NSW Greenhouse Gas Abatement Scheme and the regulatory incentives on network industries.

Additional energy efficiency schemes are currently being proposed, such as the NSW Renewable Energy Target, which will levy another \$15 per year on households.

Residential energy consumption is generally understood to have a low price elasticity of demand. In other words, large price increases deliver a relatively small reduction in demand. This low price responsiveness arises from the key role that energy consumption plays in deriving goods and services essential for human health and wellbeing. For example, water heating represents 27%, cooking represents 4%, and heating and cooling homes represents 39% of total household energy use.³

The energy consumed to undertake these basic tasks is therefore dependent on the efficiency of appliances, fitting and fixtures. It is apparent that energy efficient hot water systems and well-designed homes are at the centre of a low-consumption energy future.

¹ Diesendorf, M (2005) *Towards NSW' Clean Energy Future*. Pg 7

² Independent Pricing and Regulatory Tribunal (2007) *Residential energy use in Sydney, the Blue Mountain and Illawarra: Results from the 2006 household survey, June 2006*

³ Australian Bureau of Statistics (2006) *Household energy uses and their contribution to greenhouse gas emissions*.

2.2 Policy reforms needed to promote a low-consumption economy

It is PIAC's view that there remains an unexploited capacity to move towards a lower-consuming residential sector. As mentioned above, residential energy consumption has increased in the last 3 years, at the same time that residents have been funding energy efficiency programs.

PIAC contends that there is clear scope for more initiatives to be made that would reduce residential energy consumption levels, and that existing schemes are not being utilised to their full potential. An examination of the Energy Savings Fund (ESF) highlights this issue.

The ESF was established in 2005 to fund initiatives designed to directly reduce energy consumption. Since the fund's inception, NSW households, through energy distribution companies, have contributed approximately \$80 million towards the scheme. Table 1 illustrates where the ESF has been allocated to either the residential or commercial sector.

Table 1: Sectoral Allocation of the Energy Savings Fund⁴

	Residential	Commercial/ Industry	Cross Sectoral	Combined Total
Round 1	\$4,299,739	\$6,566,600	\$4,180,880	\$15,047,219
(% Round 1 total)	28%	44%	28%	100%
Round 2	\$1,031,935	\$12,279,777	\$0	\$13,311,712
(% Round 2 total)	8%	92%	N/A	100%
Total allocation	\$5,331,674	\$18,846,377	\$4,180,880	\$28,358,931
(% combined total)	19%	66%	15%	100%

The Table illustrates that in the operation of the scheme just 19%, a mere \$5.3 million, of allocated funds have gone towards directly helping households to reduce their energy consumption.

The Owen Inquiry should identify where there currently exists regulatory, legislative, scheme-based and market-based disincentives to undertake effective household energy efficiency. Acting to address any market and regulatory failures would curb energy consumption among the residential sector and defer the need for additional electricity generation facilities. Further, establishing a comprehensive suite of demand management and energy efficiency strategies would, in the long term, assist in lowering household energy bills.

PIAC contends that building new energy generators would create other problems for residential consumers. Firstly, it would create a disincentive for households to reduce their consumption, maintaining high energy bills for consumers. Additionally, without incentives for households to reduce their consumption, it is likely the level of residential consumption would continue to increase, and the NSW Government may have to revisit this Inquiry in the near future to determine whether additional generation expansion is necessary.

Secondly, the NSW Government has committed to cut emissions by 60% by 2050.⁵ As government policy is to move towards a low emission generating base, any new expensive generators that are built run the considerable risk of becoming costly stranded assets in the future, to be paid off by consumers.

⁴ Figures taken from the Department of Water and Energy's website on 2 July 2007:
<http://www.deus.nsw.gov.au/energy/Energy%20Savings%20Fund/Energy%20Savings%20Fund.asp>
and does not include figures for the Public Facilities Program.

⁵ <http://www.nsw.gov.au/stateplan/spme3b.aspx>

As an alternative to building additional, expensive generating facilities, PIAC calls on the Owen Inquiry to review the effectiveness of current demand management and energy efficiency activities.

2.3 Proposed desalination plant and new energy generation

PIAC understands that a critical driver for new base load capacity is the development of the proposed desalination plant in Sydney. Whilst concerns regarding household water pricing are outside the scope of this Inquiry, PIAC maintains deep concerns about the cost impact that the development of a desalination plant would have on energy consumers, particularly if it is used to justify the development of a new base load generator.

PIAC calls on the inquiry to articulate what proportion of future energy consumption will be required to meet the energy needs of the desalination plant versus household, industrial and commercial energy needs.

3. Investment Conditions

While we note that the Inquiry has secured the assistance of Morgan Stanley investment bankers to provide expert assistance, PIAC is concerned that the needs of investors may not necessarily align with the needs of consumers.

Given the capital intensive and 'lumpy' nature of investment in electricity generation, consumers will be ultimately paying for any infrastructure investment for generations to come. Therefore, due consideration of the interests of consumers need to be undertaken in the Inquiry.

We also note that the private sector has tended to socialise the risk inherit in the energy industry, relying on the Government to meet the costs incurred by their business decisions that have led to market failures. This was demonstrated most recently when State owned corporations were forced to take on 10,000 customers of failed energy retailer Energy One.

Whilst PIAC understands that investment is important in ensuring supply, it is consumers of this essential service that will bear the cost. PIAC submits that consumers have more interest in ensuring that electricity remains competitively priced than investors. We urge caution in encouraging the private sector to invest in the energy industry at any cost. It is likely that household will end up paying for poor investment decisions.

3.1 Retail Price Regulation

It is the strong view of consumer groups that the future of retail price regulation must not be determined in the context of this inquiry. Through the Ministerial Council on Energy, the NSW Government has endorsed a process to first assess the competitiveness of the retail energy market and then identify classes of customers that require ongoing regulated electricity prices. That assessment will take place in 2009. Investment decisions must not pre-empt the finding of the 2009 review.

The current regulated retail prices are in place until June 2010 and the NSW Government has reserved the right to continue to regulate retail electricity prices beyond then. The Inquiry must not assume that retail price regulation will disappear beyond that point in time, and therefore, any commitment of private funds to the energy market should not proceed on the assumption or condition that retail price regulation will be removed.

It will always be the role of the NSW Government to ensure that all households have access to electricity services at a fair and reasonable rate. Retail price regulation is designed to ensure that

households have access to essential energy services within the context of a complex and emerging marketplace. It establishes the benchmark charge for households unable to participate in the marketplace and provides a guiding 'price to beat' for those customers who choose to enter into a competitive market contract.

To be clear, some customers will always need to be provided with electricity at a regulated price. This includes residents of residential parks and retirement villages who cannot establish an independent contractual arrangement. It includes households who are unattractive to profit-based retailers due to consumption level, geographic location or credit history. And, as is in the recent case of failed energy retailer Energy One, it applies to customers whose retailer goes bankrupt and must accept supply from a designated energy retailer.

In the developing competitive retail market, retail price regulation provides the 'price to beat' for second tier retailers. It is also the most commonly accepted point of differentiation by customers attempting to find the most competitive retail offer. An effectively competitive energy market may eventually emerge in the retail electricity industry, however, it is unlikely to do so without government intervention.

Great Britain's energy market provides a good illustration of this point. When price regulations were removed, despite many new entrant energy retailers entering the market, the price of energy for households increased by 100%. Since that time, household energy prices have not decreased, yet the number of retailers has reduced so that 6 companies now have control of 99% of the market place. Recent evidence demonstrates that customers are unable to enjoy the few price benefits delivered by a deregulated energy market.

3.2 Industry structure and Competition Policy

PIAC understands that the Inquiry does not intend to examine the question of the privatisation of the retail sector in the NSW energy market. PIAC expects that any debate regarding the privatisation of an essential service would be done through a transparent consultative process, involving clear and explicit terms of reference, and input from all relevant stakeholders.

However, it is appropriate to raise the issue of privatisation in the context of how it would effect the current development of the energy market.

Increasing the competitiveness of the retail electricity industry is the stated policy of the NSW Government. PIAC sees the benefit of an effectively competitive retail marketplace, but believes that the energy market is a long way from reaching that position.

At this stage in the development of the market, an emerging issue is the number of competing energy businesses. By retaining the current ownership structure, consumers will be assured of a larger number of competing firms in the marketplace, with a greater capacity to achieve effective competition in the retail energy market. There is a great risk that in privatising NSW retailers, market concentration will reach unacceptable levels, stifling effective competitive markets. Uncompetitive markets provide poor outcomes for household consumers.