



public interest
ADVOCACY CENTRE LTD

Prices, profits and priorities

**Submission in response to the Australian Energy Market
Commission's Approach Paper: 2016 Retail Market Review**

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Introduction

The Public Interest Advocacy Centre

The Public Interest Advocacy Centre (PIAC) is an independent, non-profit law and policy organisation that works for a fair, just and democratic society, empowering citizens, consumers and communities by taking strategic action on public interest issues.

PIAC identifies public interest issues and, where possible and appropriate, works co-operatively with other organisations to advocate for individuals and groups affected. PIAC seeks to:

- expose and redress unjust or unsafe practices, deficient laws or policies;
- promote accountable, transparent and responsive government;
- encourage, influence and inform public debate on issues affecting legal and democratic rights;
- promote the development of law that reflects the public interest;
- develop and assist community organisations with a public interest focus to pursue the interests of the communities they represent;
- develop models to respond to unmet legal need; and
- maintain an effective and sustainable organisation.

Established in July 1982 as an initiative of the (then) 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 Services Program. PIAC also receives funding from NSW Trade and Investment for its work on energy and water, and from Allens for its Indigenous Justice Program. PIAC also generates income from project and case grants, seminars, consultancy fees, donations and recovery of costs in legal actions.

Energy and Water Consumers' Advocacy Program

The Energy + Water Consumers' Advocacy Program (EWCAP) represents the interests of low-income and other residential consumers of electricity, gas and water in New South Wales. The aim of the program is to develop policy and advocate in the interests of low-income and other residential consumers in the NSW energy and water markets. PIAC receives policy input to the program from a community-based reference group whose members include:

- Council of Social Service of NSW (NCOSS);
- Combined Pensioners and Superannuants Association of NSW;
- Ethnic Communities Council of NSW;
- Salvation Army Eastern Australia Conference;
- St Vincent de Paul Society of NSW;
- Physical Disability Council NSW; and
- Tenants Union of NSW.

Assessing if competition is fulfilling its primary promise

The Public Interest Advocacy Centre (PIAC) thanks the Australian Energy Market Commission (AEMC) for the opportunity to provide comment on the AEMC's approach paper for the third annual review of energy retail competition in National Electricity Market (NEM) states and territories.¹ The paper sets out the AEMC's intended approach for the review and seeks stakeholder submissions on its approach and on the state of competition.

Electricity bills are made up of several components, including generation costs, network costs, 'green schemes' and costs associated with other public policy initiatives, and retail costs. In Victoria, South Australia and NSW where retail prices are deregulated, effective competition is required to ensure that households do not pay more than the efficient cost for energy services.

The competitive market indicators that the AEMC will use for its assessment are:

- customer activity in the market;
- customer satisfaction with market outcomes;
- barriers to retailers entering, expanding or exiting the market;
- the degree of independent rivalry in the market; and
- whether retail energy prices are consistent with a competitive market.

PIAC agrees with the AEMC that an assessment of competition cannot be based on observing one indicator at one point in time. Multiple indicators are required to form a more complete picture of the state of competition. Information on a range of indicators needs to be considered collectively before judgement can be formed on the overall state of competition. For example, a high degree of choice for consumers needs to be accompanied by appropriate, accessible and reliable information if the choice is to be effectively operationalised.

Notwithstanding this, one of PIAC's main concerns is an unexplained increase in retail costs, and PIAC encourages the AEMC to examine this issue as part of its current and future reviews of competition. A high number of suppliers in competition with each other can be expected to benefit consumers in a number of ways; for example, by encouraging the provision of a variety of different products that give consumers a range of options to choose from that suit their particular needs and circumstances. However, PIAC takes the view that the ultimate promise of the competitive market is that it will lead to lower prices for consumers. Price is the main concern for most households and it is certainly one of the most pressing concerns for the vulnerable consumers who the AEMC has decided to focus on in its 2016 review.²

In this vein, PIAC submits that it would be useful for regulators, policy makers and consumers to know whether there is evidence of competition genuinely pushing prices down (in real or nominal terms). PIAC notes that the AEMC has again stated in relation to retail prices that it will 'draw from a range of information to assess this competitive market indicator, including our own pricing analysis, the work of consumer representatives, regulators and other government bodies'.³ PIAC reiterates the recommendation it made in response to the 2015 Review that the AEMC examine

¹ AEMC, *Approach Paper: 2016 Retail Competition Review*, October 2015. Available at: <http://aemc.gov.au/getattachment/c405e286-330e-475d-8d4a-7b773c446e10/Approach-Paper.aspx>

² AEMC, *Approach Paper: 2016 Retail Competition Review*, October 2015, p 16-17

³ AEMC, *Approach Paper: 2016 Retail Competition Review*, October 2015, p 14

the Tariff Tracking Project run by the St Vincent De Paul Society and Alvis Consulting. The project has been tracking changes to residential energy tariffs and reporting on household impacts since 2010. Initially, it only covered Victoria but it has since expanded to include New South Wales, Queensland, South Australia, Tasmania and the Australian Capital Territory. Their rationale for tracking changes to domestic energy prices is to document price increases, analyse market developments and inform the broader community about bill impacts and potential savings to be made.⁴

The AEMC states in its approach paper that while net margins provide an indicator of competition and may be considered, they are not, in themselves, determinative.⁵ PIAC maintains that retailer profit margins are a useful indicator of the effectiveness of competition. In particular, they are able to show that, where profit margins are persistently very high, retailers may be earning profits in excess of the efficient cost of supply.

PIAC has previously expressed concern about the prices in the Victorian market, where research suggested that costs were increasing as the market developed.⁶ It appears that this could now also be the case in the deregulated NSW market. Overall, the most recent findings show that the NEM average for the retail cost component is a significant \$600 per customer per annum.⁷ The St Vincent de Paul Society argues that the retail component of bills is too high in the deregulated, competitive electricity market and that this is either because the cost of competition is high or because competition is ineffective. In particular, their evidence shows that the retail component is significantly higher in deregulated retail markets compared to regulated markets.⁸ While they do not have a detailed breakdown of the retail cost and margin component, they state that it appears that operating in a competitive market is either very expensive or the competitive market is ineffective.

There are two main issues that PIAC wishes to raise in this context. The first is that the deregulated market places an expectation on consumers to remain engaged in the market in order to ensure that they pay the lowest price or find the product that best meets their needs. Accordingly, PIAC believes there is a risk that consumers who 'set and forget' their electricity supply arrangements, or are not able to effectively navigate the complexities of the competitive market, will pay more than they need to for essential energy services.

The second is that, as the competitive retail market develops, retailers will continue to put greater effort into gaining and retaining customers. The cost of this greater effort in terms of larger marketing departments, more market research and staff to design new products, will ultimately be passed on to consumers through final retail prices. While retailer effort to attract new customers may appear to be a sign of a competitive market, the increased costs passed through will deliver poorer outcomes for consumers. Consumers should not pay higher than efficient costs for an

⁴ See Dufty, G and Mauseth Johnston, M, *The National Energy Market – Still Winging It: Observations from the Tariff Tracking Project*, September 2015. Available at:

https://www.vinnies.org.au/icms_docs/228265_National_Energy_Market_Still_Winging_It.pdf

⁵ AEMC, *Approach Paper: 2016 Retail Competition Review*, October 2015, p 14-16

⁶ PIAC, 2014, *The Next Piece of the Puzzle*, 5 Available at:

<http://www.piac.asn.au/publication/2014/03/next-piece-puzzle>

⁷ See Dufty, G and Mauseth Johnston, M, *The National Energy Market – Still Winging It: Observations from the Tariff Tracking Project*, September 2015, p 15-25

⁸ See Dufty, G and Mauseth Johnston, M, *The National Energy Market – Still Winging It: Observations from the Tariff Tracking Project*, September 2015, p 20

essential service in order to fund increased retailer activity and operations. If this is occurring, PIAC is of the view that the market is failing to deliver an efficient outcome for consumers and that effective competition cannot be said to exist in such an instance.

PIAC considers that it is very important that the operation and outcomes of the competitive market are effectively monitored, to ensure they are occurring in what is truly in the long-term interests of consumers. As PIAC submitted to previous AEMC reviews of competition, it is crucial that on-going monitoring seeks to understand how the competitive retail electricity market develops. Such monitoring serves both as a tool for consumer advocates such as PIAC and as a potential basis for government intervention in the market. In particular, by tracking price movements, and the movements in other cost components such as green schemes, the AEMC should be able to determine whether increases in retail costs are working to cancel out lower costs in other areas of the energy price cost stack.

Recommendations

PIAC recommends that the AEMC:

- *examine whether the competitive market has resulted in reduced electricity prices, in real or nominal terms, in any areas of the NEM.*
- *examine retailer costs and profit margins, to determine whether the market is working to minimise retail costs and deliver competitive prices for residential consumers.*
- *have regard to the research produced by the St Vincent de Paul Society's Energy Tariff Tracking Project as part of its review of the effectiveness of competition.*