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NATIONAL ENERGY REGULATOR

Energy market reform has been on the Federal Government's agenda since the Council of Australian Governments (CoAG) commissioned the Warwick Parer report, *Towards a Truly National and Efficient Energy Market*, which was released in December 2002. The Ministerial Council on Energy's communique from their meeting on 1 August 2002 outlined a comprehensive package of recommendations that were to be considered by CoAG at their meeting on 29 August 2003.

The recommendations included:

- establishing two new statutory commissions by 1 July 2004, funded by an industry levy:
 - Australian Energy Market Commission with responsibility for national energy rule-making and market development
 - Australian Energy Regulator (AER) with responsibility for market regulation.
- the new commissions will initially be responsible for electricity wholesale and transmission in the jurisdictions

that form the National Electricity Market (NEM) and it will be extended in 2005 to include gas transmission for all jurisdictions other than Western Australia. WA and the NT will be able to join for electricity and WA for gas by agreement.

- the National Electricity Code Administrator (NECA) is to be abolished and it is PIAC's understanding this is to occur from 1 July 2004.
- agreement to the objective of an agreed national regulatory framework for distribution and retailing (other than retail pricing) under the AER for implementation in 2006 to be considered by CoAG.
- in all jurisdictions where full retail competition is operating, each jurisdiction align their retail price caps with costs, and periodically review the need for price caps.

Further, following consideration of these recommendations by CoAG, the Ministerial Council on Energy will implement a comprehensive workplan involving the State, Territory and Commonwealth Governments.

The upshot was that CoAG did not consider these recommendations on 29 August because there was a lack of agreement on health funding.

PIAC was also concerned that before the CoAG meeting there was an indication by the Minister, the Hon Frank Sartor that NSW had suggested to CoAG that the AER should also take over retail pricing of energy which is currently undertaken by the NSW Independent Pricing and Regulatory Tribunal (IPART). This concern along with another concern we have about the transfer of distribution pricing led PIAC to write a letter to the Premier outlining our concerns about these issues before the CoAG meeting was held.

PIAC's main concerns about these proposals include:

- a national regulatory regime will dilute the many hard won consumer protection mechanisms that have been developed for the NSW electricity industry
- the Electricity Tariff Equalisation Fund (ETEF) will be either harder to maintain or will be abolished. PIAC has been one of the few organisations that have publicly supported the ETEFF

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because it shields residential consumers from the volatility of pricing in the NEM.

PIAC believes that careful consideration needs to be given to both the pricing and regulatory regimes that are currently in place in NSW before the NSW Government rushes into any wholesale transfer of their powers to the AER.

SYDNEY WATER TARGETS POOR FOR IMPROVED SEWERAGE SERVICE

A new policy introduced by Sydney Water has targeted some of the most financially disadvantaged households for improved sewer services.

Sydney Water are progressively moving through areas of Sydney with a backlog sewerage program - connecting properties to sewer mains in cases where houses may have been built before the mains were constructed. This is done in conjunction with local government. The most recent phase of the program has been directed to the areas of Bundeena, Gerringong, Picton and the Blue Mountains.

A major driver for this program is the improved health and amenity for individual households and the wider community through ending reliance on backyard septic tanks. In addition, connections to sewer mains relieve residents of the cost of regular septic tank pump-outs. However, backlog sewer connections can be costly. The average connection costs \$3000 but this can be as high as \$10,000. As a result, property owners are required to meet a share of these costs.

Sydney Water has become aware of a small number of cases where families are in such severe financial difficulties that they cannot afford the expense of regular septic tank pumpouts and

yet they are unable to finance the cost of a sewer connection. Recognising the considerable health risks posed by the possible failure of aged backyard septic systems or the lack of regular pumpouts and the financial barriers facing these families, Sydney Water has moved to introduce a limited scheme of financial assistance.

In conjunction with the St. Vincent de Paul Society and other charitable organisations, Sydney Water has devised a Disadvantaged Customer (DAC) Policy for backlog sewer connections. This policy is based on a close working relationship between Sydney Water and the charitable organisations. It is the charities who assess the financial hardship of individual families and their eligibility for assistance with backlog sewer connections. This assessment is done on the basis of a strict set of criteria developed by Sydney Water in consultation with the St. Vincent de Paul Society and includes both health and financial factors including access to commercial loans.

The level of assistance provided in each case is capped. The policy itself has been introduced for an initial 12 month period. To date ten properties have been connected to sewer mains under this policy.

PIAC welcomes this innovative approach from Sydney Water to alleviating the extreme hardship faced by these households.

PIAC RESEARCH ON THE SOCIAL IMPACTS OF DISCONNECTIONS AND RESTRICTIONS

The NSW Government has funded the Utility Consumers' Advocacy Centre (UCAP) this financial year to undertake research on the social impacts of energy disconnections and water restrictions. UCAP's Reference Group determined this area of

research as a priority for the funding.

UCAP has established a Steering Committee to oversee the research and the steering committee includes representatives from:

- Ministry of Energy and Utilities
- Energy and Water Ombudsman of NSW
- Sydney Water
- Country Energy
- Council on the Ageing representing the UCAP Reference Group.

UCAP has also written to all NSW utilities informing them that the research is underway. The Research Steering Committee selected Urbis Keys Young to undertake the first part of the research that is to do a literature review of the methodologies for undertaking the research. After the literature review is completed, the actual research will be done. It is expected that the research project will be completed by April 2004.

MINISTER ANNOUNCES CONSERVATION MEASURES

The NSW Minister for Energy and Utilities, the Hon. Frank Sartor, has made two recent announcements intended to deliver significant reductions in consumption of energy and water by households in the state.

The first was that from 1 July 2004 all newly built housing will be required to meet a benchmark of a 40 per cent reduction in the level of water use compared with current standard designs and a 25 per cent reduction in greenhouse gases associated with energy consumption. Together these standards will require a significant increase in the use of water-efficient showerheads, dual-flush cisterns and natural sources of lighting and heating.

PIAC welcomes this move by the NSW Government since it will not only have a positive environmental impact but also permit the deferral of some very costly capital investment by the energy and water utilities.

However there remains the issue of existing housing stock. PIAC believes the successful REFIT pilot project, undertaken in the Hunter region with funding from EnergyAustralia, provides a strong model for existing homes. EnergyAustralia has indicated some interest in extending REFIT following its introduction of block pricing for retail customers on 1 July. PIAC and others have identified some concerns with the impact of block prices on low-income households.

The NSW Government had committed itself prior to the State election to providing \$300,000 for a similar program directed to low-income households in the Illawarra. PIAC hopes to discuss with Minister Sartor how and when this commitment will be realised.

The second announcement by the Minister was a proposal to introduce a form of block tariffs for household use of water. This would see the price for water rise significantly once consumption passed a pre-determined threshold. It is believed the higher block could price water as high as \$5 per kilolitre compared with the current flat rate of 95c for residents of Sydney, the Hunter and the Illawarra.

As with electricity, PIAC has concerns for the impact of such reforms on low-income people.

The Minister has directed IPART to investigate these matters. This will ensure that as wide a range of views as possible are aired prior to any decision.

ELECTRICITY AND GAS RETAIL PRICING

The Minister for Energy, the Hon Frank Sartor has asked IPART to review the regulated electricity default tariffs. Gas retail pricing will be considered at the same time but does not require a request by the Minister. The changes in tariffs as a result of the review will come into effect from 1 July 2004 and continue until 30 June 2007. The Government's intention to continue to provide price regulation for default electricity customers (that is, customers that have not changed their retailer by entering into a negotiated contract) is welcome. In addition, the Government has also extended the Electricity Tariff Equalisation Fund (ETEF) arrangement for the same period.

The matters that the Tribunal has to consider include:

- all allowance for electricity for electricity purchase costs based on an assessment of the long-run marginal cost of electricity generation, given the characteristics of the demand of customers remaining on regulated tariffs
- appropriate retail costs
- appropriate retail margin
- an allowance for retailer compliance with any Commonwealth mandatory renewable energy target (MRET) requirements and the licence requirements relating to the NSW Greenhouse Gas Benchmark Scheme
- energy losses as published by the National Electricity Market Management Company (NEMMCO)
- network charges as determined by the Tribunal and the Australian Competition and Consumer Commission (ACCC)

- fees (including charges for ancillary services) as imposed by NEMMCO under the National Electricity Code
- an allowance for expected movements in regulated components and NEMMCO fees.

In recognition that the default tariff level is critical in encouraging energy companies to compete in the retail market, the Tribunal has to:

- ensure that regulated tariffs cover the costs listed above while recognising consumer's ability to adjust to new prices
- consider options for restructuring tariffs to promote demand management.

Also, the Determination should ensure, as far as practicable, that:

- regulated retail tariffs and regulated retail charges are at cost reflective levels for all small retail customers by 30 June 2007;
- the setting of any 'price constraint' should allow the further rationalisation of regulated retail tariffs and movement to full cost recovery over the determination period with regard to the smooth transition for customers; and
- alternative ways be considered to facilitate transition to full cost recovery by 2007, or by an appropriate later date, such as the setting of regulated retail tariffs at cost reflective levels for all connections and new customers.

The Tribunal should also consider and report on the basis for regulating miscellaneous charges and security deposits.

From PIAC's point of view there is nothing that is unusual about the above terms of reference. The difference in this review is that the review includes both gas and electricity which should be an

opportunity to compare costs (where appropriate) between the industries. While not wanting to foreshadow some of the debates which will be had during the review, the need to create 'headroom' for second tier retailers so that they can undercut the regulated tariff is almost given, just as it was during the last review.

ELECTRICITY METERS REVIEWED AGAIN

The debate over whether new technology 'time of use' meters should be forced onto residential customers in the national electricity market has been renewed. IPART and the other state and territory based regulators have convened a 'joint jurisdictional review' of metering arrangements for small retail customers (those using less than 160MWh of electricity per year). This is in line with the terms of a decision on the National Electricity Code made by the ACCC in 2001. That decision focussed on the introduction of interval meters which record not only the amount of electricity consumed but the timing of consumption.

The decision of the ACCC followed proposals by some stakeholders, backed by the Victorian Office of the Regulator General (ORG), to amend the Code to force residential electricity customers to acquire the new meters. This would have meant the introduction of full retail competition (FRC) including a requirement that all households install and pay for new meters - irrespective of whether they wanted the new technology or were likely to switch retailers in the new environment.

The ACCC decided the issue would be settled by the jurisdictional regulators following a 2003 review. The timing was, in part, intended to allow for all stakeholders to gain some

experience with FRC and to test whether or not the 'market' supported the widespread take-up of the new technology.

In the interim very little has changed in terms of the views of the various stakeholders. Equally, it is clear that the 'market' shows little enthusiasm for interval meters. There is little or no sign of small customers seeking out interval meters, nor of electricity retailers introducing contract options based on interval metering. Some electricity distributors have begun quietly to install interval meters. However, it appears that all small customers continue to have their usage measured by the established method of 'accumulation' (ie. total consumption over two or three monthly periods).

The NSW Government had decided prior to the ACCC ruling that it would not pursue a compulsory roll-out of the new meters. Indeed, it declined the option of requiring the new meters to be installed on a 'new and replacement' basis. Both options were calculated not to be economically viable. Yet, for example, the Victorian Essential Services Commission (successor to the ORG) has maintained its insistence that full interval metering is vital to a fully functioning competitive retail market for small customers.

The arguments in support of a mandatory roll-out of interval meters continue to centre on:

- increasing competition and the switching of customers between retailers;
- making the electricity industry more efficient;
- ending cross-subsidies between groups of customers;
- encouraging households to use less electricity during peak periods such as very hot summer afternoons and very cold winter

evenings; and

- lower risks for energy retailers in the wholesale electricity market.

Despite orthodox economic theory it is by no means clear that interval meters can achieve any of these goals - let alone all of them simultaneously.

As it did in the earlier debates, PIAC has focussed on the differential between costs and benefits likely to be faced by residential electricity customers. There is increasing evidence both in Australia and overseas that giving greater play to market forces results in higher costs for these consumers. In Australia the bulk of residential customers are being bypassed by competition. Most remain 'captive' to the incumbent retailers and ignored by the competing retailers. In Victoria and South Australia the majority of households are experiencing significant price rises.

The use of interval meters will impose considerable costs both for the equipment and its installation. The proposed mandatory roll-out would reduce this problem by achieving economies of scale and spreading the cost of new meters across all households. In other words, mandatory interval meters would simply replace one cross-subsidy with another.

PIAC has been interested to pursue with IPART and the NSW industry the possibility that interval meters might have a use in encouraging better environmental outcomes through reduced consumption at peak times. In addition, high air-conditioning use is blamed for rising pressure for large investment in distribution networks. However, it is unlikely that interval meters will lead to reduced consumption during periods of severe weather.