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Independent Review of the Electricity and Gas Retail Markets
Department of Environment, Land, Water & Planning
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RE: Response to the Bipartisan Independent Review of Electricity and Gas Retail Markets in Victoria

EnergyAustralia welcomes the opportunity to make a submission to the Government's Response to the Review of Electricity and Gas Retail Markets in Victoria (the Review) - Consultation Paper.

EnergyAustralia has actively engaged throughout the Review process to date and provided:

- A detailed submission with 16 recommendations
- A private briefing to the Independent Panel
- Input at the Independent Panel's public roundtable
- Feedback through Ministerial meetings and Departmental meetings

We have readily engaged in this Review because we believe there are clear improvements that can be made in the retail market to benefit consumers.

Energy is a vital social good and offering customers the best possible value and service drives much of what we do at EnergyAustralia. We do this by delivering competitive pricing, innovative energy solutions and customer-centric service. We reward customer loyalty with lower rates and the opportunity to go 100% carbon neutral at no cost to them. We also choose to differentiate through making choices like removing paper bill fees and over the counter service fees.

Consistent with our approach, EnergyAustralia provides in-principle support to the Review's Recommendations 3-11 which, if implemented effectively, will improve the market and benefit energy consumers.

It is unclear to us why the Government is simultaneously considering Recommendation 1, a Basic Service Offer (BSO). A BSO will have the opposite effect on the market by constraining competition and shifting focus to cost cutting measures. This will come at the expense of services to customers and a reduction in innovation and product offerings.

Ultimately a BSO will undermine the benefits of Recommendations 3-11 and deliver poorer outcomes to customers. It is not logical to pursue both paths simultaneously, especially in the absence of an independent Regulatory Impact Statement (RIS) necessary for a major structural change like the BSO.

Instead we suggest the Government continue its cooperative implementation of Recommendations 3-11, allow them to take effect and for consumers to respond, and then assess their effectiveness. This will also allow the Victorian Government to take into account the findings of the electricity retail market review being undertaken by the Australian Competition and Consumer Commission (ACCC), and any further reforms coming out of that process.

After this probationary period, the Government could consider implementation of its BSO if the market is found to be delivering insufficient outcomes for consumers. It would also allow for a full RIS is undertaken to determine the most effective and efficient rectification.

In response to the proposed removal of standing offers (Recommendation 2), EnergyAustralia contends that this tariff does have a purpose – albeit a limited one. The standing offer is a default no frills offer that should only be used by retailers when a customer is unknown; for example, to guarantee energy supply when moving home.

We therefore see no reason that a known customer should be put onto a standing offer tariff by their retailer or third party. Further, it is non sensical that we are regulated to offer customers a standing offer tariff when it is clearly not in their best interests. EnergyAustralia is particularly concerned that there are concession customers on standing offer tariffs – this is patently irresponsible from a consumer good perspective. We continue to promote the benefits of market offers to this cohort and have seen dramatic decreases in overall standing offer customer numbers.

It is on these customers that the Government should focus its efforts. This could be done by ensuring retailers must make efforts targeting concession customers to move from standing offer tariffs onto market offers at least twice every year.

EnergyAustralia is confident that by working together, retailers, community groups and government will deliver superior outcomes for consumers than a re-regulation of prices. We would be happy to discuss these further with you.

If you have any questions in relation to this submission please contact Sara Williams, Policy and Advocacy Lead, on (03) 8628 1742.

Regards

A handwritten signature in blue ink, appearing to read "Kim Clarke".

Kim Clarke
Chief Customer Officer

About Us

EnergyAustralia is one of Australia's leading energy companies, providing gas and electricity to 2.6 million household and business customer accounts in New South Wales (NSW), Victoria, Queensland, South Australia (SA) and the Australian Capital Territory.

EnergyAustralia controls over 4,500MW of generation in the National Electricity Market (NEM). We have a modern energy portfolio underpinned by coal and gas power plants and complemented by newer energy sources like wind, solar and batteries.

In Victoria, we provide gas and electricity to around 20% of households. We also service 15% of small business electricity needs and 19% of their gas needs.

EnergyAustralia is the only major vertically integrated energy retailer based in Victoria with approximately 2000 employees throughout the Melbourne CBD, metropolitan and regional locations. In 2016 our contact centre, based at Geelong, was awarded best contact centre in the large centre category.

As an energy retailer we acknowledge the important role we play in supporting vulnerable customers who are unable to pay their energy bills. We do this via a dedicated hardship program, *EnergyAssist*, which we deliver in cooperation with Kildonan Uniting Care. *EnergyAssist* supports customers via individual case managers who provide tailored advice about payment plans, government grants, financial counselling, energy efficiency information, home energy audits and appliance swaps. *EnergyAssist* has been independently ranked the number one retailer program by Victorian financial counsellors.

In Victoria, we have 14,000 customers participating in *EnergyAssist* every year. In 2017, EnergyAustralia boosted *EnergyAssist's* funding by an additional \$10 million to ensure its reach goes even further.

Concerns about introduction of the BSO

As noted through our previous submissions, briefings and meetings with the Victorian Government, EnergyAustralia strongly opposes the introduction of a regulated price signal as proposed by the Independent Panel and subsequently designed by the Department of Environment, Land, Planning and Water.

By not including the cost of acquiring and retaining customers in a retailer's allowable cost stack, the Victorian Government has disregarded a fundamental aspect of delivering a diverse and competitive market. This is in direct contradiction to the regulatory approaches taken in other jurisdictions, such as that of the NSW Independent Pricing and Regulatory Tribunal (IPART) which allowed for advertising and new customer acquisition costs to help foster retail competition.

Indeed, it is particularly confusing that the Terms of Reference provided to the Essential Services Commission (ESC) by the Victorian Government to set a benchmark BSO actively excludes marketing costs, while in parallel the Government is seeking to enhance market accessibility and advertising so that customers are better able to shop around. It defies logic that the ongoing costs imposed through regulatory changes would not be recoupable. Regulatory changes such as the introduction of Recommendations 3-11 impose millions of dollars in initial and ongoing expenses that are imposed directly by government. These should be reasonably recouped on a cost pass-through basis.

Even if Victoria chooses to impose a light touch regulated benchmark approach, the reality of not allowing for a retailer's reasonable acquisition and retention costs will create a false price signal, further confusing customers and eroding confidence in the market.

Furthermore, the fact that Victoria has already had price deregulation for 10 years means that such re-regulation will not only constrain but diminish innovation, investment, competition, services and jobs in the sector.

Innovation

In Victoria, there are 27 electricity retailers and 14 gas retailers competing to sell you energy.¹ Competition is fierce and retailers have sought to differentiate themselves by innovating and carving out new approaches, tariffs, partnerships and levels of customer service.

The concept of innovation is often brought to life for people by something transformative, such as the jump in telecommunications from landlines to mobile phones to the smart phone. However, many innovations are not this dramatic; they are incremental changes that improve choice, value and convenience in people's lives.

Innovation in the energy sector is continuing to gain momentum as technology and business processes evolve to unlock new and better opportunities to service customers. The reality is that for every ten new products or approaches that EnergyAustralia trials, one will be a winner and the rest will be written off. But that one winner can make a difference to our customers; these include practical changes such as billing frequency, live web chats, phone apps that provide energy usage monitoring and alerts for unusually high consumption.

Benefits can also reach beyond the energy sector through cross-promotions and loyalty schemes, enhancing value for consumers according to their preferences.

Some examples of recent innovations introduced by Energy Australia are:

- In November 2016, EnergyAustralia launched Go Neutral – a program that enables customers to offset their electricity's carbon emissions at no additional cost and supports domestic abatement projects.
- In February 2017, we launched a partnership with Virgin's Velocity Frequent Flyer program – this enables residential customers to earn points and travel vouchers through their gas and electricity plans.
- In September 2017, we launched the Redback Smart Hybrid System which combines a solar inverter, battery enclosure and intelligent software into a seamless package. Paired with solar panels and batteries, Redback delivers a holistic energy generation, storage and management system.
- In October 2017, EnergyAustralia announced a 50MW demand response trial across NSW, SA and Victoria. This provides households immediate financial benefits for reducing usage in peak times plus avoided investment costs into the future.
- In November 2017, we launched Secure Saver – this guarantees customers' energy prices are capped for 2 years, plus any price reductions during that period are passed through.
- In January 2018, we partnered with Amazon Alexa – a cloud based service that enables customers to manage their bills, energy use and seek efficiency tips via simple voice commands.
- In January 2018, we announced that we would not be charging paper bill fees and over the counter fees for all our customers nationwide.

¹ ESC, Developing a reference price methodology for Victoria's energy market, <https://www.esc.vic.gov.au/wp-content/uploads/2018/03/RMR-Pricing-Consultation-Paper-for-Developing-a-Reference-Price-Methodology-20180320.pdf> p7

EnergyAustralia has already achieved over 100,000 customers in both Go Neutral and Velocity - demonstrating customers' clear interest in the benefits to be gained outside their traditional electricity bill - and more than 200,000 customers in Secure Saver.

If retailers are denied the ability to effectively differentiate and compete due to the introduction of a regulated retail price that excludes acquisition and retention costs, these new offers and services will not exist in the Victorian energy market.

Investment

One of EnergyAustralia's chief concerns around the introduction of a BSO is that it has the potential to make the entire electricity value chain less stable.

It will be incredibly hard - if not impossible - for the ESC to accurately cost the wholesale component of a customer's bill.

In the past when prices were regulated, jurisdictions adopted different methods of calculating wholesale energy purchase costs - based on constructs such as long run marginal costs, market modelling and other considerations.

In reality, none of the retailers hedged wholesale electricity costs exactly as modelled. Instead, a dynamic market evolved with retailers adopting different energy purchasing strategies, with competition seeing retailers who hedged well being able to offer lower prices to customers. It remains true to this day that it is incumbent on retailers to strategise and negotiate on their customers' behalf to try to get the lowest possible wholesale price in order to remain competitive. Setting a BSO which dictates a wholesale allowance will reduce the dynamic competition in hedging that has emerged over time.

A BSO can also introduce instabilities into the wholesale market. If the ESC sets wholesale purchase allowances in a BSO below the prevailing market rate, there will be insufficient revenue for retailers to purchase forward contracts from generators. Uncontracted energy will lead to greater revenue uncertainty for generators and affect maintenance programs, reducing the reliability of existing power stations. In addition, the introduction of regulated wholesale prices introduces a new risk when retailers consider investing in future generation. Unsurprisingly, more risk and uncertainty means reduced investment in new power stations and energy solutions. A lack of timely and well-planned generation investment can lead to higher wholesale electricity prices as we have recently seen with the closure of Hazelwood Power Station.

The opposite scenario will prevail if the ESC overprices the wholesale component, which provides certainty and stability to generators and retailers, but means that customers will be paying more for electricity than would occur through the efficiencies of a market price.

Therefore anything but pure cost pass-through of the agreed price between retailers and wholesalers will be sub-optimal for market stability. That said, if accurate wholesale cost pass-through is the approach ultimately taken by the ESC, there will be a multitude of BSOs across the market given each retailers' divergent pricing and hedging strategies. Allowing a BSO per retailer will only add to consumer confusion. Ultimately, none of the approaches to determining wholesale costs within a BSO will deliver simplified outcomes for customers.

Competition

EnergyAustralia is highly concerned that under a BSO, retailers will no longer be able or incentivised to compete on price. Price competition is a precondition for a functional market that achieves the best outcomes for customers.

We recognise there are diverse views on whether price dispersion is a sign of the market working, or a sign of market failure. Market failure is only true if those paying higher rates are unable to engage in the market to find better deals. Instead it may be a conscious choice as to how they value their time and effort, and is reflective of a typical competitive market where those who shop around get a better deal than those who do not. Surely the greatest focus must be on helping those who are vulnerable or who face unique barriers to engagement such as people on a concession, people in financial hardship, or Culturally and Linguistically Diverse (CALD) communities.

It is particularly important to note that there is evidence Victorian consumers most in need are the ones accessing lower prices. At present, of EnergyAustralia's 110,000 electricity customers on a concession, 96.5% are on a market offer. This is higher than the overall population of Victorian households on market offers (around 91%) and demonstrates that concession customers are engaged and shopping around to get a better deal.

That said, EnergyAustralia is concerned there is a cohort of concession customers who remain on the standing offer – it is patently inappropriate from a consumer good perspective. As EnergyAustralia has repeatedly advised government, we are limited in switching our concession customers onto market offers because of the requirement for Explicit Informed Consent. While we recognise the importance of this protection for customers, we would support the Victorian Government working with us to find ways of capturing the remainder of our concession customers (3.5%) to help them make the switch to a market offer. On this basis, we welcome the Victorian Government's recent commitment to an energy brokerage service for concession and vulnerable customers.

It is on these customers that the Government should focus its efforts – much like the recent reforms introduced by the NSW Government. Effective from 30 January 2018, the NSW Social Programs for Energy Code ensures retailers must attempt to move concession customers from standing offers onto market offers at least twice every year. Retailers are also required to report to government on the efforts they have made to inform and engage concession customers who remain on standing offers. Retailers who do not comply are exposed to penalties.²

EnergyAustralia also agrees with the Victorian Government's assertion that the standing offer alone does not deliver competitive outcomes to Victorian customers – it is a default no frills offer that is most frequently used to guarantee energy supply when a customer is unknown; for example, when moving home. It serves a necessary albeit limited purpose in the market which is not relevant to the vast majority of customers.

There is no reason we foresee that a known customer should be put onto the standing offer by their retailer or a third party. The Victorian Government could look at measures to guarantee known customers are not put onto standing offers into the future.

Service and Jobs

EnergyAustralia has significant concerns about the BSO's potential impact on staffing numbers and services offered to customers, as these cannot be sustained under a regulated price. Most electricity retail operations are located in Victoria because Victoria led the way in establishing competitive retail markets. EnergyAustralia alone employs 2,000 staff in Victoria throughout multiple locations. Without the ability to recoup customer acquisition and retention costs, significant operations within our business would no longer be viable.

² See Section A5.14 Reporting and Section E2 Assistance with Market Offers of the "NSW Social Programs for Energy Code" www.resourcesandenergy.nsw.gov.au/__data/assets/pdf_file/0011/749954/NSW-Social-Programs-Code.pdf

Under a BSO, our call centre staffing would be cut to save costs. There would be minimal financial ability to base our call centres in Australia and our 300-strong award-winning staff in Geelong would face the prospect of their jobs likely being shipped offshore to lower cost call centres.

Equally, there would be minimal incentive or ability to fund our NextGen area, which is our hub for innovation, design, prototype, test and transition in new products, solutions and services. That's another 70 Victorian-based staff who would face downsizing and be re-orientated to deliver services and products to other states.

And of course we would no longer be able to fund our New Offers or Marketing teams as there would be no bespoke or innovative tariffs coming into the Victorian market. That's another 50 Melbourne-based jobs that would be lost.

Deferring the BSO

EnergyAustralia is confident that the existing improvements being made by the Victorian Government as well as numerous other processes will help consumers. These include:

- Prime Minister's retailer roundtable reforms, including national rule changes recently completed or underway to tighten billing and marketing practices.
- Outcomes of the ACCC's Retail Electricity Pricing Inquiry – by 30 June 2018.
- Implementation of the Payment Difficulty Framework – by January 2019.
- Implementation of a Victorian comparator rate – by 1 July 2019.
- ESC's Report on competitiveness and efficiency of the Victorian retail market - by 31 December 2019

Given the likelihood of negative impacts arising from a BSO, EnergyAustralia strongly recommends the Government allow its existing reforms (Recommendations 3-11 and the Payment Difficulty Framework) to be completed, allowing time for consumers to respond and assess their effectiveness, before imposing such a fundamental change.

As part of this process, we again encourage the Government to undertake an independent RIS to fully assess the potential costs and benefits of a regulated price signal.