



30th March 2018

Mr Paul Murfitt
Executive Director, Energy Reform
Department of Environment, Land, Water and Planning
8 Nicholson St East Melbourne VIC 3002

Submitted by email to EnergyMarket.Review@delwp.vic.gov.au

Dear Mr Murfitt

RE: Consultation Paper: Response to the Bipartisan Independent Review of the Electricity and Gas Retail Markets in Victoria

ERM Business Energy welcomes the opportunity to respond to the Department of Environment, Land Water and Planning (DELWP)'s Consultation Paper: Response to the Bipartisan Independent Review of the Electricity and Gas Retail Markets in Victoria (the Consultation Paper). The Consultation Paper seeks feedback on the specific recommendations from the Independent Review of the Electricity and Gas Retail Markets in Victoria (the Review), surrounding the introduction of a Basic Service Offer (BSO) and Recommendation 4, relating to contract periods, practices and variations.

About ERM Business Energy

ERM Power Retail Pty Ltd, which trades as ERM Business Energy, is a subsidiary of ERM Power Limited, an Australian energy company operating electricity sales, generation and energy solutions businesses. Since launching in 2007, ERM Business Energy has grown to become the second largest electricity provider to commercial businesses and industrials in Australia by load¹, with operations in every state and the Australian Capital Territory. ERM Business Energy has increasing success in the small business market. www.ermpower.com.au

General Comments

The Victorian Government's pursuit and implementation of recommendations 1 & 2 of the Review is likely to severely harm competition in the Victorian retail energy market. On the whole, competition has brought benefits to both the wholesale and retail segments of energy markets. Provided that competitors can operate on a level playing field and that new competitors are able to enter the market, competition should continue to benefit consumers in the long term. That is not to say that energy markets are working perfectly at present. There are definite improvements that can be made that would ultimately improve outcomes for consumers.

¹ Based on ERM Power analysis of latest published financial information.

We believe some of the recommendations of the Review are likely to have a positive impact on promoting a greater understanding of offers and accessibility to assistance for those in need. As such, we largely support recommendations 3-11 of the Review Report, albeit with some important amendments we have detailed below. We do not support recommendations 1 and 2, and believe price regulation will be a retrograde step for Victoria, thwarting competition, innovation and development of the Victorian energy market to the detriment of consumers.

Comments on the Basic Service Offer

There are various drivers behind recent increases in electricity prices stemming from right across the supply chain – from network tariffs to state and national environmental schemes, to a tight supply-demand balance in the wholesale market and even questionable tactics by some retailers. This was made clear in the ACCC’s electricity price inquiry and more recently the findings of the Australian Energy Regulator’s (AER) advice on the impact of the closure of Hazelwood Power station, pointing to the closure having a significant impact to wholesale electricity prices². The Victorian Government’s focus on retailers is therefore akin to treating the symptom and not the cause. Retailers are being held entirely responsible for issues occurring in other parts of the supply chain. The ACCC’s preliminary report into energy prices highlighted improvements and we encourage the Victorian Government to take a prudent approach and wait for the results of the ACCC’s inquiry before considering whether or not to implement the BSO.

A cost benefit analysis assessing the impact of the BSO should be a requisite to any consideration of a BSO

We note that it is the Government’s intention to commission the Essential Services Commission to develop a methodology for a ‘reference BSO price’ for electricity and gas offers for residential and small business customers. This methodology would then supposedly inform the ESC of the efficiency of the market and the Government’s consideration of pursuing a BSO. The Review’s recommendation for a BSO was made in the absence of any rigorous market assessment and it is our view the impact of its introduction may have alarming consequences on competition. We strongly believe it would be prudent for the Government to seek an independent cost-benefit test to ensure the impact on the market is fully analysed and assessed as part of any work to consider the BSO’s introduction. Simply determining the methodology for a BSO design will not test the impact of the BSO on Victorian consumers who are likely to face costly and harmful consequences of a more concentrated market.

It is deeply concerning that a regulated BSO would deliberately close Victoria to energy retail competition by not accommodating for any headroom, acquisition or retention costs, and therefore not allowing new or smaller retailers to operate in the market. With this approach, we are concerned that the BSO will be at a level that will only allow incumbent, dominant retailers to operate economically in the market. In fact by restricting these cost inputs, the presumption is that a new retailer cannot win a BSO customer without running uneconomically. We question a policy that would seek to provide further concentration of market power to incumbent retailers and harm consumers over the longer term with restriction to choice, innovation and product diversity.

The rationale for a BSO is founded on the assumption that standing offer customers are those that do not engage. We encourage the Government to be mindful that most standing offer customers of second tier retailers are on this contract type as an interim arrangement (deemed contract). According

² AER electricity wholesale performance monitoring - Hazelwood advice, March 2018, page 2

to Victorian's regulations, customers must be placed on a deemed/ standing contract if the customer has not entered into a market agreement. This circumstance presents while the customer transfers out to another retailer or the customer has failed to enter into another market agreement at the expiry of their contract. In ERM Business Energy's case, approximately 97% of our small business customers are on market offers³; our standing contracts apply to only approximately 3 % of our small business customers. Overwhelmingly this 3% are on the deemed arrangement for a short period of time. Any cost benefit analysis must assess the true nature of deemed standing arrangements and any distorting effects of the introduction of a BSO on second tier retailer offerings.

Costs to customers stemming from Victoria further isolating itself from the national retail regulatory regime should not be ignored

We are disappointed that the Review Report continues to ignore the costly regulatory burden of retailing across markets with different compliance obligations. The fact that Victorian continues to regulate itself away from the compliance regime adopted by the other states in the NEM comes at a cost, adding to customers' bills and should not be ignored. Retailers meeting differing obligations across jurisdictions face limited opportunities to leverage economies of scale, particularly in Victoria where there are different compliance obligations around compliance reporting, metering, marketing, contracting, billing and various other service transactions.

For our multisite customers with operations across various states, the difference of Victoria from other NEM states that operate under the National Energy Customer Framework is revealed. Unlike in other states, our Victorian multisite customers are restricted from aggregating sites to form a large customer as a provision equivalent to Rule 5 of the National Energy Retail Rules is not included in the Victorian Energy Retail Code. Instead, Orders in Council deal with customer definitions in Victoria and define a 'relevant customer' on the basis of an individual supply point, and not on the basis of the aggregate of each supply point from which the customer consumes electricity or gas. Further under section 36(1) of the Electricity Industry Act, a term of a contract for the supply of electricity to a 'relevant customer' is void to the extent that it is inconsistent with terms set by the ESC relating to specific matters. As a result of these restrictions in Victoria, multisite customers must be treated as single sites and this adds to the cost of serving these customers. Retailers are unable to leverage the cost efficiencies of aggregation and customers are unable to realise the benefits of convenience and flexibility presented by innovative consolidating billing design and the adoption a more streamlined approach to contracting.

We would urge the Government to exclude multisite business customers from any BSO and consider law changes to Orders and the Electricity Industry Act to allow for aggregation of multisite business premises to a meet the large customer threshold as permitted in other NEM states. A BSO would further ingrain the departure of Victoria away from the compliance approach of other NEM states and exacerbate the onerous compliance costs of the distinctly Victorian regulatory regime.

Methodology of the BSO regulated price – a single flat tariff will not align to existing network tariffs

In setting a BSO price, we are unsure how the proposed 'flat tariff' would accommodate retailers' requirements to offer a flexible tariff should a customer exercise their right opt in, or accommodate those small business customers that have a demand tariff. It seems that a flat tariff BSO is inconsistent

³ Based on ERM data as at the end of February 2018.

with network tariffs available and would require obligations on the distributor to ensure that the network tariff assigned aligns to a flat retail structure.

Presenting offers in dollar terms (recommendation 3A) is problematic for small business customers

We caution any attempt to create a dollar comparison price on small business customers that have demand tariff arrangements. The AER, in its recent commentary surrounding the release of the Draft AER Retail Pricing Information Guidelines, rightly acknowledges the approach “presents significant challenges” and that it is not feasible, and proposes to not require comparison pricing for small business energy plans⁴. The approach of comparison pricing as described in recommendation 4 of the Review Report should not apply to small business customers due to the difficulties in segmenting this group and the likelihood of misleading customers through generalisations about usage estimates that must be made to create a comparative price.

We urge the Government to consider other opportunities for retailer price comparisons of small businesses, through allowing greater transparency in the presentation of offers, with retail energy charges discernible from network and environment charges. In the case of network charges, which are regulated, there should be no difference between retailers. Therefore for presentation and comparison of prices, unbundling these charges would help demonstrate the true difference in prices between different retailers and tariff structures.

Contract variations and fixing all market offers for 12 months.

We understand that certainty around prices brings confidence to customers in selecting an offer. However, an attempt to separately monitor a 12 month freeze window for each contracted customer is unworkable or will create exorbitant costs stemming from operational monitoring and the complex design of contracting systems required to accommodate it. Put simply, this approach will be complex, costly and will increase the price of energy. A much easier way to meet the objectives of this recommendation would be to restrict price changes to once per calendar year, with the exception of accommodating changes in law, changes in metering (e.g. for PV installations) or network tariff reassignments. Under this arrangement, retailers would only be able to make one price adjustment per year, at the timing determined by the retailer and subject to reasonable notification to customers.

Please contact me if you would like to discuss this submission further.

Yours sincerely,

[signed]

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⁴ AER Notice of Draft instrument: AER Retail Pricing Information Guidelines, January 2018, Page 15.