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Best practice market regulation includes best practice consumer regulation

All Australian Governments have committed to improving the economic and environmental performance of energy markets and delivering greater benefits to households, small business and industry by pursuing the effective operation of an open and competitive national energy market.

The release in late April of the first exposure draft of legislation to implement new national energy retail and distribution laws is one part of this larger process of pursuing national energy market reform that has now been ongoing for the better part of a decade. Unsurprisingly, consumer representatives take a strong interest in this part of the reform process as it will result in new laws governing retailer and distributor relationships directly with consumers. More generally, however, the new laws are an important piece of the overall puzzle as they will determine how effectively the demand-side of the market operates to encourage the open and competitive market, and consequent benefits, that Australia seeks from undertaking these energy market reforms.

The proposed national retail law and retail rules, at least as reflected by the first exposure draft of the legislation, remain a far cry from best practice consumer protection laws. It is hard to avoid the impression that they are partly the result of a process of negotiation and trade-off between the different jurisdictions without an overall focus on what regulation is ultimately best going to facilitate the two central end goals of: confident consumers able to drive effective competition in a modern energy market; and vulnerable consumers protected against undesirable social policy outcomes, given failures of supply deny access to an essential service to members of our community.

This is more disappointing considered in the light of regulatory developments in other policy areas, including general economic or markets regulation and financial services regulation, in which the Federal Government with the agreement and support of the State and Territory Governments is currently progressing important legislative reforms through parliament to ensure Australia's regulatory frameworks continue to reflect best practice market regulation. These reforms reflect a growing sophistication in Australian policy-makers' understanding of what is best practice, including that how consumers act, and what happens to consumers in markets, is important for delivering better market outcomes.

This understanding now needs to be applied in the energy policy arena. There are numerous examples of areas in which the proposed national energy retail legislation falls short of best practice, including:

- **Payment Plans** – The proposed laws do not ensure that consumers will have the right to a payment plan to assist them manage their energy bills in the short term. This right is fundamental to confidence in the market and to preventing consumers from

falling into greater hardship that would trigger the need for more extensive financial hardship program assistance.

- **Marketing** – The proposed laws do not require key information about an energy contract to be provided to consumers before they enter into the contract and do not require retailers to meet basic standards relating to their selling conduct, training of marketing representatives or verification processes to ensure a consumer genuinely understands and agrees to entering into a contract. These issues are central to ensuring informed decisions by consumers driving efficient outcomes in the national energy market. The mere fact that consumers switch energy retailers in small or large numbers does not indicate whether the market is or is not operating effectively and delivering overall economic benefits to the community. Rather, consumers drive competition when they engage in search and switching in the market in an informed manner and choose whether or not to switch to a new supplier based on decisions that accurately reflect their preferences. Poor marketing conduct can severely disrupt this process and result in inefficient and costly market behaviour (not to mention financial impacts and/or distress for the individual consumer).
- **Late payment fees** - Currently banned in Victoria (in recognition that they generally punish people who are already struggling to pay their bills), the draft legislation allows for such fees to be levied. Further, they represent a windfall gain for retailers because retailers already price the cost of late payments into their overall prices for standing offers.
- **Wrongful disconnection** - In Victoria, consumers who have been wrongfully disconnected are entitled to a wrongful disconnection payment of \$250 per day they are disconnected. A wrongful disconnection is when the retailer disconnects the consumer without having followed the processes they are obliged to follow, including offering payment plans. This obligation was introduced in Victoria to provide a practical market incentive for retailers to comply with their obligations following practical difficulties in enforcing compliance in this area and a resulting jump in the number of Victorian households being disconnected. No such measure has been included or considered under the draft legislation.
- **Security deposits** – The proposed laws allow a consumer to be disconnected if they do not pay a security deposit for energy services, but consumers are not given the right to pay a security deposit via a payment plan as an alternative to an up-front lump sum payment, even if they cannot afford the up-front amount.
- **Enforcement and remedies powers** – The laws contain more limited powers for the regulator or consumers to seek to enforce compliance or pursue remedies for breaches of the law than in other comparable areas, even while reforms expanding enforcement and remedies powers in these other areas are progressed.
- **Hardship programs** - The quality of current hardship programs in Victoria is in jeopardy as the current draft legislation does not set out the same level of standards for these programs that direct targeted assistance to the most disadvantaged Australians, and the regulator (to be the AER) will no longer be required to approve retailers' proposed programs, meaning the regulator will only be able to monitor retailer compliance with obligations they have largely set for themselves.

Further, we now have less room to get these laws wrong. The proposed consumer laws come at a time when Australian markets are increasingly being deregulated but competition may or may not be effective to different degrees to protect consumers from unreasonable prices. Tougher economic conditions combined with measures that will increase energy prices such as the introduction of a Carbon Pollution Reduction Scheme and the mandated rollout of smart meters will subject consumers to greater risk of hardship.

The second exposure draft of the legislation is due to be released in October or November this year. Consumer representatives are hopeful that governments are listening to consumer concerns and will make improvements to the laws, but we are also prepared for any further steps we may need to undertake to try to secure best practice consumer protections for all Australians.

We welcome feedback on the information provided in *On the Wire*. Further, we encourage you to forward the newsletter throughout your networks. Production of *On the Wire* is funded by the [Consumer Advocacy Panel](#). To subscribe to *On the Wire*, please email info@consumeration.org.au with "On the Wire" in the subject line. The next edition of *On the Wire* is scheduled for release in September/October 2009.

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1. Regulatory developments

1.1 Ministerial Council on Energy update

The [Ministerial Council on Energy](#) (MCE) convened in Darwin on 10 July 2009 for its 20th meeting.

Key items on the agenda included:

- Noting that the Australian Energy Market Operator (AEMO) replaced the National Energy Market Management Company (NEMMCO) on 1 July 2009;
- Noting that the Council of Australian Governments (COAG) has amended the Australian Energy Market Agreement for the pass-through to regulated retail tariffs of both carbon costs under the Carbon Pollution Reduction Scheme (CPRS) and costs associated with the expanded Renewable Energy Target (RET);
- Approval of the market design for the gas Short Term Trading Market; and
- Agreement to revised timing for the National Energy Customer Framework (NECF) and to the release by the MCE Standing Committee of Officials (SCO) of a Decision Regulation Impact Statement for the NECF.

A full copy of the communiqué from the MCE's 20th meeting can be found [here](#).

More information on the MCE can be found [here](#).

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1.2 National Energy Customer Framework (NECF)

On 30 April 2009 the Ministerial Council on Energy released the First Exposure Draft of the new national energy consumer laws for consultation. The package of laws included a proposed National Energy Retail Law (NERL), National Energy Retail Regulations (Regulations) and National Energy Retail Rules (Rules), accompanied by an Explanatory Memorandum.

Stakeholders participated in the six week consultation period including attending workshops held in Melbourne, co-ordinated by the Department of Resources, Energy and Tourism over two and a half days.

The second exposure draft of the legislation is due to be released towards the end of the year, following the consideration of stakeholder submissions to the first draft. Input from additional work streams regarding issues including smart meter consumer impacts and a retailer of last resort regime may also be included in the second exposure draft.

The MCE is still aiming to have the legislation introduced into the South Australian parliament by Spring of next year.

The MCE SCO has also released a [Decision Regulation Impact Statement \(RIS\) - A National Framework for Regulating Electricity and Gas \(Energy\) Distribution and Retail Services to Customers](#) following the release of the first draft of the NECF legislation. The decision RIS draws largely on input to the MCE SCO process in 2008 and does not include feedback from consultation on the first draft of the legislation. It discusses the process to date, obligations under the Australian Energy Market Agreement and summarises its recommendations for national energy consumer laws as:

- Impose an obligation to supply on retailers;
- Assign the financially responsible retailer as the retailer designated with the obligation to supply;
- Require that the obligation to supply be met by requiring standard contracts to be offered to all residential customers and to non-residential customers who consume energy up to an annual usage threshold, and by requiring market contracts to be offered to non-residential customers who consume more energy than the lower annual usage threshold referred to above but less than a second (higher) annual usage threshold. Non-residential customers who consume more energy per year than the higher annual usage threshold will not be owed an obligation to supply;
- Implement energy specific regulation where general consumer protection laws are silent and also where national and jurisdictional laws are inconsistent;
- Implement a hardship regime for energy customers;
- Include a tripartite model of interaction between distributor, retailer and customer to allocate liabilities and set out contractual responsibilities, using a model retail support contract between retailers and distributors and a model deemed contractual relationship between distributors and energy customers;

- Adopt a business authorisation regime to limit entry into the market for retailers only (not distributors);
- Enhance the existing enforcement and compliance regime in the national energy and gas laws; and
- Do not change the statutory objective in the national energy market laws but give clear guidance in the law regarding the role of customer hardship programs.

Consumer representatives were disappointed in particular with the recommendation regarding the statutory objective. The Decision RIS makes it clear that changing the statutory objective would have limited if any impact on retailers, distributors and regulators and would benefit consumers while not changing the objective would also have little if any impact on retailers, distributors and regulators but costs to consumers, yet the MCE SCO did not recommend changing the objective. Instead it created a third option which it then recommended, that of leaving the objective unchanged and providing additional statutory guidance only on the customer hardship provisions 'to ensure the policy intent for including a customer hardship regime is not removed over time through the application of a statutory objective which focuses on economic efficiency for the long-term interests of customers'.

With this third option, the MCE SCO has sensibly recognised that the long-term interests of customers taken as one group will not ensure that hardship programs are properly regulated, given that such programs are designed specifically to assist a smaller group of consumers, those experiencing hardship, in recognition of energy's nature as an essential service. However, the new energy consumer laws will regulate other consumer issues as well, whereas the existing statutory objective was drafted for the laws regulating only supply-side market issues. The existing statutory objective therefore simply does not accommodate the broader scope of the policy issues covered in these new laws.

More information on the NECF can be found [here](#).

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1.3 Australian Energy Market Operator (AEMO)

The AEMO is now up and running. It combines six former industry bodies from both the electricity and gas markets:

- National Electricity Market Management Company (NEMMCO)
- Victorian Energy Networks Corporation (VENCorp)
- Electricity Supply Industry Planning Council (ESIPC)
- Retail Energy Market Company (REMCO)
- Gas Market Company (GMC)
- Gas Retail Market Operator (GRMO)

The primary roles of AEMO include managing the National Electricity Market (NEM) and the retail and wholesale gas markets of eastern and southern Australia and overseeing the system security of the NEM electricity grid and the Victorian gas transmission network. New functions

include responsibility for national transmission planning and the establishment of a Short Term Trading Market for gas.

More information on AEMO can be found [here](#).

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1.4 Australian Energy Market Commission (AEMC) update

Submissions to the AEMC's *Review of Energy market Design in Light of CPRS and MRET: 2nd Interim Report* have closed.

The AEMC review is considering the way energy markets function and whether any changes are required in relation to the design of those markets in light of the upcoming introduction of the Carbon Pollution Reduction Scheme and the Renewable Energy Target.

In jurisdictions where retail prices are still regulated, the AEMC has proposed that regulated retail tariffs be adjusted regularly to accommodate carbon cost pass-throughs, with these regular adjustments to occur on an ongoing basis for an unspecified time period. We have concerns that frequent adjustments of retail prices for an indefinite period force consumers to bear the full burden of price volatility, even though they are the parties in the market least able to manage or mitigate volatility. Over time, difficulties for energy businesses in forecasting price volatility should reduce and this should remove the need for frequent adjustments of regulated prices. Frequent adjustments of regulated retail prices should be a transitional measure and current arrangements for reviewing regulated prices should return once the initial implementation of the new schemes has been undertaken.

More information on the AEMC can be found [here](#).

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1.5 National Smart Meter Program and the Victorian Advanced Metering Infrastructure

Following the results of the Cost Benefit Analysis in 2008 and subsequent MCE decisions for a mandated rollout of smart meters nationally in jurisdictions where the benefits outweigh the costs, work is moving at quite a pace on the national program.

The National Smart Meter Program has been convening working groups, overseen by the Department of Resources, Energy and Tourism, since March this year. The work groups and their roles include:

- **Business Requirements** - providing recommendations on a Smart Metering Infrastructure (SMI) Functional Specification;
- **Business Processes & Procedures** - developing recommendations on the revised processes to support the provision of the smart metering services;
- **Regulation** - proposing modifications to existing regulatory arrangements including the National Electricity Rules; and
- **Pilots & Trials** - assessing pilots and trials work already undertaken and identifying key findings that should be taken into account in the development of the SMI Functional Specification and SMI NEM Operating Model and any gaps.

In addition, the Department of Resources, Energy and Tourism, which retained management of a fifth work stream on consumer impacts, released a paper on 19 August - 'Smart Meter Customer Protection and Safety Review - Draft Policy Paper One' - which is intended to identify customer protection and safety issues raised by the rollout of smart meters that may need to be considered in the development of the National Energy Customer Framework, including:

- Distributional impacts of time-related pricing;
- Customer billing;
- Prepayment metering;
- Direct Load Control (DLC);
- Supply Capacity Control;
- Remote De-energisation (in plain English, remote disconnection);
- Retailer marketing through in-home displays; and
- Embedded generation.

More information on Draft Policy Paper One can be found [here](#).

Meanwhile, as the National Smart Meter Program advances Victorians bravely lead the way with their Advanced Metering Infrastructure (AMI), or smart meter, rollout with the first phase of the rollout to Victorian households due to begin in September.

Consumer representatives continue to have considerable concerns regarding the impacts of the rollout of smart meters, including the robustness of existing consumer protection regulation to deal with new issues and, significantly, the cost to consumers of the rollout.

More information on the national smart meter program can be found [here](#) and on the Victorian program can be found [here](#).

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1.6 Australian Energy Regulator (AER) update

Draft Determination - Victorian advanced metering infrastructure review; 2009-11 AMI budget and charges applications

On 31 July 2009 the AER released its Draft Determination for the Victorian advanced metering infrastructure review covering the metering charges that Victorian distribution businesses will be allowed to pass through to retailers for the period 2010 and 2011 to cover the cost of installing the new smart meters (which will be passed through to customers by retailers on their bills). Following the Victorian Government's Order in Council setting the requirements for the AER's decision, the AER has applied broad parameters in assessing the recovery of costs for 'prudential' expenditure by distribution businesses. Initial costs for meters per annum are alarming, not to mention those forecast for 2011 (and which will be subject to a further price determination at this time next year to cover subsequent years).

The initial annual charges for the average small customer with a single phase single element smart meter are:

2010

2011

CitiPower	\$104.79 (236% increase)	\$113.00 (+8% increase)
Jemena	\$67.79 (151% increase)	\$130.52 (+93% increase)
Powercor	\$96.67 (177% increase)	\$111.48 (+ 15% increase)
SP AusNet	\$75.88 (110% increase)	\$94.23 (+24% increase)
United Energy Distribution	\$71.80 (222% increase)	\$92.12 (+28% increase)

These charges represent an average increase in a household's annual electricity bill of \$53 (above the current metering charges) in 2010, with a further average increase of \$25 per year in 2011. This average, however, does not recognise the significant increases facing consumers in specific distribution areas, as outlined above. Based on the rollout timeframes, only 25% of consumers will have their new meter by mid 2011 while the remaining 75% of consumers should receive theirs by the end of 2013. In the meantime, however, all consumers will have been paying for their meter, each year, from 1 January 2010. Any purported benefits cannot accrue to customers until they have the new meter installed and functionality is enabled, whereas the costs of the meters will be passed through to customers immediately.

The AER's final determination is due 31 October 2009.

Customer Consultative Group

The AER has recently invited consumers to apply to its inaugural consumer consultative group. This initiative is welcome given the AER will soon become the responsible regulator under the new energy consumer laws. As a cross-jurisdictional regulator, it will be important that a broad cross-section of Australian consumers, including metropolitan, regional and rural consumers in a range of States and Territories, are represented.

More information on the AER can be found [here](#).

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2. Consumer advocacy and other information

2.1 Utilities and Affordability – Mark Henley, Uniting Care Wesley Adelaide

Most of this article is an extract from a presentation made to the SA State Wage Case in early July.

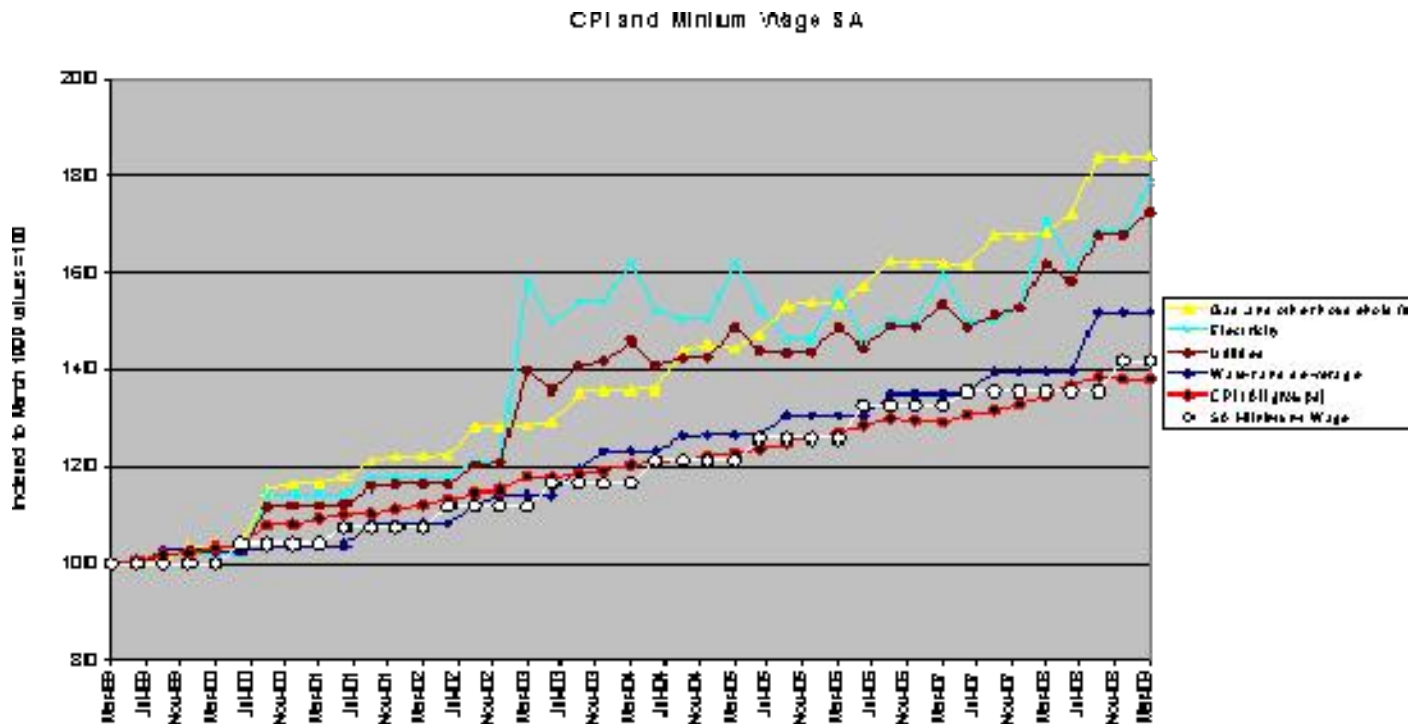
The prices paid for utilities, in aggregate, have increased at a much more rapid rate than CPI over the last decade, particularly since 2003, when Full Retail Contestability (Privatisation) was introduced for South Australian standing energy markets. Effective regulation set distribution and retail price paths that had the effect of reducing the rate of increase of energy bills during 2005-2007, after the average price shock of 25% for household electricity consumers in 2002-03. Trend prices for electricity and gas have been for ongoing increases in prices paid by household consumers, since 2007.

Prices for gas and other household fuels, while volatile due to international markets, have experienced trend rises against CPI since 2000. Price rises were dramatic during 2008.

The price of water has also increased significantly since 2008.

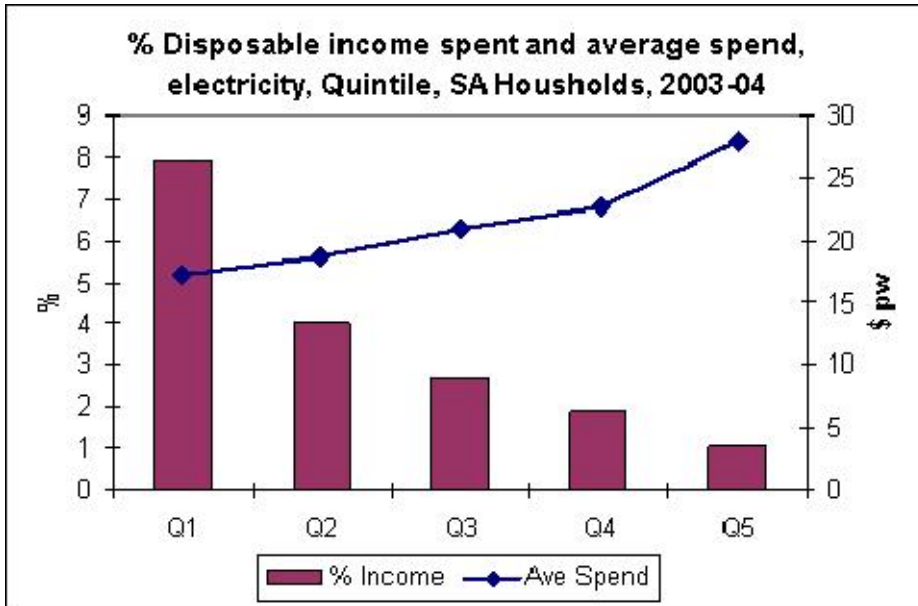
Graph 1 shows that the rate of growth has been greatest for 'gas and other household fuels' followed very closely by 'electricity'. The series third from the top of the graph is an aggregated utilities measure with water price increases being in the middle of the collection of graphs. The lowest two series are for CPI and the SA minimum wage, which has trended very closely with CPI over the last decade

The net impact of utility price rises on low and modest income household budgets over the last 5 years, in particular, has been profound. It must be noted that these services are essential services, meaning that they are necessary for health and safety of all households in 21st century society.



Graph 1

The cost impacts on essential services on households are highly income sensitive. For example, the poorest 20% of South Australian households are probably paying 12% over the past six years (an increase from the 8% in the period 2002/03, as per the graph) of their available income on electricity at the moment, while the wealthiest 20% pay about 1% of income, despite using about 50% more electricity than low income households. This is shown in graph 2.



Graph 2

We have taken the disaggregated Consumer Price Index for SA for the decade 1999 – 2009 and set all March 1999 values for each item in the CPI basket of goods to a score of March 1999 = 100. Changes were then calculated for each item from the CPI, as an index, based on March 1999. This enables the relative price changes to be compared easily, since all items are coming from the same base.

The item with the largest index increase for the decade, was “Property, Rates and Charges”, with an index score of 187. This is explained by the large rises in housing prices over much of the ‘housing boom’ of the past decade. The next four largest increases were Gas and other Household Fuels (also 187), Electricity (179), Rent (176) and Utilities overall (173). The CPI index value in March 2009 was 138. This approach reinforces what we already knew, energy prices are rising at a faster rate than other household costs, creating hardship for growing numbers of households.

Victoria's electricity price index grew from 100 to 170, while the Victorian CPI index rose to 135 over the decade from March 1999. Victoria and South Australia were the first two Australian States to introduce privatisation into electricity markets, and are amongst the most competitive markets in the world according to the Australian Energy Market Commission. Both States have seen electricity prices rise faster than most other households costs and increase at least at double the rate of growth for inflation.

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2.2 Putting the Brakes on Climate Action - the Ministerial Council on Energy – Jane Castle, Total Environment Centre

Australia’s energy market is at the core of our climate change problem. By 2020, emissions from electricity and gas are projected to spiral by up to 64% while the national greenhouse reduction target is supposed to descend by -5% to -25%.

Unless the National Electricity Market (NEM) is fixed, climate change policies will be dampened. The new report, **Role of the NEM in responding to climate change policies**,

by McLennan Magasanik Associates (MMA), commissioned by Total Environment Centre concludes that:

- efficient and clean development is being frustrated by the energy market;
- even with emissions trading, other market failures present barriers to the entry of renewable and low emission generators;
- there are stark conflicts between the objectives of the NEM and climate change policies;
- the lack of an environmental objective for the NEM has constrained opportunities for demand reduction and energy efficiency;
- energy ministers have not fully exploited their role to provide national leadership so that environmental impacts are integrated into energy sector decision making.

Total Environment Centre commissioned the report as a part of its response to the Australian Energy Commission's Review of Energy Markets in the light of Climate Change Policies. The Review provided the potential for a robust debate on the role of the NEM in responding to the challenge to reduce greenhouse emissions. But, primarily due to the limited terms of reference provided by the MCE, the AEMC has only looked at the effects of the Carbon Pollution Reduction Scheme (CPRS) and the Renewable Energy Target (RET) on the NEM, rather than how the NEM can help facilitate climate change policies.¹

MMA has investigated impediments that the NEM has created to climate change policies and identified points where the NEM may be dampening or obstructing their efficient implementation.

The report has found that:

Emissions trading and the NEM

- Even with the implementation of emissions trading, other market failures are likely to persist in the NEM and continue to present barriers to the entry of renewable and low emission generators. (p. 46)
- While emissions trading will be the major policy instrument in response to climate change, rectifying other market failures that impede the entry of renewable and low emissions generation into the NEM would enable this target to be met at a lower cost. (p. 45)

Renewable energy and embedded generation

- NEM rules do not allow small scale distributed generation and demand side response to directly participate in the wholesale market. (p. 45)
- The market barriers that impede distributed generation, in particular, solar PV, have led to inefficient investment decisions, such as over-investment in networks and underinvestment in distributed energy solutions. (p. 42)
- The NEM is designed to be 'technology neutral', assuming that all generation technologies operate on a level playing field. Low emission technologies are disadvantaged, however, as new entrants have to face technical requirements that existing generators did not have to meet, which increases the cost structure of new entrants, which is exacerbated by their higher capital costs. (p 32)
- The benefits of embedded generation are not fully recognised in terms of network benefits and loss reduction. (p. 47)

Saving energy – demand response, energy efficiency

- The current approach to networks encourages increasing energy sales in the short term and expanding the regulated asset base in the long term, both of which are largely dependent on demand. This counters any incentive to reduce demand. (p. 27)
- There are no direct pricing signals designed to draw a strong demand side response and the low energy prices that do exist do not provide a strong incentive for demand reductions. (p. 37) Total Environment Centre believes that better price signals are required, accompanied by strong protections for low-income households.
- There is no evidence that the procedures for the National Transmission Planner include relevant support for demand side planning. (p. 33)
- Solutions that lower peak demand or provide distributed generation may be more efficient and environmentally friendly, but encounter significant barriers. (p. 36)
- The cross-ownership of both generators and retailers by individual companies creates a perverse incentive to sell as much energy as possible during times of high prices. This works against efforts to achieve a more efficient level of electricity generation transmission and distribution. (p. 68)

Total Environment Centre is recommending that COAG urgently initiates an overhaul of energy policy to ensure that energy policy goals and the energy market framework are more appropriately aligned with climate policy.

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ⁱ p. 20.