



independent competition and regulatory commission

Final Report
**Retail Prices for
Non-contestable
Electricity Customers**

**Report 8 of 2006
April 2006**

The Independent Competition and Regulatory Commission (the Commission) was established by the *Independent Competition and Regulatory Commission Act 1997* (ICRC Act) to determine prices for regulated industries, advise government about industry matters, advise on access to infrastructure and determine access disputes. The Commission also has responsibilities under the Act for determining competitive neutrality complaints and providing advice about other government-regulated activities.

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Foreword

The Treasurer has made a reference to the Independent Competition and Regulatory Commission (the Commission) to review the competitive state of the market for the supply of electricity to franchise customers as the basis for determining whether there is a continuing need for a price direction in relation to those customers, and, if the need for such a direction exists, to provide a direction to operate from the expiration of the current price direction on 30 June 2006. The Treasurer's reference is made under s. 15 and s. 16 of the *Independent Competition and Regulatory Commission Act 1997* (ICRC Act).

In the Australian Capital Territory (ACT), the retailing of electricity to customers consuming more than 160 megawatt hours per year (MWh/yr) was made contestable from 1998.¹ The electricity supply industry in the ACT was opened to retail competition for customers consuming more than 100 MWh/yr from 1 July 2001.² Following the recommendation that full retail contestability (FRC) be introduced for all customers in the ACT, the government opened the market for customers using less than 100 MWh/yr to competition from 1 July 2003.³

While the government decided to open the market to all customers, certain transitional arrangements were maintained. These were intended to ensure that customers were able to remain on non-negotiated contracts with the incumbent retailer. A regulated maximum tariff was applicable to such customers for a period of three years. During the designated transitional period, the government undertook to consider whether these arrangements would need to be extended for an additional period.

In this investigation, the Treasurer has sought advice from the Commission on the need for the transitional arrangements to continue and, if so, the form and duration of price protection that should apply to franchise contracts in future. In reaching its determination, the Commission is required to have regard to a number of matters, including:

- the potential effect of the new national energy regulatory environment
- arrangements for retailer of last resort
- retail prices charged by ActewAGL Retail (ActewAGL) in other jurisdictions
- retail prices charged by other incumbent retailers in other jurisdictions.

The investigation is also to have regard to the terms of s. 20 of the ICRC Act.

The Commission released an issues paper in November 2005 and considered submissions made in response to that paper in reaching its draft decision, released in February 2006. In turn, the submissions made in response to the draft decision were taken into account when this final decision was formulated.

Paul Baxter
Senior Commissioner
April 2006

¹ *Utilities Act 2000* (Utilities Act).

² Disallowable Instrument 2001–93.

³ Independent Competition and Regulatory Commission (ICRC), *Final Report: Full Retail Contestability in Electricity in the ACT*, July 2002. Disallowable Instrument 2003–20.

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Executive summary

In September 2005, the ACT Government sought the Commission's advice on whether the transitional franchise tariff (TFT) should be continued beyond June 2006 and, if so, at what level. In addressing this issue the Commission was required to examine:

- the competitive state of the market for electricity supplies to franchise customers in the ACT, as the basis for determining the need for a continuation of the TFT.
- if a further period for the TFT is necessary, at what level the tariff should be set and for how long.

In delivering the recommendations contained in this report, the Commission has considered a range of other legal and administrative matters that are relevant to any decision on the future of a TFT, and the steps that would be required to implement a decision to move to unregulated retail pricing of electricity in accordance with the nationally endorsed competition policy objectives.

Competitive state of the market

In assessing the competitive state of the market, the Commission concluded that the competitiveness of the market cannot be determined by a single characteristic or indicator. As such, the Commission has identified the following characteristics to be consistent with a competitive market:

- the existence of a number of competing retailers and/or the imminent potential entry of new competitors.
- actual and/or potential competition between these retailers.
- innovation in the products and services offered to consumers by active retailers.

Based on these characteristics, the Commission considered the evidence available, and made the following observations and conclusions about the ACT retail electricity market:

- Currently there are three retailers actively operating in the small customer segment of the ACT market. These retailers are active in other States and are able to compete within the retail profit margin currently applying to the TFT.
- There is the imminent possibility of entry by Aurora Energy, offering a prepayment meter service.
- Retailers currently operating in other States are also licensed in the ACT and, despite the strong market presence of the incumbent supplier, ActewAGL Retail, do not regard the barriers to entry into the ACT market as insurmountable.
- Discounts on the TFT of up to 10% are now on offer in the ACT, whereas previously there was no discounting of this type.
- Customer churn is continuing to increase.
- The incumbent supplier has been active and successful in promoting both its brand name and the benefits of remaining with that supplier rather than moving to competitors that are active in the marketplace.

- There is widespread advertising in the print media and electronic media, particularly by the incumbent supplier.
- A range of service options are available in the ACT market, similar in style to those offered in other States. These service options were not previously available in the ACT, and have been developed in response to the competitive market.
- The options currently available generally involve some form of bundling of several services (usually at least electricity and gas services).

The Commission has considered the characteristics of a competitive market evident in the ACT, including an assessment of the current underlying competitive state of the market in the ACT and the role that potential competition plays in the dynamics of the market. In addition, the Commission has considered the current national energy market reform program, including the recent statements from the Council of Australian Governments (COAG) indicating that energy retail price regulation will be phased out once effective competition can be demonstrated. Based on this assessment, the Commission considers that the ACT retail electricity market exhibits the characteristics of a competitive market and that the continuation of a regulated retail tariff is no longer required.

Consumer impact

In addition to assessing the competitive state of the market, the Commission had regard to the requirements of s. 20 of the ICRC Act including the protection of consumers against the abuse of monopoly power; standards of quality, reliability and safety; the need for greater efficiency in the provision of regulated services and the social impacts of the decision. In particular, the Commission was conscious of the need to consider the continuation of safeguards should the regulated tariff be removed.

The Commission considered the intended role of the TFT and concluded that the TFT had never been intended to operate as a ‘safety net’ for vulnerable customers, noting that the TFT was calculated on a cost-reflective basis. However, the Commission recognises and supports the role of government initiatives designed to provide a ‘safety net’ for relevant consumers. To this end, the Commission expresses its support for the continued targeted use of Community Service Obligation (CSO) payments, rebates and concessions, and the involvement of agencies such as the Essential Services Consumer Council (ESCC), Care Financial Counselling Service, ACT Council of Social Service and others, in assisting vulnerable customers. The retention of funding for the CSO payments and support provided under this safety net program in the ACT is fully supported by the Commission and is a matter for attention by government lest the changes envisaged under the move to a national regulatory regime expected within the next twelve months remove the funding source for this CSO activity.

In addition, the Commission was conscious of the commitment from ActewAGL to continue to offer a ‘deemed contract’ that would ensure the continuation of the protections that currently exist under the *Utilities Act 2000* (Utilities Act) and the Consumer Protection Code (the Code) should the regulated tariff be removed. The Commission has given careful consideration to this issue and the need to formalise the legislative arrangements for a ‘deemed contact’ that will protect existing consumer safety net arrangements.

Final recommendation

Based on its assessment of the competitive state of the market for electricity, the Commission has concluded that the removal of the regulated retail tariff will assist in providing further opportunities for competition to evolve and deliver a wider range of benefits to customers in the ACT.

Therefore, the Commission recommends that the TFT be discontinued.

Implementation

The Commission's recommendation that the TFT be discontinued cannot be applied without consideration of other related matters. In particular, the removal of the regulated tariff for electricity supply has implications in terms of the current arrangements that exist under the Utilities Act and the Code. The Utilities Act will need to be amended, regardless of when the TFT is discontinued, in order to address issues relating to the application of the standard customer contract, and the link between the application of the standard customer contract and the existence of franchise tariff customers.

It is expected that these amendments could be made during 2006 as part of the process of amending the Utilities Act in anticipation of the transfer of regulatory responsibility for electricity to the AER at the end of 2006. As these amendments will not be made prior to 1 July 2006, when the current TFT arrangements expire, the Commission recommends that the TFT remain in operation for a further 12-month period (until 30 June 2007) and be discontinued from 1 July 2007.

As an interim arrangement for the 2006–07 year, the Commission proposes to apply a consumer price index (CPI)-related price adjustment to the current TFT such that the TFT for the 12 months from 1 July 2006 will increase from its current rate by the movement in the CPI for the 12-month period ended 31 March 2006.

The Commission is of the opinion that such an interim price direction will allow sufficient time for the necessary amendments to the Utilities Act to occur to implement a 'deemed contract'. If this occurred, price regulation would cease as of 1 July 2007. However, the Commission reserves the right to initiate a reference for an investigation into a variation of this price direction if, by 31 January 2007, the Commission is of the view that the appropriate amendments to the Utilities Act are unlikely to be in place by 30 June 2007 (thus constituting a 'price variation trigger' for the purposes of s. 20A(3)(c) of the ICRC Act).

The Commission notes that its conclusion that the retail electricity market is sufficiently competitive to allow the removal of the regulated tariff is based on its assessment of a regulated market. As such, the Commission takes the view that it would be premature to conclude that 'effective competition' has been 'demonstrated' as required by COAG in its criteria for the removal of retail price regulation. For the purposes of this report, the Commission considers that sufficient competition would allow for the removal of the TFT but may still require some form of regulatory oversight whereas effective competition would allow the removal of all regulatory oversight.

The Commission recommends that a three-year transition period be implemented from 1 July 2007 to 30 June 2010 (or three years from the time at which price regulation ceases), during which time

the Commission would monitor the market to ensure that the characteristics of effective competition were being exhibited. The Commission would expect ActewAGL to notify the Commission and the ACT Government of any changes to the 'deemed contract' tariffs during the period. At the end of the three years, the Commission or the ACT Government would be in a position to conclude whether effective competition had indeed been demonstrated.

Further comments

The increasing rate of 'churn' in the retail market as retail customers transfer from the regulated tariff to a competitive tariff offered by competing electricity retailers is an indication of the growing awareness of the opening of the electricity market to competition. However, the Commission recognises that there is a continuing need to inform consumers of the existence of this competitive market and the range of options available to consumers. To this end, during 2006, the Commission will undertake an awareness campaign to highlight the existence of full retail contestability in the ACT, and the opportunities it provides. It is the Commission's intention that the awareness campaign will provide practical advice to households about the various competitive offers available. The Commission is considering the introduction of a 'comparator tool', to be available on its website, along the lines of those adopted in South Australia and Victoria.

The Commission is concerned to ensure the continuation of the current 'safety net' arrangements which operate through the ESCC. To this end, the Commission is conscious that the funding of the ESCC is heavily reliant on licence fees collected from companies whose regulation is soon to be transferred to AER. The Commission wishes to stress the need for the ACT Government to address the matter of the future funding of the ESCC.

1 Introduction

1.1 Background to the inquiry

One of the ACT's major commitments in the National Competition Policy, signed in 1995, was an undertaking to develop a national electricity market (NEM) delivering benefits of integration and competition to the economy and consumers. Together with the other jurisdictions in the NEM, the ACT effectively entered into the national market arrangements at the end of 1997. Among the policy commitments made by the governments was an agreement to a phased opening of the retail electricity market to full retail contestability (FRC), which enables retailers other than the incumbent to enter the market. Customers are then able to select the retailer that they consider provides the most appropriate price and service package. Each jurisdiction was responsible for determining when it would open its retail electricity markets to competition by rolling back the monopoly supply arrangements of the incumbent retailers. Those decisions were to be guided by reviews of the costs and benefits of opening retail markets in each jurisdiction.

In the ACT, customers whose electricity consumption is above 160 megawatt hours per year (MWh/yr) were made contestable from 1998. The threshold was lowered to 100 MWh/yr from July 2001.⁴ From 1 July 2003, customers below the 100 MWh/yr threshold (essentially, households and small businesses) were made contestable, opening the ACT market fully to retail competition.⁵ This enabled all customers to enter into negotiated customer contracts, also called market contracts, with ActewAGL or other retailers. The government's decision was made, consistent with the Independent Competition and Regulatory Commission's (the Commission's) advice that a small net benefit existed in favour of contestability, subject to certain transitional arrangements intended to ease customers' entry to a contestable market for electricity supply. Those transitional arrangements were to have effect for three years, ending on 30 June 2006.⁶

Included in the transitional arrangements was the implementation of a regulated tariff, referred to as the 'transitional franchise tariff' (TFT). The TFT, which is offered by ActewAGL Retail (ActewAGL) as part of the standard customer contract, sets a maximum price that initially applied to all franchise customers. A franchise customer is any customer who consumes less than 100 MWh/yr and who remains on the standard customer contract offered by ActewAGL.⁷

From 1 July 2003, franchise customers became free to enter into negotiated contracts with ActewAGL, or other retailers, and pay alternative prices. These 'non-franchise' customers are no longer on the standard customer contract and therefore do not receive the regulated TFT. For ease of reference in this report, customers consuming less than 100 MWh/yr (whether they are paying the regulated TFT under a standard customer contract, or a competitive tariff under a market contract) are termed 'small customers'.

⁴ Disallowable Instrument 2001–93.

⁵ Disallowable Instrument 2003–20.

⁶ ICRC, *Final Determination: Investigation into Retail Prices for Non-contestable Electricity Customers in the ACT*, Report 5 of 2003, May 2003.

⁷ Franchise customers are defined under the Utilities Act and subsequent declaration (Disallowable Instrument 2003–20) as those customers who are not non-franchise customers. Non-franchise customers are customers who consume more than 100 MWh/yr or who have elected to enter a negotiated contract.

The transitional arrangements also included an undertaking that the government would review the arrangements before the transitional period expired, to determine whether the arrangements were still required.

On 22 September 2005, the Treasurer issued a reference to the Commission to investigate whether there was a need for the transitional arrangements to continue and, if so, what form and duration of price protection should apply to franchise contracts in future. The full text of the reference is given in Appendix 1.

In November 2005, the Commission released an issues paper as the first step in addressing the terms of reference. Submissions made in response to the issues paper were taken into account by the Commission in the development of the draft decision it released in February 2006.

The Commission received submissions on the draft decision from the ACT Council of Social Service, ActewAGL Retail, AGL, Care Financial Counselling Service, Country Energy, the Essential Services Consumer Council, EnergyAustralia and TRUenergy. The Commission considered these submissions before reaching the final decision set out in this document.

1.2 Structure of the final decision

Chapter 2 contains an overview of the draft decision.

Chapter 3 introduces the main issues raised in submissions in response to the draft decision.

Chapter 4 provides a discussion of the issues raised in submissions in response to the draft decision.

Chapter 5 contains the Commission's conclusions and final recommendations.

Appendix 1 presents the terms of reference for the inquiry.

Appendix 2 provides a summary of the submissions made in response to the draft decision.

Appendix 3 discusses issues relevant to the standard customer contract.

Appendix 4 summarises the Commission's assessment of how the matters listed in s. 20 of the *Independent Competition and Regulatory Commission Act 1997* (ICRC Act) are addressed by this decision.

2 Overview of the draft decision

The Commission released its draft decision on retail prices for non-contestable electricity customers in February 2006.⁸ In the draft decision, the Commission stated that it had interpreted the terms of reference to require the Commission to consider two distinct issues.⁹ First, ‘to consider the competitive state of the market for the supply of electricity to franchise customers as the basis for determining the continuing need for a price direction’. The Commission stated that if it was found that there was sufficient competition in the retail electricity market in the ACT, it could be concluded that there is no need for the continued existence of a regulated franchise tariff. However, the Commission noted that if this conclusion is reached it then becomes necessary to investigate the administrative and legal implications of removing the regulated tariff.

Alternatively, the Commission stated that if it was concluded that the market is not sufficiently competitive, it would be necessary for the Commission to ‘provide a price direction and recommend the duration of any price direction to operate from 1 July 2006, following the expiration of the current price direction on 30 June 2006’.

In reaching the conclusions in the draft decision, the Commission had regard to the matters included under s. 2 of the terms of reference: the new national electricity regulatory environment, applicable requirements of the National Electricity Law and the National Electricity Code; arrangements for a retailer of last resort; the retail prices charged by ActewAGL in other jurisdictions; and the retail prices charged by incumbent retailers in other jurisdictions as well as the requirements of s. 20 of the ICRC Act.¹⁰

In addressing the matter of the competitive state of the market for the supply of electricity to franchise customers in the ACT, the Commission concluded that the competitiveness of the market could not be determined by a single characteristic or indicator. As such, the Commission outlined the characteristics of what it considered to be a competitive market. These characteristics were:

- the existence of a number of competing retailers and/or the imminent potential entry of new competitors
- actual and/or potential competition between these retailers
- innovation in the products and services offered to consumers by active retailers.¹¹

In assessing whether the ACT exhibited these characteristics, the Commission took into account a range of indicators including the size of the ACT customer base, the number of licensed and active retailers, the level of customer awareness, the range of tariff offers, the degree to which customers are ‘churning’ to alternative retailers and accepting market offers of the incumbent retailer, retail margins, the existence of possible barriers to entry and the use of tariffs as a social policy tool.

⁸ ICRC, *Draft Decision: Retail Prices for Non-contestable Electricity Customers*, Report 2 of 2006, February 2006 (ICRC draft decision).

⁹ The terms of reference are provided in Appendix 1.

¹⁰ The retailer of last resort is the electricity supplier that supplies electricity to a customer whose other supplier of electricity ceases to be lawfully able to supply electricity. The retailer of last resort provision differs from the obligation to supply. The obligation to supply exists only for customers on the standard customer contract.

¹¹ A definition of potential competition is provided in Section 4.2.2.

Based on its assessment of these issues, the Commission drew the following conclusions on the three characteristics of a competitive market:

- The existence of a number of competing retailers and/or the imminent potential entry of new competitors
 - The Commission concluded that the size of the retail market in the ACT does not adversely impact on the competitiveness of that market and that in practice, the number of electricity retailers in the ACT, operating actively or with imminent intention to do so, is sufficient to ensure a competitive market.
 - The investigation of barriers to entry indicated that there were no barriers impacting upon the competitive state of the market. The Commission found that retailers currently operating in other states are also licensed in the ACT and, despite the strong market presence of the incumbent supplier, ActewAGL, these retailers do not regard the barriers to entry to the ACT market as insurmountable.
- Actual and/or potential competition between these retailers
 - The Commission found that the level of customer awareness is such that customers are generally aware of FRC. However, the Commission has decided that during 2006 it will undertake a major program to promote the availability of competing electricity supply arrangements for small consumers, and provide advice on how to interpret supply offers made by competing electricity retailers.
 - The Commission found that there has been widespread advertising in the print and electronic media about the availability of contestable electricity supply offers, and that one supplier has undertaken an extensive door-to-door campaign seeking to sign up customers for its services. In addition, the Commission found that in response, the incumbent supplier has been active in the promotion of both its brand name and the benefits of remaining with that supplier rather than moving to competitors that are active in the marketplace. The Commission concluded there is no evidence of any non-competitive behaviour in that process.
 - The Commission noted that discounts on the TFT of up to 10% are now on offer in the ACT, where previously there was no discounting of electricity supplies for household consumers other than for off-peak electricity.
 - The Commission concluded that, while there are difficulties in assessing the competitive state of the market based on a single indicator, the customer ‘churn’ level in the ACT is consistent with that of a competitive market and is showing signs of increasing.¹²
 - The Commission also analysed retail margins and found that margins are sufficient in the ACT to elicit competition and that there is no evidence that retailers are focusing their attention on specific classes of small customers to the exclusion of others.
- Innovation in the products and services offered to consumers by active retailers
 - The Commission found that there is a range of price and service options available in the ACT market, similar in style to those offered in other parts of Australia. These offers were not previously available in the ACT, and have been developed in response to the

¹² Customer churn refers to the number of customers who have switched to alternative retailers, that is, left their original retailer and entered into a contract with a new retailer.

competitive market. The offers currently available involve some form of bundling of services (usually at least electricity and gas services).¹³

- There is the possibility of the introduction of a prepayment metering service that will be available as a competitive option for consumers and is expected to incorporate a new time-of-use tariff option.

The Commission concluded that there was sufficient evidence that the market in the ACT is competitive and that, therefore, there is no longer a ‘continuing need for a price direction’. As such, the Commission’s draft decision recommended that the TFT be removed. This would assist in providing further opportunities for competition to evolve and deliver a wider range of benefits across the ACT market.

The Commission has committed to undertake an awareness campaign during 2006 restating the existence of FRC in the ACT and highlighting the range of competitive offers available. The Commission also noted that some submissions on the issues paper pointed to the TFT as a safety net tariff for vulnerable customers. The Commission observed that to interpret the TFT in this manner is to misunderstand the role of the TFT as the TFT was introduced as a transitional arrangement as part of the process of introducing FRC. The Commission noted that the appropriate way to provide support for vulnerable customers is via targeted support programs of the type already available in the ACT. The Commission expressed its support for the continued use and development of such targeted assistance packages to support customers experiencing payment difficulties. In addition, the Commission noted that the change in the national regulatory arrangements may impact on the funding of organisations such as the ESCC and highlighted this as an area requiring government attention.

The Commission also noted that the removal of the TFT would have implications on the current arrangements that exist under the *Utilities Act 2000* (Utilities Act) and the Consumer Protection Code (the Code). The Commission pointed out that the Utilities Act and the Code will need amendment to address issues related to the standard customer contract. The Commission envisaged that these amendments could be made during 2006 as part of the process of amending the Utilities Act in preparation for the transfer of regulatory responsibility for electricity to the Australian Energy Regulator at the end of 2006. However, the Commission noted that these amendments would be unlikely to occur prior to 1 July 2006, and as such, recommended that the TFT remain in operation for a further 12 months until 30 June 2007 at which point the TFT would be discontinued. The Commission proposed to apply a Consumer Price Index (CPI) related price adjustment to the current TFT offered for the 12 months from 1 July 2006 to 30 June 2007.

The proposed amendments to the Utilities Act would result in all customers becoming either contestable contract customers or ‘deemed contract’ customers. ActewAGL would continue to be required to offer a default tariff to customers who did not want to accept any of the competitive service offers available. This default tariff would be offered as a deemed contract arrangement. In addition, ActewAGL would continue to maintain its obligation to supply as determined under the Utilities Act.¹⁴

¹³ Bundling refers to the situation where a retailer offers a contract containing more than one service. For example, retailers in the ACT are offering contracts that ‘bundle’ electricity supply, gas supply and telecommunication services.

¹⁴ The obligation to supply exists under the Utilities Act and requires an electricity supplier, on application by a person, and in accordance with the supplier’s standard customer contract, to supply electricity to premises owned or occupied by the person.

Furthermore, the Commission would continue to have a role in monitoring the default tariff. This role involves considering the reasonableness of any increase in the default tariff greater than the CPI increase. In addition, the ACT Government would continue to retain the right to refer to the Commission an inquiry into retail electricity prices if ActewAGL, as the incumbent retailer, appears to be misusing any market power, or that the competitive market was not functioning effectively.

3 Submissions on the draft decision

The Commission received submissions on the draft decision from the ACT Council of Social Service (ACTCOSS), ActewAGL, AGL, Care Financial Counselling Service (Care ACT), Country Energy, the Essential Services Consumer Council (ESCC), EnergyAustralia and TRUenergy.

In general, the submissions from ACTCOSS, Care ACT and the ESCC expressed concerns about the conclusions of the draft decision. These submissions were in contrast to the submissions received from ActewAGL, AGL, Country Energy, EnergyAustralia and TRUenergy, which generally supported the draft decision to recommend the removal of the regulated tariff. A detailed summary of the submissions is in Appendix 2.

The major issues identified in the submissions can be broadly classified as follows:

- the national regulatory framework
- the Commission's assessment of the competitiveness of the ACT market, including
 - whether actual or potential competition should be considered when assessing the competitiveness of the market
 - the number of active retailers
 - the range of products on offer
 - the level of customer awareness of FRC
- the transitional period prior to the removal of the TFT
- the provision of consumer safeguards should the regulated tariff be removed.

A discussion of these issues is contained in Chapter 4.

4 Issues raised in response to the draft decision

4.1 National regulatory framework

The draft decision included an overview of the national regulatory framework within which the Commission's review is being conducted. This included the views of the Ministerial Council on Energy (MCE) and the Productivity Commission and the roles of the Australian Energy Market Commission (AEMC) and the Australian Energy Regulator (AER). The following discussion reviews these matters and provides an update based on the latest communiqué released by the Council of Australian Governments (COAG).¹⁵

A paper produced by the MCE on user participation in the energy market noted in relation to retail tariffs that:

In effect, they [regulated retail tariffs] are used to protect consumers from the possible exercise of retailer market power and to achieve a measure of price equality between various customer groups.

In the absence of fully effective retail competition, regulated energy pricing should seek to balance the provision of commercial viability for retailers with consumer protection goals. This is a legitimate and ongoing role for government.

However, regulated energy price setting has the potential to conflict with, and impede efficient market outcomes if prices are not set at cost reflective levels. Predictable and transparent government interventions would assist to achieve efficient outcomes while still facilitating legitimate social objectives.¹⁶

The MCE paper noted that it:

acknowledges the important transitional role performed by retail price regulation but is concerned that inappropriate or entrenched regulation may negatively impact on retail market development.

Furthermore, the MCE noted the following specific problems with retail regulation:

- inappropriately regulated prices that can dampen the development of a fully competitive market by making it less attractive for competing companies to provide innovative products to consumers
- possible discouragement of elements of investment or innovation due to market uncertainty over future price regulation
- price regulation for franchised load customers that reduces the opportunity for consumers to access products and/or market signals that could lead to load reductions at peak times
- continued adjustment and long-term use of price regulation, which may entrench perceptions of the need for price regulation in a number of customer market segments.

¹⁵ The Council of Australian Governments (COAG) comprises the Prime Minister, state premiers, territory chief ministers and the President of the Australian Local Government Association. Its role is to develop and monitor the implementation of nationally significant policy reforms.

¹⁶ Ministerial Council on Energy Standing Committee of Officials, *Improving User Participation in the Australian Energy Market—Discussion Paper*, March 2004, p. 17.

In this context, the Commission's draft decision noted the recent Productivity Commission inquiry into improving energy efficiency.¹⁷ Finding 14.2 of that inquiry was that:

Removing retail price caps (as soon as effective competition has been established), and exploring opportunities to improve the efficacy of price setting arrangements for network operators will improve the economic efficiency of electricity markets.

The draft decision also discussed the future of retail price regulation, with specific mention given to the Australian Energy Market Agreement and how this related to the roles of the AEMC and AER. The initial proposal was that distribution and retail regulation would transfer to the AEMC but retail price regulation would remain with the individual jurisdictions.¹⁸ However, the issue of retail tariffs was on the agenda of the most recent COAG meeting, held on 10 February 2006. In relation to the MCE reform agenda, the communiqué issued after the February 2006 meeting stated that:

Governments have agreed to implement significant energy market reforms under the auspices of the Ministerial Council on Energy (MCE). The MCE is bringing forward further initiatives for the consideration of COAG, including arrangements for the certification of energy access arrangements on a nationally consistent basis, time bound commitments to transfer retail and distribution regulation to a national framework and the phase out of retail price regulation where effective competition can be demonstrated. These new initiatives will be formalised in amendments to the Australian Energy Market Agreement 2004 and are included in this document on that basis.¹⁹

The communiqué included the following key initiatives of the current reform agenda:

Economic Regulation

- Establish a national distribution and retail framework (1 January 2007). Transfer distribution functions to the AER and AEMC (1 January 2007), other functions to be transferred (1 January 2008).

Retail Pricing

- A phase out of energy retail price regulation where effective competition can be demonstrated (reviews commencing 1 January 2007) and the process of responding to advice from the AEMC reviews will be agreed by the MCE by 1 July 2006.²⁰

The Commission concludes that this communiqué indicates that retail regulation will transfer to the AEMC by 1 January 2008 and that regulated pricing will be phased out once 'effective competition can be demonstrated'.

This conclusion is supported by some of the submissions on the Commission's draft decision. AGL stated that the draft decision 'to phase out retail price regulation is consistent with the intent and will of COAG'.²¹ Similarly, ActewAGL stated that:

Any move to continue regulation in a competitive retail market would be totally out of step with the thrust of national energy market reforms. At the most recent Council of Australian Governments

¹⁷ Productivity Commission, *The Private Cost Effectiveness of Improving Energy Efficiency*, 31 August 2005.

¹⁸ Australian Energy Market Agreement, s. 8.1(c).

¹⁹ COAG meeting communiqué Attachment B, *National Competition Policy Review Appendix A—Ministerial Council on Energy Reform Agenda*, 10 February 2006, p. 8.

²⁰ COAG meeting communiqué Attachment B, *National Competition Policy Review Appendix A—Ministerial Council on Energy Reform Agenda*, 10 February 2006, p. 8.

²¹ AGL, *Response to ICRC Draft Decision* (AGL submission), p. 1.

(COAG) meeting, on 10 February 2006, State and Territory Governments restated their commitment to removing retail price regulation where there is effective retail competition.²²

While the Commission considers that the removal of retail price regulation has advantages in providing further opportunities for competition to evolve and deliver benefits to customers, it notes there are inherent difficulties in demonstrating that ‘effective competition’ exists in a market that continues to have a regulated retail tariff in place. The Commission takes the view that the existence of the regulated tariff may restrict the development of a truly competitive market and that it is therefore impossible to conclude that effective competition has been demonstrated while a regulated tariff remains. As such, the Commission considers a transitional period may be required during which no regulated tariff exists before it can be concluded that effective competition has been demonstrated. This matter is discussed in greater detail in Section 4.4.4.

4.2 Assessment of the competitiveness of the ACT market

In the draft decision, the Commission found that there was sufficient evidence to conclude that the market in the ACT was competitive and that the removal of the TFT would assist in providing further opportunities for competition to evolve and deliver a wider range of benefits for customers in the ACT. The submissions on the draft decision discussed a number of issues relating to this conclusion. This section provides an overview of the ACT market, and a discussion of the issues raised in response to the Commission’s assessment of the competitive state of the market.

4.2.1 Overview of the ACT retail electricity market

Customers

The ACT market consists of approximately 145,000 electricity customers. A typical residential customer in the ACT, using 7,500 kilowatt hours per year under the TFT, will face a yearly bill of approximately \$971.

In terms of customer numbers, the ACT market is relatively small in comparison with markets in other jurisdictions. The 2004–05 ACT customer base of 145,000 compares with approximately 2.6 million in New South Wales, 2.25 million in Victoria, 1.7 million in Queensland, 740,000 in South Australia and 255,000 in Tasmania.²³

However, while the ACT market is small in customer numbers compared with most other Australian markets, it is a geographically concentrated pool of customers with relatively high energy requirements, given the relatively cold winters and warm summers experienced in the ACT. Also, the state markets are not perceived as single markets in themselves, but as collections of regional markets (for example, the Sydney–Newcastle–Wollongong market, or the Brisbane–Gold Coast–Sunshine Coast market). These regional markets extend over large areas and are still relatively large in terms of customer numbers, exceeding the size of the ACT market.

²² ActewAGL, *Retail Prices for Non-contestable Electricity Customers—Response to ICRC Draft Decision* (ActewAGL submission), p. 5.

²³ ICRC, Annual Report 2004–05, pp. 34–35; McLennan Magasanik Associates, *Demand Forecasts for Distribution Network Services in Queensland*, July 2004, pp. iv–v; Aurora Energy, *Quarterly Electricity Network Performance Report 1st April 2005—30th June 2005*, July 2005, p. 3.

Retailers

Before the introduction of FRC, ActewAGL was the only electricity retailer in the ACT. This situation differed from that in other jurisdictions, where there were typically a number of incumbent retailers operating in geographically defined areas. In the ACT, the introduction of FRC for customers of particular sizes from 1998, which culminated with the introduction of FRC for all customers on 1 July 2003, provided the first opportunity for alternative retailers to enter the ACT market.

There are currently 15 licensed retailers in the ACT market:

- ActewAGL Retail
- AGL Electricity
- AGL Victoria
- Aurora Energy
- Country Energy
- Energex
- EnergyAustralia
- EnergyOne Proprietary Limited
- Ergon Energy Proprietary Limited
- Integral Energy
- Origin Energy Electricity Limited
- Powerdirect
- Red Energy
- TRUenergy Proprietary Limited
- TRUenergy Yallourn Proprietary Limited.

While 15 retailers now hold licences in the ACT, not all are currently active in the residential market. Only ActewAGL, EnergyAustralia and Country Energy are currently active in the residential market in the ACT.

Ten of the 14 retailers other than ActewAGL licensed in the ACT (AGL Electricity, AGL Victoria, Aurora Energy, Country Energy, Energex, EnergyAustralia, Ergon Energy Proprietary Limited, Integral Energy, Origin Energy Electricity Limited and TRUenergy Proprietary Limited) are incumbent operators in their respective jurisdictions.

The number of licensed retailers in the ACT is comparable to the number of retailers licensed in New South Wales, Victoria and South Australia, the other jurisdictions to have introduced FRC.

Consumer awareness activities

Of the 145,000 electricity customers in the ACT, approximately 130,000 are small customers consuming less than 100 MWh/yr. Since 1 July 2003, all small customers have had the opportunity to either remain as franchise customers on the TFT or elect to become non-franchise customers and select a competitive market tariff offered by either the incumbent retailer or an alternative retailer. However, for a small customer to take advantage of competitive market offers, it is necessary for the customer to be aware that a competitive market exists.

To coincide with the introduction of FRC the Commission released a pamphlet, entitled ‘Informed choice: Which electricity retailer is best for me?’, aimed at increasing the level of awareness within the community of the opportunities available under FRC. In addition, the Commission established a reference point on its website to provide information on FRC. Information on FRC and various competitive market offers can also be found on the websites of the ACT Government and energy retailers. Furthermore, several of the retailers operating in the ACT regularly advertise in local newspapers and on radio and television. EnergyAustralia is currently undertaking a doorknocking marketing campaign across all suburbs of Canberra.

Tariff offers

The majority of additional tariff offers available since the introduction of FRC are in the form of bundle offers. ActewAGL offers a customer who bundles four services with ActewAGL (retail electricity, retail gas, internet service provision and telecommunications services) a discount of 10% on their electricity account relative to the TFT. Under another ActewAGL offer, customers who bundle three of the above services (including electricity) receive a 5% discount plus other rewards.

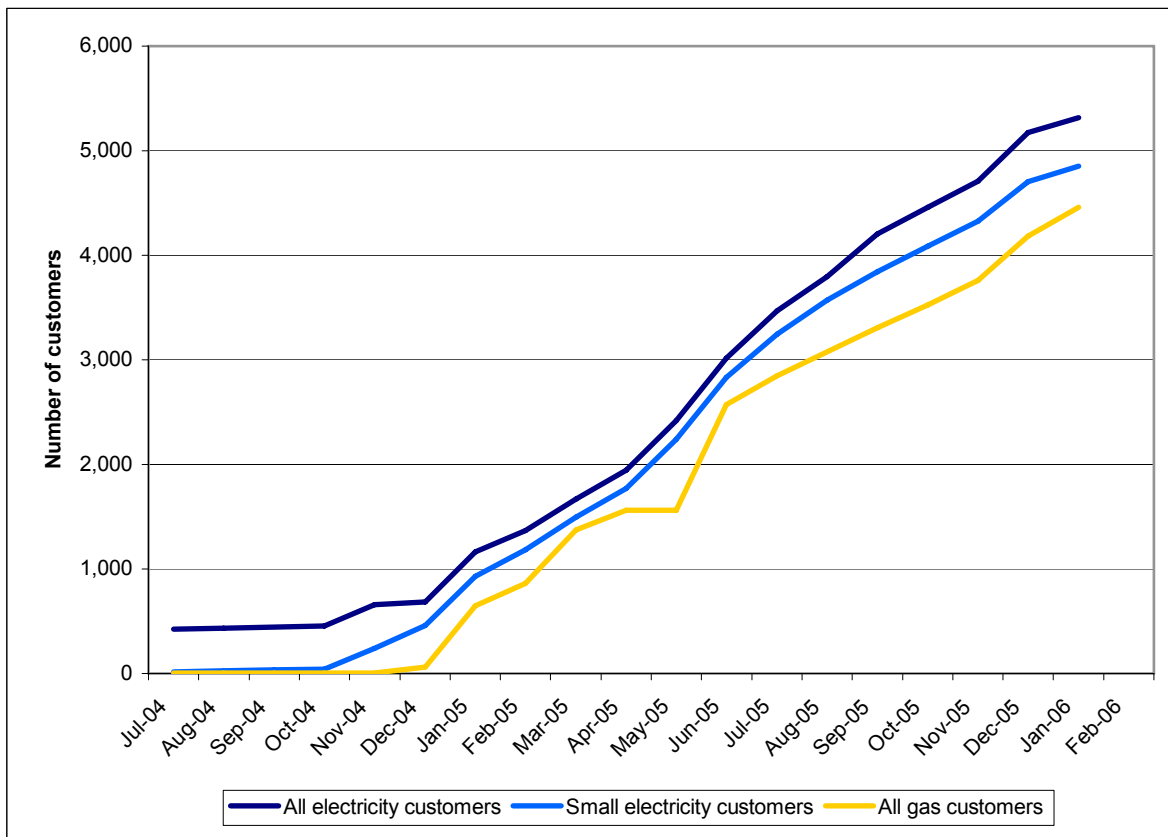
Similarly, EnergyAustralia offers the option of three bundle packages with discounts of up to 8%, while Country Energy offers discounts of between 3% and 5%.

Customer churn

In the issues paper, the Commission noted that approximately 15,500 residential customers had elected to enter into negotiated contracts with ActewAGL to June 2005. In addition, the issues paper noted that approximately 2,500 residential customers had elected to enter into negotiated contracts with electricity retailers other than ActewAGL to June 2005.

Since the release of the issues paper, the Commission has received updated information on the number of customers entering into negotiated contracts with ActewAGL and other retailers. To the end of February 2006, over 20,000 ActewAGL customers had elected to enter into negotiated contracts with ActewAGL, while approximately 5,000 customers had elected to enter into negotiated contracts with alternative retailers. These 25,000 customers who have entered into negotiated contracts represent approximately 17% of the retail electricity market in the ACT. However, the existence of the TFT is potentially limiting the uptake of negotiated contracts. Customers may be postponing entering into such contracts because they expect that additional offers will be made once the TFT has been removed.

Figure 4.1 ACT customer churn, electricity and gas



Source: ActewAGL

4.2.2 Actual and potential competition

The Commission concluded in the draft decision that it was appropriate to consider potential competition as well as actual competition when assessing the competitive state of the market. As such, it is necessary to define potential competition. The Competition Directorate-General of the European Commission provides the following definitions:

Potential competition

Pressure exercised upon incumbent firms by the possibility that new or existing firms will enter a specific market (potential competitor). New entrants may be attracted by above normal profits made in this market by incumbent firms, possibly as a result of weak competition. Additional firms entering the market will increase the overall quantity supplied with the effect that prices fall and above normal profits disappear. Thus, the possibility of market entry has a certain “disciplinary effect” on the behaviour of incumbents. However, the threat of potential competition is relatively small when entry barriers are high.

Potential competitor

A firm is treated as a potential competitor if there is evidence that this firm could and would be likely to undertake the necessary additional investments or other necessary switching costs to enter the relevant market in response to a small and permanent increase in prices. This assessment has to be based on realistic grounds, the mere theoretical possibility to enter a market is not sufficient. Market entry needs to take place sufficiently fast so that the threat of potential entry is a constraint on the market participants' behaviour. Normally, this means that entry has to occur within a short period, for example a period of maximum 1 year for the purposes of the block exemption Regulation on Vertical Restraints. However, in individual cases longer time periods can be taken into account. The time period needed by companies already active on the market to adjust their capacities can be used as a yardstick to determine this period.²⁴

The Commission considers it reasonable to adopt this definition of a potential competitor. In the context of the ACT retail electricity market, the current electricity retail licence holders can all be considered to be potential competitors. These firms have already overcome the regulatory hurdle, meeting the Commission's licensing requirements, and are therefore well placed to attract customers, including small customers, if profitable to do so.

In its submission, ACTCOSS argued that, in considering potential competition as well as actual competition when assessing the competitive state of the market, the Commission had failed to consider the level of consumer apathy. ACTCOSS reiterated its view that those who had taken advantage of discount offers were, 'in the main, early adopters who took advantage of a discount offered for doing what they had always done.'²⁵ In addition, the submission argued that 'people don't go shopping for things they already have and are satisfied with.'²⁶

The Commission considers that, if those taking up the discounting offers were all early adopters and customers did not go shopping for things they already had, a plateau in the number of customers entering into market contracts could be expected. However, the numbers of both customers entering into market contracts with ActewAGL and customers switching to alternative retailers have continued to increase. Since the release of the issues paper, the number of customers who have entered negotiated contracts with alternative retailers has doubled, to reach approximately 5,000, while the number of customers who have entered into negotiated customer contracts with ActewAGL has increased by 4,500 to reach over 20,000. The Commission considers this continued growth in the number of negotiated customer contracts to be an indication of the competitiveness of the ACT retail electricity market. Furthermore, the Commission is of the opinion that the customers entering into market contracts represent a greater segment of the market than early adopters only, and that customers are indeed seeking alternative suppliers for a service they already receive.

The submission from ACTCOSS also questioned the Commission's reference to the Australian Competition Tribunal's decision in the Qantas Airways Limited case when discussing the role of potential competition in constraining the actions of an incumbent firm. ACTCOSS argued that substitutes such as road and rail exist for Qantas passengers, whereas electricity is an essential service, and therefore the Qantas case is irrelevant.²⁷

²⁴ Directorate-General for Competition, European Commission, *Glossary*, 2003, europa.eu.int/comm/competition/general_info/p_en.html

²⁵ ACTCOSS, Submission on ICRC Report No. 2 of 2006—Draft Decision on Retail Prices for Non-contestable Electricity Customers (ACTCOSS submission), p. 9.

²⁶ ACTCOSS submission, p. 11.

²⁷ ACTCOSS submission, p. 9.

In the draft decision, the Commission argued that it was appropriate to consider potential competition when assessing the competitiveness of the market. The Commission argued that the threat of competition from potential new entrants to the market or the expansion of existing firms in the market constrained the actions of the incumbent firm. As an example, the Commission cited the decision of the Australian Competition Tribunal in the 2004 Qantas Airways Limited case. The Commission's argument was that a dominant firm may be constrained by potential entry, or the potential expansion of rivals, and maintain prices near competitive levels.

The Commission cited the following comments made by Professor Ordover, an expert for Qantas:

- Competitive constraints occur at the margin, and impact on the marginal passenger. Rivals or potential competitors do not need to appeal to all the incumbent's passengers to exercise a competitive constraint on them. Rather, it is necessary only that enough customers are affected at the margin to make any increase in fares by the incumbents unprofitable.
- Constraints imposed by entrants do not depend on an immediate ability to increase capacity, but on their ability to implement a sound business plan over a well-defined period of time.
- Incumbents will be constrained from charging supra-competitive fares not by the threat of entry on a particular route, but by the potential for new entrants to enter trans-Tasman routes [the market] and gain profitable market share.²⁸

The Commission notes that the Qantas case is referring to possible entry on trans-Tasman routes. Given that, the Commission considers ACTCOSS to be mistaken. There are limited substitutes for travel between Australia and New Zealand, and parallels can be drawn between the principles outlined by Professor Ordover in the Qantas case and the ACT electricity market. The Essential Services Commission (ESC) of Victoria has also argued that incumbent local retailers are constrained by the threat of entry from other competitors.²⁹

The submission from ACTCOSS also noted the recent decision of the Australian Government that Telstra's line rental charges will continue to be regulated and that Telstra must continue to offer untime local calls. ACTCOSS argued that this was based on equity considerations for disadvantaged customers and that the same equity considerations should apply to essential services such as electricity.³⁰

However, while the Commission acknowledges that there is an Australian Government policy to regulate some services provided by Telstra, there are significant differences between the electricity and telecommunications markets. The Commission notes the current energy market reform agenda being pursued through COAG. This reform agenda includes the removal of retail tariff regulation. Therefore, while Australian Government policy for telecommunications continues to regulate line rental charges and conditions, the Australian Government policy for retail electricity requires the introduction of competition and the removal of regulatory controls. The comparison between telecommunications and retail electricity is therefore invalid.

²⁸ *Qantas Airways Limited*, ACompT 9 (Qantas), 2004.

²⁹ Essential Services Commission of Victoria, *Final Report to Minister: Special Investigation—Review of Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity*, Background Report, June 2004, p. 24.

³⁰ ACTCOSS submission, p. 9.

The ESCC had also argued that ‘that the best indication of a competitive market is actual competition and the widespread adoption of competing price offers—and this is not yet the actuality of the ACT electricity market’.³¹

The Commission considers that relying on actual competition, presumably measured through customer churn, creates a requirement to arbitrarily select a level of churn at which point the market is deemed to be ‘competitive’. For example, is the retail electricity market competitive when 10% of customers have chosen to enter into market contracts, or would 25%, 50% or 100% be more appropriate?

The Commission considers that in order to make a thorough assessment of the competitiveness of the market it is necessary not only to consider a single characteristic of the market—for example, the level of customer churn—but also to understand the underlying market structure and the dynamics of the market. The Commission has therefore considered both potential and actual competition. While single indicators such as market churn, as suggested by the ESCC, may provide a useful description of a market at a particular point in time, an assessment of potential competition is necessary to evaluate the overall competitiveness of the market.

The Commission considers evaluating actual and potential competition to be appropriate, based on its broad assessment of the current market and its interpretation of rulings such as the Qantas case. It is the mere existence of potential competitors that constrains the ability of incumbent firms to exercise market power and raise prices. According to the definition of potential competitors given by the Competition Directorate-General of the European Commission, the Commission considers that there are sufficient electricity retailers that can be classified as potential competitors in the ACT market to support the conclusion that potential competition exists. Further evidence includes the fact that Aurora Energy is considering entering the market with prepayment meters, and the fact that new retailers, such as Red Energy, have recently been licensed.

4.2.3 Number of active retailers

There are 15 licensed electricity retailers in the ACT, three of which (ActewAGL, Country Energy and EnergyAustralia) are active in the small customer market.

The ESCC argued that many of the 15 licensed retailers have simply taken a defensive position and have no real intention of entering the small customer market. The ESCC argued that this ‘defensive position may arise from the fact that they already have large electricity customers in the ACT or because they wish to ensure that they can enter the ACT market quickly if there is a radical change in the market environment’.³²

While the Commission acknowledges that most of the licensed retailers are currently inactive in the small customer market, the argument that these retailers are licensed so that they can quickly enter the ACT market supports the Commission’s use of potential competition when assessing the competitiveness of the market. It is the view of the Commission that, if electricity retailers have become licensed so that they can rapidly seek active entry to the market, this acts as a constraint on the actions of those already operating in the market, especially the incumbent retailer, ActewAGL.

³¹ Essential Services Consumer Council (ESCC), *Response to ICRC Report No. 2 of 2006* (ESCC submission), p. 2.

³² ESCC submission, p. 2.

The Commission retains its view, stated in the draft decision, that given its consideration of potential competition, the number of electricity retailers actively operating in the ACT, the number of currently inactive licensed retailers, and the actual and potential competition that exists between these retailers, there is a sufficient number of retailers to ensure a competitive market for retail electricity in the ACT.

4.2.4 Range of products on offer

The draft decision cited the bundling offers (whereby customers can bundle services, typically electricity and gas, to receive a discount) that have been introduced by competing retailers since the introduction of FRC as indicators of a competitive market.

However, ACTCOSS argued that it:

does not see bundling of existing products, even when offered by a new entrant, as a range of products. That does not mean that ACTCOSS believes that the offers interstate should be extended into the ACT. We do not, for example, want to see Qantas Frequent Flyer points attached to utilities bills through credit card debit schemes. The ESC found that there was a range of incentives offered in Victoria under competitive contracts, including:

- Brand alliance with non-energy products (including football teams)
- Dual Fuel Billing
- Fixed Pricing
- Green Energy
- Competitions
- Product and Service Vouchers.

There is also a product from TruEnergy that is targeted specifically at consumers on rebates and concessions.

ACTCOSS does not advocate that all these products become part of the contract horizon in Canberra. We merely point out that the offerings to Canberra residents are not as varied as those interstate.³³

The Commission notes that, while some of the offers available in Victoria are not available in the ACT, there exists a range of products in addition to bundled electricity and gas. ActewAGL offers Green Energy, off-peak tariffs and time-of-use tariffs for residential and commercial customers.

In addition, EnergyAustralia offers customers the opportunity to win prizes for electing to pay via its Regular Payment Option. Under this arrangement, an estimate of annual consumption is made and a fixed amount is paid every month or fortnight in an attempt to smooth bills over the year.³⁴ It is the Commission's understanding that EnergyAustralia introduced this payment option only recently. The Commission considers the introduction of new arrangements such as this to be a response to competition between retailers and, therefore, a further indication of a competitive market. In addition, the Commission is currently involved in drafting a prepayment metering code which, once complete, will facilitate the entry of prepayment meters to the ACT market.

³³ ACTCOSS submission, p. 12.

³⁴ EnergyAustralia, *Regular Payment Option*, 2004, www.energyaustralia.com.au/energy/ea.nsf/Content/ACT+Regular+Payment+Option

The Commission is also of the opinion that the existence of the regulated tariff may be stifling the introduction of further products, and that its removal may therefore lead to an increase in the number and variety of tariff offers, possibly including further discounts.

4.2.5 Customer awareness of competition

ACTCOSS stated that the Commission had placed great faith in newspaper, radio and television advertising and pamphlets as means of notifying customers of retail competition. ACTCOSS argued that there was a lack of stimulus for customers to seek new electricity retailers. The submission also pointed to the lack of information available on the Commission's website about the existence of FRC in the ACT, and noted that regulators in other jurisdictions, including South Australia and Victoria, had 'comparator' tools on their websites that assist consumers to evaluate tariff offers.

In the draft decision, the Commission committed to undertaking an awareness campaign to promote the advantages of FRC from a domestic perspective during 2006. It is the Commission's intention that the awareness campaign will provide practical advice to households about the various competitive offers available. The Commission is also considering the introduction of a 'comparator tool' along the lines of those adopted in South Australia and Victoria.

4.2.6 Conclusion

The Commission concluded in the draft decision that the electricity retail market was sufficiently competitive to allow the discontinuation of a regulated tariff. The Commission also stated that it considered that the removal of the regulated tariff would assist in providing further opportunities for competition to evolve and deliver a wider range of benefits across the ACT market. In response, submissions were received, from ACTCOSS, Care ACT and the ESCC, which disagreed with this conclusion. The Commission has addressed some of the arguments presented by these organisations in the preceding sections.

However, based on its analysis of the need to consider potential as well as actual competition, the number of retailers, the range of products on offer, and the level of customer awareness, the Commission maintains the view that the retail market in the ACT is sufficiently competitive to allow the removal of the regulated tariff, and that its removal will assist in the introduction of further opportunities for competition to evolve. In reaching this conclusion, the Commission noted the submissions from ActewAGL, AGL, Country Energy, EnergyAustralia and TRUenergy, which supported the Commission's conclusion that the ACT retail electricity market was sufficiently competitive to allow the removal of the TFT.

The Commission's conclusion that the electricity retail market is sufficiently competitive to allow the removal of the regulated tariff has been made in the presence of a regulated tariff. This is a problem that all jurisdictions face as they assess the competitiveness of markets which include significant tariffs that were set not by market participants but by regulators.

4.3 Transition period

In the draft decision, the Commission stated that it considered there to be insufficient time before the current TFT expires on 30 June 2006 for the necessary amendments to be made to the Utilities Act and the Code to address the issues related to the standard customer contract.³⁵ The Commission therefore proposed to implement an interim price direction to apply for the 12 months from 1 July 2006 to 30 June 2007. The Commission argued that this interim price direction would provide adequate time for the required changes to be made to the Utilities Act and Code.

The Commission proposed the following CPI-related price adjustment regime to apply from 1 July 2006 to 30 June 2007:

- Default retail tariffs will be available to all tariff customers whose consumption is below 100 MWh/yr.
- Customers consuming less than 100 MWh/yr may return to default retail tariffs at any time.
- Default retail tariffs should be broadly reflective of published industry benchmarks.
- ActewAGL will advise the Commission of proposed increases to default retail prices at least 40 days before the date of effect.
- Where the Commission determines that a proposed price increase is at the CPI or less than the CPI, the Commission will conduct no further review.
- In the event that the Commission determines that a pricing proposal involves an average increase to retail prices greater than the CPI ('CPI plus proposal'), the Commission will determine whether the proposed increase is reasonable.
- The Commission will receive advice from ActewAGL as to the basis of any CPI plus claim.
- Where the Commission determines that a CPI plus proposal is reasonable, based on ActewAGL's explanation, the Commission will conduct no further review.
- The Commission will not review a CPI plus proposal where ActewAGL demonstrates that this is the result of one or more cost pass-through events or other relevant market factors. Cost pass-through events are changes in: wholesale market conditions; the form of market arrangements adopted in the ACT market; National Electricity Market Management Company (NEMMCO) fees and charges; Mandatory Renewable Energy Target (MRET)/greenhouse levies; network tariff variations; and other fees, taxes and imposts.
- In the event that the Commission seeks to conduct a review of the CPI plus proposal, the Commission may undertake a review of the relevant components, taking into account published industry benchmarks, and prepare a final report on ActewAGL's proposal no later than 20 days before the day on which the proposal is to take effect.
- The Commission will apply the movement in the CPI for the ACT for the 12-month period to 31 December 2005 over the previous 12-month period to 31 December 2004 in assessing the CPI-based price adjustment to take effect from 1 July 2006.

The Commission's draft decision stated that ActewAGL would continue as the retailer of last resort under this arrangement and that this role would not be affected by the implementation of the proposal to discontinue the TFT from 1 July 2007.

³⁵ The issues related to the standard customer contract and the removal of the TFT are discussed in Section 4.4 and Appendix 3.

In responses to the draft decision, the proposal to implement an interim price direction to allow the necessary changes to the Utilities Act and Code was supported by ActewAGL, AGL, Country Energy and EnergyAustralia.³⁶ The ESCC stated that, while it disagreed with the Commission's recommendation to remove the retail tariff, it supported the decision to implement an interim arrangement to allow the amendments to the Utilities Act and Code to be made.³⁷

The Commission notes that amendments to the Utilities Act and Code are required during 2006 regardless of the recommendation to remove the TFT. They are required to enact the transfer of regulatory responsibility for electricity to the AER at the end of 2006.

The Commission retains the view that it would be appropriate to implement a CPI-related adjustment should an interim price direction be adopted for the period from 1 July 2006 to 30 June 2007. The Commission considers that a CPI calculation based on the ABS-weighted average of eight capital cities for the previous two calendar years (that is, 2.67%) would be appropriate.

4.4 Consumer safeguards

The submissions received on the draft decision raised the following matters on the role of the TFT and the safeguards available to customers should the TFT be removed:

- the intended role of the TFT
- consumer protection issues and ActewAGL's commitment to maintain a standard customer contract
- the future funding of the ESCC
- the threat of re-regulation.

4.4.1 Role of the TFT

The draft decision included a discussion of the use of electricity prices as a social policy instrument. The Commission noted that:

the current TFT arrangements were not implemented as a means of protecting vulnerable consumers. Rather, the TFT was introduced as a transitional measure to assist in the implementation of FRC in the ACT, and was calculated on a cost-reflective basis so that ActewAGL could recover the legitimate costs of supplying electricity.³⁸

³⁶ ActewAGL submission, p. 6; AGL submission, p. 4; Country Energy, *Response to ICRC Draft Decision* (Country Energy submission), p. 1; EnergyAustralia submission.

³⁷ ESCC submission, p. 1.

³⁸ ICRC draft decision, p. 34.

ACTCOSS, in its response to the draft decision, noted the following comments made by the Treasurer when discussing the introduction of FRC in the ACT:

The government is conscious of the need to protect smaller users who are not in a position to evaluate various offers that may be made from new suppliers, or in fact may receive few offers from new suppliers because they just do not represent an attractive proposition.

For this reason, government has decided to have a transitional period, initially of three years. During this period, those customers that do not wish to exercise their choice of electricity retailer will be able to continue to be supplied by ActewAGL at a regulated price.³⁹

As also cited by ACTCOSS, the Treasurer went on to state that:

A decision that the transition is complete will be one that is balanced by social outcomes rather than being determined solely by economic imperatives. Three years after the introduction of the transitional period, the government will evaluate whether there is an ongoing need for transitional arrangements.⁴⁰

The Commission acknowledges that a consequence of setting a regulated tariff is that it enables customers who do not wish to exercise their choice of electricity retailer to continue to be supplied by ActewAGL at a regulated price. However, the Commission notes that the Treasurer made a commitment to reassess the operation of the TFT after three years. This evaluation of the ongoing need for the transitional arrangements is the subject of the current review.

In the draft decision, the Commission concluded that the nature of the ACT market had altered sufficiently since the introduction of the TFT in 2003 to allow the removal of the regulated tariff. In reaching this conclusion, the Commission considered both economic and social outcomes, as foreshadowed in the Treasurer's speech of 2003. As a result of its consideration of social outcomes, the Commission developed a framework to ensure the continuation of the protections currently available under the Utilities Act and Code once the TFT ceases to operate. These include the offering of a deemed contract and the continuation of an obligation to supply.

In addition, the Commission drew attention to the work of the ESCC and raised the future funding of the ESCC as a matter the government needs to address. The Commission also committed to undertake an awareness campaign to highlight the opportunities that exist under FRC. Furthermore, the Commission addressed the matters raised under s. 20 of ICRC Act, which include the protection of consumers against the abuse of monopoly power; standards of quality, reliability and safety; the need for greater efficiency in the provision of regulated services and the social impacts of the decision. These considerations are summarised in Appendix 4.

In addition, the draft decision noted that the Commission had considered the arguments in favour of the TFT as a 'safety net' for more vulnerable customers. In the draft decision, the Commission stated that the TFT was calculated to ensure the cost-reflective pricing of electricity. The Commission went on to state that there are more appropriate tools than the TFT for meeting social policy objectives, and that the Commission continues to support the use of community service obligations (CSOs), concessions and rebates for customers experiencing payment difficulties.⁴¹

³⁹ Legislative Assembly for the ACT: 2002 Week 13 Hansard (19 November), p. 3742.

⁴⁰ Legislative Assembly for the ACT: 2002 Week 13 Hansard (19 November), p. 3743.

⁴¹ ICRC draft decision, pp. 34–35.

Furthermore, the Commission received comments from retailers supporting this view. In response to the draft decision, ActewAGL stated that it:

endorses the Commission’s draft conclusions that the TFT was never intended as a form of safety net or social policy instrument, and other more targeted forms of assistance are to be preferred within the ACT. These specific forms of assistance, together with the provisions of the Consumer Protection Code and ActewAGL’s customer hardship programs have provided adequate protection for consumers in the ACT, and will continue to do so in an unregulated market.⁴²

AGL stated that it:

supports the Commission’s view that restricting general retail tariffs via regulation is a poor means of addressing social policy issues and that targeted assistance programs by government to be a more effective and equitable way to address customer difficulties.

Price regulation and assistance to customers in financial hardship should be managed as two separate issues. Effective and efficient assistance to customers in financial hardship requires adequate, well targeted and transparent community service obligations.⁴³

Similarly, TRUenergy stated that it was:

encouraged by the Commission’s view that the TFT does not form part of any safety net for vulnerable customers. It is borne out by economic theory as well as universal experience that competition is the best way to ensure prices are set at efficient levels in a market. The question as to whether energy could be any lower in price (i.e. is the market effectively competitive) is therefore very different to the question as to the capacity of all members of the community to pay for it, and as the Commission notes this was never the function of the TFT in any case.

Neither of these questions can be resolved by simply regulating the price. Appropriate access to and the development of targeted assistance to those in the community experiencing payment difficulties will provide the safety net to vulnerable customers. Retailers can often assist with payment arrangements where this hardship is temporary, but where hardship is permanent or chronic in nature the continuation of and preservation of support programs and mechanisms’ currently operating in the ACT will be essential.⁴⁴

The Commission is conscious of the discussion paper recently released by the ACT Government in relation to ACT energy policy.⁴⁵ The discussion paper raises the question of CSOs and states that:

The Government currently provides disadvantaged consumers with financial support through a program of rebates administered by the Department of Disability, Housing and Community Services. A combined rebate of \$189.11 per annum is currently provided to meet the cost of electricity and/or gas utility bills.

The Government has in place legislation and procedures to manage supply shortages of energy services so that essential and reasonable supply is maintained as far as practicable to all community members.⁴⁶

The discussion paper seeks comments on the ‘ways in which disadvantaged energy consumers could be better recognised and supported’. The Commission supports this approach by the ACT Government and considers it a recognition of the role that targeted support measures can play in an overall social support framework.

⁴² ActewAGL submission, p. 5.

⁴³ AGL submission, p. 1.

⁴⁴ TRUenergy submission, p. 1.

⁴⁵ ACT Government—Office of Sustainability, *A Discussion Paper for an ACT Energy Policy*, March 2006.

⁴⁶ ACT Government—Office of Sustainability, *A Discussion Paper for an ACT Energy Policy*, March 2006, p. 28.

The Commission retains its view that the TFT was never intended to be a safety net measure for more vulnerable customers, while acknowledging that some segments of the community may have viewed the regulated retail tariff as operating in this manner. The Commission continues to support the arrangements that exist for more vulnerable customers, including the targeted use of CSOs, rebates and concession arrangements, as well as the services provided by the ESCC, Care ACT, ACTCOSS and other support agencies.

4.4.2 Consumer protection mechanisms

The standard customer contract essentially is legislated to act as a ‘default contract’ where a customer applies to ActewAGL for an electricity supply but does not wish to enter into a negotiated customer contract, or where ActewAGL provides a service to a person who has not applied for that service. The obligation to supply electricity to a customer is relevant only when a customer is on a standard customer contract. In addition, many of the protections available under the Code are relevant only to a standard customer contract.

The draft decision raised the problem that, if the Commission concludes there is no longer a need for a regulated retail tariff and therefore ceases to issue a price direction, the standard customer contract currently offered by ActewAGL will cease to meet the requirements of the Utilities Act.

As a result of the standard customer contract lapsing, there would effectively no longer be a ‘default contract’ for customers nor an obligation for the utility to supply electricity. Furthermore, ActewAGL would technically be in breach of the Code when supplying the customers currently on the standard customer contract.

To address this issue, the Commission proposed in the draft decision that the Utilities Act be amended to legislate for a ‘deemed contract’. The ‘deemed contract’ would effectively take the place of the current standard customer contract and, in effect, continue the protections available under the Code, including the obligation to supply. In the draft decision, the Commission suggested that these amendments should be made during 2006–07. The Commission therefore proposed to implement an interim price direction to apply from 1 July 2006 to 30 June 2007 to allow sufficient time to make the necessary amendments.

The Commission received submissions addressing the issues of offering a ‘deemed contract’ and the protections available to more vulnerable customers.

In its submission, ActewAGL restated its intention that, if the TFT were removed, it would continue to offer a standard customer contract that would be available to all customers, with no fixed term, and would allow customers the ability to opt in or out of the contract at any time. The Commission interprets the commitment from ActewAGL to continue to offer a standard customer contract to refer to the ‘deemed contract’ as discussed by the Commission in the draft decision.

In addition to the commitment to continue to offer a standard contract, the ActewAGL submission noted that there are various support mechanisms available to more vulnerable customers, and cited the arrangements that exist for the gas retail market in the ACT:

The current arrangements for supporting those in need—through the ESCC, rebates, consumer protection provisions, ActewAGL’s hardship program and ActewAGL’s provision of a standard contract—have worked effectively in the case of the ACT retail gas market, which has been unregulated since 2004. ActewAGL firmly believes that they will continue to provide the appropriate means to effectively support electricity customers in need.⁴⁷

The AGL submission identified a model of ‘shared responsibility’ that it believed could be applied to matters of financial hardship, and stated that AGL:

believes that a model of ‘shared responsibility’ is the most effective and efficient arrangement to deal with issues of financial hardship, and that assisting customers in financial hardship is a mutual social obligation to be shared between retailers, governments, customers and welfare and community groups.⁴⁸

AGL also stated that:

ActewAGL, the incumbent retailer, has submitted that it intends to maintain a standard customer contract in the event that the Commission decides a price direction is not required. AGL suggests that this arrangement would be similar to that in place in for the gas market in the ACT, whereby ActewAGL had maintained a competitive unregulated default price for customers who choose not to participate in the competitive market or are between market contracts. AGL is not aware of any customer protection issues arising for gas customers and as such, will strongly support the adoption of the same approach for electricity.⁴⁹

The submission from Country Energy, while being supportive of the decision to remove the regulated tariff, acknowledged the need for appropriate interim measures to allow time for the amendment of the Utilities Act to address the issue of standard customer contracts.⁵⁰

Country Energy considers the proposal contained in the draft decision to be appropriate, and agrees with the intention to allow the changes to the Utilities Act required to enact the transfer of electricity distribution and retail services to the AER to occur concurrently. However, the submission states that, while there is an obvious need to provide for an appropriate alternative to a negotiated customer contract, it is necessary to recognise that these arrangements should be sufficiently limited so as to not restrict the incentives for customers to seek competitive offers.

The ESCC submission stated that:

While it disagrees with the ICRC’s central conclusion, the ESCC recognises that the ACT Government may be minded to accept the analysis of the ICRC on this matter [the removal of the TFT]. In this case, the ESCC is broadly supportive of the other conclusions of the ICRC ... and recommends that they be accepted by Government as they will provide important safeguards for financially vulnerable electricity consumers in the ACT.⁵¹

⁴⁷ ActewAGL submission, p. 6.

⁴⁸ AGL submission, p. 4.

⁴⁹ AGL submission, p. 4.

⁵⁰ Country Energy submission, pp. 1–2.

⁵¹ ESCC submission, p. 1.

The ‘other conclusions’ referred to by the ESCC are:

- further public information programs on the availability of competitive tariff offers are required;
- the current TFT be extended to 30 June 2007 (with a CPI adjustment) because of legislative difficulties in implementing full retail contestability (FRC) by 1 July 2006;
- after 1 July 2007, there be a statutory “deemed customer contract” which would apply in default to customers who do not enter a contestable contract; and
- the ACT Government should retain the right to refer to the ICRC terms of reference for an inquiry into retail electricity prices in the ACT in case of misuse of market power or failure of market competition.⁵²

Care ACT expressed a similar view to that espoused by the ESCC. That is, while not supporting the recommendation to remove the TFT, Care ACT supported the recommendations of the Commission in relation to dealing with vulnerable consumers.

The Commission considers the approach suggested in the draft decision, whereby an interim price direction is implemented from 1 July 2006 to 30 June 2007, to be appropriate. Such an interim price direction would allow the necessary amendments to be made to the Utilities Act to ensure that the existing consumer protection provisions were retained. The Commission takes the view that such amendments, focused on establishing a ‘deemed contract’, would ensure the protections currently available under the standard customer contract, including the obligation to supply, were continued. The Commission notes that such amendments to the Utilities Act would coincide with the amendments required as part of the transfer of distribution and retail regulation to the AER.

In addition to the protections that would be available under a ‘deemed contract’, the Commission is aware of the other support mechanisms available, including government support programs in the form of CSOs, rebates and concession arrangements; services provided by the ESCC, Care ACT, ACTCOSS and other support agencies; and assistance from retailers. The Commission considers that these arrangements will continue to ensure sufficient protections for more vulnerable customers.

4.4.3 Future funding of the ESCC

The discussion of consumer protection matters raises the issue of the future funding arrangements for the ESCC. In the draft decision, the Commission highlighted the fact that the funding of the ESCC relies heavily on licence fees collected from companies whose regulation will be transferred to the national regulator.

The ESCC, as part of its submission on the draft decision, provided a series of recommendations. The final recommendation stated:

The ACT Government should give attention to how the ESCC is to be funded by industry when the new national regulatory arrangements take effect.⁵³

⁵² ESCC submission, p. 1.

⁵³ ESCC submission, p. 4.

Similarly, Care ACT stated that:

The ESCC and the mechanisms it oversees are of vital importance to our client group and to vulnerable and disadvantaged consumers in the ACT generally. It is a process that took many years to evolve and, in our view, is the best approach to dealing with hardship issues currently in operation in Australia. In a city/jurisdiction that experiences some of the most extreme variations in climactic conditions in the country, with all the attendant risks that flow from a lack of access to utility services, any reduction in the ESCC's powers and capacity would be unacceptable.⁵⁴

ACTCOSS stated that:

The ICRC notes the ESCC will not have access to funding through licensing fees once the NEM regulatory arrangements at the end of 2006. ACTCOSS is also very concerned at this potential erosion of safeguards.⁵⁵

The Commission restates its opinion that the funding of the ESCC after the regulation of retail and distribution energy has been transferred to the AER is a matter that the government must address.

4.4.4 Re-regulation

In the draft decision the Commission proposed to implement an interim price direction to apply from 1 July 2006 to 30 June 2007, to allow time for the necessary amendments to the Utilities Act to occur, at the end of which period the TFT would be withdrawn.⁵⁶ The draft decision stated that, even with the cessation of the TFT arrangements from 1 July 2007, the ACT Government would retain the power to issue a reference to the Commission should the Commission conclude after 30 June 2007 that the de facto default tariff offered by ActewAGL exhibited monopoly pricing characteristics.⁵⁷

The submission from ActewAGL noted that the threat of re-regulation will 'provide a strong incentive for ActewAGL'.⁵⁸ The ESCC argued that the ACT Government must retain the power to re-regulate retail electricity prices in the ACT if there is an abuse of market power or failure of market competition.⁵⁹

The Commission notes that, since the release of the draft decision, COAG has met and revised the MCE reform agenda. The agenda now includes the following:

Economic Regulation

- Establish a national distribution and retail framework (1 January 2007). Transfer distribution functions to the AER and AEMC (1 January 2007), other functions to be transferred (1 January 2008).

Retail Pricing

- A phase out of energy retail price regulation where effective competition can be demonstrated (reviews commencing 1 January 2007) and the process of responding to advice from the AEMC reviews will be agreed by the MCE by 1 July 2006.⁶⁰

⁵⁴ Care Financial Counselling Service submission, p. 1.

⁵⁵ ACTCOSS submission, p. 13.

⁵⁶ ICRC draft decision, p. 41.

⁵⁷ ICRC draft decision, p. 42.

⁵⁸ ActewAGL submission, p. 8.

⁵⁹ ESCC submission, p. 4.

⁶⁰ COAG meeting communiqué Attachment B, *National Competition Policy Review Appendix A—Ministerial Council on Energy Reform Agenda*, 10 February 2006, p. 8.

The result of these reform items is that, once effective competition has been demonstrated, retail price regulation will be removed and there will be no opportunity for the ACT Government to issue a reference to the Commission, regardless of whether the default tariff offered by ActewAGL exhibits monopoly pricing characteristics.

The Commission's conclusion that the electricity retail market is sufficiently competitive to allow the removal of the regulated tariff is based on its assessment of a regulated market. It is the Commission's view that removing the TFT would assist in providing further opportunities for competition to evolve and deliver wider benefits across the ACT market.

However, the Commission considers that, due to the constraints imposed by the regulated tariff, it is not yet possible to conclude that 'effective competition' has been 'demonstrated.' It is the Commission's opinion that a transition period, during which no regulated tariff exists, may be required to demonstrate whether effective competition exists. During this transition period, some continuing need for regulatory oversight is necessary.

The Commission considers that a three-year transition period from the date the regulated tariff is removed, throughout which time the Commission would monitor the market to ensure that effective competition was occurring, may be appropriate. The Commission envisages that the ACT Government would be able to monitor the market throughout this period, so as to be in a position to conclude whether effective competition had indeed been demonstrated.

In the draft decision, the Commission stated that it was favourably disposed to the proposal made by ActewAGL that, even under a post-TFT arrangement, ActewAGL would advise the Commission in advance of the proposed annual price adjustment for the default tariff, and that similar adjustment rules based on movements in the CPI as outlined for the 2006–07 financial year would apply.⁶¹ In line with the approach outlined by the Commission to monitor developments in the ACT market, the Commission considers it appropriate for ActewAGL to provide the Commission with notification of intended price changes as they occur.

The Commission considers it necessary to mention that an increase in the tariff offered by ActewAGL does not necessarily indicate that the market is non-competitive or that ActewAGL is engaging in monopoly pricing. It is entirely possible that an increase in prices may be due to cost pressures such as increases in generation costs. Similarly, ActewAGL retaining constant tariffs does not necessarily indicate a competitive market, because underlying costs may fall.

⁶¹ ICRC draft decision, p. 42.

5 Conclusion

5.1 Recommendation

The Commission has conducted an assessment of the current characteristics of the ACT market including the level of customer churn in the market, the number of currently licensed retailers, the current range of products and offerings, and the level of awareness of FRC. In addition, the Commission has considered the underlying market structure in the ACT, based on the Commission's assessment of the role that potential competition plays in the dynamics of the market and the associated constraints that potential competition places on those retailers currently operating in the market.

In its analysis, the Commission has also been mindful of the national energy market reforms that are occurring. These include the recent statements from COAG indicating that energy retail price regulation will be phased out once effective competition can be demonstrated.

Based on its assessment of the ACT market, and being cognisant of the national energy market reforms, the Commission retains the view expressed in the draft decision that the ACT market is sufficiently competitive to allow the removal of the regulated tariff. It is the Commission's opinion that the removal of the TFT will assist in providing further opportunities for competition to evolve and deliver a wider range of benefits for customers in the ACT. Therefore the Commission recommends the removal of the TFT. The timing for the removal of this arrangement is discussed further below.

The Commission also considered the implications of the proposed withdrawal of the TFT in terms of the requirements of s. 20 of the ICRC Act. Under this section of the Act, the Commission is required to consider a wide range of matters relating to the impact of its decisions on consumers and service providers. The Commission has examined each of these issues (see Appendix 4) and is of the view that all the requirements of s. 20 have been met by the conclusions and recommendation contained in this report.

5.2 Implementation

The Commission has identified that removing the TFT from 1 July 2006 would have the unintended consequence of nullifying the standard customer contract. Standard customer contracts would become negotiated customer contracts under the Utilities Act. This would have implications for ActewAGL and its compliance under the Code and would effectively neutralise the obligation to supply. In response to this, the Commission recommends that the Utilities Act be amended to provide for a 'deemed contract' which would in effect replace the standard customer contract. Such a contract would ensure the protections prescribed by the Utilities Act were retained.⁶²

However, the Commission acknowledges that there is insufficient time to undertake such amendments before the current TFT expires on 30 June 2006. Therefore, the Commission

⁶² The suggested alterations to the Utilities Act are detailed in Appendix 3.

recommends that an interim price direction be imposed to apply from 1 July 2006 to 30 June 2007. The Commission notes that the proposed timing of those amendments to the Utilities Act coincides with the requirement to amend the Utilities Act to enact the transfer of regulatory responsibilities for energy to the AER by 1 January 2007.

As discussed in Section 4.3, the Commission requires that ActewAGL adjust its prices to apply from 1 July 2006 to 30 June 2007 in accordance with the following restrictions and methodology:

- Default retail tariffs will be available to all tariff customers whose consumption is below 100 MWh/yr.
- Customers consuming less than 100 MWh/yr may return to default retail tariffs at any time.
- Default retail tariffs should be broadly reflective of published industry benchmarks.
- ActewAGL will advise the Commission of proposed increases to default retail prices at least 40 days before the date of effect.
- Where the Commission determines that a proposed price increase is at the CPI or less than the CPI, the Commission will conduct no further review.
- In the event that the Commission determines that a pricing proposal involves an average increase to retail prices greater than the CPI ('CPI plus proposal'), the Commission will determine whether the proposed increase is reasonable.
- The Commission will receive advice from ActewAGL as to the basis of any CPI plus claim.
- Where the Commission determines that a CPI plus proposal is reasonable, based on ActewAGL's explanation, the Commission will conduct no further review.
- The Commission will not review a CPI plus proposal where ActewAGL demonstrates that this is the result of one or more cost pass-through events or other relevant market factors. Cost pass-through events are changes in: wholesale market conditions; the form of market arrangements adopted in the ACT market; NEMMCO fees and charges; MRET/greenhouse levies; network tariff variations; and other fees, taxes and imposts.
- In the event that the Commission seeks to conduct a review of the CPI plus proposal, the Commission may undertake a review of the relevant components, taking into account published industry benchmarks, and prepare a final report on ActewAGL's proposal no later than 20 days before the day on which the proposal is to take effect.
- The Commission will apply the movement in the CPI for the ACT for the 12-month period to 31 December 2005 over the previous 12-month period to 31 December 2004 in assessing the CPI based price adjustment to take effect from 1 July 2006.

The Commission requires that the CPI calculation be based on the ABS weighted average of eight capital cities for the previous two calendar years, that is, that a CPI of 2.67% be adopted, when calculating 2006–07 tariffs.

The Commission is of the opinion that such an interim price direction will allow sufficient time for the necessary amendments to the Utilities Act to occur to implement a 'deemed contract'. If this occurred, price regulation would cease as of 1 July 2007. However, the Commission reserves the right to initiate a reference for an investigation into a variation of this price direction if, by 31 January 2007, the Commission is of the view that the appropriate amendments to the Utilities Act are unlikely to be in place by 30 June 2007 (thus constituting a 'price variation trigger' for the purposes of s. 20A(3)(c) of the ICRC Act).

The Commission notes that its conclusion that the retail electricity market is sufficiently competitive to allow the removal of the regulated tariff is based on its assessment of a regulated market. The Commission takes the view that it would be premature to conclude that ‘effective competition’ has been ‘demonstrated’ as required by COAG in its criteria for the removal of retail price regulation. For the purposes of this report, the Commission considers that sufficient competition would allow for the removal of the TFT but may still require some form of regulatory oversight whereas effective competition would allow the removal of all regulatory oversight.

The Commission recommends that a three-year transition period be implemented from 1 July 2007 to 30 June 2010 (or three years from the time at which price regulation ceases), during which time the Commission would monitor the market to ensure that the characteristics of effective competition were being exhibited. The Commission would expect ActewAGL to notify the Commission and the ACT Government of any changes to the ‘deemed contract’ tariffs during the period. At the end of the three years, the Commission or the ACT Government would be in a position to conclude whether effective competition had indeed been demonstrated.

5.3 Further comments

During 2006, the Commission will undertake an awareness campaign to highlight the existence of FRC in the ACT and the opportunities it provides. It is the Commission’s intention that the awareness campaign will provide practical advice to households about the various competitive offers available. The Commission is considering the introduction of a ‘comparator tool’, to be available on its website, along the lines of those adopted in South Australia and Victoria.

The Commission is also conscious that the funding of the ESCC is heavily reliant on licence fees collected from companies whose regulation is soon to be transferred to AER. The Commission wishes to stress the need for the ACT Government to address the matter of the future funding of the ESCC.

Appendix 1 Terms of reference

Australian Capital Territory

Independent Competition and Regulatory Commission (Reference for Investigation) Determination 2005 (No 1)

Disallowable instrument DI2005–218

made under the *Independent Competition and Regulatory Commission Act 1997*, s. 15 (Nature of industry reference) and s. 16 (Terms of industry references)

Reference for investigation under s. 15

Pursuant to s. 15(1) of the Act, I refer to the Independent Competition and Regulatory Commission (the ‘Commission’) the provision of a price direction for the supply of electricity to franchise customers for a period to operate from the expiration of the current price direction on 30 June 2006.

Reference for requirements in relation to investigation under s. 16

Pursuant to s. 16(1) of the Act, I specify the following requirements in relation to the conduct of the investigation:

1. The Commission is to consider the competitive state of the market for the supply of electricity to franchise customers as the basis for determining the continuing need for a price direction. If such a need exists, the Commission shall provide a price direction and recommend the duration of any price direction to operate from 1 July 2006, following the expiration of the current price direction on 30 June 2006.
2. In undertaking the review, the report should have regard to the requirements of s. 20 of the Act, as well as the following:
 - (a) while having regard to the new national electricity regulatory environment, any applicable requirements of the National Electricity Law and the National Electricity Code;
 - (b) the arrangements for Retailer of Last Resort;
 - (c) the retail prices charged by ActewAGL in other jurisdictions; and
 - (d) the retail prices charged by incumbent retailers in other jurisdictions.
3. The Commission must produce its final report in time sufficient to allow ActewAGL Retail to make any necessary administrative changes to its billing system and to provide information on any new tariff to customers.

Ted Quinlan MLA
Treasurer

22 September 2005

Appendix 2 Overview of submissions

The Commission received submissions on the draft decision from the ACT Council of Social Service (ACTCOSS), ActewAGL, AGL, the Essential Services Consumer Council (ESCC), Care Financial Counselling Service, Country Energy, EnergyAustralia, a private ACT resident and TRUenergy. This appendix provides a summary of these submissions.

ACT Council of Social Service

ACTCOSS stated that it disagreed with the Commission's draft decision to recommend the removal of the transitional franchise tariff (TFT) and argued against the draft decision's reliance on potential competition.⁶³

The submission argued, contrary to the Commission's statement in the draft decision that to interpret the TFT as a safety net mechanism was to misunderstand the purpose of the tariff, that the regulated tariff was an integral part of protection measures for low-income households. The submission cited comments made by the Treasurer, at the time of the introduction of the TFT, stating that:

The government is conscious of the need to protect smaller users who are not in a position to evaluate various offers that may be made from new suppliers, or in fact may receive few offers from new suppliers because they just do not represent an attractive proposition.

For this reason, government has decided to have a transitional period, initially of three years. During this period, those customers that do not wish to exercise their choice of electricity retailer will be able to continue to be supplied by ActewAGL at a regulated price.⁶⁴

In addition, the submission cited a submission from Charles Rivers Associates to the 2003 review of electricity and gas standing offers undertaken by the Victorian Government, which supported the argument that the purpose of standing offers is to provide a safety net for small customers.⁶⁵

ACTCOSS stated that it was concerned about the ability of the ESCC to continue to function to protect the interests of low-income consumers if the changes outlined in the draft decision were adopted. The submission suggested that the legal opinion of community legal practitioners be sought regarding the possible impact of the proposed changes to the *Utilities Act 2000* (Utilities Act) on the operations of the ESCC.⁶⁶

ACTCOSS argued that the draft decision contained a lack of relevant and robust data on consumer behaviour, and argued that there was a need for an independent qualitative and quantitative analysis of the ACT market.⁶⁷

In regard to the Commission's assessment of the competitiveness of the ACT market, ACTCOSS argued that the Commission had not considered the apathy of customers. ACTCOSS reiterated its view that those who have taken advantage of bundling offers are, in the main, early adopters who are receiving a discount for doing what they have always done. Furthermore, the submission

⁶³ ACTCOSS submission, p. 5.

⁶⁴ Legislative Assembly for the ACT: 2002 Week 13 Hansard (19 November), p. 3742.

⁶⁵ ACTCOSS submission, p. 6.

⁶⁶ ACTCOSS submission, p. 6.

⁶⁷ ACTCOSS submission, p. 8.

argued that there was no evidence that those customers who had accepted offers had undertaken any form of price comparison for the services offered to ensure they would get the most competitive price for those services.⁶⁸

In support of its argument that there is a need for a regulated retail electricity tariff, the submission noted the recent decision by the Australian Government to continue regulation of Telstra's line rental charges and maintain untimed local calls.⁶⁹

The complexity of the customer transfer process was raised as a barrier to entry.⁷⁰

In regard to the issue of customer awareness, ACTCOSS submitted that in reality people do not go shopping for products that they have and with which they are satisfied. In addition, the submission stated there was a lack of information available on the Commission's website and that an interactive tool such as those available on the Essential Services Commission of South Australia website may prove useful.⁷¹

ACTCOSS stated that it did not consider the bundling of existing products as representing a range of products. The submission pointed to the range of products available in Victoria, which include brand alliances with non-energy products (including football teams), dual fuel billing, fixed pricing, green energy, competitions and product and service vouchers, and stated that the offerings available in the ACT were not as varied as those on offer in other states. However, ACTCOSS claimed that it did not wish to see the introduction of Qantas Frequent Flyer points attached to utilities bills through credit card debit schemes.⁷²

A further issue raised in relation to bundling, particularly of non-alike products, is that it creates the potential for customers to lose access to discrete protection measures. In addition it was claimed that allowing credit products to become part of the utility contract exacerbates debt management problems, because the debt accrues to the credit card company, not the utility.⁷³

ACTCOSS also raised concerns that the final decision on the introduction of prepayment meters was yet to be made and that it was therefore inappropriate to describe their implementation as imminent.⁷⁴

ACTCOSS stated that prices were likely to rise, given that at the current price few competitors are willing to enter the market. ACTCOSS stated that:

This has grave implications for consumers across the board in Canberra, given the high differential temperatures, long cold winters and increasingly hot summers, coupled with the declining costs of electric appliances, particularly reverse cycle air-conditioning, plasma TV screens and home movie systems.⁷⁵

⁶⁸ ACTCOSS submission, p. 9.

⁶⁹ ACTCOSS submission, p. 9.

⁷⁰ ACTCOSS submission, p. 10.

⁷¹ ACTCOSS submission, p. 11.

⁷² ACTCOSS submission, p. 12.

⁷³ ACTCOSS submission, p. 12.

⁷⁴ ACTCOSS submission, p. 12.

⁷⁵ ACTCOSS submission, p. 13.

The submission supported the undertaking from ActewAGL to maintain a standard customer contract but argued that this was an undertaking of the current board only.⁷⁶

In conclusion, ACTCOSS stated that it did not believe that there was sufficient information available on the features of the ACT market to make an informed decision on the operation of the market.⁷⁷

ActewAGL Retail

ActewAGL expressed its support for the Commission's draft decision, particularly agreeing that:

- The ACT retail electricity market is competitive;
- The TFT be discontinued;
- The TFT was never intended as a safety net or social policy instrument, and there are other more appropriate and targeted tools that should be used for meeting social policy objectives;
- To allow time for amendments to the Utilities Act, a temporary price direction should apply from 1 July 2006 to 30 June 2007, with the CPI-related price adjustment regime to apply; and
- If the ACT Government requires future price directions, the CPI-related adjustment regime should be used.⁷⁸

However, the submission expressed concerns on several aspects of the draft decision and requested that the Commission clarify the proposed arrangements for any temporary price direction. The submission argued that it would be inappropriate to require ActewAGL to notify all price adjustments and apply the CPI framework to all adjustments if the TFT were removed, as this could curtail or impede the proper operation of a competitive market.⁷⁹

The submission stated that there are over 20,000 ActewAGL customers who have chosen to switch to negotiated contracts and that other retailers are continually enticing customers to their negotiated contracts.

ActewAGL stated that to continue regulation in the competitive retail market is out of step with the thrust of the national energy market reforms. ActewAGL cited the most recent Council of Australian Governments (COAG) meeting, where the state and territory governments restated their commitment to removing retail price regulation where there is effective competition. The submission argued that, because the ACT electricity market is competitive, retail price regulation should be removed. In addition, the submission stated that customers should not be forced to bear the costs of maintaining retail price regulation.⁸⁰

The submission endorsed the Commission's draft conclusion that the TFT was never intended as a form of safety net or social policy instrument and other more targeted forms of assistance are preferable. ActewAGL stated that:

Pensioners and health care cardholders receive rebates and eligible customers in financial hardship receive support from the Essential Services Consumer Commission (ESCC). ActewAGL also provides support for those in need through the Staying Connected policy and the Customer Council,

⁷⁶ ACTCOSS submission, p. 13.

⁷⁷ ACTCOSS submission, p. 14.

⁷⁸ ActewAGL submission, p. 3.

⁷⁹ ActewAGL submission, p. 4.

⁸⁰ ActewAGL submission, p. 5.

which comprises representatives from CARE ACT, the Salvation Army, the Smith Family, the Financial Counsellors Association of Australia, the Country Women's Association, the Australian Consumers' Association and the Council on Ageing National Seniors. The other retailers in the ACT market also offer support programs for those in financial hardship.

ActewAGL will continue to offer a standard customer contract, available to all customers, with no fixed term and the ability to opt in or out of the contract at any time. This will provide a safety net for customers who are unable or unwilling to take up negotiated contracts with ActewAGL or competing retailers.

The current arrangements for supporting those in need—through the ESCC, rebates, consumer protection provisions, ActewAGL's hardship program and ActewAGL's provision of a standard contract—have worked effectively in the case of the ACT retail gas market, which has been unregulated since 2004. ActewAGL firmly believes that they will continue to provide the appropriate means to effectively support electricity customers in need.⁸¹

ActewAGL supported the proposal to implement a temporary price direction from 1 July 2006 to 30 June 2007 to allow time for the amendment of the Utilities Act but stated that, for consistency with other Commission decisions, the weighted average of eight capital cities CPI should be adopted as the escalation factor. In addition, the submission sought clarification on the temporary price direction and the implementation of the 'price variation trigger'.⁸²

ActewAGL stated that it did not support the suggestion put forward in the draft decision that, if the government chose not to make the suggested amendments to the Utilities ACT, a limited price direction could be issued that applied only to a more narrowly defined class of 'franchise' customer.⁸³

The submission supported the CPI-based approach to regulation outlined by the Commission for use should the government require the continued existence of a regulated tariff. However, ActewAGL stated that there should be an opportunity to provide input on this approach before the final decision is released.⁸⁴

ActewAGL stated that if the TFT were to be removed it would be inappropriate for ActewAGL to be burdened with ongoing regulatory restrictions on how it could adjust prices. ActewAGL stated that it would continue to advise the Commission in advance of proposed changes. The submission pointed to the example of the retail gas market in the ACT, where ActewAGL has voluntarily notified the Commission of intended price changes, and price changes so far have been limited to CPI adjustments.⁸⁵

The submission concluded by noting the threat of re-regulation, observing that the minister could at any time issue an industry reference to the Commission for a review of ActewAGL's prices.⁸⁶

AGL

AGL stated that it agreed with the Commission's assessment that the ACT market is competitive and regulation of retail tariffs could be removed. The submission expressed its support for

⁸¹ ActewAGL submission, pp. 5–6.

⁸² ActewAGL submission, p. 6.

⁸³ ActewAGL submission, p. 7.

⁸⁴ ActewAGL submission, p. 7.

⁸⁵ ActewAGL submission, p. 7.

⁸⁶ ActewAGL submission, p. 8.

market-based retail energy pricing, and stated that competition is the best mechanism for producing efficient prices, providing the price signals for new investment and providing incentives for the most efficient use of energy.⁸⁷

In addition, the submission supported the Commission's views that regulation of general retail tariffs is a poor means of addressing social policy issues and that targeted assistance programs by government are a more effective and equitable way to address customer difficulties. The submission states:

Price regulation and assistance to customers in financial hardship should be managed as two separate issues. Effective and efficient assistance to customers in financial hardship requires adequate, well targeted and transparent community service obligations.⁸⁸

AGL argued that a model of 'shared responsibility' is the most effective and efficient arrangement to deal with issues of financial hardship, and that assisting customers experiencing hardship is a mutual social obligation to be shared between retailers, governments, customers and welfare and community groups.⁸⁹

AGL noted that ActewAGL had stated its intention to maintain a standard customer contract in the event that a price direction ceased to apply. The submission suggested that this arrangement would be similar to that which currently exists for gas supply and stated that AGL, being unaware of any customer protection issues arising for gas customers, supports a similar approach for electricity.⁹⁰

The submission noted that the draft decision was consistent with the intent and will of COAG's energy market reforms, one of which is to phase out energy retail price regulation.⁹¹

AGL supported the transitional arrangements suggested by the Commission, whereby tariffs are adjusted by CPI during 2006–07 until the necessary amendments to the Utilities Act have occurred. The inclusion of a 'price variation trigger', such as the time at which the legislation is amended, was also supported. However, the submission argued that the Commission must implement an agreed timetable to ensure that the required legislative changes are completed by 1 July 2007.⁹²

Care Financial Counselling Service

Care Financial Counselling Service (Care ACT) stated that it agreed with and endorsed the submission made by the ESCC. The Care ACT submission made particular mention that it did not support the Commission's conclusion that the ACT market is genuinely competitive. However, the submission acknowledged that the recommendations contained in the draft decision in regard to dealing with vulnerable customers were useful and offered its broad support for these recommendations.

⁸⁷ AGL submission, March 2006, p. 1.

⁸⁸ AGL submission, March 2006, p. 1.

⁸⁹ AGL submission, March 2006, p. 4.

⁹⁰ AGL submission, March 2006, p. 4.

⁹¹ AGL submission, March 2006, p. 1.

⁹² AGL submission, March 2006, p. 4.

The Care ACT submission also noted the recommendation, contained in the ESCC's submission to the Commission, which stated that:

The ACT Government should give attention to how the ESCC is to be funded by industry when the new national regulatory arrangements take effect.⁹³

In relation to this recommendation, Care ACT stated:

The ESCC and the mechanisms it oversees are of vital importance to our client group and to vulnerable and disadvantaged consumers in the ACT generally. It is a process that took many years to evolve and, in our view, is the best approach to dealing with hardship issues currently in operation in Australia. In a city/jurisdiction that experiences some of the most extreme variations in climatic conditions in the country, with all the attendant risks that flow from a lack of access to utility services, any reduction in the ESCC's powers and capacity would be unacceptable.⁹⁴

Care ACT addressed the issue of prepayment meters and stated that it did not accept that their arrival in the 'ACT market will add to consumer choice safely or fairly'.⁹⁵

Country Energy

Country Energy supported the recommendation to discontinue the TFT. It acknowledged the need for appropriate interim measures to address the issue of standard contracts once the current price direction ceases, and supported those suggested by the Commission.⁹⁶

The submission noted that there is a need for an appropriate alternative to a negotiated contract. However, Country Energy stated that, in ensuring that the most vulnerable customers have access to 'safety net' arrangements, these arrangements should be sufficiently limited so as to not restrict the incentives for customers to seek competitive offers.⁹⁷

The submission noted that the Commission had outlined the circumstances under which a deemed contract could apply. However, while accepting the need for such arrangements, the submission stated that the deemed contract arrangement should be a finite arrangement, as is the case in other jurisdictions, because this would ensure that such provisions would not lower the rate of potential transfers and ultimately threaten the viability of competition.⁹⁸

Essential Services Consumer Council

The ESCC disagreed with the Commission's conclusion in the draft decision that the electricity market in the ACT is sufficiently competitive to allow the cessation of a regulated tariff. Rather, the ESCC considers that the current TFT arrangements should continue until 30 June 2009, with a further review of the ACT electricity market to be undertaken late in 2008.⁹⁹

The ESCC argued that the conclusions reached in the draft decision should have been based on actual competition, not potential competition, as actual competition gives the best indication of a competitive market. The submission claimed that, while there are 15 licensed retailers in the ACT

⁹³ Care Financial Counselling Service submission, p. 1.

⁹⁴ Care Financial Counselling Service submission, p. 1.

⁹⁵ Care Financial Counselling Service submission, p. 2.

⁹⁶ Country Energy submission, p. 1.

⁹⁷ Country Energy submission, p. 1.

⁹⁸ Country Energy submission, p. 2.

⁹⁹ ESCC submission, p. 1.

market, most retailers have taken a defensive position and have no real intention of entering the ACT market unless something changes radically. It argued that the cost of the licence was insignificant in terms of the retailers' overall operations and, therefore, being licensed did not indicate a specific intention to enter the market. The submission argued that these licensees could not be considered as even potentially competitive, in a practical sense, given the present and forecast nature of the market.¹⁰⁰

The ESCC argued that, while its primary concern is the interest of those in lower socioeconomic groups, it is aware of the general approach to the provision of utilities within the middle income group. The ESCC claimed that customers in this group see little, if anything, to be gained from moving from the TFT to other offers, and rely to a great extent upon the protection provided by the TFT and the overall regulatory and consumer protection framework.¹⁰¹

However, while disagreeing with the Commission's recommendation to remove the TFT, the ESCC acknowledged that the government may accept the Commission's recommendation. The ESCC stated that in this instance it would broadly support the recommendations of the Commission in regard to various safeguards for financially vulnerable consumers. The submission stated that it was particularly concerned to ensure that, from 1 July 2007:

- the ACT Government retains the power to re-regulate retail electricity prices if there is an abuse of market power or failure of market competition;
- there are robust "deemed customer contract" arrangements in place which provide an adequate safety net for customers who do not enter contestable contracts; and
- the commitments regarding default customer pricing and a price vetting role for the ICRC after 1 July 2007, made by ActewAGL in its submissions and accepted by the ICRC in its Draft Report, are publicly confirmed by ActewAGL to the ACT Government before the Government acts upon the ICRC's Final Report.¹⁰²

The submission noted the changing national regulatory environment and stated that there will be a need to address the industry funding of the ESCC once the national arrangements are implemented.¹⁰³

¹⁰⁰ ESCC submission, p. 2.

¹⁰¹ ESCC submission, p. 2.

¹⁰² ESCC submission, p. 1.

¹⁰³ ESCC submission, p. 2.

The submission concluded by providing a series of recommendations. These were:

1. TFT arrangements should be continued until 30 June 2009, with a further review of competition in the ACT electricity market to be undertaken late in 2008.
2. The ICRC should set prices for the TFT in 2006–09 on the basis set out in sections 4.6 and 4.7 of its Draft Decision.

If the ACT Government accepts the ICRC's Recommendation to cease the TFT on 30 June 2007, the ESCC makes the following Recommendations.

3. The ACT Government must retain the power to re-regulate retail electricity prices in the ACT if there is an abuse of market power or failure of market competition.
4. From 1 July 2007, there should be robust "deemed customer contract" arrangements in place which provide an adequate safety net for customers who do not enter contestable contracts.
5. Prices for the deemed customer contracts should be set in accordance with the process outlined in sections 4.6 and 4.7 of the ICRC's Draft Decision.
6. The commitments regarding default customer pricing and a price vetting role for the ICRC after 1 July 2007, made by ActewAGL in its submissions and accepted by the ICRC in its Draft Report, should be publicly confirmed by ActewAGL to the ACT Government before the Government acts upon the ICRC's Final Report.

In addition, the ESCC makes a further recommendation which aligns with comments made by the ICRC in its Draft Decision.

7. The ACT Government should give attention to how the ESCC is to be funded by industry when the new national regulatory arrangements take effect.¹⁰⁴

EnergyAustralia

EnergyAustralia supported the Commission's recommendation in regard to the:

- extension of the transitional franchise tariff (TFT) for electricity for a further 12 months from 30 June 2006 until 30 June 2007; and
- discontinuance of the TFT, effective from 1 July 2007.¹⁰⁵

TRUenergy

TRUenergy supported the recommendation in the draft decision that the TFT be discontinued. In addition, the submission stated that TRUenergy was encouraged by approaches to price monitoring that revert to regulation only if evidence suggests that competition is not sufficiently functioning in a market or that there is misuse of market power.¹⁰⁶

The submission from TRUenergy expressed support for the view that the TFT does not form part of any safety net for vulnerable customers and argued that, based on economic theory and universal experience, competition is the best way to ensure prices are set at efficient levels in a market.

¹⁰⁴ ESCC submission, p. 4.

¹⁰⁵ EnergyAustralia submission.

¹⁰⁶ TRUenergy submission, p. 1.

TRUenergy stated that:

The question as to whether energy could be any lower in price (i.e. is the market effectively competitive) is therefore very different to the question as to the capacity of all members of the community to pay for it, and as the Commission notes this was never the function of the TFT in any case.

Neither of these questions can be resolved by simply regulating the price. Appropriate access to and the development of targeted assistance to those in the community experiencing payment difficulties will provide the safety net to vulnerable customers. Retailers can often assist with payment arrangements where this hardship is temporary, but where hardship is permanent or chronic in nature the continuation of and preservation of support programs and mechanisms' currently operating in the ACT will be essential.¹⁰⁷

¹⁰⁷ TRUenergy submission, p. 1.

Appendix 3 Standard customer contract issues

Implications of discontinuing the price direction for the standard customer contract

ActewAGL has submitted that it ‘will continue to offer a standard customer contract, available to all customers, with no fixed term and the ability to opt in or out of the contract at any time. This will provide a safety net for customers who are unable or unwilling to take up negotiated contracts with ActewAGL or competing retailers.’¹⁰⁸

Under the *Utilities Act 2000* (Utilities Act), a utility may provide a utility service to a person under either a negotiated customer contract or a standard customer contract.¹⁰⁹ The standard customer contract essentially is legislated to act as a ‘default contract’ where a customer applies to a utility for an electricity supply but does not choose to enter into a negotiated customer contract or where a utility provides a service to a person who has not applied for that service. In addition, the obligation to supply electricity to a customer is only relevant when that customer is on a standard customer contract.¹¹⁰

A customer contract is a standard customer contract for the purposes of the Utilities Act only if the Commission approves the terms of that contract.¹¹¹ The Commission can approve the terms of a standard customer contract only if it is satisfied the terms are consistent with specified criteria when the standard customer contract is in force.¹¹² These criteria include that charges payable under the contract would be consistent with the relevant price direction made by the Commission.¹¹³ The Commission also must be satisfied these criteria are met in approving any variation of the terms of a standard customer contract.¹¹⁴

Thus, a decision not to issue a new transitional franchise tariff (TFT) price direction from 1 July 2006 would have the unintended consequence of invalidating the status of the standard customer contract. This is because the Commission could no longer be satisfied that the terms of the contract were consistent with a key criterion: namely, that charges payable under the contract would be consistent with the relevant price direction made by the Commission.

In terms of the current situation, the Commission has already approved ActewAGL’s standard customer contract, and did so when a relevant price direction was put into place. This applied from 1 July 2003. However, if a price direction were no longer in place, ActewAGL would be free to set its own prices. To do so means varying the standard customer contract. With no price direction operating, the Commission has no power to approve or refuse to approve any proposed variation to the standard customer contract.

The Utilities Act is silent on the status of a standard customer contract approved under a price direction once a price direction ceases to apply, whether that occurs on 1 July 2006 or any date

¹⁰⁸ ActewAGL submission, p. 6.

¹⁰⁹ Utilities Act, s. 92. For the limited exceptions to this requirement see s. 96 of the Utilities Act.

¹¹⁰ Utilities Act, s. 80. The obligation to supply does not apply to a customer on a negotiated customer contract.

¹¹¹ Utilities Act, s. 87.

¹¹² Utilities Act, s. 89.

¹¹³ Utilities Act, s. 89(2)(b).

¹¹⁴ Utilities Act, s. 93.

thereafter. However, in the absence of a price direction there is doubt that the standard customer contract remains a standard customer contract for the purposes of the Utilities Act, particularly once ActewAGL varies that contract.¹¹⁵

Under the Utilities Act if a contract is not a standard customer contract it can only be a negotiated customer contract. There is no other alternative. Accordingly, it is arguable that, in the event the Commission does not issue a price direction, thus effectively removing retail price regulation, every standard customer contract agreed between ActewAGL and a customer pursuant to the Utilities Act will become a negotiated customer contract as soon as ActewAGL varies any part of the standard customer contract after 1 July 2006.

Effect on customers

If the Commission does not issue a new TFT price direction, from 1 July 2006 or, more likely, the date on which ActewAGL varies the standard customer contract—whichever is the later—the standard customer contract that ActewAGL currently has in place with most ACT electricity customers will cease to exist. Instead, every agreement between ActewAGL and a customer will be categorised as a negotiated customer contract.

This categorisation would apply to any ‘standard customer contract’ that ActewAGL maintained in the absence of a price direction. In effect, such contracts could only be ‘standard’ negotiated customer contracts. For the purposes of the Utilities Act as currently drafted, ActewAGL’s offer to retain a standard tariff contract, and to allow customers to opt in and out of that contract, is a voluntary offer that has no regulatory enforcement.

Any negotiated customer contract (including ActewAGL’s proposed ‘standard’ negotiated customer contract) must meet all relevant requirements of the Consumer Protection Code (the Code) and other consumer protection legislation. This means it must contain provisions that allow for a cooling-off period of ten business days and allow for the contract to be rescinded within six months of the date of commencement.¹¹⁶ An electricity retailer supplying electricity to a customer under a negotiated customer contract must also give at least four weeks notice of when the contract period is due to expire, and meet obligations relevant to the disconnection of supply, the repayment of any security deposits and the making available of such a contract to the customer.¹¹⁷

In most cases customers can easily transfer to and maintain supply under negotiated customer contracts. However, in the absence of a statutorily endorsed standard customer contract, there is no alternative under which a customer can be supplied electricity. Further, there is no obligation to supply. Thus, to ensure customers continue to be provided with the current protections requires that the Utilities Act be amended to legislate for a ‘deemed contract’.

¹¹⁵ See also Utilities Act, s. 92(3)(c), which provides that the standard customer contract is unenforceable by the relevant utility to the extent to which it does not comply with the requirements set out in s. 89(2)(a) and s. 89(2)(b).

¹¹⁶ Consumer Protection Code, clauses 24 and 25.

¹¹⁷ Consumer Protection Code, clauses 26, 23, 27 and 28.

Effect on ActewAGL

In the absence of other regulatory changes, if the Commission decided not to issue a new TFT price direction, ActewAGL would be required (before 30 June 2006) to contact all the customers with whom it currently has standard customer contracts and ask them to agree to negotiated customer contracts (the proposed ‘standard’ negotiated customer contracts or others) that meet the requirements of the Code. While this would be a costly and time-consuming exercise for ActewAGL to undertake, the Commission notes that the exercise also could stimulate competition. This is because the exercise is likely to encourage consumers to consider the range of options and deals offered by all electricity retailers operating in the ACT, including ActewAGL, before entering into a negotiated customer contract.

It is arguable there is insufficient time in which to achieve the objective of transferring all customers onto negotiated customer contracts that meet the requirements of the Code. This could be addressed by amending the Code to allow a few months grace before the requirements of the Code apply to those contracts remaining to be transferred.

A problem that would remain, however, is that ActewAGL would likely encounter some customers who would refuse to sign a negotiated customer contract. In the absence of any alternative, given the requirements of the Code, ActewAGL would in effect be supplying electricity to those customers under a contract that was in breach of the Code.

Solutions

In the absence of a new price direction, to ensure that ActewAGL is not compelled to supply electricity in breach of the Code requires that the Utilities Act be amended to legislate for a ‘deemed contract’ to apply in certain circumstances. The Commission recommends this course of action.

However, it is arguable that there is insufficient time to make the necessary legislative amendments before the current price direction expires. Therefore, the Commission proposes to make an interim direction to maintain the status of the standard customer contract until the necessary amendments are completed. Should the government reject the approach of amending the Utilities Act, the Commission would continue to regularly issue price directions in accordance with the methodology outlined in Chapter 5 in order to maintain the standard customer contract.

Amendments to the Utilities Act

The Commission recommends that the Utilities Act be amended to create a ‘deemed contract’.

For example, Division 6.2 of the Utilities Act, which currently sets out the requirements for standard customer contracts, could be amended by:

- replacing references to ‘standard customer contracts’ with ‘deemed contracts’
- deleting the requirement that any charges payable under the contract would be consistent with the relevant price direction (s. 89(2)(b))

- amending s. 92(1)(b) to ensure the deemed contract applies only in very specific circumstances, such as applying only to those customers
 - who have not agreed to a negotiated customer contract prior to the date from which a price direction ceases to apply
 - whose existing negotiated customer contract has expired without them agreeing to a new one
 - who have moved into a premises and commenced consuming electricity without first agreeing to a negotiated customer contract with the retailer
 - or
 - who have otherwise been disconnected from supply.

References to ‘standard customer contract’ elsewhere in the Utilities Act, such as in s. 80, the obligation to supply provision, also would need to be replaced with ‘deemed customer contract’.

If the Utilities Act were amended as suggested, all those customers who had not agreed a negotiated customer contract would thereafter default to the deemed contract. This would remove any need to amend the Code.

Interim price direction

The Commission is aware of the difficulties that may arise in any attempt to amend legislation within a tight timeframe. It is also aware that the government will have to amend the Utilities Act during the course of 2006 in preparation for the transfer of responsibility for electricity distribution and retail regulation (except retail pricing) to the Australian Energy Regulator, due to occur by 1 January 2007.

The Commission proposes to issue an interim price direction to apply from 1 July 2006 to 30 June 2007, as outlined in Chapter 5 of this final decision, to allow sufficient time to amend the Utilities Act. However, the Commission reserves the right to initiate a reference for an investigation into a variation of this price direction if, by 31 January 2007, the Commission is of the view that the appropriate amendments to the Utilities Act are unlikely to be in place by 30 June 2007 (thus constituting a ‘price variation trigger’ for the purposes of s. 20A(3)(c) of the ICRC Act).

Appendix 4 ICRC Act considerations

When making any direction about prices in a regulated industry, the Commission is required to take into account a number of issues identified in s. 20 of the *Independent Competition and Regulatory Commission Act 1997* (ICRC Act). The Commission’s conclusions on each of those matters, considered in regard to its final recommendations on the transitional franchise tariff (TFT) for electricity, are summarised in the following table.

ICRC Act s. 20 issues	Commission conclusions
The protection of consumers from abuses of monopoly power in terms of prices, pricing policies (including policies relating to the level or structure of prices for services) and standard of regulated services	The Commission considers that competition, both current and imminent from existing and new entrants, will ensure appropriate efficient pricing of electricity and the provision of service options that will best meet the needs of consumers.
Standards of quality, reliability and safety of the regulated services	Competitive market conditions will ensure service standards are met. The existing technical regulations relating to safety and quality of electricity provided will remain unchanged.
The need for greater efficiency in the provision of regulated services to reduce costs to consumers and taxpayers	Competition is acknowledged as the optimal method for ensuring efficient provision of services, and the Commission has concluded that existing and potential imminent competition will ensure the efficiency of the provision of electricity services to small consumers.
An appropriate rate of return on any investment in the regulated industry	The Commission’s analysis of the retail margins currently included in the TFT applying in the ACT confirm that they are consistent with the margins included in regulated and contestable retail price offerings in other states.
The cost of providing the regulated services	The margin analysis undertaken by the Commission in the draft decision incorporates the full flow-on of network and generation costs. The margin analysis also demonstrates that retailers are able to recover their retailing costs in the current TFT tariffs, and decisions by retailers to discount below the TFT price indicate a further margin within which retailers are able to compete and remain viable in this market. Withdrawal of the TFT in a competitive market will still allow retailers to recover their costs.
The principles of ecologically sustainable development mentioned in s. 20(5) of the Act	Pricing of electricity to reflect its actual cost, including charges such as greenhouse gas emission costs, provides a clear signal to consumers of environmental and ecological sustainability issues and encourages best use of energy resources. The recommendation will not alter the pass through of these costs as is at present included in electricity prices.
The social impacts of the decision	The Commission has examined the social implications of the recommendation, and has highlighted the continuing need for funding of targeted assistance (including for the operation of the Essential Services Consumer Council) for vulnerable households.
Considerations of demand management and least cost planning	Greater opportunities for competition in the ACT market are expected to bring new service offers, including time-of-use tariffs, which will have a positive impact on better demand management.
The borrowing, capital and cash flow requirements of persons providing regulated services and the need to renew or increase relevant assets in the regulated industry	The Commission’s margin analysis, as contained in the draft decision, has confirmed that the margins allowed in the TFT are adequate to meet the financing needs of the electricity retailers, and the margins applying on discounted electricity offerings are consistent with margins offered by competitive retailers in other jurisdictions.
The effect on general price inflation over the medium term	There is not expected to be any significant impact on price inflation from this decision as retailers compete to maintain or expand their customer bases.
Any arrangements that a person providing regulated services has entered into for the exercise of its functions by some other person	Not applicable.

Glossary and abbreviations

ACT	Australian Capital Territory
ACTCOSS	ACT Council of Social Service
ActewAGL	ActewAGL Retail
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
Care ACT	Care Financial Counselling Service
COAG	Council of Australian Governments
Code, the	Consumer Protection Code
Commission, the	Independent Competition and Regulatory Commission
CPI	consumer price index
CSO	community service obligation
ESC	Essential Services Commission of Victoria
ESCC	Essential Services Consumer Council
FRC	full retail contestability
ICRC	Independent Competition and Regulatory Commission
ICRC Act	<i>Independent Competition and Regulatory Commission Act 1997 (ACT)</i>
MCE	Ministerial Council on Energy
MRET	Mandatory Renewable Energy Target
MWh/yr	megawatt hours per year
NEM	national electricity market
NEMMCO	National Electricity Market Management Company
TFT	transitional franchise tariff
Utilities Act	<i>Utilities Act 2000 (ACT)</i>