2 May 2017

Mr Joe Dimasi
Senior Commissioner
Independent Competition and Regulatory Commission
PO Box 161
Civic Square ACT 2608

Email: icrc@act.gov.au

Dear Mr Dimasi

RETAIL PRICES FOR SMALL ELECTRICITY CUSTOMERS FROM 1 JULY 2017 – DRAFT REPORT

Origin appreciates the opportunity to respond to the Independent Competition and Regulatory Commission's (Commission) Draft Report on setting retail electricity prices in the Australia Capital Territory (ACT) from 1 July 2017.

Origin notes the Commission's proposal to alter the methodology for applying the retail margin as well as the decision not to grant a competition allowance. Origin has concerns that this pricing approach will significantly understate the cost to retailers of servicing customers in the ACT. The proposal to limit the growth in the retail margin to the change in CPI does not align with the risks faced by retailers operating in the market. Further, the exclusion of customer acquisition and retention costs (CARC) fails to recognise that these costs apply to all retailers, including incumbent retailers, in the ACT.

Origin agrees that it is important to manage retail price increases, however, we do not believe that this should deflect from the objective of establishing efficient and cost reflective retail prices in 2017-18. If it is found that there are customer segments that will see significant increases in their annual bill, Origin suggests that the Government may need to provide some sort of additional financial support (ie one off rebates) to these energy users to assist them. The need to manage the price increases should not be to the detriment of retailers recovering their true costs.

Origin strongly believes that regulated retail tariffs should reflect the costs of supplying electricity in the ACT. Cost reflective tariffs not only provide price signals to customers to manage consumption, but they encourage competition.

Further comments on the proposed regulated pricing framework for electricity customers are set out below.

Energy Purchase Costs

It is noted that the Commission's Draft Report only includes energy cost data relevant to the end of February 2017. As the Commission would be aware, extreme weather conditions over the 2016-17 summer lead to significant increases in demand and thus forced energy contract costs to record average levels. It is thus anticipated that energy costs will be higher in the Final Report once the wholesale contract prices are further updated.

Network Costs

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Origin notes that the network prices utilised in the Draft Report only includes a small network component increase. This is given the uncertainty surrounding the Federal Court's decision on the 2015 New South Wales Network Regulatory Pricing Determinations[1].

Origin supports the Final Report including the network prices approved by the Australian Energy Regulator in June 2017 to ensure they align with the prices retailers will billed by the networks in the next financial year.

Retail operating costs

Retail operating costs need to reflect the actual costs retailers incur in supplying customers in the ACT in order to encourage business efficiencies, innovation and thus competition in the ACT electricity market. Origin argues that CARC costs are actual costs incurred by a retailer and should be included to reflect the everyday costs incurred by a retailer in supplying electricity customers in the ACT.

As highlighted in our submission to the Issues Paper, the inclusion of CARC in retail operating costs has been accepted in all recent past and current regulated pricing determinations in other jurisdictions across Australia. Current determinations include the Queensland regional pricing determination whereby the Queensland Competition Authority has benchmarked retail operating costs which includes an allowance for CARC[2]. Further in Tasmania, where the market is the second smallest in the NEM, the Regulator has recognised that competition needs to be promoted and has allowed for the inclusion of CARC[3]. Origin thus cannot understand why, in this instance, the Commission has chosen a different theoretical approach to determining retail operating costs.

It should be noted that CARC is determined to not only allow for acquisition costs but also retention costs for a retailer defending its customer based in a competitive market. In all jurisdictions where Origin is an incumbent electricity retailer, it must use campaigns and discounts in order to win new customers and maintain an existing customer base. Origin anticipates that the same applies to ActewAGL in the ACT with these costs rising in recent years as competition is slowly increasing.

Origin thus believes the Commission's requirement to determine *"efficient costs incurred by a retailer in providing retail services to its customers"*[4] requires the Commission to include a competition allowance to recognise that these costs are incurred and to further encourage the development of competition in the ACT electricity market.

Competition and Retail Margin

A retail margin is intended to ensure that a retailer is compensated for efficient costs and that a retailer earns a normal commercial margin for providing a product or service. The proposal to exclude a competition allowance (ie CARC), a headroom allowance and then limit the retail margin change to CPI rather than actual increases in the cost base will not reflect a retailer's true cost of supply nor fulfil the objectives of providing a competitive retail market.

The benefits of retail competition in energy markets has been evident in recent years with retailers broadening their focus from offering the lowest prices to improving customer service and experience. Retailers not only offer competitive price discounts, but customers benefit from added

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[1] ICRC, Standing offer prices for the supply of electricity to small customers from 1 July 2017 – Issues Paper, October 2016, pxv.
[2] Queensland Competition Authority, Final Determination, Regulated retail electricity prices for 2016-17, p24.
[3] Office of the Tasmanian Economic Regulator, Standing Offer Pricing Investigation 2016 - Final Report, p58
[4] Ibid, p14.

services such as metering solutions, distributed generation options (ie solar, batteries) and product offerings to assist with bill management (eg Origin's Predictable Plan offer). Effective competitive markets have seen significant improvements in customer service with these benefits noted by the Australian Energy Market Commission (AEMC) in their review of competition.

The AEMC has recently found that competition in the ACT is not as effective as other jurisdictions and customers are not appropriately engaged in the energy market[5]. In our view, this is due to the risk that electricity tariffs will not reflect a retailer's actual cost of supply. If Retailers are confident that regulated retail prices will reflect a retailer cost to supply, retailers will enter the market and appropriately educate and engage customers on the best product option for them.

Origin does not support the proposed retail margin methodology changes as it will not adequately compensate a retailer for supplying small customer in the ACT. The actual movement in the regulated retailer's cost base is significantly greater than CPI. Origin believes the regulated retail margin needs to be reasonable and a cap on the increase will not incentivise retailers to provide products and services. This is to the detriment of consumers.

Cost Reflective Tariffs

The Draft Report notes that the amended approaches with regards to the application of retail margin and the decision to exclude a competition allowance *"will mitigate the prospective price increases to a small degree"*.[6]

Origin strongly believes that assistance to customers should not be on the retail cost element of tariffs. Retailers should be entitled to recover the full costs of supplying customers on standard tariffs and any assistance should be managed through Government policies. Government financial support could be in the form of rebates, one off payments or additional concession payments.

Closing

In summary, Origin is concerned that the Commissions' proposed pricing methodology does not take into account the long established direction of reform and the move to competitive energy market frameworks. Regulated retail tariffs should be set at a level that is sufficient to protect and promote competitive market offers. Customers not only see price benefits from competitive markets, but are offered additional product and service offerings as retailers enter the market. We urge the Commission to reconsider its pricing methodology to further allow competition to develop in the ACT and for customers to access additional price and service benefits.

Should you have any questions or wish to discuss this information further, please contact Caroline Brumby on (07) 3867 0863.

Yours sincerely

R.K.M Robt

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[5] AEMC, Retail Competition Review 2016 – Final Report, pii.
[6] ICRC, Standing offer prices for the supply of electricity to small customers from 1 July 2017 – Issues Paper, October 2016, pxv.