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13 December 2013

NERL Review - Issues Paper on Methodology for Review
Essential Services Commission of South Australia
GPO Box 2605
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By email: escosa@escosa.sa.gov.au

NERL Review: Methodology for Review

Thank you for the opportunity to respond to the Issues Paper (the Paper) for the Methodology of the Essential Services Commission of South Australia (ESCOSA) review of the introduction of the National Energy Retail Law (NERL).

We recognise that ESCOSA has been given a very challenging task and agree with ESCOSA that consulting on a methodology now is prudent.

However, Simply Energy does not believe that the methodology ESCOSA proposes to use is the correct approach or sufficiently developed to be able to derive any robust conclusions given the many factors that can influence a customers' relationship with the industry. The issues we have with the methodology are as follows:

- It presumes there is national consistency in retail regulation where no such national consistency exists.
- It ignores the derogations that South Australia made to the National Energy Customer Framework (NECF) which has forced us to maintain state-specific processes to manage those derogations.
- ESCOSA has not addressed how the methodology will distinguish the impact of NECF upon the outcomes ESCOSA observes, from changes deriving from other broader industry developments and economic trends.

Additionally, any operational benefit we may have received from South Australia adopting NECF will be lost if the extensive retailer annual reporting requirements envisaged are implemented.

In our view, the scope of the review ESCOSA plans to undertake appears to go beyond what is required to assess the benefits of the NECF. We also note that ESCOSA's review appears solely focussed upon the performance of the retail sector whereas large parts of the NECF apply to the distribution network sector, which is not included in the review. It is unclear to us why the network sector has not been included in this assessment.

We recognise that ESCOSA is under an obligation to perform this review, but we believe there are better approaches and we recommend that ESCOSA uses 2014 to consult more with us to change the methodology to one that will provide robust conclusions to the issues that ESCOSA must consider. There is time available for this consultation as the report is not scheduled for release until October 2015.

As a first step, we would welcome the opportunity to discuss the challenges posed by this review in a forum with other retailers.

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Please don’t hesitate to contact James Barton, Regulatory Policy Manager, if you wish to discuss this submission further.

Yours sincerely

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SUBMISSION TO THE NERL REVIEW: METHODOLOGY FOR REVIEW ISSUES PAPER

This submission sets out Simply Energy's response to the NERL Review Issues Paper: Methodology for Review.

Scope of the review

Simply Energy is concerned by the breadth of the analysis that the Essential Services Commission of South Australia (ESCOSA) is intending to undertake for this review. The scope of the analysis that ESCOSA intends appears to go beyond what is required to assess the benefits of the National Energy Consumer Framework (NECF) and creates the impression of an assessment of the benefits of a price deregulated, fully contestable retail sector. By way of example, an assessment of the extent to which retailers differentiate prices for new and existing customers appears to have little to do with assessing NECF and more to do with assessing price deregulation.

Coverage

The methodology proposed appears solely focussed on the performance of retailers under the NECF. However, about a third of the regulations specified under NECF impose obligations on distributors. Why is ESCOSA not assessing the performance of the distribution sector against the NECF?

ESCOSA's proposed methodology

ESCOSA has interpreted the terms of reference for the review as two high-level questions:

Question 1: Has NECF adversely affected customer protection in pursuit of national consistency?

ESCOSA intends to answer this question by examining the extent to which the NERL provisions reflect South Australia's pre-NECF energy framework to:

- Determine whether any adverse impacts identified are driven by the approach adopted by relevant parties (such as retailers and the Australian Energy Regulator (AER)) rather than legislative intent, and
- Assess the nature of the interaction between customers and retailers and, in turn, both parties with the AER. ESCOSA will identify any adverse outcomes from these interactions compared to how these parties deal with a local regulator.

ESCOSA proposes using a time series of metrics to discern broad trends in customer protection outcomes and examine trends in complaints to retailers and the ombudsman to make a qualitative assessment of the extent to which customers consider dealings with retailers have improved.

Our primary concern with ESCOSA's methodology is that ESCOSA has not addressed how it will distinguish the impact of NECF upon these metrics from changes deriving from other broader industry developments and economic trends. As ESCOSA acknowledges, the step change in customer protection obligations that resulted from the implementation of NECF was very small, and as a result any trend in these metrics will be more strongly influenced by other factors than changes arising from NECF.

By way of example, since April 2013 Simply Energy has observed an increase in the number of disconnections occurring in the South Australian market. Our disconnection procedures and hardship policy processes have remained largely unchanged with the implementation of NECF, and as a result the implementation of NECF cannot be identified as the cause of the increase in disconnections.

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The rising trend of disconnection is the result of more customers simply not being able to afford their energy bill due to the resulting increases in network prices. Rising indebtedness has resulted from large increases in network tariffs in January 2013 (approx. 20%) that started to flow through to customers' bills in March-April 2013. Slower economic growth and job losses across the South Australian economy will also be influencing this outcome.

As this example shows, consumer outcomes are more likely to be influenced by changes to other factors such as incomes or even weather driven consumption changes than the small differences between the old ESCOSA regulations and the NECF. ESCOSA's methodology should be amended to provide for this.

Additionally, we are not confident that relying on ombudsman complaint levels is going to provide ESCOSA with any clear insight on the success of NECF. For example, the Energy and Water Ombudsman for South Australia's (EWOSA) Annual Report 2012-13 shows an increase in complaints but a decline in the number of systemic issues. It is unclear to us what conclusions can be drawn from this in relation to NECF.

Complaints can be driven by a range of matters unrelated to the regulatory framework in place. The rise in network costs flowing through retailer bills is likely to have resulted in increased billing complaints to EWOSA. We often witness a rise in ombudsman complaints following attention given to the industry by certain media commentators in South Australia. There are many other factors that can affect how a consumer views retailers.

Again, the methodology does not currently specify how ESCOSA will determine whether a complaint has been driven by changes in the customer protection framework due to the implementation of NECF or whether it is the result of other factors that can influence consumer behaviour.

Question 2: Has NECF resulted in efficiencies?

ESCOSA is proposing to assess the technical, allocative and dynamic efficiencies arising from NECF and how those benefits have been distributed. In particular, ESCOSA comments that:

> Given that a key impetus for NECF was the achievement of economies in operation for retailers that operate across State and Territory borders, there should be some onus on retailers to be forthcoming in demonstrating efficiencies achieved.[1]

We query whether the achievement of operational efficiencies was a key impetus for the creation of NECF. In our view, if the achievement of operational efficiencies had been such a strong motivator then jurisdictions would have been keen to avoid derogations from the framework. The opposite has been the case.

The website of the Standing Committee of Energy and Resources (SCER) notes that:

> The NECF is expected to facilitate an increase in retail competition by reducing regulatory complexity and lowering barriers for energy retailers to enter into the market across participating states and territories.

The SCER does not reference operational efficiencies as a benefit arising from the NECF.

That said, we recognise that ESCOSA is tasked with assessing efficiencies that have derived from NECF.

[1] ESCOSA 2013 NERL Review: Issues paper p. 8

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Given the task, we have a number of concerns with the approach that ESCOSA is proposing to use for this assessment:

1. There is an unstated assumption in the methodology that national consistency in retail regulation has been achieved and thus retailers must now be benefiting from demonstrable efficiency gains. Simply Energy does not experience national consistency in retail regulation as only a minority of our customer base is subject to NECF. The methodology does not recognise that national consistency in retail regulation does not currently exist.

2. Even where markets we operate in have moved to NECF, there are significant derogations that require us to retain state-specific processes and procedures that add to our costs. The methodology does not take account of these inconsistencies. For example, ESCOSA does not highlight the effect that retaining the customer threshold for application of NECF at 160MWh/yr will have had on our costs as it requires us to maintain unique processes for the South Australia market.

3. The methodology overlooks other regulatory and industry changes and their impact upon the efficiency of our operations. For example, inefficiencies are created from managing the various feed-in tariff schemes that South Australia now has in place, in administrating a state-specific concessions framework and managing the increasingly complex, resource-intensive and inefficient Residential Energy Efficiency Scheme (REES). The methodology does not address how ESCOSA is proposing to isolate any efficiency derived from the NECF from other cost impacts driven by other changes.

4. It is very unclear to us what an analysis of retail margins will tell ESCOSA about the success or failure of the NECF. Besides the difficulties of establishing a meaningful estimate of retail margins, whether margins have increased, decreased or stayed the same since February 2013 will be influenced by such a broad sweep of factors outside of NECF that it will be impossible for ESCOSA to make any substantive conclusions. Price and costs fluctuate continually as industry factors and competitive dynamics change and retail margins constantly change in response to these dynamics.

5. Reinstating the extensive jurisdictional annual reporting obligations that have only this year been removed will eliminate the one operational efficiency gain to which we could point.

In summary, the decision by some jurisdictions not to adopt NECF, the derogations that were made where NECF was adopted, and the continuing variations between the jurisdictions in other non-NECF regulatory requirements means that we do not have national consistency in retail regulation, the assumption behind the expectation that we have achieved demonstrable efficiencies.

Review of pricing outcomes

The Paper proposes that ESCOSA will review retail prices as part of the review and will require retailers to provide pricing information to support the review.

We are concerned that the Paper's proposal in relation to the review of pricing outcomes, if adopted, will move the review away from assessing the impact of the introduction of NECF and towards a review of retail pricing in South Australia.

The Paper proposes a review of prices that attempts to distinguish between the prices paid by customers on market contracts that are not open to new customers, and those paid by customers on contracts that are open to new customers.

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We do not understand what this has to do with the implementation of NECF, especially as the Paper states that ESCOSA's interest in reviewing prices in this way comes from historical data that it collected from retailers to support its price regulation process, which predates NECF.

The Australian Energy Market Commission (AEMC) has been conducting a review of retail price trends, and we suggest that any concerns about price trends in South Australia are addressed using the data developed by that review.

Additionally, we are concerned that ESCOSA's justification for this review is based on information provided by retailers for a quite different purpose – being the setting of regulated prices. Consequently, we are worried that detailed information provided to the NERL review may be used to justify further reviews which have nothing to do with the reasons given for the collection of the information.

Pricing reporting requirements

ESCOSA puts forward two options for retailers to report to them on prices. ESCOSA's preference is for option one, a detailed reporting framework based on the relative price movement (RPM) model that was in use before price deregulation. The Paper states that this will allow for a robust quantification of the pricing information, and that retailers have existing systems to report this data.

Although this is presented as a temporary measure, this is an example of a reimposition of jurisdictional reporting regulations that were expected to cease with the transition to NECF. Option one will be a significant additional compliance burden.

Option two is a less detailed framework, requiring retailers to provide average data. While this is less onerous than option one, it still represents a reimposition of jurisdictional reporting.

Instead of these options, we recommend that the review uses public data only, as proposed for a similar review in Queensland.