



**The Office of the SOUTH AUSTRALIAN
INDEPENDENT INDUSTRY REGULATOR**

Security Deposits & Interest on Late Payments and Security Deposits

Public Discussion Paper

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1. PREFACE

1.1 *Retail Code requirements of Industry Regulator*

The Retail Code under the Independent Industry Regulator Act (IIR Act) requires the Industry Regulator to make certain determinations. In particular, the Retail Code provides that the Industry Regulator must approve:

- **Interest on late payments (Clause 6.3.3)**
The amount of interest which may be charged on late payments;
- **Level of Security Deposits (Clause 8.1)**
The amount of a security deposit;
The average quarterly and monthly bills for each category of customer (this determines the maximum security deposit allowable);
- **Interest on Security Deposits (Clause 8.4)**
The interest rate and terms and conditions on which interest is payed, on security deposits held by the retailer.

This Paper discusses the issues associated with these three areas.

1.2 *Key Dates*

Following an assessment of the submissions received on this discussion paper, the preliminary conclusions of the Industry Regulator will be reported in a Draft Report to be released by 1 October 2000. A short period for further submissions will then be allowed and the Industry Regulator will issue a final report and make determinations as to the levels of security deposits, and the interest payable on late payments and security deposits, by 1 November 2000. Determinations by the Industry Regulator will apply from 1 January 2001.

1.3 *Submissions*

The Industry Regulator invites submissions from interested parties, focussing on the issues raised in this discussion paper, and other relevant issues that the Industry Regulator should take into account. Where possible factual data and/or analysis should be included with submissions.

Submissions addressing some or all of the issues raised should be addressed to

Security Deposit Submissions
SA Independent Industry Regulator
GPO Box 2605
ADELAIDE SA 5001

Facsimile: (08) 8463 4326

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Submissions should reach the Office of the SA Independent Industry Regulator on or before **1 September 2000**.

1.4 Confidentiality

It is the view of the Industry Regulator that the issues raised in this discussion paper are important issues for community debate and that submissions received will be similarly important.

Accordingly, all submissions received will be available for public inspection at the SAIRR office and may be made available on the SAIRR web-site or in hard copy from the SAIRR office. In addition, submissions may be referred to in draft or final versions of the report on these issues.

2. INTRODUCTION

2.1 Retail Code

The Retail Code under the Independent Industry Regulator Act came into operation on 11 October 1999 (and was varied on 23 December 1999) and regulates the terms on which a retailer can sell electricity to customers, except for contestable customers (ie customers who use more than 160 MWh per annum) who have negotiated their own customer sale contract.

From 1 January 2003, the Retail Code will apply to all customers who consume less than 30MWh per annum.

Currently there is only one licensee who holds a retail licence to which the Retail Code applies. That licensee is AGL South Australia (AGL).

2.2 Purpose of this paper

The Industry Regulator is required to make determinations under the Retail Code relating to the level of security deposits, and interest rates for late payments and on security deposits.

To assist in clarifying and developing the issues which form the basis for this paper, preliminary discussions were held with AGL, the only retailer in South Australia to which the Retail Code presently applies.

In putting forward this discussion paper for public debate and comment, the Industry Regulator is endeavouring to obtain wide community input to assist in the determination of these matters.

Any proposals and suggestions in this paper are for discussion purposes only. The Industry Regulator has not formed a view on any of the issues raised.

Submissions received in response to this discussion paper will assist the Industry Regulator to assess the potential impacts of determinations made under the Retail Code.

2.3 The Retail Code and other information

Background information about the role and functions of the SAIIR and a copy of the Retail Code is available from the SAIIR web-site, www.saiir.sa.gov.au, in the Electricity Industry/Regulatory Framework section.

3. SECURITY DEPOSITS

3.1 Retail Code Provisions

The Retail Code makes the following provision:

8. SECURITY DEPOSITS AND ALTERNATIVES

8.1 Security Deposits

8.1.1 The Retailer may require a retail code customer to provide a security deposit at the time the retail code customer makes an application for [connection] or an application for reconnection after being disconnected..., or before selling electricity to the retail code customer.

Subject to approval and annual review by the Industry Regulator and Clause 8.3.3 (which deals with increases in security deposits):

- (a) the amount of a security deposit for a retail code customer who is on a quarterly billing cycle must not be greater than 1.5 times the average quarterly bill; and*
- (b) the amount of a security deposit for a retail code customer who is on a monthly billing cycle must not be greater than 2.5 times the average monthly bill*

The average quarterly and monthly bill for each category of customer will be as determined by the Industry Regulator from time to time.

3.2 Present level of security deposits

At present security deposits of \$100 are payable to AGL by both residential and business customers.

This level of security deposit was initially approved by State Cabinet in July 1999, and confirmed by the Industry Regulator on 22 March 2000, pending the completion of this review of security deposits and associated issues by the Industry Regulator.

3.3 Average Quarterly and Monthly Bills

The Retail Code sets out a cap on security deposits, such that the security deposit for a customer on a quarterly billing cycle cannot be more than 1.5 times the average quarterly bill and for a customer on a monthly billing cycle the security deposit cannot be more than 2.5 times the average monthly bill.

The present level of security deposits is not set by reference to the average quarterly and monthly bills – it is an amount, which is less than the cap provided in the Retail Code.

In general, AGL advises that residential customers are billed quarterly, whereas non-residential customers are billed quarterly or monthly depending on their level of consumption.

In order to make an assessment of the cap on security deposits (that is the maximum level at which security deposits could be set), the Industry Regulator requested AGL to undertake an analysis of its billing data, using billing data for the period March 1999 to February 2000.

This analysis took into account the level of bills for all quarterly billed customers (approximately 722,000). AGL advise that the average quarterly bill for residential customers in the one year period analysed was \$202. This equates to a maximum security deposit of up to \$300 for quarterly billed customers.

For business customers it is difficult to identify a meaningful single average bill given the very large variation in business usage. For this analysis, AGL took into account all monthly-billed customers using less than 160MWh per annum (approximately 10,000). AGL advise that the average monthly bill for customers using less than 160MWh per annum, in the one-year period analysed was \$615. This equates to a maximum security deposit of up to \$1,500 for monthly billed customers.

3.4 When can a security deposit be required?

The Retail Code provides:

8.2 Residential Customers

A retailer must not require a residential customer to provide a security deposit unless:

- (a) the residential customer has left a previous supply address without settling an outstanding electricity debt, the debt remains outstanding, and the residential customer refuses to make arrangements (acceptable to both parties) to pay the debt; or*
- (b) the residential customer has within the previous two years been responsible for the use of electricity contrary to clause 5 [illegal use of electricity]*
- (c) the residential customer is a new customer and has refused or failed to produce acceptable identification and credit history information; or*
- (d) the retailer has, offered the residential customer an instalment plan or other payment option and the residential customer has refused, or failed to agree, to the offer.*

8.3 Business Customers

8.3.1 *A retailer must not require a business customer to provide a security deposit unless:*

- (a) the business customer does not have a satisfactory credit rating; or*
- (b) the business customer does not have a satisfactory electricity account payment history.*

8.3.2 *A retailer must accept from a business customer a bank guarantee as an alternative to a cash security deposit*

8.3.3 *...A retailer may increase a business customer's existing security deposit where that security deposit is insufficient to secure the business customer's current electricity usage taking into account the limits on security deposits ... using the average of the customer's last three bills.*

It is clear that the Retail Code does not envisage that all customers will pay a security deposit.

The Retail Code only permits a retailer to require a security deposit from a residential customer when the customer has previous unpaid bills, has misused electricity, has not produced acceptable identification and credit history, or when the customer has refused an offer of an instalment Plan.

For business customers a security deposit can only be required where the business customer has an unsatisfactory credit history or account payment history.

AGL advise that as at May 2000, it held security deposits from 24,885 residential customers, which is approximately 4% of residential customers.

In relation to business customers, as at May 2000, security deposits were held from 1,390 business customers, which is approximately 1.5% of business customers.

3.5 When must a security deposit be repaid to the customer

When a retailer holds a security deposit from a customer the Retail Code makes specific provision for the return of the deposit:

8.5 Return of security deposit

8.5.1 *(a) Where a retail code customer has been required by a retailer to pay a security deposit and:*

(I) the retail code customer completes 12 months (or such lesser time agreed with the retail code customer) of paying its bills by the pay by dates for those bills; or

(II) the retail code customer ceases to purchase electricity from the retailer at the supply address...

the retailer must return the security deposit and any interest

(b) if the amount of the security deposit is \$100 or less the retailer may pay the security deposit to the credit of the retail code customer's next bill

(c) subject to clause 8.7 if the amount of the security deposit is more than \$100, the retailer must.... pay the amount in accordance with the retail code customer's instructions...

8.5.2 *[if no customer instructions, security deposit must be credited to next bill]*

8.5.3 *[bank guarantee to be returned within 10 business days]*

Therefore, the security deposit should be returned to the customer on the fulfilment of certain conditions. It may be used to offset any amount owed by the retail code customer to the retailer or the distributor.

These provisions ensure that the retailer will not keep any security deposit in the long term, provided the customer fulfils certain conditions.

3.6 Level of security deposits – Annual review by the Industry Regulator

The amount of security deposit which a retailer may require a customer to provide is subject to approval and annual review by the Industry Regulator (see Retail Code: Clause 8.1.1.).

The amount of security deposit for both quarterly and monthly billed customers is currently \$100, which is well below the capped maximum.

AGL has advised the Industry Regulator that it considers the level of security deposits for residential customers is currently appropriate, but that for business customers the current level of security deposit is inadequate. A security deposit of \$100 is insufficient security against the typical outstanding debt left by a business customer who is unable to pay electricity bills.

While Clause 8.3.3 of the Retail Code does provide a mechanism for increasing the level of a security deposit where a security deposit is insufficient to secure a business customer's current electricity usage, this mechanism may be of little use if, by the time an assessment is made, the customer is not in a position to pay an increased security deposit. Accordingly, AGL's preferred position is that the level of up front security deposits for business customers are increased.

If the Industry Regulator were to determine the amount of security deposit at the maximum cap for business customers, it would remain open for a retailer to require a lesser amount of security deposit for a particular customer or category of business customers.

In preliminary discussions with AGL, the following proposal for the level of security deposits has been put forward for consideration:

- Security Deposit - quarterly billed customer – residential - to remain at \$100.
- Security Deposit – quarterly billed customer – business – up to \$300: depending on customer usage level.
- Security Deposit – monthly billed customer – business - up to \$1,500: depending on customer usage level.

The Industry Regulator invites submissions on the required level of security deposits for Retail Code customers, particularly focussing on, but not limited to the following issues:

- What are the cost impacts on electricity retailers from security deposits being set at their present levels?
- How would these cost impacts be affected by the level of security deposits being increased?
- If electricity retailers make cost savings as a result of being permitted to charge a higher level of security deposit, how can those savings be shared among retail customers?
- Should the amount of security deposit be set at the maximum level permitted by the Retail Code ie. 1.5x the average quarterly bill and 2.5x the average monthly bill (leaving the retailer free to charge any amount of security deposit up to that amount)?
- Should the amount of security deposit for residential customers remain at \$100? Why? If not, should it be increased according to the maximum cap formula or to some other figure?
- Should the amount of security deposit for business customers remain at \$100? Why? If not, should it be increased according to the maximum cap formula or to some other figure?
- Any other comments on the factors which should be taken into account in setting the level of security deposits.
- Views on the proposal that:
 - Security deposit for residential customers remain at \$100.
 - Security deposits for quarterly billed business (non-residential customers) increase from \$100 to a maximum of \$300.
 - Security deposits for monthly-billed business (non-residential customers) increase from \$100 to a maximum of \$1,500.

3.7 Licences issued prior to 11 October 1999

While AGL holds a licence issued by the Industry Regulator, to which the Retail Code applies, there are a number of other retail electricity licences that were issued by the Technical Regulator prior to the Electricity Act being significantly amended on 11 October 1999. These other retail licences remain valid and are currently being administered by the Industry Regulator. These licences contain a condition that the licensees comply with a Retail Code issued by the Technical Regulator at the time of granting the licence. These licences relate primarily to remote or off-grid areas of the State.

The applicable Code has slightly different provisions with regards to the amount of and the circumstances in which a security deposit can be required.

Clause 9 of the applicable Code provides:

9. Refundable Advances and Alternatives

Refundable Advances

- 9.1 *Subject to clause 9.3 the Licensee may require a customer to provide a refundable advance before the commencement of supply.*
- 9.2 *Subject to approval and annual review by the Technical Regulator the amount of refundable advance must be not more than 1.5 times the average quarterly bill*
- 9.3 *The Licensee must not require a customer to provide a refundable advance before the commencement of supply unless:*
 - 9.3.1 *the customer has left a previous supply address without settling an outstanding electricity usage debt, the debt remains outstanding and the customer refuses to make an arrangement to repay it; or*
 - 9.3.2 *the customer has within the previous 2 years been responsible for the illegal use of electricity; or*
 - 9.3.3 *the customer is a new customer and has refused to supply acceptable identification*
 - 9.3.4 *the Licensee has, in accordance with clause 8 offered the customer an instalment plan or other payment option and the customer has refused or failed to agree to the offer.*

The applicable Code is clear in its requirements. A retailer is not able to claim a security deposit from every customer, and there is to be an approval and annual review of the amount of the refundable advance.

The Industry Regulator is aware of instances where the pre October 11 Retail Code has been breached by those retailers to which it continues to apply. The main example of such a breach is in the demands by some of those retailers that all new and transferring customers lodge a security deposit.

Two specific concerns with the Retail Code applying to holders of pre October 11 retail licences have been raised with the Industry Regulator:

First, there are some retailers to which the Code applies, particularly remote area municipal councils, which have policies requiring all new and transferring customers to pay a security deposit, regardless of payment history, credit rating or provision of suitable identification documents. These retailers assert that because they supply itinerant populations which leave large amounts of unpaid electricity bills, they have had to adopt such policies. It would appear that the actions of these retailers are in breach of the provisions of the applicable code, even if the justification for their actions is understandable.

Second, there are concerns of consumers that they are disadvantaged if blanket policies (for example, requiring the payment of a security deposit when transferring premises within the same town even if the customer has an acceptable payment history), which are not sanctioned by the applicable retail code, are permitted.

The issues surrounding these licences and the applicable Code provisions are canvassed in more detail in a Discussion Paper: **Review of Licences and Exemptions Issued prior to October 11 pursuant to the Electricity Act**, issued by the Industry Regulator in June 2000 (copy available from www.sairr.sa.gov.au or from the SAIRR Office).

However, it is appropriate that this Paper seek submissions on the provisions of the pre-October 11 Retail Code.

The Industry Regulator invites submission on:

- Should the security deposit rules be different for remote and rural electricity retailers and consumers? If so, what should the rules be?
- What are the special or unusual factors that apply to the retailing of electricity in remote and rural areas that impact upon the level and role of security deposits relative to metropolitan/on-grid situations?

3.8 Other Matters

The Retail Code provides that the level of security deposit is subject to approval and annual review by the Industry Regulator.

The Industry Regulator invites comment on:

Processes and procedures which should be adopted for future annual review of security deposits.

4. INTEREST PAID ON SECURITY DEPOSITS

4.1 Retail Code Provisions

The Retail Code makes the following provision:

8.4 Interest on Security Deposits

Where a retailer has received a security deposit from a retail code customer, the retailer must pay to the retail code customer interest, if any, on the deposit at a rate and on terms and conditions as approved by the Industry Regulator

4.2 Current position

Since October 11 1999, AGL has been paying interest on security deposits at the rate of 0.1% per annum. The Industry Regulator approved this level of interest to be paid on security deposits on 22 March 2000, subject to the completion of this review of security deposits, interest and associated issues.

The primary issue relates to the level of the interest rate given the small amount held on behalf of each customer. As a comparison, the Office of Consumer and Business Affairs which holds residential tenancy bond money in South Australia pays 0.1% interest on bond money which averages \$500 per tenant and is held for an average of one year.

Origin Energy in South Australia takes a security deposit from gas customers who are renting property, and pays interest at the rate of 2% pa.

It is important to note that the amount of interest approved by the Industry Regulator is a minimum only, and a retailer may choose to pay a higher amount at their discretion.

The Industry Regulator invites submissions on:

- Whether the interest rate on security deposits should be increased and if so, what would be an appropriate level of interest given the relatively modest amounts of security deposit held per customer?
- Whether any terms and conditions for the payment of interest be specified and if so what should they be? (for example, should interest be paid only on deposits held for more than a certain period; on what basis should the interest be calculated: should differing amounts of interest be paid on differing amounts of security deposit?)
- Should all retailers subject to the Retail Code be required to pay the same level of interest, or should the rate differ based on number of customers, amount held or some other factor? (This issue will particularly arise in relation to retailers retailing to small users ie. under 30 MWh per annum after 1 January 2003).

5. INTEREST CHARGED ON LATE PAYMENTS

5.1 Retail Code Provisions

The Retail Code provides:

6.3.3 Particulars on each bill

A retailer must include at least the following particulars on each bill:

...

(n) the amount of interest approved by the Industry Regulator for late payment

...

Customer Sale Contract

11.3 Late payments

If you do not pay your bill on time, we may require you to pay our reasonable costs of recovering that amount from you. You may also be required to pay interest on the outstanding amounts as set out in our price list.

5.2 Current position

At present no interest rate has been approved by the Industry Regulator to apply to late payments. A \$5.60 administrative fee for late payment is charged by AGL.

A variety of organisations have late payment interest charges, for example:

Australian Taxation Office:	13.08% pa
Emergency Services Levy:	12.8% pa

However, a more relevant comparison is between utility providers. The following table outlines the position with respect to interest rates and other charges on late payments in other jurisdictions and with other utilities.

Utility	Interest	Other Charges
SA Water	No interest charged.	Late payment fee \$5.50.
Origin Energy	No interest charged.	\$15 late fee charged after 3 warnings then \$50 disconnection fee.
Telstra	No interest charged.	Disconnection is relatively quick as it does not require a site visit and reconnection charges of \$50.00 applies.
Council Rates	Initial fine of 5% of the amount owing of the account. [Further interest charges applying from one month after the due date.]	

Utility	Interest	Other Charges
Energy Australia (NSW)	The contract states that they can charge interest from date payment is due at Federal Court Rate.	Can recover costs.
Integral Energy (NSW)	No interest charged.	\$5 reminder fee charged 10 days after due date.
North Power (NSW)	The contract states that they can charge interest from date payment is due at a rate prescribed by the Supreme Court.	Can recover costs.
Solaris (AGL) Victoria	No interest charged.	No other charges notified.
CitiPower (Victoria)	No interest charged.	No other charges notified.
TXU Electricity (Victoria)	No interest charged	No late payment fee. \$20 site visit fee to collect payment. Reconnection fees apply.

On the basis of the above table it appears that the practise of charging interest on late payments is relatively rare amongst utilities. However, the Retail Code approved in late 1999 provides for such charges and there may be sound reasons for introducing such charges (eg. to prevent abuse of the payment system, and to minimise cross subsidisation by consumers who pay on time). Equally, if customers are having great difficulty in paying for their electricity supply the imposition of late payment interest will not assist the customer's predicament.

It is noted, however, that AGL and other retailers bill customers on behalf of ETSA Utilities and that interest accrues for late payments made by retailers to ETSA Utilities. This rate is the bank bill rate plus 2%. (currently around 6.2%+2%)

It is acknowledged that when electricity users persistently pay bills late the retailer is effectively being used as the provider of an interest free overdraft facility.

An analysis of billing data for a 6 month period September 1999 – February 2000 by AGL indicated that almost 5,000 business customers had not paid their account within 31 working days of the account being sent. By this stage the customer has received the original account, a reminder notice, and a final notice. This figure does not include the number of business customers who request (and are granted) extension of time to pay.

It may be argued that for business customers, the supply of electricity should be treated no differently from the supply of any other service and that late payment should attract an appropriately discouraging level of interest. In addition, it may be that late payments

impose a cost burden on the electricity retailer which ultimately must be borne by all consumers through higher prices.

The Industry Regulator invites comment on:

- What is the cost impact of late payments on electricity retailers and would these impacts be off set by the imposition of an interest charge on late payments?
- If electricity retailers make cost savings as a result of being able to charge interest on late payments, how can those savings be shared among other customers?
- Whether an interest rate for late payments should be set and if so on what basis?
- Should the Industry Regulator set terms and conditions under which late payment interest can be charged?
- Should an amount for interest on late payments be set only for business customers?

6. NEXT STEPS

This discussion paper has outlined the issues and suggested matters on which submissions may focus.

Comments are sought from interested parties on the matters raised in this paper. Submissions should reach the Office of the SA Independent Industry Regulator on or before **1 September 2000**.

Following consideration of submissions received, the Industry Regulator will release a Draft Report which will set out the views of the Industry Regulator on each of the matters to be determined pursuant to the Retail Code, canvassed in this discussion paper.

It is expected that the Draft Report will be released by 1 October 2000. The Draft Report will be available for a further short period of public consultation. Final submissions and comments will form the basis for the final report to be released by 1 November 2000. The final report will make determinations as to level of security deposits, and the interest payable on late payments and security deposits as required by the Retail Code. Determinations by the Industry Regulator will apply from 1 January 2001.