ENERGY CONSUMERS' COUNCIL

Comments on

ESCOSA's Inquiry Into Retail Electricity Price Path Discussion Paper

The Essential Services Commission of South Australia (ESCOSA) has invited written submissions from interested parties in relation to their inquiry into the retail electricity price path.

1. General Comments

1.1. The Energy Consumers' Council (ECC) made several submissions to ESCOSA's 2004 Standing Contract Price Review, suggesting a reduction in the Standing Contract Price. The ECC considers that there is still scope for a reduction in the Standing Contract Price.

1.2. The ECC notes that a number of studies, such as the confirmation of the AGL's 2003 Cost by Deloittes and the assessment of retail operating costs, had not been completed at the time of release of the discussion paper. In addition, key information has been made available to ESCOSA, which has not been released for public comment.

1.3. The ECC considers that careful scrutiny should be made of the AGL's Retail Price Path submission and that judgements should be made by persons with sufficient skill and capability to analyse the submission and who have access to all of the necessary information to make an informed judgement.

1.4. The ECC would like to reiterate its comments from the 2004 Electricity Standing Contract Price Review that ESCOSA needs to be cautious in accepting at face value from those who have a vested interest in a higher retail tariff outcome.

2. Socially Responsible Tariffs

2.1. The ECC notes that AGL's submission allows for further unwinding of cross subsidies and that individual tariffs may vary by CPI + 5%. While the ECC is generally supportive of removing cross subsidisation, it is conscious of the need to maintain the supply of electricity at an affordable level. The ECC urges ESCOSA to give particular consideration to actions which may increase the burden on low income households. Where possible, these actions should be considered in conjunction with opportunities to reduce costs to low income households, such as by rebalancing costs to account for lower air-conditioning loads (and hence lower contributions to demand peaks).

2.2. The ECC notes ESCOSA's position that non-tariff approaches be used to address social issues. The ECC, however, considers that there may still be potential for the development of more socially responsible tariffs which will consider the needs for a basic supply of electricity to all consumers at reasonable costs.

2.3. In particular, the ECC considers there is potential for the Standing Contract Price to be adjusted to encourage greater uptake of demand side measures such as time of use or multi-part tariffs, which could ultimately lead to reduced costs for all consumers. The ECC urges ESCOSA to consider the potential to refine the Standing Contract Price structure as opportunities arise.

3. Wholesale Energy Costs

3.1. The ECC still considers there is potential for the effective electricity wholesale price component of the Standing Contract Price to be adjusted downwards. In particular, ESCOSA should have regard for potential decreases in contract prices.

3.1.1. The ECC notes that the Allen Consulting Group (AGC) has provided a report to ESCOSA suggesting that AGL's actual contracts from 2001-2004 relating to the period 2005 – 2008 have been examined, and are reasonable. The Council however does not have access to this report, or information concerning the proportion of load contracted, or the criteria used by ACG to judge AGL's costs as being prudent.

3.1.2. The ECC notes ESCOSA's comments that AFMA prices do not reflect prices in a market where a large load has already been contracted by AGL. The ECC, however, considers that AGL has not clearly demonstrated that the costs of supply are higher, or that a prudent retailer would be unable to obtain a lower price on its purchases.

3.1.3. The ECC is of the view that ESCoSA should consider that there is now less risk in the market. For example, contributing factors such as the Heywood Interconnector being less utilised with power often flowing to Victoria. As a result there are less times of constraint, as there was historically, which made the pool price rise in SA vs Vic. In addition, the ECC has heard that there is a major user in the State that has quite effectively taken Pool Price pass through and has not had major issues on balance.

4. Retail Operating Costs

4.1. The ECC considers that there would be opportunities for a standalone retailer to achieve the same efficiencies as a stapled retailer. For example, negotiations between the retailer and distributor, or other businesses could provide benefits to both organisations.

4.2. The ECC considers an assessment of retailers' actual operating costs needs to be made in order to set this figure. The ECC notes that:

4.2.1. ESCOSA's discussion paper says "no regulator in the past few years has examined a retailer's actual operating costs".

4.2.2. ESCOSA's review of AGL's actual costs was not complete at the time the paper was released.

4.2.3. In fixing a retail operating figure, in addition to actual costs, ESCOSA should consider the costs that would be incurred by an efficiently operated retailer, and the efficiencies that could be reasonably be expected to be gained over the coming three years.

5. Retail Margin

5.1. The Council strongly urges ESCOSA to consider a flat retail margin, rather than a percentage of total costs.

5.2. The ECC notes AGL's justification that it is required to pay network costs even when customers default on their payments. The ECC considers that ESCOSA should consider whether an allowance to AGL is required to account for bad debts that must be passed on to ETSA, and if so, this should be built in as a separate cost to the retail operating costs. If this is to occur, the ECC urges ESCOSA to consider an amount which will ensure that no perverse incentives are provided for poor debt management.

5.3. ESCOSA also suggests that AGL be provided with a greater margin to account for being the only standing contract retailer. The ECC has the following comments regarding this matter:

5.3.1. 20% of consumers have already moved to market contracts. As time passes this figure is likely to increase, allowing greater diversification of the market, and reducing the alleged need to account for risk.

5.3.2. The ECC considers AGL's position as the only standing contract retailer to be similar to having a greater market share and that this is insufficient justification for greater margins.

5.3.3. At most, a small concession could be added to account for the need for additional transfers, in the unlikely event that other retailers (including AGL) cease to offer market contracts.

5.3.4. A higher market share means that common costs are spread over a greater customer base.

5.3.5. The ECC notes that AGL has already been given special consideration for being the standing contract retailer as justification for greater wholesale energy costs.

5.4. ESCOSA uses return on investment as a benchmark in setting the retail margin.

5.4.1. A breakdown of the current value of AGL SA, however, has not been made publicly available. AGL's 2004 Annual Report, shows that its consolidated intangible assets consist primarily of licenses with the goodwill portion being amortised at a higher rate.

5.4.2. The ECC considers that the goodwill portion of AGL's intangible assets (forming part of the purchase price) of AGL SA primarily reflects the potential for greater profit and should not be considered in determining a retail margin for AGL SA.

6. Headroom

6.1. In its December 2003, final report on the 2004 Electricity Standing Contract Price, ESCOSA rejected the ECC's argument that headroom should not be built into the standing contract price as a justification for competition. While ESCOSA noted that no particular % for headroom had been included in its price above the prudent costs, ESCOSA also noted that it believed headroom was available though the declining wholesale energy prices.

6.2. Considering the terms of reference for the current review include the requirement that the proposed standing contract prices exclude any specific allowance for headroom, the ECC urges ESCOSA to carefully examine whether any efficiencies gained from cheaper wholesale contracts could be returned to consumers.

6.3. AGL and other retailers~~,~~ are currently offering market contracts at 5-8% cheaper than the standing contract price. The ECC considers that a tariff containing no headroom should be reasonably competitive with market contracts.

7. Other Comments

7.1. The ECC is concerned that AGL is seeking a price path which is effectively of the form "CPI-X", with X set at 0, but with no analysis or explanation of why X should be set at 0.

7.2. The ECC urges ESCOSA to examine what level of X regulators of electricity retailers in other jurisdictions have set (and on what basis).

7.3. The ECC takes the view that the benefits of improvements in productivity within electricity retailers should be shared with electricity consumers.