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Review of the Effectiveness of Energy Retail Market Competition in South Australia

Phase 2 Report for ESCOSA

NERA

Economic Consulting

Project Team

Greg Houston

Jennifer Fish

Robert McMillan

Yuliya Hedynach

NERA Economic Consulting
Darling Park Tower 3
201 Sussex Street
Sydney NSW 2000
Tel: +61 2 8864 6500
Fax: +61 2 8864 6549
www.nera.com

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Executive Summary

Competition in electricity and gas retail markets has been introduced in all states across Australia in response to the energy reforms recommended over a decade ago by the Hilmer Committee and agreed to by the Council of Australian Governments (COAG). In South Australia, competition for energy customers was introduced in a staged manner from 1998, starting with large industrial and commercial customers. Full retail contestability (FRC) was finally achieved in the South Australian electricity retail market in January 2003 and in the gas retail market in July 2004 when competition was opened to small energy customers, ie, those that consume less than 160 megawatt hours (MWh) of electricity or 1 TJ of gas per annum.

While all small energy customers are now able to choose their own retailer, those that have not switched from incumbent retailers AGL and Origin Energy are protected under South Australia's current regulatory framework. AGL and Origin are both required to offer standing contracts to small customers, with terms and conditions and associated tariffs regulated by the Essential Services Commission of South Australia (the 'Commission'). It is anticipated that as competition for small customers develops, the need for the continued regulation of standing tariffs will be reduced and such regulations will either be removed or their scope narrowed to protect only those customers for whom competition is not considered effective.

In 2004 the Commission developed a monitoring framework to assess the extent to which competition has progressed in both the South Australian electricity and gas retail markets. Under this framework, the Commission collects data and reports on seven indicators of competition on a bi-annual basis. This report expands on the Commission's monitoring activities by considering the extent to which competition in these markets can be considered 'effective'. In part, it is intended to inform the Commission for its upcoming review of AGL and Origin's standing tariffs later this year.

In order to assess the effectiveness of competition in the South Australian energy retail markets, we have considered the structure of these markets as well as the conduct and performance of participants within them. An assessment of these factors together provide some indication as to the strength of competitive constraint imposed by new entrant retailers and whether, in the absence of retail price regulation, incumbent retailers AGL and Origin would have the ability to raise or maintain prices above the efficient cost of service for one or more types of customers, either independently or in conjunction with other new entrant retailers.

Our assessment suggests that competition in both the electricity and gas retail market for small customers is generally effective for most customers. Nine competitors have entered the electricity retail market since the introduction of FRC in January 2003 and in that time have managed to capture 36 per cent of all residential and 25 per cent of all small business customers in the state. An additional 23 per cent of residential and 9 per cent of small business electricity customers have also switched to market contracts with incumbent retailer AGL.

While there have been fewer entrants in the gas retail market, due largely to capacity constraints along the two pipelines that serve the South Australian market, this has not

limited the rate of customer switching to gas market contracts. Despite the fact that competition for small gas customers was opened 18 months after that for electricity, around the same percentage of residential gas customers have switched to market contracts with new retailers and an additional 12 per cent have moved to market contracts with Origin Energy. A much smaller percentage (around 10 per cent) of small business customers have moved to market contracts although this does not appear to be due to any structural impediment to competition.

Pricing pressure from new entrant retailers has led to all retailers offering at least one market contract at a discount to the standing contract where the discount ranges from 2 to 12 per cent for electricity and 2 to 6 per cent for gas. Most retailers also incorporate other price and non-price benefits in at least some of their offers, further enhancing the value of these contracts relative to the AGL and Origin standing contracts. These discounts are generally consistent across all consumption levels and profiles and are also made available to financially disadvantaged customers. Such customers are actually more likely than other customers to have switched to electricity market contracts and are no less likely to have switched to gas market contracts.

Those customers for whom competition does not yet appear to be effective include all small gas customers located in regional areas of South Australia and small business gas customers across the state. Competition for regional gas customers in the north of the state appears to be limited by capacity constraints along the laterals that connect the Moomba to Adelaide Pipeline (MAPS) with Envestra's regional distribution network. Customers served by these laterals are only able to obtain gas supplies from incumbent retailer Origin. It is unclear whether competition for these customers will ever be open given the limited amount of firm capacity available on these laterals and the extent to which Origin requires this capacity in order to serve other larger commercial or industrial customers in these regions. Given that demand in these regions is largely concentrated between a few large users, it may be that the only viable market outcome is for almost all customers in these regions to be served by a single retailer. To the extent that this is the case, the retention of standing contract price regulation for these customers would be desirable.

It is unclear why competition for small business gas customers, and to a lesser extent small business electricity customers, has been less intense than that for residential customers. All retailers have market contracts available to small business customers, with differing price and non-price features. However, direct marketing to small business gas customers is not common, with only around 16 per cent of such customers indicating that they have been contacted directly by a retailer with a market offer. When combined with the apparent unwillingness of small business customers to search pro-actively for information regarding market contracts or to contact retailers in regard to available offers, it is not surprising that switching rates among these customers is relatively low.

One explanation for the lack of competition for this customer segment may be that the number and consumption of these customers is small relative to the residential gas customer base and that the search costs for retailers in identifying these customers is relatively high. A proportion of these customers are also likely to be located in regional areas where Origin is the natural supplier. It may also be the case that retailers are unable to offer market contracts at a sufficient discount to encourage these customers to switch given current standing contract rates, although this was not raised by retailers as an issue in

the context of this review. Whatever the reason, competition for this customer segment does not yet appear to be effective and further consideration may need to be given as to how this could be improved going forward.

Looking forward there is little reason to suggest that competition for both electricity and gas customers will not continue to become more intense. At present there do not appear to be any material constraints on new entry and expansion in the electricity retail market, although we note that the trend is towards increased retailer and generator consolidation and vertical integration. Retailers have raised concerns that further consolidation in the industry, particularly by incumbent retailer AGL, may have the potential to raise barriers to expansion for non-vertically integrated retailers by reducing the availability of adequately priced hedging products. While this is an understandable concern, we note that any future acquisitions will be scrutinised by the Australian Competition and Consumer Commission (ACCC) for their likely impact on competition in both the electricity generation and retail markets. Even where such integration may place non-vertically integrated retailers at a disadvantage, it is not clear that competition between vertically integrated retailers AGL, Origin, TRUenergy and EA-IPR partnership will not be sufficiently effective to protect consumers against the exercise of market power by one or more market participants.

In the case of gas some of the constraints that may have delayed the entry of new retailers in the past appear to have eased with the expiry of a number of contracts for carriage on the MAPS in December 2005. New entrants that were previously unable to contract firm capacity on either the MAPS or SEA Gas prior to this date may now be capable of competing, at least for those customers located in Adelaide, through the negotiation of contracts for gas supply from Moomba. We note that two retailers currently hold a gas retail licence but are not currently active participants in the market and two others have recently applied for a gas retail licence. If these retailers are capable of securing competitively priced gas supplies from producers at Moomba there may be further entry in this market over the coming years. The extent to which such entry is likely or sustainable, however, depends on the willingness or ability of gas producers at Moomba to contract additional firm supplies to new entrant retailers in the face of declining gas reserves from the Cooper Basin.

Planned investment for Envestra's distribution network over the coming years also has the potential to increase the intensity of competition for gas customers in Adelaide as retailers gain better access to customers located in the northern suburbs by means of SEA Gas. TRUenergy, one of the four retailers that currently serve the Adelaide region, currently has limited access to customers in northern Adelaide due to constraints within the gas distribution network. To the extent that the planned construction of another gate station at Elizabeth alleviates this constraint for both TRUenergy and other retailers that may have limited capacity for supply from MAPS, it can be expected to increase competition for these customers. However, we note that it is unclear at this stage when this gate station will be constructed and the extent of the increase in potential customers for TRUenergy that would result.

1. Introduction

This Phase 2 report represents the second in a series of reports prepared as part of the Essential Services Commission of South Australia's ("the Commission's") Review of the Effectiveness of Energy Retail Market Competition in South Australia.

Full retail contestability was introduced in the South Australian electricity and gas markets in January 2003 and July 2004 respectively. In line with its obligations under section 6 of the ESC Act, the Commission has developed a framework for monitoring the impact of full retail contestability within these markets. Under this framework, the Commission collects and publishes information from both retailers and customers in order to monitor the development of electricity and gas retail markets by reference to seven indicators of competition.

The current review represents a further development and refinement of the Commission's existing framework and six-monthly monitoring reports. The purpose of this assessment is to draw conclusions on the overall effectiveness of electricity and gas retail competition for small residential and business customers in South Australia and to make recommendations as to the means by which the Commission's retail market activities could be amended to enhance retail market competition for these customers.

In light of the Commission's upcoming review of standing contract prices for both electricity and gas later this year, the Commission is particularly interested in determining whether there are any competition concerns in relation to the small customer segment that may influence the Commission's view of the appropriate form of regulation to be applied.

The remainder of this report is structured as follows:

- § section 2 sets out the background to the introduction of retail contestability in South Australia;
- § section 3 sets out the framework for our analysis;
- § section 4 defines the relevant market for analysis;
- § section 5 considers the structure of the electricity and gas retail markets in South Australia;
- § section 6 considers the market conduct of participants within the electricity and gas retail markets in South Australia;
- § section 7 considers aspects of market performance that assist in determining the degree to which retailers are competing with one another; and
- § section 8 concludes on the extent to which competition in the electricity and gas retail markets can be considered 'effective'.

2. Background

Competition in energy markets has been an area of focus in Australia since the introduction of the National Competition Policy and related reforms (NCP Reforms) in the early 1990's. These reforms encompassed a range of measures designed to reduce barriers to intra and inter-state competition in energy markets, starting with the structural separation of the competitive and monopoly elements of these industry, ie, the separation of generation and retail from the transmission and distribution functions, and the introduction of access regimes for these monopoly elements. The reforms also included timelines for the introduction of full retail contestability in both electricity and gas retail markets.

2.1. Overview of the South Australian Electricity Sector

2.1.1. Structure of the SA Electricity Industry

Prior to the review of the state's electricity industry in June 1998, the South Australian electricity industry consisted of two entities: South Australia Generation Corporation (trading as Optima) and ETSA Corporation. On completion of its review, the South Australian Government recommended that the state's electricity industry be restructured into three generation companies, a transmission company and distribution/retail company, with appropriate ring-fencing arrangements put in place to ensure adequate separation of these two functions.

In accordance with these recommendations, Optima was restructured into three new generation companies: Optima Energy, Flinders Power and Synergen. ETSA Corporation was disaggregated to form ElectraNet SA, a transmission company, and a distribution and retail business were maintained as subsidiaries under a holding company. The distribution and retail subsidiaries were called ETSA Utilities Pty Ltd and ETSA Power Pty Ltd.

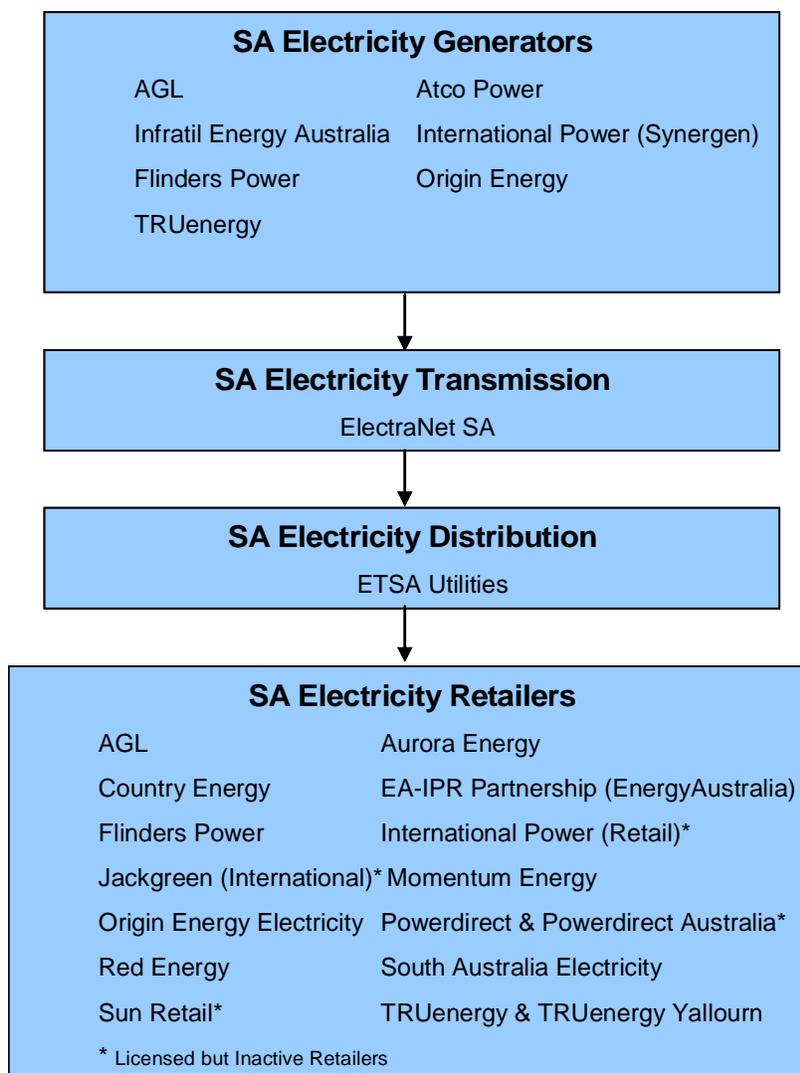
The South Australian electricity industry has changed considerably since the late 1990's and now comprises seven principal generators, one transmission company, one distribution company and fourteen retail companies, as shown in figure 2.1 below.

2.1.2. Electricity Purchasing Arrangements

Almost all South Australian generators are required to sell, and retailers required to purchase, their electricity through the National Electricity Market (NEM). The NEM is a wholesale market for electricity supply. It interconnects the South Australian electricity network with that of Victoria, New South Wales, Queensland, the ACT and Tasmania

The National Electricity Market Management Company (NEMMCO) is the central market and systems operator of the NEM. NEMMCO schedules generators to run throughout the day based on bid prices submitted by each generator, where the schedule is determined on the basis of the lowest to highest bid. The wholesale electricity price paid by retailers is established by NEMMCO based on the bid price of the last generator scheduled to supply within each half hour period. Wholesale prices fluctuate through the day and between seasons in response to a wide range of factors. In order to manage the risk of price fluctuations, generators and retailers typically enter into hedge contracts which specify the price at which they agree to trade energy supplies.

Figure 2.1
Structure of the South Australian Electricity Industry as at 31 December 2006



2.1.3. Timeline for Retail Contestability

Retail contestability for South Australian electricity customers was introduced in stages over a four year period from December 1998 to January 2003.

Retail licences were issued on 11 October 1999. At that time, a number of retail licences were issued, including to ETSA Power (now AGL), EnergyAustralia, North Power (now Country Energy), Flinders Power, Boral Energy Electricity (now Origin) and Eastern Energy (now TRUenergy). ETSA Power was the only retailer permitted to supply small electricity customers at this time. Other retailers served only those customers that were deemed contestable, which included large customers consuming more than 750MWh of electricity per annum.

Full retail contestability (FRC) was achieved on 1 January 2003 when competition was opened for small customers consuming less than 160 MWh per annum. A summary of the timeline for electricity retail contestability in South Australia is set out in table 2.1 below.

Table 2.1
Timeline for Electricity Retail Contestability in South Australia

Consumption Level p.a.	Eligible Date for Contestability	Approximate No. of Customers
≥ 4 GWh	20 December 1998 (One week after market start)	167
≥ 750 MWh	1 July 1999	635
≥ 160 MWh	1 January 2000	2,600
All customers	1 January 2003	720,000

Source: ESCOSA

2.1.4. Regulation of Standing Retail Tariffs

The South Australian government conferred retail pricing powers on the Commission as part of the consumer protection measures designed to support the introduction of retail contestability.

The Commission regulates only those tariffs for small customers that have not entered into a market contract, where small customers include both residential and small business customers. As the prescribed retailer under the Electricity Act 1996, AGL SA (formerly ETSA Power) is required to offer electricity to small customers, with associated terms and conditions, at a standing contract price.

The Commission's most recent standing offer price determination was made in December 2004. This determination sets out the price path to apply to AGL SA's standing contracts for the period 2005-2007. Under this determination, AGL SA's retail tariffs (ie, the cost components over which it has control) are set under an average price cap, with side-constraints imposed for individual tariff changes. AGL SA is permitted to pass on network tariff charges relating to the provision of distribution network services and recovery of transmission charges by ETSA Utilities.

The current ESCOSA price determination allowed for an average price increase of 1.2 per cent on 1 January 2005 and provided for further price changes each July over the 2005 – 2007 period.

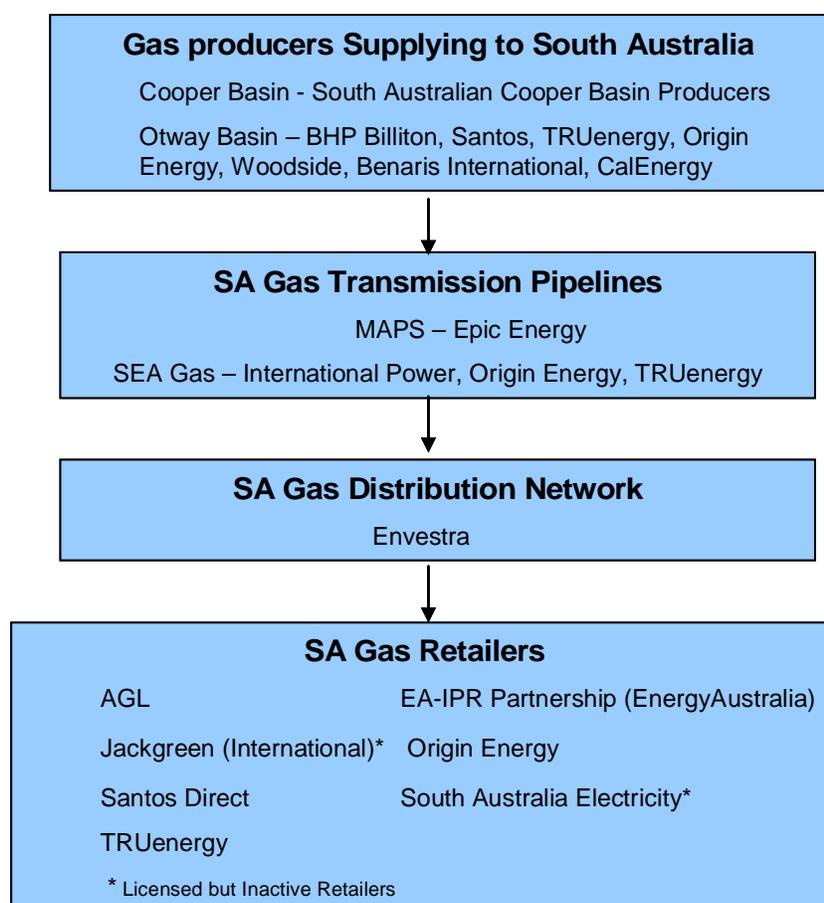
2.2. Overview of the South Australian Gas Sector

2.2.1. Structure of the SA Gas Industry

Natural gas is supplied to South Australia from the Cooper Basin in the far north of the state and the Otway and Bass Gas Basins just off the coast of Victoria. Gas is transported from these production fields to customers in Adelaide and other regional areas via two major transmission pipelines; the Moomba to Adelaide Pipeline System (MAPS) and the SEA Gas pipeline, and a gas distribution network.

The current structure of the South Australian gas industry is set out in figure 2.2 below.

Figure 2.2
Structure of the South Australian Gas Industry



2.2.2. Gas Purchasing Arrangements

Unlike electricity, there is no formal or centralised wholesale market for gas supplies. Gas retailers operate in a contract carriage market, which requires them to have contractual arrangements in place with gas producers, transmission pipeline owners and the distribution network operator Envestra for the purchase and transportation of gas from production fields

to customers' premises. The ability for new retailers to supply customers, particularly small customers, is therefore limited by the availability of uncontracted gas reserves and firm capacity on both transmission and distribution pipelines.

The Retail Energy Market Company (REMCo) is the retail market administrator for South Australia. REMCo commenced operations in South Australia in July 2004 and is responsible for the transfer of responsibility for gas delivery points between retailers, managing daily allocations of gas usage to retailers, and managing and developing the rules for the operation of the retail gas market. Unlike NEMMCO, REMCo does not establish the wholesale price to be paid for gas by retailers. Such prices are set through the contractual arrangements that each retailer has with providers in the gas supply chain.

2.2.3. Timeline for Retail Contestability

As was the case for electricity, contestability for South Australian gas customers was also introduced in a phased manner from 1998.

Gas licences were first issued to TRUenergy (formerly Eastern Energy) and Origin Energy Retail (formerly Boral Energy), SA's incumbent gas retailer, in April and September 1998. At that time TRUenergy was able to serve large customers that consumed over 100 TJ of gas per annum.

While small gas customers, ie, those consuming less than 1 TJ per annum, were considered 'contestable' from July 2001, the REMCo market systems were not in place to allow for mass transfers until July 2004. FRC was therefore not achieved, in a practical sense, until July 2004. A summary of the timeline for gas retail contestability in South Australia is set out in table 2.2 below.

Table 2.2
Timeline for Electricity Retail Contestability in South Australia

Consumption Level p.a.	Eligible Date for Contestability	Approximate No. of Customers
> 100 TJ	1 April 1998	
> 10 but < 100 TJ	1 July 1999	174
Industrial and Commercial Customers < 10 TJ	1 July 2000	250 (5 to 10 TJ p.a.) 2,500 (1 to 5 TJ p.a.)
All customers	1 July 2001 – Systems not in place to handle mass transfers until 1 July 2004	340,000

Source: ESCOSA

2.2.4. Regulation of Standing Retail Tariffs

To protect small retail gas customers as competition develops in the retail gas market, Origin Energy was required to offer a standing contract to existing small customers, at a regulated gas retail price. Small retail gas customers are defined as those using less than 1 TJ of gas per year.

The most recent gas standing contract price path determination was made by the Commission in June 2005. The determination sets out the price path to apply to standing contract prices for the three year period commencing 1 July 2005 and ending 30 June 2008. The form of regulation adopted was an average price cap for each category of charges relating to residential and small/medium businesses.

For 2005/06 the average retailer price cap was \$9.857/GJ and the price path was determined to increase annually by the change in CPI+2.5 per cent for the remainder of the period.

2.3. Monitoring of Retail Competition

The Commission developed a framework for monitoring the development of energy retail competition in South Australia in 2004. Under this framework, the Commission monitors seven main indicators of competition, being:

- § Indicator 1 – Number of Electricity Retailers
- § Indicator 2 – Customer Switching;
- § Indicator 3 – Barriers to Entry;
- § Indicator 4 – Information Asymmetries;
- § Indicator 5 – Price/Service Mix;
- § Indicator 6 – Impacts on Low-Income Groups;
- § Indicator 7 – Innovation.

The Commission reports the results of its monitoring activities on a bi-annual basis. The latest monitoring report was published in May 2006.

3. Framework for Analysis

Competition can be defined as a process of rivalry among firms, where the price and output decisions of each market participant are constrained by the actions of others. Competition is not an absolute concept; rather, different types of competitive rivalry can be observed depending on the nature of the market in question.

Markets may range from being perfectly competitive to pure monopolies. Perfectly competitive markets are characterised by a large number of buyers and sellers each producing a homogenous product, with perfect knowledge of the conditions of supply and demand. In such markets, the cost of entry is low and producers are free to enter and exit the market over time. Because of this, the degree of competition between suppliers is generally high. Producers are effectively price-takers and have no real power to increase prices above marginal cost.

By contrast, in markets characterised by high barriers to entry, including high up-front capital costs and economies of scale relative to demand, the most efficient outcome may be for only one producer to supply the entire market. However, in markets characterised by natural monopoly and where customers have little bargaining power, it is possible for the monopolist to exert its market power by raising prices and limiting output so as to earn above-normal profits.

In reality, most markets fall somewhere in between these two extremes. For example, some markets may be oligopolistic, with high barriers to entry and only a few suppliers. Other markets may be monopolistic, with relatively low barriers to entry and with a number of suppliers that produce differentiated products that are highly, but not perfectly, substitutable for one another. In each of these markets firms may compete with one another in different ways. For example, in markets for the sale of a homogenous product, suppliers are likely to compete on the basis of price given the level of capacity in the market. In monopolistic markets, suppliers may compete by consistently developing new products over time, in an attempt to maintain a price premium over other products or market share.

In undertaking any competition analysis it is important to distinguish between the type of competitive rivalry observed in the market and the degree of competition between players in that market. The type of competitive rivalry that exists in a market is generally a function of the product or service being produced as well as the nature and relative size of the costs of production. While some forms of market structure are more conducive to aggressive competition between suppliers, ie, perfectly competitive and monopolistic markets, this does not mean that those market structures that only encourage the entry of a small number of sellers cannot be considered highly competitive. For example, vigorous competition can occur between a limited group of individually powerful and well matched suppliers in an oligopolistic market.

3.1. Effective Competition

Even where it is possible to assess the extent to which market participants compete with one another, the question arises as to what point can one say that the level of competition in a market is 'effective'?

In 1975 the Trade Practices Tribunal (now the Australian Competition Tribunal) considered the meaning of the term effective competition, noting the following:¹

“The basic characteristic of effective competition in the economic sense is that no one seller, and no group of sellers acting in concert, has the power to choose its level of profits by giving less and charging more. Where there is workable competition, rival sellers, whether existing competitors or potential entrants in the field, would keep this power in check by offering or threatening to offer effective inducements....”

In our view, effective competition requires that both prices should be flexible, reflecting the forces of demand and supply, and that there should be independent rivalry in all dimensions of the price-product-service packages offered to consumers.”

This view suggests that the benchmark for effective competition need not be based on the theoretical construct of a perfectly competitive market or that prices should be at or very close to the long-run cost of supply. Rather, it implies that for competition in a market to be considered effective, there should be sufficient rivalry between existing or potential competitors to keep the market power of all producers in check. In other words, the level of competition should be sufficient to ensure that no one producer can earn significant above-normal profits, or continue to provide a sub-optimal range of products or services through the exercise of its market power.

This interpretation is similar to that adopted by the Essential Services Commission of Victoria (ESC) in its assessments of the effectiveness of energy market retail competition in both 2002 and 2004.² In its 2002 review the ESC identified the following characteristics that competitive markets would normally possess:³

- § a sufficient number of buyers and sellers and/or freedom of entry and exit so that customers remain contestable and free to exercise choice;
- § rivalrous and innovative conduct on the part of sellers and the widespread exercise of market choice by well informed buyers; and
- § differentiated products and services that reflect innovations on the part of sellers in response to the preferences of customers, and prices that reflect the efficient cost of those products and services.

In this review, the ESC explicitly recognised that full retail competition for the small customer retail segment was in its infancy and that there were market developments

¹ *Re Queensland Co-operative Milling Association and Defiance Holdings Ltd* (1975), APTR 40-012, at 17 and 245.

² See ESC, *Special Investigation: Review of the Effectiveness of Full Retail Competition for Electricity – Final Report*, September 2002, p.18 and ESC “*Special Investigation: Review of the Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity – Background Report*”, June 2004, p.4.

³ ESC, *Special Investigation: Review of the Effectiveness of Full Retail Competition for Electricity – Final Report*, September 2002, p.18.

occurring that were yet to fully manifest themselves.⁴ In its later review in 2004, the ESC also noted that the market was still in its formative stage but that competition was generally effective in constraining prices and was likely to become effective for a much larger proportion of small energy customers over the next few years as competition continues to build and the effects of measures to enhance competition are felt.⁵

Given that full retail contestability was only introduced for electricity customers in South Australia in January 2003 and for gas customers in July 2004, we would not expect competition to have fully matured in these ‘markets’. However, if the conditions for competition are present, we would expect to observe new entry for a range of customer classes, the emergence of new types of competitive contract offerings with varying terms and conditions, and some level of customer switching between retailers in response to these competitive offerings. Where such evidence suggests that smaller new entrants have imposed some level of constraint on the incumbent retailer and that competition from these new entrants is likely to strengthen over time, and expand into customer segments where new entrants have not had a significant presence, then we would consider the market to be effectively competitive.

In light of the above, in assessing whether energy retail markets are effectively competitive one must look beyond a simple analysis of market structure and assess whether the interaction between buyers and sellers in the market is such that no one producer or group of producers has the ability to exert its market power.⁶ A useful analytical framework for such an assessment is therefore to consider:⁷

- § the definition of the bounds of the relevant market or markets for consideration;
- § the structure of the relevant markets;
- § the conduct of participants (both suppliers and consumers) with each relevant market; and
- § the performance of participants within each relevant market.

3.2. Defining the Relevant Markets

Market definition is an important first step in any competition analysis since it identifies the relevant arena in which competition is to be assessed. The process of defining the relevant market typically involves consideration of four primary market dimensions:

⁴ ESC, *Special Investigation: Review of the Effectiveness of Full Retail Competition for Electricity – Final Report*, September 2002, p.78.

⁵ ESC “*Special Investigation: Review of the Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity – Overview Report*”, June 2004, p.3-4.

⁶ That is, to raise prices significantly above the efficient cost of supply over the long term.

⁷ Note that in developing the framework for this assessment the Commission has asked us to consider the approach adopted by other regulators such as the Victorian Essential Services Commission (ESC) for the consideration of the effectiveness of retail competition in other jurisdictions as well as the approach that the Australian Energy Markets Commission (AEMC) intends to adopt for all future reviews of retail competition in Australia.

- § *Product* – a market consists of buyers and sellers that consume or produce products that are substitutable for one another;
- § *Geographic* – the geographic bounds of a market is limited to the smallest area over which consumers or producers have a significant influence over price;
- § *Functional* – the functional bounds of the market require consideration of the extent to which the activities of participants at different stages of the supply chain are separable; and
- § *Time* – the temporal dimension of the market refers to the period over which substitution possibilities should be considered.

For the purpose of the current review the market definition is influenced by the fact that the review is limited to the retailing of energy to small customers as defined in South Australia.

3.3. Assessment of Market Structure

After defining the relevant markets for analysis it is possible to assess the structural characteristics of each. Such analysis provides some indication of the type of competitive rivalry to be expected between market participants and the scope for effective competition within those markets.

Competition authorities such as the Australian Competition and Consumer Commission (ACCC) generally consider the following market structure characteristics when conducting competition assessments:⁸

- § *the number of customers and suppliers* – the existence of only a small number of suppliers may reflect structural characteristics of the market such as economies of scale and scope but may also be an indicator of the extent to which suppliers have the ability to exert their power in a market, particularly where there are a large number of small customers with little bargaining power;
- § *the history of entry, exit and consolidation in the market* – evidence of market entry and exit demonstrates the extent to which new entrants may be capable of overcoming entry barriers. Consolidation or vertical integration between suppliers may reflect structural factors such as economies of scale and scope or dynamic competitive pressures and opportunities over time, but may also provide more integrated firms with the ability to increase and potentially to exert their market power.
- § *the market share of suppliers and the level of market concentration over time* – market concentration refers to the relative number and size of participants in a market, ie, it refers to how evenly market shares are allocated between suppliers. While the existence of a small number of suppliers with large market shares may be indicative of structural features of the market, it may also be indicative of the ability for one or more

⁸ These market structure characteristics are considered by the ACCC when conducting merger assessments and when assessing whether corporations have the requisite degree of market power to be in breach of various competition provisions contained in the Trade Practices Act 1974.

suppliers to exercise market power by unilaterally raising prices or coordinating behaviour with other suppliers in ways that discourage competition and new entry;

§ *barriers to entry, expansion and/or exit* – barriers to entry refer to any feature that puts prospective new entrants at a disadvantage relative to incumbent firms. The presence of entry barriers may suggest that existing market participants are not disciplined by the threat of new firms emerging in the market and may therefore have opportunities to exert their market power by raising prices above the cost of supply. Potential entry barriers in energy retail markets include incumbent retailer advantages in terms of branding and customer awareness, economies of scale and scope, limited access to wholesale energy supplies, the availability of hedging instruments to minimise price risk and regulatory compliance costs.

3.4. Assessment of Market Conduct

Market structure is not the only feature that affects the level of competition in a market. For any given market structure, the degree of rivalry between suppliers will be influenced and evidenced by their conduct within the market.

Market conduct may be considered in terms of both supplier conduct and consumer conduct. On the supply side, evidence of suppliers aggressively marketing their product or service and potential instances of anti-competitive or misleading or deceptive conduct will help to inform the degree to which suppliers are in fact competing with one another. On the demand side, evidence of customers switching suppliers over time in response to price or quality differentials provides some indication of the extent to which customers are responsive to competitive pressures in the market.

In competitive retail markets one would expect to observe specific types of conduct from retailers and customers alike. Evidence of retailers actively competing for customers through a variety of advertising and marketing channels, and the continued development of market offers that meet the changing needs and preferences of customers are both indicative of a high degree of competition. Evidence of anti-competitive or misleading and deceptive conduct may also be indicative of competitive pressures or, alternatively, could reflect the ability and willingness of retailers to exert their market power over consumers.

On the demand side, the most useful indicator of the effectiveness of competition is the extent to which customers have responded to competitive offers either by switching retailers or entering into market contracts with the incumbent retailer. Switching may be viewed as an outcome of the effectiveness of retailer actions in motivating customer responses. The rate of customer switching will be affected by:

- § the extent to which retailers are actively promoting their market offers, which will in part be affected by the margin available under the standing tariff; and
- § customers' awareness of the choices available to them, which will vary depending upon their receptiveness to the sales channels utilised by retailers.

In an effectively competitive market, customers are likely to be well informed about available offers and will switch or retain their electricity and gas supply services with those retailers that offer the most favourable terms and conditions. However, customers may find

the search for, and evaluation of information costly and time consuming. Effective competition can therefore be expected to motivate retailers to recognise such costs and undertake targeted marketing campaigns in order to make it easier for customers to make informed decisions.

Even where retailers do not target certain customer classes, effective competition may still be supported by active customer participation. Individual customers may seek to participate in the market via the services of customer aggregation providers. Such services seek to increase demand to levels that improve the financial attractiveness of these customers to retailers and enhance the collective bargaining power of these customers. Such measures may be useful in rural and regional areas where higher customer acquisition costs may dissuade retailers from actively seeking out individual customers.

3.5. Assessment of Market Performance

In addition to the conduct of market participants, the degree of competition will be informed by the ‘performance’ of the market, or participants within the market.

One of the primary measures of market performance is the extent to which prices reflect the efficient long-run cost of supply, where such costs include a reasonable profit margin that provides suppliers with an incentive to invest and allows them to recover the costs incurred in acquiring customers. We note that while an assessment of the margins available to suppliers is a useful indicator of the extent to which suppliers compete with one another, such analysis is difficult to conduct, particularly in markets where there are significant fixed or common costs that may be allocated differently by suppliers across their individual customer bases. Given this difficulty, we have not conducted a margin analysis for the purpose of this review.

Another broad indicator of market performance is the extent to which suppliers have developed innovative and differentiated products for customers that are to some degree tailored to the needs and preferences of particular customer groups.

In energy retail markets, different customer groups may benefit from contracts with different tariff structures depending on the nature of their consumption profile. The development of various offers by retailers that provide different levels of savings to customers with different consumption profiles in comparison to the standing contract is evidence of competition at work. In an effectively competitive market one would expect to see retailers developing new and different products over time, with different price and non-price terms, that provide value to customers with different needs and preferences.

For the purpose of the current assessment we have assessed various measures of market performance, which take account of the range of products offered by retailers and the extent to which competition between retailers has benefited low-income consumers.

4. Market Definition

As noted in section three, market definition is a necessary first step in assessing the effectiveness of retail competition. The purpose of defining a market is to identify the bounds within which market participants operate. Once these bounds have been identified, it is then possible to assess the relative strength of constraints imposed on market players and the extent to which one or more players may possess market power.

In general terms, a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution - at least in the long-run – if given a sufficient price incentive. As the Trade Practices Tribunal (now the Australian Competition Tribunal) commented in the *Queensland Cooperative Milling Association (QCMA)* case:⁹

‘A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them ... Within the bounds of a market there is substitution – substitution between one product and another, and between one source of supply and another, in response to changing prices ... It is the possibilities of such substitution which set the limits upon a firm’s ability to “give less and charge more”. Accordingly, in determining the outer boundaries of the market we ask a quite simple but fundamental question: if the firm were to “give less and charge more” would there be, to put the matter colloquially, much of a reaction.’

The process of defining the relevant market typically involves consideration of four primary market dimensions; product, geographic, functional and time. In most cases, the main focus is on both the product and geographic dimensions. Generally, producers that supply different products, or that are located in different areas, are considered to operate within the same market if:

- § a substantial number of consumers are willing and able to substitute the good or service of one producer for the other in response to a change in the relative price of the products of both (referred to as demand-side substitution); and/or
- § producers can easily switch supply from one product to the other in response to a change in the relative price of both products (referred to as supply-side substitution).

Whether demand or supply side substitution is feasible, or likely, ultimately depends on factors such as consumer attitudes, technology, geographic distance, and cost and price incentives. If enough consumers or producers are capable of substituting demand or supply so as to defeat a small but substantial non-transitory increase in price (SSNIP) by a hypothetical monopolist above the competitive level, then those consumers and producers should be considered to operate within the same market.

The key issues that arise in defining the relevant markets for the purpose of assessing the effectiveness of energy retail competition in South Australia concern:

⁹ *Re Queensland Co-operative Milling Association Ltd and Defiance Holdings Ltd* (1976), ATPR 40-012 at 17,247.

- § the substitutability of electricity and gas supplies, ie, whether electricity and gas are in the same product market;
- § the relevance or otherwise of different classes of customers, ie, whether there is one or more product markets for the supply of energy to residential vs. small business customers vs. large commercial users and industrial users; and
- § the *geographic* bounds of the relevant markets, ie, whether there is one or more geographic markets for the supply of energy to metropolitan vs. regional customers.

We consider each of these issues in more detail in the sections below.

4.1. Are Retail Electricity and Gas in Separate Product Markets?

Electricity and gas are both energy sources and there is undoubtedly a degree of inter-fuel competition between them. Gas can and does form a viable substitute to electricity for a range of end-uses, most notably cooking and heating. However, even in its fully reticulated form gas does not represent a perfect substitute for electricity for a large range of essential end-uses such as lighting and domestic and business applications, ie, powering appliances such as computer hardware, white-goods or other household appliances. The ability for consumers to substitute gas for electricity is therefore limited.

The limitations on the ability of consumers to substitute gas for electricity suggest that separate markets are likely to exist for these two energy sources. This conclusion is informed by the fact that end-uses for which there is no viable substitute energy source for electricity are likely to constitute a significant and largely unavoidable quotient of final energy expenditure. In order for customers to have an incentive to switch from electricity to gas for those end-uses where the two energy sources are substitutable, the financial benefit from switching would also need to be more than outweighed by the switching costs involved, including the expenditure that would need to be incurred in purchasing gas powered appliances.

The scope for supply-side substitution between retail activities in the electricity and gas sectors is likely to be similarly limited. Economies of scope do exist between the two functions, since many of the assets used in electricity and gas retail activities are essentially common: including contracting functions, brand names and in-house or third-party call centres. However, despite these synergies, it seems unlikely that an existing electricity- or gas-only retailer could readily expand or switch to gas/electricity retailing following an increase in the relative price of the alternative energy source.

As the ESC outlined in its 2004 review of energy retail markets, there are fundamental differences between electricity and gas retailing that would make ready transitioning between the two difficult. The principal hurdle for retailers is that the provision of electricity and gas require different wholesale, transmission, distribution, use of system and customer agreements.¹⁰ The time and effort that would be required to enter into contractual arrangements with parties at each stage in the energy supply chain and in complying with

¹⁰ ESC “*Special Investigation: Review of the Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity – Background Report*”, June 2004, p.30.

other administrative requirements would significantly hinder the ability of suppliers to switch production plans quickly so as to exploit favourable price differentials. Such switching would likely occur over a longer time frame and would arguably be better characterised as market entry as opposed to supply side substitution.

The geographic bounds of these markets are also likely to be different in that gas is not reticulated over the same geographic area as electricity. This would limit the ability of electricity retailers to leverage off their existing customer base to increase gas supplies in response to a significant price differential.

Having said that, where a retailer already supplies both fuels there is the potential for an element of supply-side substitution. Dual-fuel retailers are perhaps in a position to vary their marketing priorities between electricity and gas supplies according to the relative margins available for the sale of each. Expansion by dual-fuel retailers would therefore enhance the scope for shorter-term supply-side substitution. However, the existence of dual fuel retailers selling a bundled offering of electricity and gas does not influence the extent of demand-side substitutability. While such retailers may be able to take advantage of price or margin differentials by targeting specific consumer groups, this does not alter the extent to which customers can effectively substitute these two energy sources.

On balance, we consider that at the current time there are likely to be separate product markets for the retail of electricity and the retail of gas. Given the degree of substitutability between these two energy sources, the influence that one has on the price and quality offerings in the supply of the other is likely to be limited. While these energy sources will likely remain imperfect substitutes in the near future, we note that the degree of substitutability may increase over time as gas powered appliances become more widely available and consumers' willingness to install gas connections increases.

4.2. Do Separate Markets Exist for Different Customer Classes?

Whether it is appropriate to define a number of markets by reference to customer classes depends upon the demand- and supply-side characteristics of customers and retailers alike. In this instance, the decision to delineate separate markets for the supply of energy to residential and small business customers as distinct from commercial and industrial customers depends most importantly on whether a firm retailing to one customer group would need to undertake substantial capital investment in order to serve the other.

The approaches employed by retailers to serve each retail customer class in South Australia are quite different. By way of example, commercial and industrial customers commonly negotiate specialised long-term contracts for the supply of substantial quantities of electricity and/or gas. By contrast, residential and small business customers tend to source much smaller quantities of supply under standard contracts made available to a large number of customers.

Given that the demand-side characteristics of these broad categories of customer are distinct, as are the systems and processes put in place by retailers to support energy sales to those customers, it seems unlikely that a retailer exclusively serving residential and small business customers could readily expand or switch to supply larger industrial and commercial customers, even if a price incentive did exist (or vice versa). This suggests that

there are separate markets for the supply of energy to residential and small business customers and the supply of energy to larger industrial and commercial customers.

Recent regulatory and legal precedent also reinforces the conclusion that supply-side factors create separate markets along customer lines. In the 2003 AGL case, for example, it was accepted by all parties that there were separate retail markets for the supply of electricity to residential and small business customers in Victoria. The ACCC submitted, and the Court accepted, that retailers competing in the commercial and industrial customer market were not immediate potential entrants into the residential and small business customer market.¹¹ Justice French concluded:¹²

'[T]he Victorian residential and small business customer market is characterised by a large number of small customers consuming relatively small quantities of electricity. The other market is characterised by a small number of customers consuming very large quantities of electricity. Because of these differences the business systems, operations and know how required to supply electricity to the former market are distinct from that required for the latter.'

For the purposes of this review it is also necessary to give special consideration to low-income customers. Whilst the retail of energy to low income customers is unlikely to constitute a separate market from the retail of energy to other small customers, it is nonetheless relevant to consider whether competition for this particular customer segment is sufficiently effective to inform the Commission's approach to its review of AGL and Origin's standing tariffs for electricity and gas supply in 2007.

4.3. What are the Geographic Bounds of the Relevant Markets?

Delineation of the relevant geographic market or markets involves the identification of the areas over which sellers can feasibly retail energy, and customers can readily substitute one source of supply for another when given an economic incentive to do so. At its broadest, the definition of relevant electricity and gas retail markets would be the nationwide or Eastern Australian market for energy in the NEM. The narrowest definition, on the other hand, would be the delineation of separate markets for the retail of electricity and gas within metropolitan Adelaide and in other rural and regional areas of South Australia.

Several factors influence the area over which energy retailers can feasibly operate. Despite the fact that most energy retailers have centralised systems and call centres that allow them to service customers in different areas, their geographic reach is constrained by a number of factors, including the requirement to hold a licence in each state jurisdiction, the physical bounds of existing transmission and distribution infrastructure, and their ability to contract wholesale energy supplies to each area. The combination of different licensing regimes due to state-based oversight of energy retail activities, the existence of state based electricity transmission and distribution networks, and the location and flow of gas transmission

¹¹ *Australian Gas Light v Australian Competition and Consumer Commission* (No.3) [2003] FCA 1525.

¹² *Australian Gas Light v Australian Competition and Consumer Commission* (No.3) [2003] FCA 1525, para 595.

pipelines to South Australia suggest that the appropriate geographic market for the purpose of our analysis may be state-wide.¹³

There appear to be few compelling reasons to favour narrower geographic markets distinguishing metropolitan and regional areas. It is not obvious that an energy retailer supplying customers in metropolitan areas would be unable to switch supply to rural or regional areas in response to price signals (and vice versa). Indeed, the main cost components of a retail business are the cost of wholesale energy supply and network tariffs. In South Australia electricity network tariffs are geographically averaged so that retailers bear no additional network costs when supplying customers in rural or regional areas. There are also no substantial differences in the cost of acquiring wholesale electricity supplies for delivery to rural areas versus metropolitan Adelaide.¹⁴

In the case of gas, wholesale costs are likely to be influenced by whether gas is sourced from Moomba, via the Moomba to Adelaide pipeline, or from basins in Victoria, via the SEA Gas pipeline. Given the location of these gas basins, the transmission pipelines that connect them to South Australia and the distribution networks that are connected to these pipelines, it is reasonable to suggest that the majority of gas that is supplied to regional areas west of Adelaide is likely sourced from Moomba whereas gas supplied to customers in the south east of South Australia is likely to be sourced from gas producers in Victoria. Gas supplied in metropolitan Adelaide and the regional areas located relatively close to Adelaide may be sourced from either Moomba or Victoria.

Despite the fact that there may be some limited substitutability in gas supplies between the far east and west of South Australia, this does not imply that there are separate markets for the sale of gas to metropolitan Adelaide and each regional area. Rather, it implies that gas retailers are able to supply both metropolitan and regional customers, but some may only be capable of supplying a subset of regions within South Australia.

On balance, we have reached the view that the relevant geographic markets are most likely state-wide. We note that this conclusion is consistent with that of the ESC in its 2004 review of the effectiveness of energy retail competition.¹⁵

Notwithstanding the appropriateness of a state-wide market, there may nonetheless be some instances where it is useful to examine the relativities of the effectiveness of competition within narrower geographic areas. It may be particularly instructive to identify sub-markets where competition between retailers appears to be ineffective, with a view to better understanding the reasons why. Accordingly, throughout this report we take the geographic

¹³ It should also be noted that French J did not accept a state-wide electricity market definition in the AGL case and rather adopted a NEM-wide geographic market for the supply of electricity. In this regard, the interconnectedness of state energy markets, and the fact that a number of energy businesses conduct retailing activities in more than one jurisdiction may have implications for the competitiveness of the South Australian retail market. However, for tractability purposes and for the practical reasons outlined above we will focus only on South Australian markets in this analysis.

¹⁴ We do note that cost differences are likely to exist for the supply of gas, where the cost that a retailer faces relative to other competitors for supply to regional areas depends on whether gas is sourced from Moomba or from gas basins in Victoria.

¹⁵ ESC “*Special Investigation: Review of the Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity – Background Report*”, June 2004, p.33.

bounds of the relevant markets to be South Australia-wide and assess the differential impact of competition within metropolitan Adelaide and rural and regional South Australia separately where relevant.

4.4. Summary of Relevant Markets

To summarise, we consider there to be two relevant markets for the purpose of this analysis:

- § the market for electricity retailing services for residential and small business customers in South Australia; and
- § the market for gas retailing services for residential and small business customers in South Australia;

Regardless of these market definitions, in certain parts of the subsequent analysis we consider the extent to which competition is effective for particular customer groups, defined either by customer type, geographic location or income level.

5. Market Structure

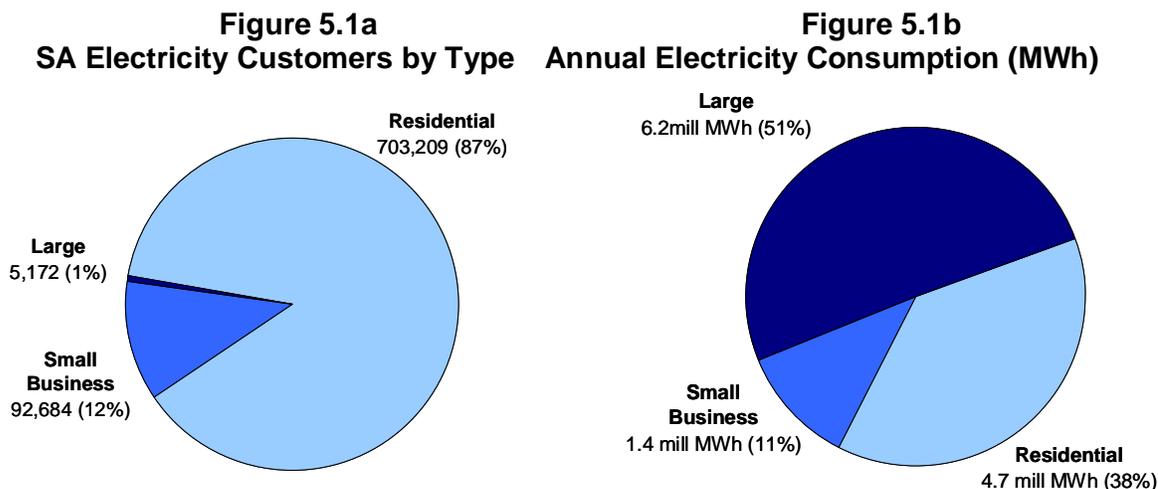
This section considers the structure of the South Australian electricity and gas retail markets, including the:

- § number and type of electricity and gas customers and their relative consumption;
- § number of retailers;
- § history of entry, exit and consolidation of retailers that supply energy to small customers since the introduction of FRC and the extent to which these retailers are vertically integrated;
- § market share of retailers and the level of market concentration; and
- § strength of barriers to entry.

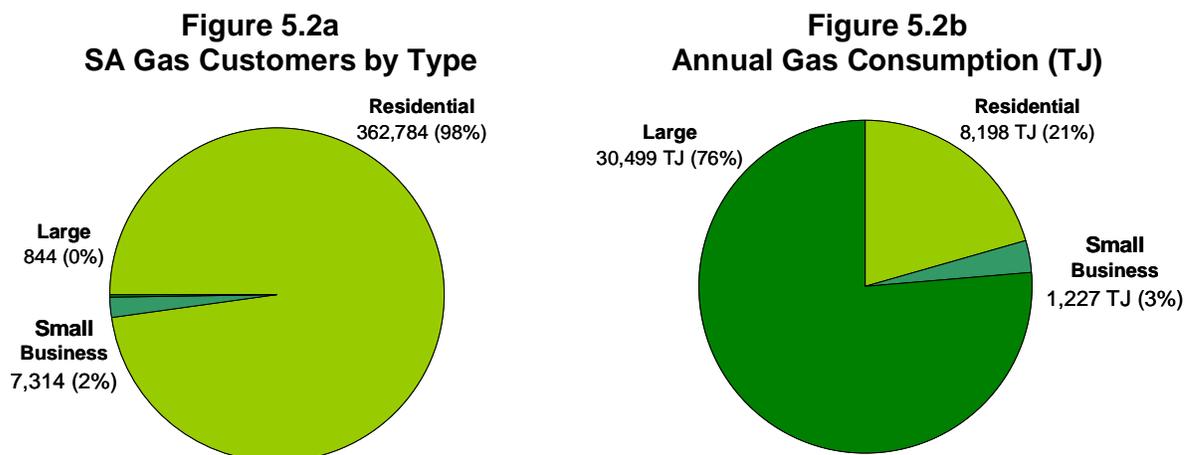
5.1. Number and Type of Customers

There were approximately 801,000 electricity and 371,000 gas customers in South Australia as at 31 December 2006, with total annual consumption of approximately 12.3 million MWh and 40,000 TJ respectively.¹⁶

The breakdown of electricity and gas customers into residential, small business and large customers and the relative annual consumption of each is set out in figures 5.1 and 5.2 below.



¹⁶ We note that it is possible that total customer numbers are overstated due to the change in the methodology for reporting customer numbers under the Commission's Guideline No. 2. Prior to June 2006 customers number were recorded as the number of National Metering Identifier's (NMI's) (electricity) or Meter Identification Registration Number's (MIRN) (gas) allocated to each retailer. From July 2006 customer numbers have been reported as the number of NMI's or MIRN's billed in the relevant quarter. This may have resulted in some customers being double counted in the quarters ended 30 September 2006 and 31 December 2006 following the transfer process, where bills were issued for the same NMI or MIRN by both the old and new retailer in the same quarter.



Source: Guideline 2 Reporting Data from ESCOSA as of December 2006.

Notes: Residential and small business customers are classified as those that consume less than 160MWh of electricity or 1TJ of gas per annum. All customers that consume more than this are classified as large customers.

Approximately 99 per cent of all electricity and gas customers in South Australia are small customers, although these customers account for only 49 per cent of total electricity and 24 per cent of total gas consumption respectively. Most if not all gas customers also have an electricity connection. Of all residential electricity customers, approximately 52 per cent also have a gas connection but of all small business electricity customers, only 8 per cent have a gas connection.

5.2. Number of Retailers

There are currently eighteen licensed energy retailers in South Australia, of which sixteen are licensed to supply electricity and seven are licensed to supply gas. All but two retailers that are licensed to supply gas also have a licence to supply electricity. There are currently one electricity and two gas retail licence applications in progress, for EnergyOne and Momentum Energy. EnergyOne is a prospective new entrant and intends to retail electricity and gas to residential and small business customers. Momentum Energy already retails electricity and intends to commence the supply of gas to both small and large customers across South Australia.

Of the sixteen licensed electricity retailers, twelve are active participants in the market. Only ten of these currently provide services to residential and small business customers. One of these (Aurora Energy) supplies residential customers in metropolitan Adelaide only and another (South Australia Electricity) supplies both residential and small business customers in metropolitan Adelaide only. Of the seven licensed gas retailers only five are actively supplying customers in South Australia, with all but one of these supplying residential and small business customers. Of the four gas retailers actively supplying small customers, at least two (AGL and TRUenergy) do not supply customers in regional areas.

Table 5.1 below lists all licensed energy retailers in South Australia and identifies those retailers that are currently active and those that currently supply residential and small business customers.

Table 5.1
Current Electricity and Gas Retailers

Retailer	Electricity			Gas		
	Licensed	Active	Selling to Small Customers	Licensed	Active	Selling to Small Customers
AGL South Australia ¹	ü	ü	ü	ü	ü	ü
Aurora Energy	ü	ü	ü	ü	ü	ü
Country Energy	ü	ü	ü	ü	ü	ü
EA - IPR Retail Partnership ²	ü	ü	ü	ü	ü	ü
Flinders Power ³	ü	ü	ü	ü	ü	ü
International Power (Retail)	ü	ü	ü	ü	ü	ü
Jackgreen (International)	ü	ü	ü	ü	ü	ü
Momentum Energy	ü	ü	ü	ü	ü	ü
Origin Energy Electricity	ü	ü	ü	ü	ü	ü
Origin Energy Retail ⁴	ü	ü	ü	ü	ü	ü
Powerdirect Australia ⁵	ü	ü	ü	ü	ü	ü
Powerdirect ⁵	ü	ü	ü	ü	ü	ü
Red Energy ⁶	ü	ü	ü	ü	ü	ü
Santos Direct	ü	ü	ü	ü	ü	ü
South Australia Electricity	ü	ü	ü	ü	ü	ü
Sun Retail	ü	ü	ü	ü	ü	ü
TRUenergy ⁷	ü	ü	ü	ü	ü	ü
TRUenergy Yallourn	ü	ü	ü	ü	ü	ü
Total	16	12	10	7	5	4

Sources: Information provided by ESCOSA. **Notes:** (1) SA standing contract retailer for electricity. AGL only supplies gas to residential and small business customers in metropolitan Adelaide but does not intend to supply small customers in all regional areas in 2006/07 (2) Partnership between Energy Australia and IPower. EnergyAustralia (3) Flinders Power Holdings GmbH, Flinders Labuan (No.1) Ltd, Flinders Labuan (No.2) and Flinders (4) SA standing contract retailer for gas (5) Powerdirect is a wholly owned subsidiary of Powerdirect Australia. (6) Red Energy only recently became an active retailer and is currently marketing to residential and small business customers, although we are unsure as to whether it currently supplies any such customers (7) TRUenergy does not currently supply or intend to supply residential or small business gas customers in regional areas west of Adelaide (Whyalla and Port Pirie) or those in South East South Australia (Mt Gambier and Riverland).

5.3. History of Entry, Exit, Consolidation and Vertical Integration

Table 5.2 below shows the number of electricity and gas retailers actively supplying residential and/or small business customers in November of each year from 2003 to 2006.

Table 5.2
Energy Retailers Supplying Small Customers, 2003 - 2006

Year	Active Retailers	No
Electricity		
2003	AGL SA, Origin Energy Electricity, TXU/SPI Electricity (TRUenergy) ¹	3
2004	AGL SA, EnergyAustralia, Origin Energy Electricity, Powerdirect Australia, TXU/SPI Electricity (TRUenergy)	5
2005	AGL SA, Country Energy, EA – IPR Partnership ² , Origin Energy Electricity, Powerdirect Australia, TRUenergy	6
2006	AGL SA, Aurora Energy, Country Energy, EA – IPR Partnership, Momentum Energy, Origin Energy Electricity, Powerdirect, Red Energy, South Australia Electricity, TRUenergy	10
Gas		
2004	AGL SA, EnergyAustralia, Origin Energy Retail, TXU/SPI Electricity (TRUenergy)	4
2005	AGL SA, EA – IPR Partnership ² , Origin Energy Retail, TRUenergy	4
2006	AGL SA, EA – IPR Partnership, Origin Energy Retail, TRUenergy	4

Source: Information supplied by ESCOSA *Notes:* (1) Eastern Energy was issued a licence on 11 October 1999 and has since varied its name to TXU Electricity, SPI Electricity and more recently TRUenergy due to continued acquisitions (2) EnergyAustralia and IPower entered into a partnership arrangement and obtained an electricity and gas retail licence in June 2005, at which time EnergyAustralia transferred all of its small customers to the new entity.

The number of electricity retailers actively supplying small customers in South Australia has grown from 3 to 10 since the introduction of FRC in 2003. More than half of the new electricity retailers entered in 2006. In contrast to electricity, the number of active retailers in the gas market has remained stable since the introduction of FRC in 2004. No retailers have discontinued supplying small customers over the four years to 2006. Most energy retailers in South Australia also supply customers in other states, or alternatively, belong to a parent company that has other subsidiaries which operate in other states.

A number of the South Australian energy retail businesses that supply small customers have changed ownership or entered into partnerships over the last four years, although this has not resulted in a reduction in the number of suppliers, with the exception of AGL's recent acquisition of Powerdirect Australia in February 2007.¹⁷ We note that the proposed

¹⁷ Powerdirect still supplies small customers in Australia under its own retail licence but is now owned by AGL. The potential for competitive rivalry between the two retail arms of AGL will therefore be limited going forward, thus, AGL and Powerdirect should be considered a single entity for the purpose of future reviews of competition.

merger between AGL and Origin that was considered earlier this year would have resulted in a substantial change in the market had there been a consolidation of the retail arms of these two entities.¹⁸

Four retailers, being TRUenergy, International Power (partnered with EnergyAustralia in EA-IPR Partnership), AGL and Origin, are vertically integrated with interests in electricity generation and gas production. These four retailers together account for approximately 70 per cent of South Australia's principal power station capacity.¹⁹ We note that AGL and TRUenergy have proposed a swap of their respective electricity generation interests in South Australia, which would substantially increase the extent of vertical integration of AGL. The ACCC does not intend to oppose this transaction, noting that it is unlikely to result in a substantial lessening of competition in the South Australian electricity retail market.²⁰

Origin has a limited interest in gas production facilities in the Cooper and Otway Basins which both supply gas to South Australia, although we note that other parties such as Santos and BHP Billiton have larger gas production interests in these areas. TRUenergy also owns the Iona gas storage facility in Victoria. Origin, TRUenergy and International Power each have an interest in gas transmission as owners of the SEA Gas pipeline that connects gas processing facilities in Victoria to customers in Adelaide. The APA Group has recently proposed to acquire Origin's one third share in this pipeline.²¹

¹⁸ Origin recently rejected AGL's merger proposal and AGL is reportedly no longer pursuing the transaction. If AGL and Origin were to enter into negotiations for the same or a similar transaction at some point in the future, as the two largest energy retailers operating in South Australia, this would likely have an impact on competition in the South Australian electricity and gas retail market. Given the size and interests of AGL and Origin, such a deal would likely be scrutinised by the ACCC.

¹⁹ TRUenergy owns Torrens Island Power Station, South Australia's largest electricity generation plant with total capacity of 1,280 MW. International Power (partnered with EnergyAustralia in EA-IPR Partnership) owns Pelican Point (478MW capacity), Dry Creek (156 MW), Mintaro (90 MW), Snuggery (63 MW) and Port Lincoln (50 MW). AGL owns the Hallet Power station (183MW) and Origin owns Quarantine (92 MW) and Ladbroke Grove (84 MW). Other generators that do not have retail interests for small customers include Flinders Power, which owns the second and fourth largest power stations in South Australia (Northern Power Station (530 MW) and Thomas Playford B (240 MW)), ATCO Power which owns a 185 MW plant at Osborne and Infratil Energy Australia which owns a 40 MW plant at Angaston. See ESSA, *'Electricity Gas Australia 2006'*, p.55.

²⁰ AGL and TRUenergy announced a proposed swap of their South Australian electricity generation interests on 2nd February 2007. Under this arrangement AGL proposes to transfer its peaking gas-fired generator at Hallet to TRUenergy for \$117 million and acquire TRUenergy's Torrens Island generation facility, and all associated gas supply contracts and facilities, for \$417 million. Under the transaction, AGL will acquire a 10 year gas sales agreement of approximately 300 PJ which expires in 2017 as well as the majority of TRUenergy's haulage rights under the SEA Gas pipeline haulage contract. For further information in relation to this transaction see www.truenergy.com.au/About/News/News.xhtml?newsitem=176.

This transaction was considered by the ACCC for the potential impact it may have on competition within both the electricity generation and retail markets in South Australia. The ACCC announced that it would not oppose the proposed swap on 4 April 2007. The ACCC's Public Competition Assessment, which was published on 20th April 2007 can be found at www.accc.gov.au/content/index.php/ml/itemId/784137.

²¹ See Origin Energy news release, 'Origin Energy enters conditional sale agreement for its Networks business', dated 4 April 2007 at www.originenergy.com.au/news/news_detail.php?pageid=82&newsid=766.

5.4. Market Shares

Market share and market concentration measures are useful methods for assessing the degree to which one or more firms may be capable of exercising unilateral or collective market power. While market share and concentration analysis is generally a relatively straightforward process, for the purpose of this review it is necessary to consider the impact that standing contract price regulation has on these measures in both electricity and gas retail markets in South Australia.

Prior to the introduction of FRC all small energy customers were served by incumbent retailers AGL and Origin. Since these markets were open to competition, a number of customers have switched to market contracts. However, a large number of customers continue to be supplied under standing contracts. Given that the price at which services are offered under standing contracts is regulated by the Commission, a large market share does not necessarily indicate that incumbent retailers possess market power. Rather, a large market share could be indicative of customer inertia or may suggest that the margins allowed for under standing contract tariffs are not considerably different from that which would be expected in an effectively competitive market.

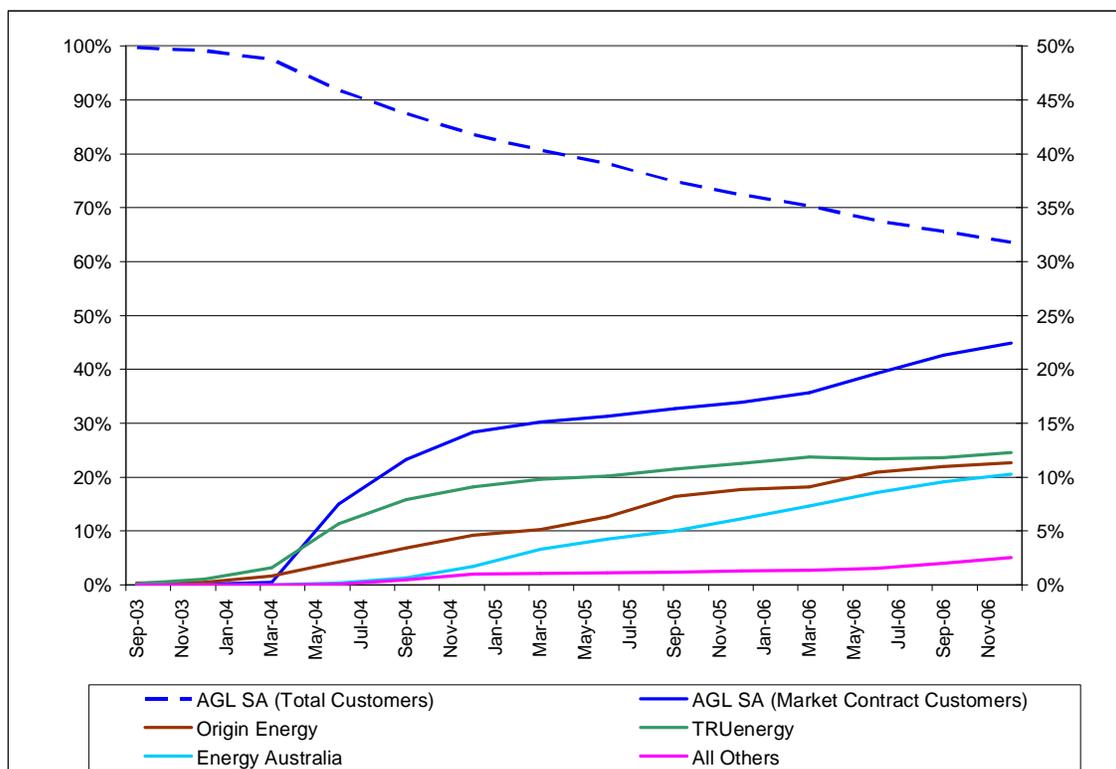
Given the extent to which retail price regulation is likely to influence the total market share of incumbent retailers, we have calculated market shares on the basis of both total customers supplied by each retailer and the total number of customers supplied by each retailer under market contracts only. We have also calculated market shares on the basis of consumption of energy. The results of this analysis are set out in Appendix A. We note that the market share analysis presented in Appendix A is not substantially different from that presented in the sections below.

The market shares of all South Australian electricity retailers for residential and small business customers for the period September 2003 to December 2006 is shown in figures 5.3 and 5.4 below.²² Note that for ease of illustration, the total market share of the incumbent retailer (represented by a dashed line) is measured against the axis on the left hand side of each figure, whereas the market shares of all new entrants and the incumbent, based on market contracts only (denoted by the unbroken lines), are measured against the secondary axis on the right hand side of the diagram.

AGL's market share for residential electricity customers has declined significantly from 100 per cent at the introduction of FRC to approximately 64 per cent in December 2006. The majority of AGL's customers are standing contract customers, which still comprise 41 per cent of all residential electricity customers.

²² Refer to footnote 16 for a discussion of the potential impact of the change in the method for recording customers from July 2006.

Figure 5.3
Market Share of SA Electricity Retailers for Residential Customers,
September 2003 - December 2006

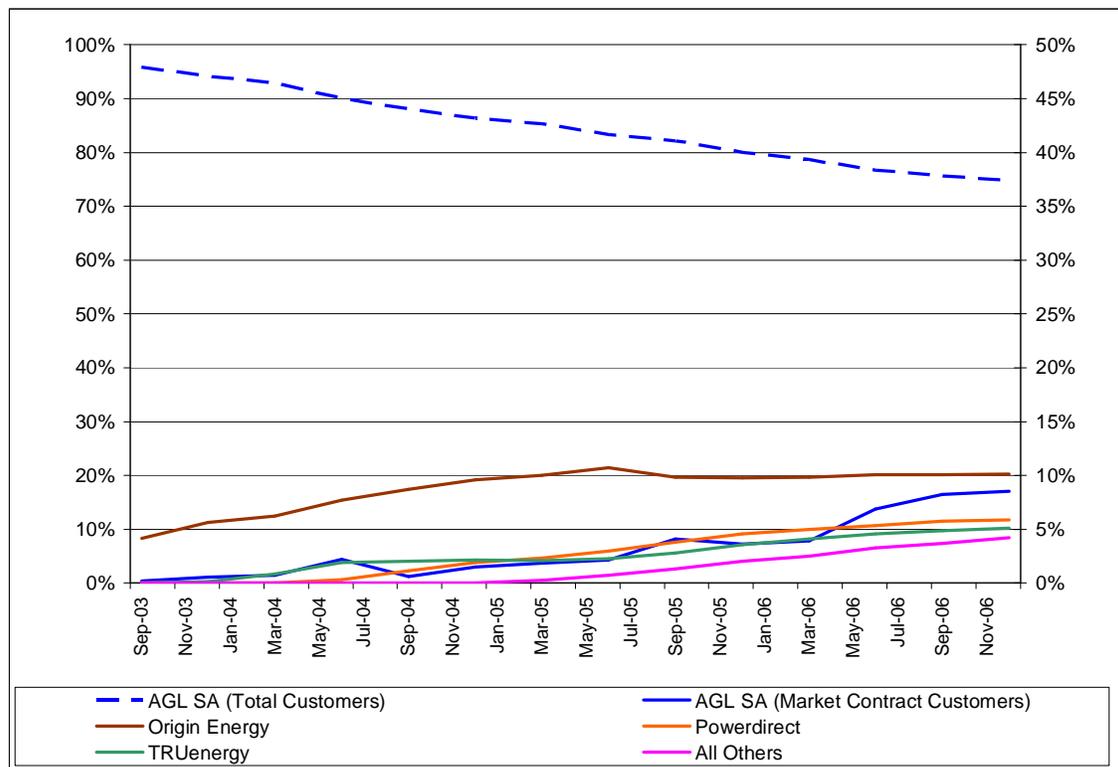


Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer number were recorded as the number of NMI's allocated to each retailer. From July 2006 customer numbers are reported as the number of NMI's billed in the same period. This may have an impact on the calculation of market shares as at 31 December 2006.

AGL has a higher share than other retailers of residential customers on market contracts, although we note that TRUenergy, Origin Energy and EnergyAustralia have each managed to attract 17 to 21 per cent of all market contract customers over the last three years (equal to 10 to 12 per cent of all residential electricity customers as at 31 December 2006 as shown in Figure 5.3).

We note that a number of AGL's market contract customers may be those pensioners and self-funded retirees that switched to market contracts over the period to August 2004 in response to the government's \$50 Electricity Transfer Rebate. We understand that these customers effectively transferred to a market contract with AGL at the same rates as the standing contract offered at the time. While the Commission estimates that these customers may potentially have represented around one third of all customers that transferred from an AGL standing to market contract in 2004, it is not possible to determine what proportion of AGL's current market contract customer base are those that switched in response to this government initiative. Since these customers entered into a contract of no fixed term, it is possible that a number of these customers may have switched to another retailer since 2004.

Figure 5.4
Market Share of SA Electricity Retailers for Small Business Customers,
September 2003 - December 2006



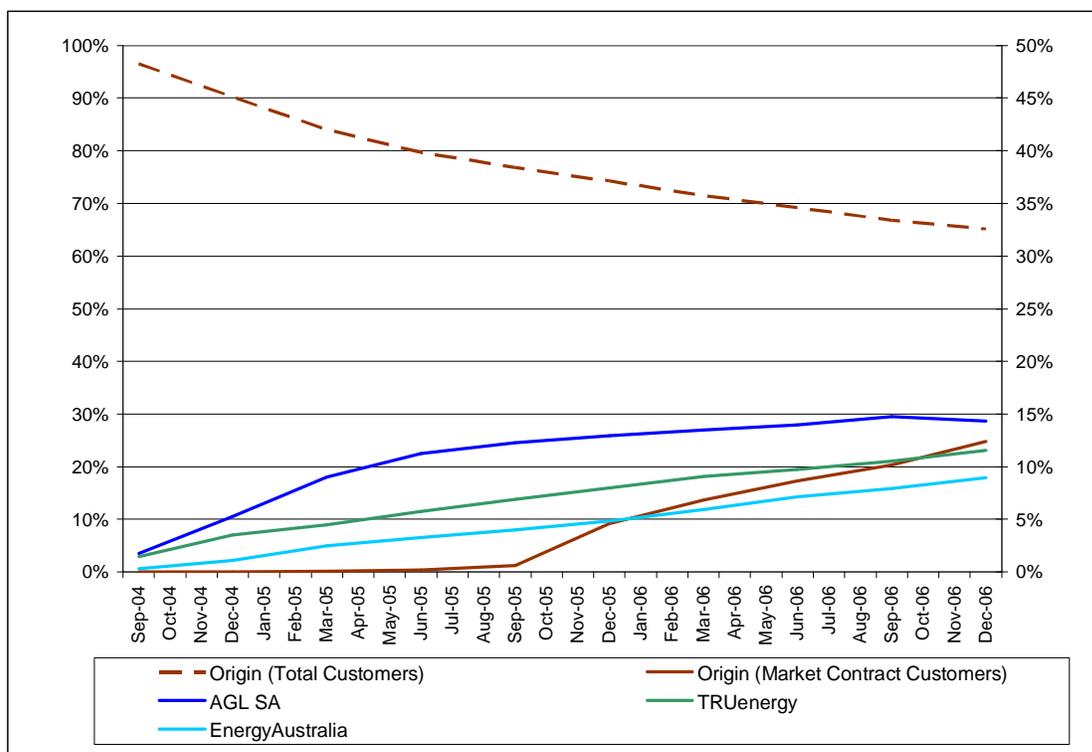
Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer number were recorded as the number of NMI's allocated to each retailer. From July 2006 customer numbers are reported as the number of NMI's billed in the same period. This may have an impact on the calculation of market shares as at 31 December 2006.

AGL's market share for small business electricity customers has also declined significantly over the last three years to approximately 75 per cent as at December 2006. The majority of small business electricity customers (66 per cent) are standing contract customers.

AGL's share of the remaining small business electricity customers under market contracts is considerably lower than that for residential customers at 25 per cent. Origin has a higher market share than AGL for these customers at around 30 per cent (or 10 per cent of all small business electricity customers as shown above) and Powerdirect and TRUenergy each have a market share of between 15 – 17 percent for these customers (or 5 – 6 per cent of all small business electricity customers as shown above). We note that AGL's share of small business customers on market contracts appears to have increased over the last year whilst the share of all other retailers has remained relatively stable.

As is the case for electricity, the market share of gas standing contract retailer, Origin Energy, has reduced since the introduction of FRC in 2004, as shown in figures 5.5 and 5.6 below.²³

Figure 5.5
Market Share of SA Gas Retailers for Residential Customers,
September 2003 - December 2006



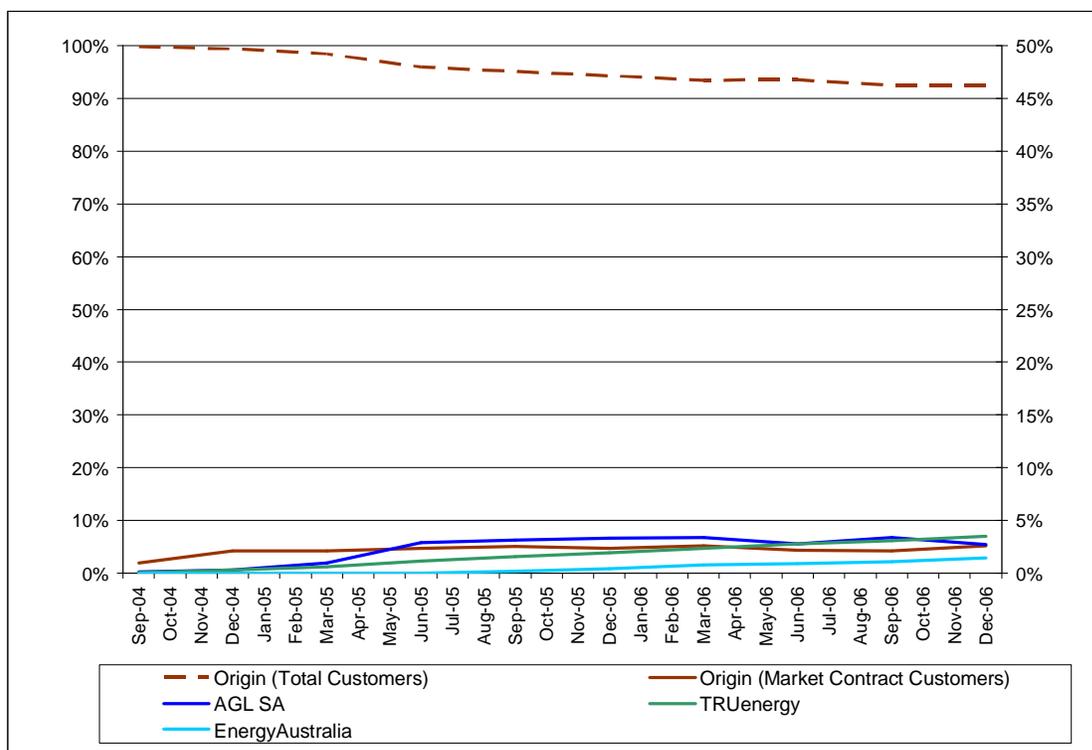
Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data *Notes:* In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer numbers were recorded as the number of MIRN's allocated to each retailer. From July 2006 customer numbers are reported as the number of MIRN's billed in the same period. This may have an impact on the calculation of market shares as at 31 December 2006.

Origin's market share for residential gas customers has fallen to 65 per cent to December 2006. Just over half (53 per cent) of all residential gas customers are standing contract customers. AGL has a higher share than other retailers of those residential gas customers on market contracts at 30 per cent (or 14 per cent of all residential gas customers as shown above) although Origin, TRUenergy and Energy Australia are not far behind at 26 per cent, 24 per cent and 19 per cent respectively (equal to 12 per cent and 9 per cent of all residential gas customers as shown above).

²³ We note that as was the case for electricity, it is possible that some customers may have been double counted resulting in inaccurate market share calculations due to the change in the methodology for reporting customer numbers under the Commission's Guideline No. 2 in June 2006. See footnote 16 for further detail.

We note that Origin only began to increase its share of residential gas customers under market contracts in September 2005. The increase in its share of these customers has been significant relative to that of other gas retailers over the period September 2005 to December 2006.

Figure 5.6
Market Share of SA Gas Retailers for Small Business Customers,
September 2003 - December 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data *Notes: In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer number were recorded as the number of MIRN's allocated to each retailer. From July 2006 customer numbers are reported as the number of MIRN's billed in the same period. This may have an impact on the calculation of market shares as at 31 December 2006.*

Origin's market share for small business gas customers has also fallen over the period to December 2006 but by a much smaller amount than its share of residential gas customers. The majority (90 per cent) of small business gas customers are standing contract customers.

Of those customers on market contracts TRUenergy has the highest share at 34 per cent (equal to only 3 per cent of all small business gas customers as shown above). AGL and Origin each have 26 per cent share and Energy Australia 19 per cent share of these customers (equal to 3 per cent and 1 per cent of all small business gas customers respectively as shown above).

Summary of Market Shares

In sum, market shares of incumbent retailers AGL and Origin and other new entrant retailers for each type of small energy customer in South Australia as at 31 December 2006 were as follows:

- § residential electricity customers – AGL has 64 per cent (41 per cent on standing contracts and 23 per cent on market contracts) and new entrant retailers 36 per cent;
- § small business electricity customers - AGL has 75 per cent (66 per cent on standing contracts and 9 per cent on market contracts) and new entrant retailers 15 per cent;
- § residential gas customers – Origin has 65 per cent (53 per cent on standing contracts and 12 per cent on market contracts) and new entrant retailers 35 per cent;
- § small business gas customers - Origin has 92 per cent (90 per cent on standing contracts and 2 per cent on market contracts) and new entrant retailers 7 per cent.

In addition to market shares we have also conducted an assessment of market concentration for both the electricity and gas retail markets. This analysis is set out in Appendix B. As expected, the analysis shows that both the electricity and gas retail market are still highly concentrated, although market concentration is falling over time as new entrant retailers continue to expand, particularly in the electricity retail market. We note that competitive outcomes can still be achieved in relatively concentrated markets with only a few suppliers, particularly where the number of players in the market is largely influenced by technical factors such as economies of scale. In order to determine whether such markets are effectively competitive it is necessary to consider the degree of rivalry between market participants through an assessment of market conduct. This analysis is set out in section 6.

5.5. Barriers to Entry or Expansion

A barrier to entry may be defined as any feature of a marketplace that places an efficient firm at a disadvantage relative to an incumbent firm.²⁴ Markets characterised by high barriers to entry have the potential to lead to competition concerns if there is scope for a single incumbent to exercise its market power or if a group of incumbent firms have the ability to co-ordinate their pricing behaviour. In the absence of the threat of new entry, incumbents may have an incentive to co-ordinate both their prices and product offerings in order to extract greater economic rents from consumers.

In order to pose an effective competitive constraint on incumbent firms, entry must be both likely and of sufficient magnitude to have an impact on the pricing and output decisions of incumbent firms. The possibility of entry alone is not enough to constrain the exercise of market power. Rather, entry must be likely in a commercial sense. Entry must also be of

²⁴ ACCC Merger Guidelines 1999, p.49.

the size that would cause market participants to react to a significant degree. As noted by the ACCC in its Merger Guidelines:²⁵

“The essential test for whether or not there is a significant barrier to entry can be expressed simply enough: it is whether the threat of entry of whatever kind will constrain incumbents to behave competitively... However we cannot speak of easy entry if the only viable entry is that which occurs on the fringe of the market in competition with that fraction of the incumbents’ business that has a high marginal cost; or if the only viable entry is of the fringe of products that fail to attack the incumbents’ core business. There must be, in Richard Schmalensee’s phrase, ‘real pressure on established firms’ profits’”

Barriers to entry or expansion may be structural, legal or strategic in nature. They include sunk costs, economies of scale and scope, restricted access to scarce resources, brand loyalty and the threat of retaliation by incumbents. A number of potential barriers to entry have been considered in previous reviews of the effectiveness of retail competition in other jurisdictions. These include:

- § potentially limited access to wholesale energy supplies and hedging products that allow retailers to protect against fluctuations in the price of such supplies;
- § costs associated with regulatory compliance, including differences across jurisdictions;
- § uncertainty over the long-term approach to retail price regulation and future energy prices for end-customers; and
- § incumbency advantages that were transferred upon the implementation of FRC, such as the existence of an established customer base.

As part of this review retailers were asked to complete a survey in which they were asked a number of questions on the perceived strength of several potential barriers to entry or expansion in electricity and gas retail markets in South Australia. A copy of this survey is set out in Appendix C. In the sections below we outline the overall responses to this survey and discuss in more detail those factors of greatest concern.

5.5.1. Retailer Survey Responses

The retailer survey was sent to 13 licensed energy retailers in South Australia and one potential new entrant retailer.²⁶ Responses were received from 9 of these retailers: AGL, Aurora Energy, Country Energy, Flinders Power, Jackgreen, Red Energy, SA Electricity, Origin Energy and TRUenergy.

As part of this survey, retailers were asked to rate, on a scale of 1 to 5, the strength of a number of potential barriers to entry or expansion, where a rating of 1 indicated that the

²⁵ ACCC Merger Guidelines 1999, p.50 as quoted from Professor Maureen Brunt (1992) ‘Australian & New Zealand Competition Law and Policy’, 19th Fordham Conference on International Antitrust Law and Policy.

²⁶ The retailers to whom the survey was delivered were AGL, Aurora Energy, Country Energy, Energy Australia (EA-IPR Partnership), EnergyOne, Flinders Power, Jackgreen, Momentum Energy, Powerdirect, Red Energy, SA Electricity, Santos Direct, Origin Energy and TRUenergy.

factor was not an issue and a rating of 5 indicated that the factor was a major issue impacting the retailer's ability to enter or expand in energy retail markets. Potential entry barriers were divided into three categories: structural barriers, regulatory barriers and incumbency advantages. The average, minimum and maximum rating given to each of these barriers is set out in table 5.3 below. There were significant variations in the response to this question with many factors receiving a minimum rating of 1 and a maximum rating of 5. On average, retailers considered the following barriers to entry or expansion to be the most significant in the South Australian retail markets:

§ access to adequate gas transmission and distribution services; and

§ regulatory barriers, including regulatory differences between jurisdictions, the extent of state regulation, regulatory uncertainty and standing offer price regulation.

**Table 5.3
Retailer Views on Strength of Barriers to Entry**

Barrier to Entry or Expansion	Electricity		Gas	
	Average	Min/Max	Average	Min/Max
Structural Barriers				
Access to energy supply at reasonable cost	2.4	1/5	2.8	1/5
Access to risk mitigation products (eg, hedging)	2.9	1/5	2.8	1/5
Access to adequate transmission and distribution services	2.5	1/5	4.4	4/5
Regulatory Barriers				
Extent of state regulation (eg, customer protection)	3.3	1/5	4.0	2/5
Regulatory differences between jurisdictions	3.6	2/5	4.0	2/5
Regulatory uncertainty	3.4	2/5	3.8	2/5
Standing offer price regulation	3.1	1/5	3.8	2/5
Incumbency Advantages				
Retailer brand awareness	3.0	1/5	2.2	1/4
Customer inertia	2.4	1/4	2.0	1/4
Access to sufficient customer data to make offers	2.3	1/4	2.0	1/4
Customer transfer process	2.8	1/4	2.6	1/5
Exit or termination fees for some customer contracts	2.8	1/4	2.4	1/4

Notes: All 9 retailers respondents rate the strength of each barrier for electricity, however only 6 respondents rate these barriers in relation to the gas retail market.

5.5.2. Structural Barriers

In order to effectively compete for retail customers, retailers must be able to source energy supplies at a reasonable cost, mitigate the risk of fluctuations in the price of such supplies and access transmission and distribution infrastructure to enable the transfer of energy to customers' premises.

5.5.2.1. Access to competitively priced wholesale energy supplies

Lack of access to competitively priced wholesale energy supply was not considered a significant issue by most respondents in either the electricity or gas retail markets, although we note that two of the six retailers that responded to this question in relation to gas supplies gave this factor a rating of four or five. It is our understanding that gas retailers may potentially face difficulties in accessing adequate wholesale supplies from Moomba for supply to the north western areas of South Australia given the level of gas reserves in the Cooper basin and the extent to which such reserves are already contracted. However, this issue was not specifically raised by any of the retailers that responded to the survey.

5.5.2.2. Access to risk mitigation products

Access to risk mitigation products was considered a significantly greater issue by some respondents, particularly in relation to electricity supplies.

Retailers may hedge against fluctuations in the electricity spot price through vertical integration into generation, which creates a natural hedge, and/or through the purchase of financial instruments. Some retailers were of the view that increasing vertical integration in the industry is reducing the number of parties that are willing to offer hedges, thereby reducing liquidity in the market to the detriment of non-integrated retailers. These retailers noted that the availability of competitively priced hedging products was not sufficient for them to effectively manage risk. Other retailers were of the view that competitively priced hedging products are available. One retailer noted that while it did not consider the availability of hedging products to be a significant barrier to further expansion in South Australia at the present time, it would be concerned by any further vertical or horizontal integration between generators and retailers.

In the case of South Australia specifically, the extent of vertical and horizontal integration between generation and retailing does not appear to have hindered entry by new retailers competing in the market for the supply of electricity to small customers. The most important factor in determining the availability of hedging products is likely to be the effectiveness of competition amongst both sellers of such products (ie, generators) and buyers (ie, retailers). While the three largest electricity retailers, AGL, Origin and TRUenergy, do have substantial generation interests in South Australia, there are a number of factors that suggest that this is not a significant barrier to entry or expansion, including:

- § there are three other generators in South Australia that do not retail electricity to residential customers, one of which (Flinders Power) owns both the second and fourth largest power stations in the state;

- § the generation interests of two vertically integrated retailers, AGL and Origin, are not sufficient to cover their retail load and so these firms are likely to be significant participants in the ‘market’ for risk management products;
- § as noted earlier, there have been several new entrants in the South Australian electricity retail market since the implementation of FRC, four of whom entered in 2006 - access to hedging products does not appear to have deterred such new entry; and
- § a number of new entrant retailers have indicated that access to hedging products has not impeded their ability to expand in South Australia, and in some instances have advised against interventionist mechanisms to address gaps in liquidity.²⁷

While access to adequate hedging products does not appear to have hindered new entry by a number of electricity retailers over the last two years, it is important to note that a study recently commissioned by the Energy Reform Implementation Group (ERIG) found that there was a lack of liquidity and depth in such products in South Australia.²⁸ In particular, the level of trade in both over the counter and exchange traded instruments listed on the Sydney Futures Exchange was lower in South Australia than in other states. In response to this ERIG suggested that a mechanism be developed to facilitate trading in South Australia, although noted that it had not had time to address the area in any detail.

Whether or not the trend toward increased vertical integration has the potential to raise barriers to entry in future and potentially impede the ability of non-vertically integrated retailers to compete remains to be seen. However, it does not appear that the most recent developments in South Australia have been of some concern to the ACCC.

For example, in giving competition clearance to the proposed swap of AGL and TRUenergy’s generation assets in South Australia,²⁹ the ACCC gave specific consideration to the effect the transaction would likely have on the ability of South Australian electricity retailers adequately to manage their risk profile by entering into appropriate hedge contracts. While the ACCC acknowledged the concerns raised by interested parties that there is poor liquidity in the market for electricity derivatives in South Australia, particularly in comparison to other regions in the NEM, it considered it unlikely that the transaction would lead to a material long term decrease in the availability of hedge products in South Australia. The ACCC noted that it did not appear that the transaction would significantly raise barriers to entry for retailing when compared to the likely scenario were the

²⁷ For example, in its submission to ERIG in response to ERIG’s discussion paper, Powerdirect noted that although liquidity levels are not directly comparable to other speculated securities, the suite of products available to participants has been increasing over time. Powerdirect were of the view that ‘rather than introducing interventionist mechanisms to redress any ‘gaps’ in liquidity or the depth of products, financial market liquidity should be encouraged through an increased integration of transmission network services with electricity markets’. See Powerdirect submission at www.erig.gov.au. We note that Powerdirect was subsequently acquired by AGL.

²⁸ ERIG, ‘Energy Reform: The way forward for Australia’, A report to the Council of Australian Governments by the Energy Reform Implementation Group’, January 2007, p.220. ERIG engaged KPMG to assist in examining the electricity trading market and the impediments to its development.

²⁹ This transaction will better align each of AGL and TRUenergy’s retail and generation interests by providing AGL with a larger share of generation in South Australia.

transaction not to proceed, and that it appeared unlikely there would be a substantial lessening of existing competition in the South Australian retail market.³⁰

5.5.2.3. Access to adequate transmission and distribution services

Another factor that was considered as a significant barrier to entry by survey respondents was access to adequate transmission and distribution services for the supply of gas. All of the six respondents that rated this factor in relation to the gas retail market gave it a rating of 4 or above.

Gas is delivered to South Australia from the Moomba gas processing plant in the Cooper/Eromanga Basin via the Moomba to Adelaide pipeline (MAPS) and gas processing facilities in the Otway Basin via the SEA Gas pipeline. Firm pipeline capacity of the MAPS was fully contracted until December 2005, although we note that in addition to Origin, AGL and International Power each had haulage contracts along the pipeline at this time. We understand that several haulage contracts along the MAPS have since expired and firm capacity is now available on this pipeline. While this has eased a constraint that may have existed before 2006, new entrant retailers may encounter difficulties in accessing firm supplies from gas producers at Moomba due to declining reserves. There may therefore be no better opportunity to offer firm gas supplies to small customers due to the removal of constraints along this transmission pipeline.

Capacity on the SEA Gas pipeline is currently fully contracted by Origin, TRUenergy and International Power under foundation shipper agreements. These agreements will remain in place until 2019. Interruptible capacity is available on the SEA Gas pipeline, although new entrant retailers would not be able to offer a firm supply of gas to residential and small business customers if they were unable to negotiate firm supplies from both gas producers and the operators of SEA Gas.

In addition to problems in obtaining firm gas supplies from Moomba and firm capacity along the SEA Gas pipeline, four retailers cited problems in obtaining adequate access to the gas distribution network and to laterals off the MAPS as a major impediment to entry and expansion in the supply of gas to retail customers in South Australia. There are four issues which are relevant to this point.

First, Origin is responsible for the operation and management of Envestra's distribution network through Origin Energy Asset Management (OEAM). Among other things, OEAM manages the haulage of gas through the network, operates and maintains the network, plans, designs and constructs network extensions, reads meters and bills retailers. While Envestra negotiates third party access with retailers, OEAM assists in this process. The potential involvement of Origin in access negotiations may in some circumstances deter new retailers from approaching Envestra for access. To the extent this currently represents a barrier to

³⁰ See the ACCC's Public Competition Assessment dated 20 April 2007 at www.accc.gov.au/content/index.phtml/itemId/784137/fromItemId/751046.

We note that in addition to the impact of the transaction on the availability of hedging products, the ACCC also considered the effects of the transaction, if any, on TRUenergy's ability and incentive to compete vigorously as a retailer of electricity in South Australia.

entry, we note that it is likely to be alleviated by the proposed sale of OEAM to the APA Group.³¹

Second, the design of Envestra's distribution network and the location of connection points to the distribution network from MAPS and SEA Gas pose problems for retailers in accessing customers in the north of Adelaide using the SEA Gas transmission pipeline. We understand from the Commission that Envestra's distribution network is designed to transport gas from north to south and that capacity constraints limit the flow of gas delivered via SEA Gas to the northern suburbs of Adelaide. In particular, we understand that it is not currently possible for a retailer to provide a firm service to customers in northern Adelaide via the SEA Gas pipeline because Envestra cannot guarantee the delivery of gas from the SEA Gas Cavan City gate station to customers in the north of the state.³² While this issue may be alleviated to some extent with the planned construction of another gate station at Elizabeth, expenditure for which was provided for in Envestra's access arrangement, this will not allow for the unconstrained flow of gas from SEA Gas to northern Adelaide. This effectively means that retailers must enter into contractual arrangements for the supply of gas from Moomba to develop a substantial presence in northern Adelaide.³³

Contractual arrangements in relation to the control of capacity at gates that connect the MAPS with Envestra's distribution network may be another factor that has the potential to impede new entry for supply to South Australia, particularly north Adelaide. In its submission to the Commission in the context of its 2006 review of Envestra's gas access arrangement, TRUenergy noted that Origin then held a monopoly over the three MAPS City Gates but that this situation was due to expire in December 2005.³⁴ In December 2005 the National Competition Council also noted that Origin had fully contracted access to 21 of the 25 gate stations through which gas is transferred off the MAPS and into the metropolitan and regional distribution systems, including the gates at Angaston, Port Pirie and Whyalla.³⁵ To the extent that Origin has retained control of these City Gates, such arrangements may deter new entry, not only through the perceived risk that access might not be granted on reasonable terms but also due to the information advantage that such control provides Origin. We note that none of the retailers surveyed addressed this issue in any detail. It therefore may not be considered a significant impediment to new entry by new retailers.

Last of all, we understand that Origin has pre-existing capacity rights on both the Port Pirie/Whyalla and Angaston laterals that connect to the MAPS and that firm capacity on

³¹ See Origin Energy news release, 'Origin Energy enters conditional sale agreement for its Networks business', dated 4 April 2007 at www.originenergy.com.au/news/news_detail.php?pageid=82&newsid=766

³² See TRUenergy submission re Envestra's Access Arrangements for the South Australian Gas Distribution System at www.escosa.sa.gov.au/site/page.cfm?u=135&t=submissionsXList&xlistId=32.

³³ Note that TRUenergy is the only retailer that currently does not transport gas from Moomba along the MAPS. Each of Origin, AGL and EA-IPR Partnership has a presence in the northern suburbs of Adelaide.

³⁴ See TXU Submission dated 15 March 2005 at www.escosa.sa.gov.au/site/page.cfm?u=135&t=submissionsXList&xlistId=32

³⁵ See NCC, 'Application for revocation of coverage of the Moomba to Adelaide Pipeline System under the National Access Regime, Final Recommendation', 14 December 2005, p.65.

these laterals is either not available to other retailers or not available in sufficient quantities to supply regional customers. Given that it is not viable to supply residential and small business customers with interruptible supply, at least not on a large scale, this could represent a barrier to entry for supply to regional areas in the north of the state. While the gas code provides for the trading of capacity rights, the holders of such rights are under no obligation to relinquish capacity to new entrants, even if a certain level of contracted capacity is not being utilised. To the extent that this is the case, it is possible that the holder of capacity rights could effectively exclude other retailers from particular geographic areas.³⁶ We note that regional customers served by the Port Pirie/Whyalla and Angaston laterals represent only a small proportion of all gas customers in South Australia and that the inability to access these customers due to the lack of available firm capacity is unlikely to pose a significant barrier to entry to the South Australian gas retail market as a whole.³⁷

In addition to concerns regarding access to the gas transmission and distribution network, respondents noted that the need to enter into various contractual arrangements with various entities along the gas supply chain was a factor that makes entry into the gas retail market relatively difficult.

On the above analysis, we conclude that structural barriers in gas retail markets may be material given the problems that retailers have cited in gaining access to certain pipelines in the north of the state and into northern Adelaide. However, while this represents a clear constraint on this geographic segment of the market, its implications for the remainder of the gas retail market remains unclear.

5.5.3. Regulatory Barriers

Behind access to gas transmission and distribution services, retailers considered regulatory barriers to be the most important potential barriers to entry or expansion in both the electricity and gas retail markets. Potential regulatory barriers include the cost of meeting obligations under state regulations³⁸, differences in regulatory arrangements and regulatory reporting requirements between different jurisdictions, uncertainty around the approach to retail price regulation and insufficient margins under regulated standing contracts.

While regulatory barriers were given an average rating of between 3 and 4 for the electricity market and around 4 in the gas market, only a few retailers provided further information on the reasons why they considered these to be significant barriers. Of those specific comments received:

³⁶ Note that for this to represent a material barrier to entry, the incumbent would need to acquire and hold significantly more capacity than it in fact required, and the cost to it of doing so would need to be outweighed by the competitive advantage it would achieve in other parts of the market.

³⁷ In its final recommendation in relation to the application for the revocation of coverage of the MAPS, the NCC noted that the capacity along the Port Pirie/Whyalla lateral that is not contracted to the largest industrial user (approximately 6 terajoules per day) represents approximately 2 per cent of all South Australian demand. Demand along the Angaston lateral represented approximately 3 – 4 per cent of total South Australian demand. See NCC, *Application for revocation of coverage of the Moomba to Adelaide Pipeline System under the National Access Regime, Final Recommendation*, 14 December 2005, para 6.96, p.64.

³⁸ Note that the obligation to abide by state regulations may not be a barrier to entry if the costs that must be incurred by the incumbent in abiding by such regulations are the same as that incurred by new entrants.

- § one retailer in noted that there is a significant amount of regulatory uncertainty as a result of the national market reform process and the transition from state-based regulation to a national approach;
- § one retailer suggested that the development of the national ‘do not call’ register has added additional complexity to marketing activities and has required a shift in retailer’s focus from telephone sales to more expensive door-to-door marketing activities; and
- § one retailer noted that the requirement for concession holders to reapply for a concession upon switching retailers is an impediment to switching for these customers.

We note that uncertainty over future regulatory arrangements may pose a barrier to new entry although this will be somewhat alleviated when the AEMC makes its recommendations on the need for continued regulation of retail prices later this year and the Ministerial Council on Energy (MCE) reveals its 2007 legislative package containing its recommendations for the national distribution and retail regulatory functions. Given that the aim of the AEMC’s review is to determine whether retail price controls should be removed, as opposed to whether they should be strengthened, it is unlikely that uncertainty over the approach to future regulation currently represents a significant barrier to new entry in South Australia. While it is possible that some potential new entrant retailers may be deterred from entering until the AEMC’s review has been finalised, this does not appear to have been a significant factor for the four retailers that entered the South Australian electricity retail market within the last year.

In relation to the development of the national ‘do not call register’, this is not likely to represent a barrier to entry if incumbent retailers are also required to engage in direct forms of marketing to attract or retain customers. On the suggestion that the need for concession holders to reapply for a concession if they choose to switch retailer may provide incumbent retailers with some advantage in retaining these customers, we note that they comprise only 30 per cent of all residential customers in South Australia, and so it is unlikely that this would significantly deter entry in the retail market for small customers as a whole. Even if some concession customers are dissuaded from switching as a result of this administrative burden, it is not clear that retailers would not have an incentive to enter with the aim of competing for other types of customers if retail margins were sufficient. It may, however, place an upper limit on retailer expansion, so long as the perceived cost of reapplying for a concession continued to outweigh the price benefits these customers could obtain by switching to a market contract. An assessment of each retailers’ share of concession recipients as set out in section 7.4.1 of this report suggests that this is not the case.

In our view, there is little evidence to suggest that regulatory barriers are significant in either the electricity or gas retail markets in South Australia. All retailers are required to comply with state regulations and we are not aware of any reasons that would suggest that new entrants face higher compliance costs than incumbents. Regulatory uncertainty may potentially deter some new entrant retailers, although such uncertainty is likely to exist at some level in any regulated market. Given recent entry in the electricity retail market, this does not appear to have been a significant factor in South Australia.

5.5.4. Incumbency Advantages

Incumbent retailers AGL and Origin likely face some advantages relative to new entrant retailers by virtue of their established customer base and their stronger brand awareness in the market. First, there is likely to be a proportion of customers for whom the perceived cost of switching, in terms of the time and effort required to investigate options and/or arrange to change retailer, is greater than the monetary benefit they would derive if they were to switch to a market contract with a new retailer. These customers could be expected to remain on standing contracts with their incumbent retailer until the discounts provided under market contracts are sufficiently large to encourage them to switch. Such customer inertia is of benefit to the incumbent since it is better able to retain such customers for whom it faces less pricing pressure. However, we note that incumbents likely face difficulties in identifying their less price sensitive customers and may ultimately encourage them to switch through the offer of discounted market contracts that meet customers' pricing thresholds.

Second, incumbents are also potentially in a better position than other retailers to attract more price sensitive customers to market contracts. As standing retailers, AGL and Origin have greater access to information in relation to customer usage patterns that allow them to identify more profitable customers and better market their offers to these customers. It is also possible that customers perceive switching to a market contract with their current retailer to be less of an administrative burden than switching to a new retailer.

We note that incumbency advantages were not rated highly by respondents as barriers to entry in either the electricity or gas retail markets, with each of these factors receiving an average rating of 3 or less. However, a significant number of customers, particularly small business customers, have either remained on standing contracts or have switched to market contracts with the incumbent retailer. To the extent that AGL and Origin make a profit on the sale of energy to these customers, this suggests that they do face some advantage over other retailers. However, this advantage does not appear to have been substantial enough to have deterred new entry, particularly in the electricity retail market.

Finally, we note that it is likely that any incumbency advantages will reduce further over time as customers continue to move from standing to market contracts and those that switched to two or three year market contracts with AGL or Origin at the early stages of FRC come to the end of their contract term.

5.6. Summary

Our review suggests that the structure of the electricity and gas retail markets in South Australia differ in terms of the extent to which they are conducive to effective competition between market participants.

The small customer electricity retail market appears to be characterised by low barriers to entry as evidenced by the fact that nine retailers have entered the market since the implementation of FRC in January 2003. Most of these new entrants supply residential and small business customers in both metropolitan Adelaide and regional areas and have increased their collective share of these customers to around 36 per cent and 25 per cent respectively over the last four years.

While AGL has a higher share than other retailers of residential customers on market contracts, TRUenergy, Origin Energy and EnergyAustralia/EA-IPR Partnership each have between 17 and 21 per cent share of these customers, suggesting that AGL is likely constrained in the price it can currently charge those customers that are aware of the fact that they can choose their own supplier and are willing to switch. In fact, AGL's high share of market contract customers may overstate the advantage that AGL has relative to other retailers at the present time given that a significant number of AGL's market contract customers may be those pensioners and self funded retirees that switched over the period to August 2004 in response to the Government's \$50 Electricity Transfer Rebate. We understand that these customers effectively transferred to a market contract with the same rates as the standing contract and therefore may not have been aware of the potential savings they could have made by moving to a market contract with another supplier. While it is not possible to determine what proportion of AGL's current market contract customer base are those that switched in response to this government initiative, the fact that many of these customers are likely still to have contracts with AGL suggests that AGL's share of market contract customers overstates any advantage that AGL may currently have in attracting customers that are responding to the competitive pressure imposed by new entrant retailers.

It is important to note that even though the market share of all other retailers has remained below 5 per cent since the introduction of FRC, most of these retailers only entered the market during 2006. The current competitive constraint imposed by these retailers is therefore not likely to be reflected in their current market share.

New entrant retailers appear to have made less headway in attracting small business electricity customers to market contracts. Incumbent retailer AGL also has a much lower share of small business customers on market contracts compared to its equivalent share for residential customers. Given that most electricity retailers that have entered the South Australian market supply both residential and small business customers, it is not immediately obvious why retailers have not implemented more aggressive expansion plans for this customer segment or alternatively, why small business customers have tended not to switch to market contracts.

Barriers to entry in the gas retail market appear to be significantly higher than those for electricity, with retailers citing inadequate access to transmission and distribution services to be the major barrier to entry or expansion in this market. This is consistent with the more limited entry that has occurred in this market since the implementation of FRC in 2004 and the fact that at least two of the four gas retailers currently supplying small customers do not supply customers outside metropolitan Adelaide.

However, high barriers to entry in and of themselves do not necessarily mean that competition between market players will be ineffective. As noted above, competition between only a few market participants in markets characterised by structural or technical barriers to entry can be vigorous depending on the conduct of participants within these markets.

Trends in retailer shares of residential gas customers are similar to that for electricity, with all three new entrant retailers each having attained a 9 to 12 per cent share of these customers over the last two and a half years. While incumbent retailer Origin currently has

a lower share of market contract customers than AGL, its share of these customers has grown at a significantly higher rate than other retailers over the last year as standing offer customers switch to market contracts with the same retailer. It is unclear whether this movement to market contracts is being led by Origin, with or without the provision of significant inducements for customers to switch, or by customers who may be actively investigating their options for alternative supply.

The large proportion of small business gas customers still on standing offer contracts suggests that competition for these customers has not been particularly vigorous, with new entrant retailers having attracted only 7 per cent of these customers between them. Only a few small business customers have moved to market contracts with Origin. While the reason for the lack of strong competition for these customers was not made clear over the course of this review, it may be the case that retailers consider this market segment to be too small to be worth the marketing effort. As shown in figure 5.2, there are only 7,314 small business gas customers in South Australia that together account for only 3 per cent of the state's total gas consumption. The total revenue currently generated from sales to these customers is in the region of \$16 million per year, which is considerably lower than the \$190 million in revenue generated from gas sales to residential customers.

6. Market Conduct

The conduct of participants within the market is an important indicator of the effectiveness of retail competition. The behaviour of retailers provides some insight into their willingness to compete for customers through the offer of competitively priced innovative retail products. Likewise, the behaviour of customers provides some insight as to the importance they place on their energy supply and the extent to which they would be willing to switch retailers when faced with a number of alternative retail products.

In this section we assess a number of behavioural characteristics of both retailers and customers that are indicative of the strength or effectiveness of competition within the relevant South Australian electricity and gas retail markets. At the end of this section we consider the observed market conduct and its implications for the effectiveness of energy retail competition in South Australia.

We note that the analysis presented in this section relies heavily on customer responses to the residential and small business customer surveys conducted by McGregor Tan Research on behalf of ESCOSA in August 2004 and February 2006. A brief description of these surveys is set out in Appendix D.

6.1. Retailer Conduct

6.1.1. Extent of market offers made by retailers

The number of market contracts offered by retailers is representative of their effort to attract new customers. In both its 2004 and 2006 surveys of residential and small business customers, the Commission attempted to assess the trend in market contract offerings by asking respondents whether they had been contacted by an energy retailer with an offer of a contract and if so, the retailer from whom the offer was made.³⁹

The number of customers who had received offers of a market contract from electricity and gas retailers increased between 2004 and 2006. In 2006, 52 per cent of residential respondents received electricity offers and 34 per cent had received gas offers, up from 44 per cent and 20 per cent in 2004 respectively.⁴⁰ A growing share of small business respondents also stated that they had received offers of contract from electricity retailers: 54 per cent, up from 38 per cent in 2004.⁴¹ However, only 16 per cent of small business

³⁹ See McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'* and *'Monitoring the Development of Energy Retail Competition – Business'*, dated February 2006 and January 2006, q. 7, 8, 32 and 33. Previous survey reports dated September 2004. We note that no time frame was selected for the respondent.

⁴⁰ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 29 and 67.

⁴¹ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.9.

respondents had received an offer of a contract from a gas retailer, down from 18 per cent in 2004.⁴²

The electricity and gas retailers from whom most offers were made are set out in table 6.1 below. While incumbent retailers AGL and Origin were named most often by those residential customers that had received an offer, the proportion of customers that also named new entrant retailers EnergyAustralia (now EA - IPR Partnership) and Powerdirect increased over the period. It is interesting to note that the proportion of residential customers that had received an electricity or gas market offer from TXU (now TRUenergy) decreased significantly from 2004 to 2006.

The trend in the number of market offers made to small business customers was different from that for residential customers. Only 16 per cent of small business customers that received an electricity market offer named AGL as a retailer from whom an offer was made, down from 27 per cent in 2004. By contrast, the proportion of respondents that named TXU/TRUenergy, Energy Australia/EA-IPR Partnership and Powerdirect increased over the period to 30 per cent, 11 per cent and 12 per cent respectively.⁴³ Of the 16 per cent of small business respondents that received a gas market offer, only 33 per cent named Origin, down from 67 per cent in 2004. AGL was named by 22 per cent of respondents whereas TXU and EnergyAustralia were each named by 11 per cent of respondents.

⁴² McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.10. We note that no time period was specified in the survey question "Have you received an individual offer of a contract from any electricity/gas retailer, including your existing retailer, for them to sell you electricity/gas?" Given this, it may be the case that some respondents may have answered yes only if they had received an offer within the last year or so where as others may have said yes if they received an offer since the introduction of FRC.

⁴³ Up from 26 per cent, 3 per cent and 9 per cent in 2004.

Table 6.1
Percentage of Respondents that Received a Market Offer by Retailer

Retailer	Residential		Small Business	
	2004	2006	2004	2006
Electricity Retailer				
AGL	39%	31%	27%	16%
TXU (now TRUenergy)	40%	24%	26%	30%
Origin	15%	22%	33%	22%
Energy Australia (now EA - IPR Partnership)	5%	11%	3%	11%
Powerdirect	2%	2%	9%	12%
Gas Retailer	2004	2006	2004	2006
Origin	32%	29%	67%	33%
AGL	45%	28%	22%	22%
TXU (now TRUenergy)	30%	24%	33%	11%
Energy Australia (now EA - IPR Partnership)	5%	14%	0%	11%

Sources: McGregor Tan 'Monitoring the Development of Energy Retail Competition – Residents', February 2006 pp.30 and 6; 'Monitoring the Development of Energy Retail Competition – Business', January 2006, pp. 10, 28 and 58.

Conclusion

Overall, the increase in the proportion of small customers who indicated that they received market offers and the rising numbers of offers made by non-incumbent retailers suggest that retailers are actively seeking customers. The one market segment in which retailers do not appear to be actively targeting customers is for small business gas customers. This may be due to the small number of these customers relative to residential gas customers or, alternatively, may be indicative of the existence of other impediments to competition for these customers.

6.1.2. Extent to which retailers make information available to customers regarding market offers

All retailers that supply electricity and/or gas to South Australian residential customers are required to publish a price fact sheet for each market offer in accordance with the Commission's Energy Price Disclosure Code ('the Code'). The Code, which was published in January 2005, requires retailers to publish the estimated annual energy bill for residential customers that consume:

- § 2MWh, 5MWh or 8MWh of electricity per annum at peak rates and 1.5MWh of electricity per annum at off peak hot water rates; and

§ 6GJ, 24GJ or 24GJ of gas per annum.

Retailers are also required to specify additional charges and any rebates attached to their market offers including the amount of any loyalty rebate, entry rebate, account establishment fees, exit fees and direct debit rebates.

In the course of preparing this report, we have reviewed the fact sheets published on each retailer's website and have conducted an assessment of retailer compliance with the obligations set out in the Code. All but two retailers published fact sheets on their website, although as noted by the Commission in its 2006 Monitoring Report, many of the fact sheets were difficult to find.⁴⁴ Of the eight retailers that did publish fact sheets:

- § three had fact sheets which were out of date, specifying the terms of offers that are no longer available and excluding the terms of the retailers' most current offers;
- § one had a number of fact sheets for each of its current offers although for some of these, the estimated annual charge was not based on current rates such that a customer would not be able to compare the offer made with that other retailers;
- § one did not specify the additional fees and charges associated with each offer on its fact sheets, although these were published under a separate 'tab' on the retailer's website.

Conclusion

Most retailers have published fact sheets although the level of compliance with the Commission's Energy Price Disclosure Code is low.

6.1.3. Evidence of anti-competitive, misleading or deceptive conduct

Evidence of anti-competitive, misleading or deceptive conduct may be indicative of the attempted exercise of market power by a dominant firm or, alternatively, may reflect a perception among retailers that customers do not adequately understand the terms of market contracts or the choices available to them. Such conduct may therefore suggest that competition is not effective.

The Commission's survey of residential and small business customers suggests that while incidences of anti-competitive, misleading, or deceptive conduct by retailers are relatively infrequent, the proportion of customers that claim to have experienced such behaviour has increased since 2004. Table 6.2 below shows the proportion of customers that experienced certain behaviour from energy retailers within the last 12 months from the date of the Commission's 2004 and 2006 survey.

The table shows that a relatively significant proportion of residential (11 per cent) and particularly small business customers (16 per cent) experienced high pressure selling, including badgering and harassment, over 2005.⁴⁵ It is interesting to note that residential

⁴⁴ ESCOSA, *Monitoring the Development of Energy Retail Competition in South Australia: Statistical Report*, March 2006, pp. 51 – 52.

⁴⁵ High pressure selling to small business customers appears to have been more common among electricity retailers as opposed to gas retailers. Of the 65 small business customers that had experienced high pressure selling over 2005, 49

customers in professional or executive occupations and those earning more than \$75,000 per annum were more likely to have experienced such behaviour from retailers.⁴⁶ This could reflect retailer's desire to sign up customers in more affluent neighbourhoods (assuming there is a positive correlation between income and energy consumption) and/or that respondents with professional or executive occupations hold different views from other respondents as to what constitutes high pressure selling.

We note that in interpreting the survey results it is important to keep in mind that attitudes to what constitutes high pressure selling may differ between respondents, and between customers and retailers, and that such behaviour may actually be reflective of a strong degree of competition between retailers.

The proportion of respondents that had experienced other types of behaviour such as the provision of misleading or deceptive information and attempts to trick customers into signing contracts was relatively low, although there was a substantial increase in the proportion of small business respondents that had experienced such behaviour in 2005 relative to 2004. As was the case for high pressure selling, such experience was more common among those that had received an offer of a contract from an electricity retailer as opposed to a gas retailer.⁴⁷

Given the rise in the number of survey respondents that have experienced such behaviour from retailers, it is informative to consider the extent to which customers have voiced their dissatisfaction with the Energy Industry Ombudsman of South Australia (EIOSA).

EIOSA received 3,846 contacts for the year ended 30 June 2006, down by 18 per cent from the previous year.⁴⁸ This was the first year in which there was a reduction in the number of contacts made since EISOA was established in August 2000, although we note that contacts for the current year to date appear to be back up around the levels seen in 2003/04.⁴⁹ It is unclear why contacts would have fallen so significantly over the 2005/06 year, although we note that it is possible that the subsequent increase in complaints could be due to increased

had received an offer of a contract from an electricity retailer whereas none of these respondents had received an offer from a gas retailer. McGregor Tan Research, *'Computer Tabulations – Business'*, 2006, confidential supporting data to *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, pp. 329 – 330.

⁴⁶ McGregor Tan Research, *'Computer Tabulations – Residents (a)'* p.506 and *'Computer Tabulations – Residents (b)'*, p.111, 2006, confidential supporting data to *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006.

⁴⁷ Of the 33 respondents that considered they had been provided with misleading or deceptive information over 2005, 24 had received an offer of a contract from an electricity retailer whereas none of these respondents had received an offer from a gas retailer. Of the 26 respondents that indicated that a retailer had attempted to trick them into signing a contract, 20 had received an offer of a contract from an electricity retailer whereas none of these respondents had received an offer from a gas retailer. McGregor Tan Research, *'Computer Tabulations – Business'*, 2006, confidential supporting data to *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, pp. 329 – 330.

⁴⁸ See Energy Industry Ombudsman SA, Annual Report 2005 – 2006, p.27. We note that the reduction of complaints occurred despite an increase in the awareness of EIOSA. Total awareness of EIOSA increased from 27.5 per cent in 2002 to 47 per cent in 2006. In 2006, 30 per cent of respondents indicated that they would turn to EIOSA when facing a dispute with an electricity or gas supplier, as opposed to 6 per cent in 2002.

⁴⁹ Information supplied by ESCOSA.

marketing activity, particularly considering that four new retailers have entered the electricity retail market within the last 18 months.

Table 6.2
Incidences of Anti-competitive, Misleading and/or Deceptive
Conduct by Retailers

Conduct		
Residential Customers	2004	2006
High pressure selling, including badgering and harassment	6%	11%
The provision of misleading or deceptive information	5%	5%
Attempt to trick customers into signing a contract	3%	4%
Actual tariffs did not match quoted tariffs	2%	2%
Transferring customers to another retailer without the customer's explicit consent	1%	1%
Not adhering to cooling off requirements	1%	0%
Small Business Customers	2004	2006
High pressure selling, including badgering and harassment	6%	16%
The provision of misleading or deceptive information	3%	8%
Attempt to trick customers into signing a contract	3%	6%
Actual tariffs did not match quoted tariffs	1%	4%
Transferring customers to another retailer without the customer's explicit consent	1%	1%
Not adhering to cooling off requirements	0%	0%

Sources: McGregor Tan 'Monitoring the Development of Energy Retail Competition – Residents', February 2006 p.17; McGregor Tan 'Monitoring the Development of Energy Retail Competition – Residents', September 2004 p.17; 'Monitoring the Development of Energy Retail Competition – Business', January 2006, p. 17; 'Monitoring the Development of Energy Retail Competition – Business', September 2004, p. 16-17.

The majority (86.7 per cent) of contacts made in 2005/06 were made in relation to electricity supplies, with only a small number of contacts made in relation to gas supplies (10.1 per cent) or dual fuel offers (3.3 per cent). Roughly half (53.2 per cent) of all enquiries and complaints related to billing and credit management, with the remaining half split between competition (24 per cent) and other issues such as quality of supply and customer service (12.8 per cent).⁵⁰ . EIOSA note that although competition enquiries and

⁵⁰ Note that as was the case for the Commission's residential and small business customer surveys, most contacts were made in relation to electricity issues (86.7 per cent). Only 10 per cent dealt with gas issues and 3.3 percent with dual fuel issues.

Contacts made were also more likely to come from customers in metropolitan Adelaide as opposed to rural South Australia (75.2 per cent compared to 24.8 per cent), from residents rather than small businesses (92.3 per cent

complaints accounted for almost a quarter of all contacts, they represent a very small percentage (0.37 per cent) of all South Australian customers that transferred to market contracts in the year to 30 June 2006 and only 0.12 per cent of all small electricity and gas customers.⁵¹

These results are comparable with that of Victoria and New South Wales. Over the year to 30 June 2006, the Energy and Water Ombudsman (Victoria) (EIOV) received 16,460 complaints in relation to electricity, gas and dual fuel supplies. Of these, approximately 82.6 per cent were in relation to retail issues, with the majority of these concerned with electricity supplies (75 per cent). As was the case for South Australia, the 2005/06 year was the first year in which there was a reduction in the number of complaints made.

Approximately 21.8 per cent of complaints made in relation to the retail of electricity and 18.4 per cent of complaints made in relation to the retail of gas were about competition issues; namely customer transfer and marketing issues. These complaints represented only 0.44 and 0.187 per cent of all customers that switched retailers in that year, and only 0.095 and 0.035 per cent of all electricity and gas customers respectively.⁵² In New South Wales, the reporting of customer complaints is much less detailed, although the number of complaints ranged from 0.01 to 1.03 per 100 customers for individual retailers for the year ended 30 June 2005.⁵³

The number of complaints made in relation to energy supplies in South Australia is comparable to that made in other industries such as telecommunications. As a proportion of all electricity customers, the total number of complaints made in relation to energy supplies was 0.57 per 100 customers for the year ended 30 June 2006. In the previous financial year, the number of complaints made in relation to telecommunications issues in South Australia was 0.478 per 100 people.⁵⁴

Conclusion

While the increase in the proportion of residential and small business customers that have experienced one or more types of potentially anti-competitive or deceptive behaviour by retailers may be cause for concern, this must be considered in conjunction with the number of enquiries and complaints made to EIOSA over the period. The small number of such contacts to EIOSA relative to the number of small customers, or small customers that have

compared to 7.1 per cent) and in relation to standing offer retailers AGL and Origin (38.36 per cent concerned AGL for electricity contacts and 48.09 per cent concerned Origin Energy for gas contacts).

⁵¹ Where customers with both electricity and gas supply are only counted as a single customer.

⁵² The number of complaints regarding electricity retail competition was 2,232 and gas retail competition was 570. The number of customers that switched retailers in that year was 507,455 for electricity and 305,410 for gas. See Energy and Water Ombudsman (Victoria), 2006 Annual Report, p. 34, 37, 44 and 50. The total number of electricity customers in Victoria as at 30 June 2006 was 2,353,401 and gas customers totalled 1,630,859. See Essential Services Commission, *Energy Retail Businesses: Comparative Performance Report for the 2005-06 Financial Year*, November 2006, pp. 2 and 11.

⁵³ Energy and Water Ombudsman NSW, *Annual Report 04/05*, p.17.

⁵⁴ Telecommunications Industry Ombudsman, *2005 Annual Report*, p.69. We note that the average number of complaints in other states was lower than this, ranging from 0.242 to 0.457 per 100 people.

actually transferred to market contracts, suggests that anti-competitive behaviour by retailers is not seen as a significant issue by small customers.

6.2. Customer Conduct and Experience

6.2.1. Customer awareness of the ability to choose retailer and existence of new entrant retailers

In its small customer surveys the Commission attempted to gauge customers' perception of their ability to choose their energy retailer by asking respondents whether they believed they could choose their own retailer or whether they thought they were obliged to purchase energy supplies from their current provider.⁵⁵

Most residential respondents were aware that they were able to choose their own energy retailer (79 per cent for both electricity and gas).⁵⁶ Awareness of the ability to choose electricity retailer was similar for customers in rural areas and those living in metropolitan Adelaide, although customers in metropolitan Adelaide appeared to be more aware than their rural counterparts of their ability to choose their own gas retailer (80 per cent vs. 69 per cent).⁵⁷ Low income customers were less likely than other customers to be aware of their ability to choose retailer (73 per cent for electricity and 74 per cent for gas) and more likely to be of the view that they were obliged to purchase from their current provider (21 per cent for electricity and 15 per cent for gas).⁵⁸

Awareness of the ability to choose retailer was similar for small business customers (75 per cent for electricity and 81 per cent for gas).⁵⁹ As was the case with residential customers, awareness of the ability to choose gas retailer was much lower among businesses customers in rural areas than in metropolitan Adelaide, although we note that there were only 9 small business respondents from regional South Australia.⁶⁰

⁵⁵ See McGregor Tan Research, 'Monitoring the Development of Energy Retail Competition – Residents' and 'Monitoring the Development of Energy Retail Competition – Business', dated February 2006 and January 2006. The relevant questions contained in the survey are questions 3 and 29 from both the residential and small business survey.

⁵⁶ See McGregor Tan Research, 'Monitoring the Development of Energy Retail Competition – Residents' dated February 2006, p.23 and 62. There was no substantial increase in awareness from the previous year. We note that awareness of ability to choose electricity retailer was higher among those who had received an offer of a contract, professionals/executives, those in paid work and those living in metropolitan Adelaide. There was higher degree of awareness of the ability to choose gas retailer among young respondents, aged 18 to 39, and those in paid employment, particularly white collar work.

⁵⁷ McGregor Tan Research, 'Computer Tabulations – Residents (a)', 2006, confidential supporting data to 'Monitoring the Development of Energy Retail Competition – Residents', dated January 2006, pp. 36 and 278.

⁵⁸ McGregor Tan Research, 'Computer Tabulations – Residents (b)', 2006, confidential supporting data to 'Monitoring the Development of Energy Retail Competition – Residents', dated January 2006, pp. 9 and 62.

⁵⁹ McGregor Tan Research, 'Computer Tabulations – Business', 2006, confidential supporting data to 'Monitoring the Development of Energy Retail Competition – Business', dated January 2006, pp. 24 and 189. We note that a somewhat surprising finding was that 12 per cent of small businesses respondents indicated that they were obliged to purchase electricity from their existing retailers in 2006, compared to 6 per cent recorded in 2004. See McGregor Tan Research 'Monitoring the Development of Energy Retail Competition – Business', dated January 2006, p.54.

⁶⁰ McGregor Tan Research, 'Computer Tabulations – Business', 2006, confidential supporting data to 'Monitoring the Development of Energy Retail Competition – Business', dated January 2006, pp. 189.

The retailers whom most respondents cited as being able to supply them with electricity and/or gas were AGL, Origin and TXU/TRUenergy. Less than 7 per cent of all residential and small business respondents cited other retailers as potential suppliers.⁶¹

Conclusion

The level of awareness among small customers of the ability to choose retailer appears to be high. We note that rural customers appear to be less aware than metropolitan customers of the ability to choose their gas retailer. This may reflect the lack of retailers providing services in competition with Origin in rural areas. While low income customers are less aware than others of their ability to choose, the difference does not appear to be so substantial as to warrant special consideration for these customers. We consider issues relevant to low income customers in greater detail in section 7.3.

The low level of awareness of retailers other than AGL, Origin and TXU/TRUenergy could be cause for concern and may suggest that the marketing efforts of these other new entrant retailers has not been sufficiently effective to encourage customers to switch. While we would not anticipate a strong level of awareness of retailers such as Country Energy and Aurora Energy that entered the market after June 2005, we would expect to see a higher degree of awareness of both EnergyAustralia (now EA-IPR Retail Partnership) and Powerdirect, both of which have been supplying energy to small customers since March 2004.

6.2.2. Customer willingness and experience in seeking information regarding market contracts

6.2.2.1. Willingness to seek information regarding market contracts

The extent of offers made by retailers becomes increasingly important as we observe that few customers are willing to contact retailers directly or take the initiative to seek information on available market offers.

The Commission's customer surveys show that only 8 per cent of residential respondents contacted one or more retailers with questions regarding available electricity offers over 2005, down from 10 per cent in 2004.⁶² The incidence of residential customers

⁶¹ Note that customers were asked what other retailers they thought they could purchase energy supplies from. It may be the case that respondents that had an electricity or gas market contract with these other new entrant suppliers did not identify these retailers in response to this question. Awareness of these retailers is therefore likely to be higher than reflected in the survey results. Most residential (over 97% and small business (over 95%) customers knew who their current electricity and gas retailer was.

McGregor Tan Research, '*Computer Tabulations – Residents (a)*', 2006, confidential supporting data to '*Monitoring the Development of Energy Retail Competition – Residents*', dated January 2006, pp. 37, 59 and 279, 288 and '*Computer Tabulations – Business*', 2006, confidential supporting data to '*Monitoring the Development of Energy Retail Competition – Business*', dated January 2006, pp. 34, 43 and 190 and 196.

⁶² McGregor Tan Research, '*Monitoring the Development of Energy Retail Competition – Residents*', dated February 2006, p. 10. The retailers that were most likely to be contacted were AGL (42%, compared to 47% in 2004), TXU (33%, compared to 38% in 2004), and Origin (26%, compared to 34% in 2004).

approaching a gas retailer was similarly low, at 6 per cent, down from 8 per cent in 2004.⁶³ Small business customers also showed little interest in contacting energy retailers, with only 12 per cent of small business respondents having contacted an electricity retailer and 9 per cent having contacted a gas retailer in 2005.^{64 65}

The willingness of customers to look for other types of information regarding available market offers was similarly low. Only 13 per cent of residential respondents indicated that they had looked for information regarding market contracts for electricity, down from 15 per cent in 2004, and only 7 per cent indicated that they had looked for information regarding market contracts for gas, down from 8 per cent in 2004.⁶⁶ The willingness of small business customers to seek information is similarly low at 14 percent for electricity and 5 per cent for gas.⁶⁷

Conclusion

Overall, the survey results suggest that very few customers actively seek out information that would assist them in making decisions regarding their electricity or gas supply. This may indicate that customers consider the time spent in searching for information to be costly relative to the benefit they would potentially derive from switching to a lower cost market contract. Alternatively, the results may suggest that retailer marketing efforts are sufficiently aggressive such that customers do not feel the need to search for any additional information in relation to market offers. Given that more than half of all residential and small business respondents indicated they had been contacted by an electricity retailer with a market offer, these customers may feel little need to search for additional information regarding such offers.

⁶³ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 10. The retailers that were most likely to be contacted were AGL (53%, up from 44% in 2004), Origin (31%, down from 49% in 2004), Energy Australia (25%, up from 4% in 2004) and TXU (22%, down from 24% in 2004).

⁶⁴ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 10 and 11. The retailers that were most likely to be contacted for electricity supplies were AGL (52%, up from 26% in 2004), TXU (29%, down from 33% in 2004), Origin (27%, up from 15% in 2004), Energy Australia (13%, up from 7% in 2004) and Powerdirect (13%, down from 19% in 2004). The retailers that were most likely to be contacted for gas supplies were AGL (2 = 40%), Origin (2 = 40%) and Energy Australia (1 = 20%).

⁶⁵ Of those customers that did contact a retailer, only a few were refused service. Only 4% of residents that approached an electricity retailer were refused and 6% of residents that approached a gas retailer were refused. Only 5 of the 48 small business respondents that enquired about electricity contracts were refused and none of the five that enquired about gas contracts were refused.

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 10 and McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 10 and 11.

⁶⁶ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 14 and 15.

⁶⁷ See McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 15.

6.2.2.2. Customer experience in finding information regarding market contracts

The vast majority of residential and small business customers that had looked for information to assist them in their decision to switch to a market contract found such information easy to obtain.⁶⁸

While retailers and their representatives remain an important source of information on available market contracts, the internet has become an increasingly powerful marketing tool.⁶⁹ Around 24 per cent of residential respondents who had looked for information regarding electricity market contracts and 28 per cent that has looked for information about gas market contracts consulted electronic sources in 2005 compared to 14 per cent and 18 per cent in 2004 respectively. Small business customers also looked to the internet as their primary source of information regarding electricity contacts in 2005, with 38 per cent using this information source, up from 20 percent in 2004. By contrast, newspaper ads lost popularity with residential and small business consumers, with only 11 per cent of residential customers looking to such adverts when assessing electricity offers (down from 22 per cent in 2004) and no small businesses using this information source in 2005.⁷⁰

Only 22 per cent of residents surveyed said they were aware of the availability of independent assistance, such as the Commission's Electricity Price Comparison Service to help in making energy decisions.⁷¹

Conclusion

Of the small number of customers that actually seek out information on available energy market contracts, most find this easy to obtain and are increasingly looking to the internet as a source of information. While knowledge of independent information sources is relatively low among residential customers, more respondents were aware of the existence of such information sources than the number of respondents that had actually looked for information regarding market contracts.

⁶⁸ Around 81% of residential respondents indicated that information on available electricity offers was easy to obtain (up from 76% in 2004) and 77% indicated that information on available gas offers was easy to obtain (down from 80% in 2004). Around 73% of small business respondents indicated that information on available electricity offers was easy to obtain (down from 74% in 2004).

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 15 – 16 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 15 - 16.

⁶⁹ Retailers were the most commonly cited source of information with 24% of residential respondents that looked for information on electricity contracts and 33% that had looked for information on gas market offers having looked to retailers for that information. By contrast, small businesses were more likely to look for information regarding electricity market offers on the internet.

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 15 – 16 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 15 - 16.

⁷⁰ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 15 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 45.

⁷¹ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 18.

6.2.2.3. Ease of understanding the information contained in contracts

In order to make informed decisions, customers must be able to understand the terms and conditions of contracts and compare contracts offered by different retailers.

In its latest customer surveys the Commission asked those customers who had received an offer of a contract or had looked for information regarding market contracts to rate how easy it was to understand and compare market offers.⁷² The Commission also asked those respondents that had looked for information regarding market contracts whether they were able to obtain sufficient information to make an informed choice and whether the information provided was important to them in making their decision to switch retailers. The response to these questions was mixed as set out in table 6.3 below.

In general, customers that had been offered a market contract directly by a retailer found those offers easier to understand than customers that had looked for information on market contracts themselves. The proportion of customers that had looked for information on electricity and gas market contracts and found that information easy to understand and compare was only moderate at between 50 – 55 per cent.

Despite the fact that all retailers have been required to publish fact sheets on each of their market offers since January 2005, there was no discernable increase in the ease of understanding of these offers. In fact, there was an increase in the proportion of residential customers that found information on gas market contracts either very difficult or quite difficult to understand.⁷³ We note that it is unclear why this would be the case, but may suggest that a number of customers have not been able to find price fact sheets on retailer's websites or, alternatively, do not find price fact sheets easy to understand and compare.⁷⁴

Even though around half of those customers that looked for information did not find it easy to understand and compare, over 70 per cent of these respondents indicated that they found the information provided sufficient for them to make an informed choice and more than 80 per cent considered that information important in their decision to switch retailers.

⁷² McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, q. 9, 34, 24 and 49.

⁷³ The proportion of residential customers that found these contracts very difficult to understand increased from 7% in 2004 to 12% in 2005 and the proportion of customers that found these offers quite difficult to understand increased from 7% in 2004 to 16% in 2005. We note that the proportion of customers that found these contracts very easy to understand also increased from 33% to 42% over this same period. McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p.87.

⁷⁴ Note that around one quarter of residential customers and around 38 per cent of small business customers that have looked for information on market contracts use the internet as an information source.

Table 6.3
Ease of Understanding and Comparing Information

Contract Type	Residential		Small Business	
	2004	2006	2004	2006
Electricity				
Proportion of customers that received an offer ¹ that considered the offer easy to understand	65%	65%	68%	64%
Proportion of customers that looked for information ² that found offers easy to understand and compare	54%	55%	46%	50%
Proportion of customers that looked for information ² that found sufficient information to make an informed choice	76%	75%	61%	73%
Proportion of customers that looked for information ² that thought that information was important in their decision to switch retailers	N/A	80%	N/A	88%
Gas	2004	2006	2004	2006
Proportion of customers that received an offer ³ that considered the offer easy to understand	68%	74%	77%	100%
Proportion of customers that looked for information ⁴ that found offers easy to understand and compare	66%	60%	0%	66%
Proportion of customers that looked for information ⁴ that found sufficient information to make an informed choice	76%	72%	0%	100%
Proportion of customers that looked for information ⁴ that thought that information was important in their decision to switch retailers	N/A	91%	N/A	100%

Sources: McGregor Tan 'Monitoring the Development of Energy Retail Competition – Residents', February 2006 and September 2004 and 'Monitoring the Development of Energy Retail Competition – Business', January 2006 and September 2004. Notes: (1) 625 residential and 221 small business customers received an offer of an electricity market contract in 2005. 525 and 152 received such an offer in 2004 respectively. (2) 161 residential and 56 small business customers looked for information regarding electricity market contracts in 2005. 185 and 49 looked for information in 2004 respectively (3) 32 residential and 9 small business customers received an offer of a gas market contract in 2005. 117 and 9 received such an offer in 2004 respectively. (2) 43 residential and 3 small business customers looked for information regarding gas market contracts in 2005. 45 and 2 looked for information in 2004 respectively.

In addition to the understanding of energy offers, the Commission also asked respondents whether they found their electricity bills easy to understand in their current format and whether the information contained in their electricity bill enabled them to make comparisons with other retailers' offers.⁷⁵

⁷⁵ McGregor Tan Research, 'Monitoring the Development of Energy Retail Competition – Residents', dated February 2006, and 'Monitoring the Development of Energy Retail Competition – Business', dated January 2006, q.27 and 52, 34, 24 and 49.

There was a high level of agreement among all respondents that both electricity and gas bills were easy to understand, with each customer group giving the ease of understanding energy bills an average rating of 4.2 to 4.4 on a scale of one to five. Most customers also considered the information contained in their energy bills easy to compare with other market offers, giving this factor an average rating of 3.4 to 3.8 on a scale of one to five.⁷⁶ There was no substantial change in responses from the previous survey.

Conclusion

It is difficult to draw any firm conclusions from the response of customers regarding the ease of understanding and comparing market offers. While a large proportion of customers that looked for information regarding market offers did not find these offers easy to understand and compare, most considered that information sufficient to make an informed choice and important in their decision to switch retailers. In general the responses suggest that the introduction of price fact sheets has not had a significant impact on customer understanding of energy market offers. This may be because such information is difficult for customers to find or understand or it could be that one year is not a sufficient time period for the assessment of the success of this initiative.

6.2.3. Customer switching

Customer switching is one of the most important markers of effective competition. It is expected that, over time, increasing numbers of customers would move from standing offer contracts with incumbent retailers AGL and Origin to market contracts with these or other new entrant retailers.

In this section we assess both actual switching rates for all South Australian electricity and gas customers, the factors that customers consider to be important in their decision to switch, and the cost of switching under market contracts.

6.2.3.1. Customer Switching 2003 - 2006

Customer switching can be measured in a number of ways. Gross switching refers to the number of monthly customer transfers between retailers. This measure includes all instances where there has been a change in the retailer allocated to a connection point, regardless of the reason for that change. An alternative measure is the level of net switching, which refers to the extent to which new entrant retailers have captured market share from the incumbent retailer over time. This measure may be considered more useful than gross switching for the purpose of assessing the effectiveness of competition as it excludes all transfers that occur due to customer move-ins⁷⁷, and more clearly shows the net impact of multiple switching.⁷⁸

⁷⁶ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 58 and 91 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 50 and 73.

⁷⁷ Customer move-in refers to a situation where a customer changes the retailer responsible for a connection point upon moving into a new residence. While this is technically considered a 'transfer' by NEMMCO and REMCO, a proportion of these transfers are likely to represent customers that wish to remain with their current retailer, ie, the

Over time it is reasonable to expect instances of multiple switching to increase as customers continue to respond to changes in the market offers made by retailers. It is also reasonable to expect the number of transfers due to move-ins to increase over time as customers move away from incumbent retailers to new entrant retailers.⁷⁹ Given this, gross switching will likely to lose some relevance over time as a measure for assessing customer behaviour from a competition perspective.

FRC was introduced for small electricity customers in South Australia over three years ago, and data from NEMMCO suggests that instances of multiple switching have increased significantly over the 18 months to November 2006.⁸⁰ Given this, we have assessed the level of net switching only for the purpose of this analysis. In addition to net switching, we have also considered the extent to which small customers have switched from standing contracts to market contracts with incumbent retailers AGL and Origin. In combination, these measures indicate the total number of customers that have switched from standing contracts to market contracts since the introduction of FRC. An assessment of gross switching is included in Appendix E.

Figures 6.1 to 6.4 below show the proportion of all residential and small business electricity and gas customers that were supplied under the following types of contracts in each quarter from September 2003 (September 2004 for gas) to November 2006:

- § standing contract with the incumbent retailer;
- § market contract with the incumbent retailer; or
- § market contract with a non-incumbent retailer.

A summary of the characteristics of those customers more likely to remain on standing contracts is set out in Appendix F.

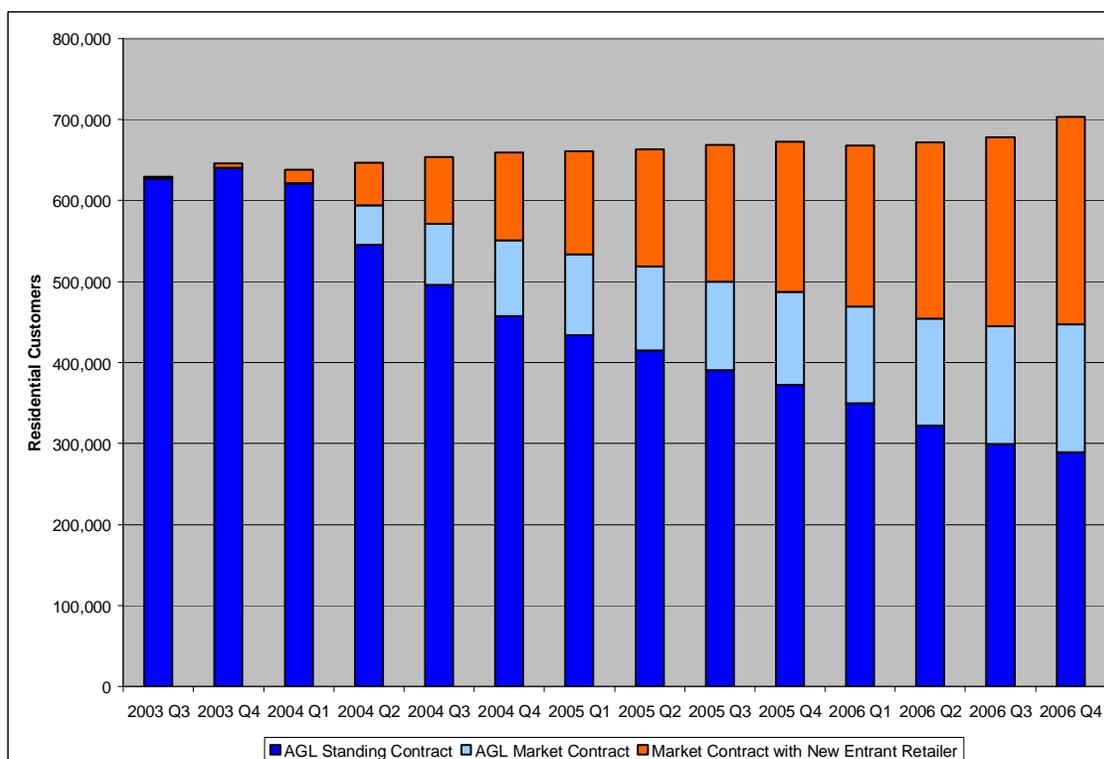
retailer by whom they were being supplied at their previous residence. These transfers therefore do not represent a switch of retailer from a competition perspective.

⁷⁸ Multiple switching refers to those customers that switch more than once, from the incumbent to a new entrant retailer and then either back to the incumbent or to another new entrant retailer. As instances of multiple switching increase, gross switching measures are difficult to interpret as it is important to distinguish between the total number of customers that are switching, either once or more than one, and those that have not switched at all.

⁷⁹ As the market share of the incumbent decreases, those customers that move residence are more likely to find that the retailer that allocated to the connection point of their new residence is not the retailer by whom they were supplied at their previous residence.

⁸⁰ NEMMCO data shows that multiple switching and/or transfers due to customer move-ins has increased in the South Australian electricity market since June 2005. NEMMCO data suggests that the number of transfers from new entrant retailers to AGL increased from an average of 1,475 per month for the six months ended 31 December 2005 to 1,827 per month for the six months ended 30 June 2006 and 2,176 per month for the five months ended 30 November 2006. The average number of transfers from new entrant retailers to other new entrant retailers also increased from an average of 1,720 per month for the six months ended 31 December 2005 to 2,300 per month for the six months ended 30 June 2006 and 3,250 per month for the five months ended 30 November 2006. For the month ended 30 November 2006, customers transferring from a new entrant retailer back to incumbent retailer AGL or other new entrant retailers represented around 37% of all transfers that month.

Figure 6.1
Net Switching by Residential Electricity Customers, Jan 2003 – Nov 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer numbers were recorded as the number of NMI's allocated to each retailer. From July 2006 customer numbers were reported as the number of NMI's billed in the same period.

As shown in figure 6.1 above, the total number of SA residential electricity customers has grown steadily from around 630,000 in September 2003 to 703,000 in December 2006.

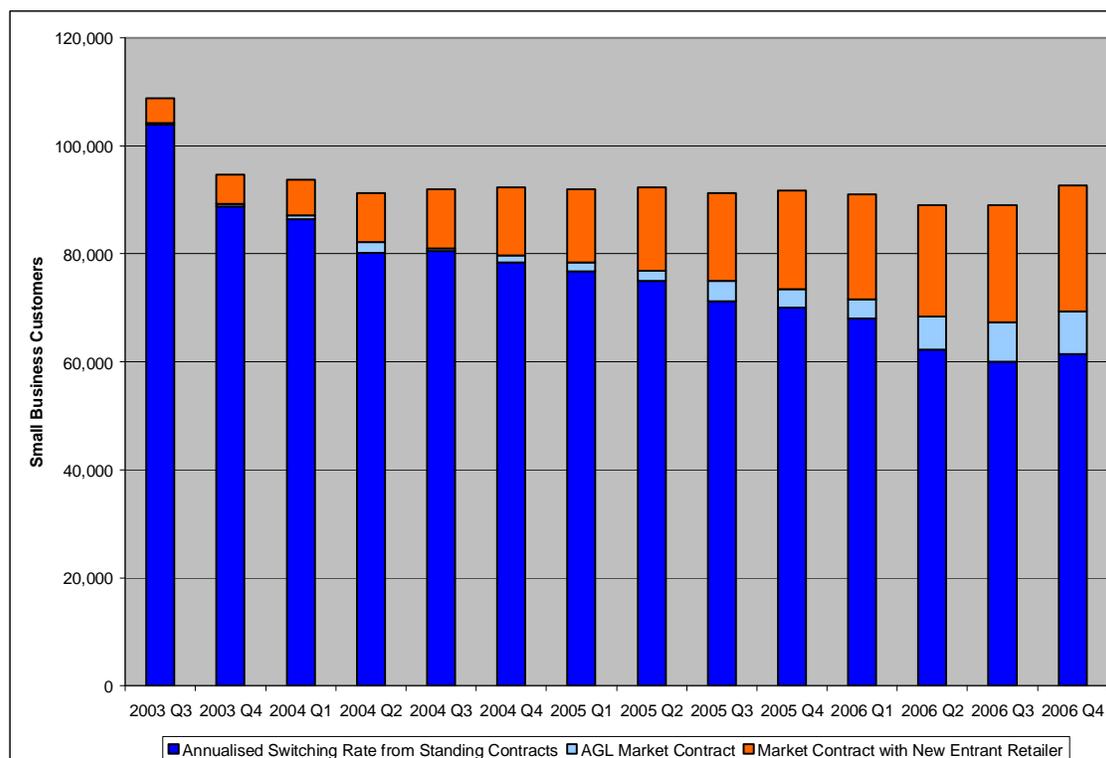
Over this time period customers have continued to move towards market contracts with both AGL and other new entrant retailers. As set out in table 6.4, the share of customers on market contracts increased by 58 percentage points over the 3 year period to December 2006.

Table 6.4
Change in Residential Electricity Customer Share by Contract Type

Customer Type	As at 31 December			
	2003	2004	2005	2006
AGL Standing Contract	99%	69%	55%	41%
AGL Market Contract	0%	14%	17%	23%
Market Contract with New Entrant	1%	17%	28%	36%
Percentage Point Change	2003 - 2006	2004	2005	2006
All Market Contract Customers	58%	30%	14%	14%

Unlike residential customers, the total number of SA small business electricity customers has fallen from around 109,000 in September 2003 to around 93,000 in December 2006, although we note this may in part be due to the change in the definition of a ‘customer’ as opposed to an actual decrease in customer numbers. Over this time period customers have switched to market contracts, mainly with retailers other than incumbent retailer AGL.

Figure 6.2
Net Switching by Small Business Electricity Customers, Jan 2003 – Nov 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data *Notes: In June 2006 there was a change in the methodology used to report customer numbers under the Commission’s Guideline No. 2. Prior to this date customer numbers were recorded as the number of NMI’s allocated to each retailer. From July 2006 customer numbers were reported as the number of NMI’s billed in the same period.*

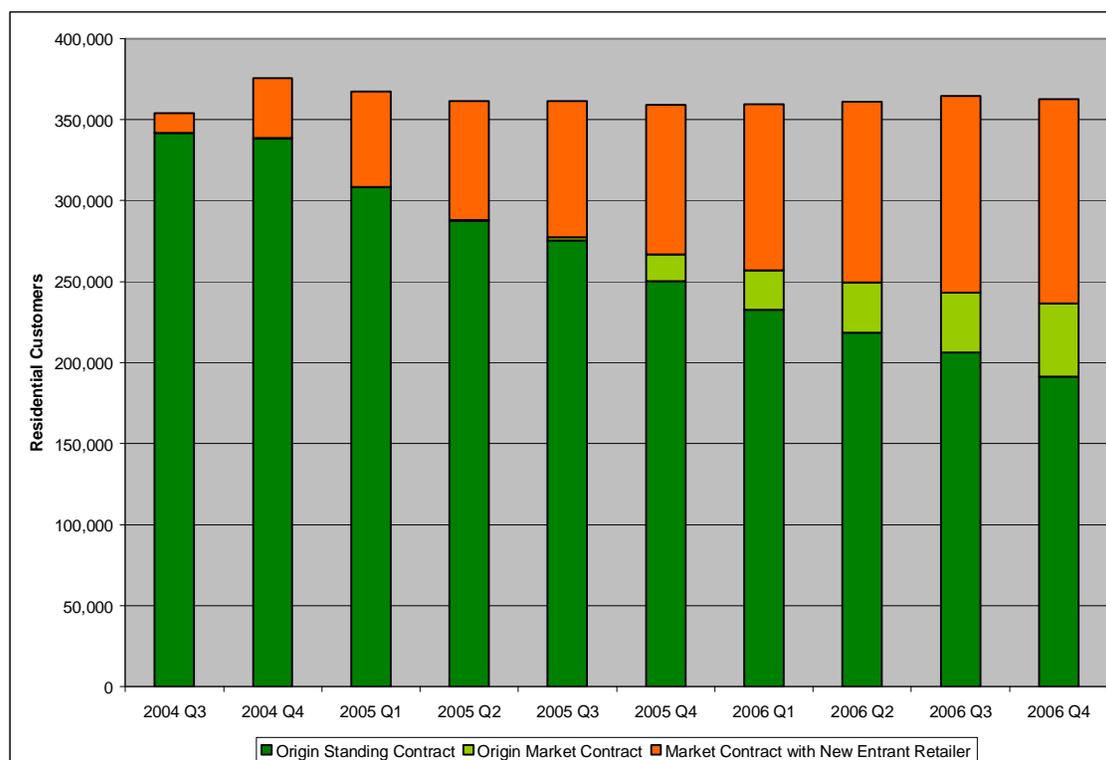
As set out in table 6.5 below, the share of customers on market contracts increased by 28 percentage points over the 3 year period to December 2006.

Table 6.5
Change in Small Business Electricity Customer Share by Contract Type

Customer Type	As at 31 December			
	2003	2004	2005	2006
AGL Standing Contract	94%	85%	76%	66%
AGL Market Contract	0%	1%	4%	9%
Market Contract with New Entrant	6%	14%	20%	25%
Percentage Point Change	2003 - 2006	2004	2005	2006
All Market Contract Customers	28%	9%	9%	10%

The total number of SA residential gas customers has remained relatively steady at around 360,000 between September 2004 and December 2006.

Figure 6.3
Net Switching by Residential Gas Customers, Jan 2003 – Nov 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer numbers were recorded as the number of MIRN's allocated to each retailer. From July 2006 customer numbers were reported as the number of MIRN's billed in the same period

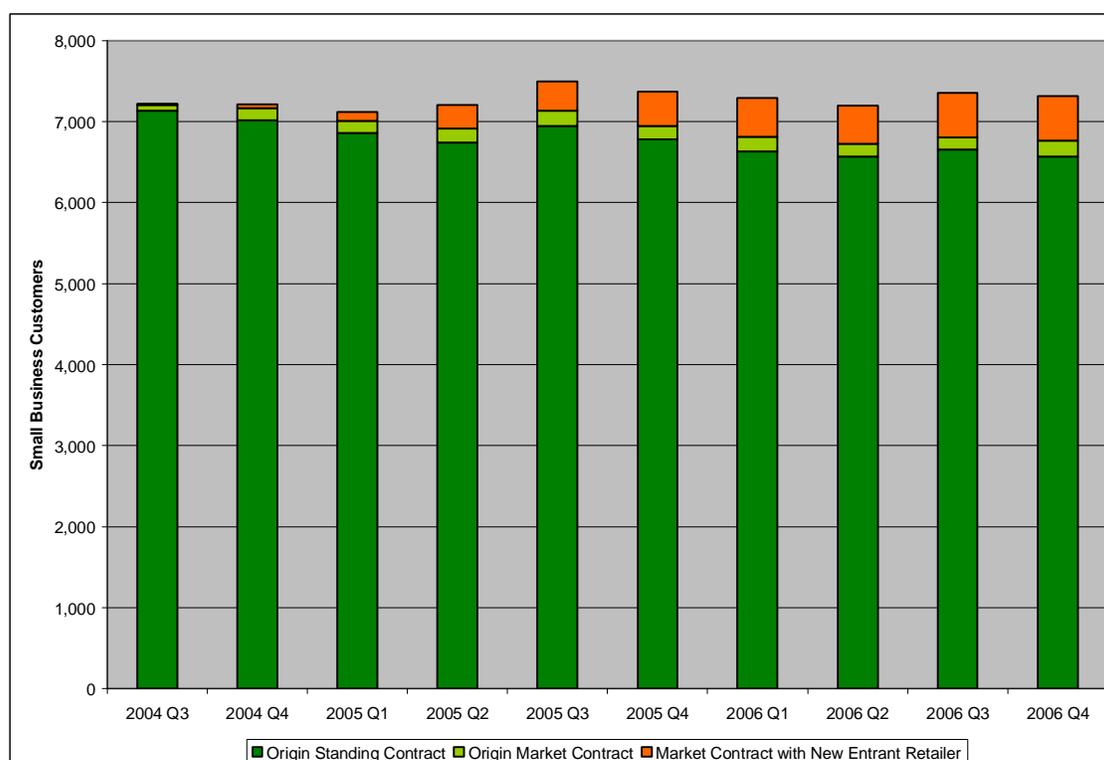
Over this time period customers have switched to market contracts, mainly with retailers other than incumbent retailer. As set out in table 6.6, the share of customers on market contracts increased by 37 percentage points over the 2 year period to December 2006.

Table 6.6
Change in Residential Gas Customer Share by Contract Type

Customer Type	As at 31 December		
	2004	2005	2006
Origin Standing Contract	90%	70%	53%
Origin Market Contract	0%	4%	12%
Market Contract with New Entrant	10%	26%	35%
Percentage Point Change	2004 - 2006	2005	2006
All Market Contract Customers	37%	20%	17%

Only a few small business customers have a gas supply and their number has not changed considerably between September 2004 and December 2006

Figure 6.4
Net Switching by Small Business Gas Customers, Jan 2003 – Nov 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** In June 2006 there was a change in the methodology used to report customer numbers under the Commission's Guideline No. 2. Prior to this date customer numbers were recorded as the number of MIRN's allocated to each retailer. From July 2006 customer numbers were reported as the number of MIRN's billed in the same period

Over this time period only very few small customers have switched to market contracts with either Origin or other retailers. As set out in table 6.7, the share of customers on market contracts increased by only 7 percentage points over the 2 year period to December 2006.

Table 6.7
Change in Residential Gas Customer Share by Contract Type

Customer Type	As at 31 December		
	2004	2005	2006
Origin Standing Contract	97%	92%	90%
Origin Market Contract	2%	2%	3%
Market Contract with New Entrant	1%	6%	7%
Percentage Point Change	2004 - 2006	2005	2006
All Market Contract Customers	7%	5%	2%

In sum, the share of all South Australian energy customers on market contracts as at 31 December 2006 was as follows:⁸¹

- § 59 per cent of residential electricity customers, with most switching occurring in 2004;
- § 34 per cent of small business electricity customers, with switching occurring relatively consistently over time at around 10 per cent of customers per year;
- § 47 per cent of residential gas customers, with most switching having occurred over 2005; and
- § 10 per cent of small business gas customers, with most switching having occurred in 2005 and very few customers switching in 2006.

⁸¹ The proportion of respondents to the Commission's 2006 small customer survey that had taken out a market contract were as follows: residential electricity customers (41%), small business electricity customers (42%), residential gas customers (32%) small business gas customers (19%). The majority of customers that had taken out a contract had switched from the incumbent retailer.

The majority of residential and business customers that had switched to a market contract found the transfer process easy (88% of residential electricity customers, 90% of residential gas customers, 83% of small business electricity customers and 73% of small business gas customers).

Very few customers that had switched used the cooling off period to cancel (3% for residential electricity customers, 2% of residential gas customers, 4% of small business electricity customers and 0% of small business gas customers).

The proportion of respondents that intended to take out a market contract within the next 12 months was significantly lower as follows: residential electricity customers (12%), small business electricity customers (17%), residential gas customers (14%) small business gas customers (16%). This question was asked of all respondents (ie, including those that had recently switched) therefore the lower percentage response is not necessarily cause for concern.

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 12, 38, 44 – 45, 74, 79-80 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 13, 35, 40-41, 63, 67-68.

On the whole, the levels of net switching observed in South Australia appear to be higher than that observed in Victoria two to three years after the introduction of FRC. In its 2004 review of the effectiveness of retail competition, the ESC noted that customer switching to non-local retailers began very slowly but was at a relatively high level by April 2004. At this time non-local retailers had approximately 13 per cent market share in the electricity retail market and 12 per cent market share in the gas retail market.⁸²

Conclusion

The high degree of switching by residential electricity and gas customers from standing to market contracts suggests that customer inertia is not a factor that has prevented new entrant retailers from gaining a foothold in either the electricity or gas retail market. The lower incidence of switching by small business customers, particularly small business customers, may be indicative of issues specific to this particular customer group.

6.2.3.2. Reasons for switching or not switching

In its 2004 and 2006 customer surveys, the Commission asked those respondents that had taken out a market contract what the main driver was in their decision to change retailers. The Commission also asked those respondents that had not taken out a market contract why they had not done so.⁸³

For those residential respondents that had taken out a market contract, the main factor that influenced their decision to switch was price/cost (68 per cent for residential respondents that had taken out an electricity market contract and 62 per cent that had taken out a gas market contract). Other less important factors included consistency of supply, discounts, vouchers and rebates, and consolidation of gas and electricity accounts under the same provider. The proportion of respondents that cited these factors as the main driver in their decision to switch ranged from 1 to 9 per cent.⁸⁴

Price/cost was also the overwhelming driver for small business customers (83 per cent of small business respondents cited this factor as the main driver for switching to electricity market contracts and 55 per cent to gas market contracts). Having one company for gas and electricity was also an important consideration for small businesses when choosing a gas contract (36 per cent considered this as their main driver to switch), although this factor appears to have had very little relevance for small business customers switching to electricity market contracts, with only 1 per cent of respondents having cited it as their main driver.⁸⁵

⁸² ESC “*Special Investigation: Review of the Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity – Background Report*”, June 2004, p.72.

⁸³ McGregor Tan Research, ‘*Monitoring the Development of Energy Retail Competition – Residents*’, dated February 2006, and ‘*Monitoring the Development of Energy Retail Competition – Business*’, dated January 2006, q. 16, 17, 41 and 42.

⁸⁴ McGregor Tan Research, ‘*Monitoring the Development of Energy Retail Competition – Residents*’, dated February 2006, p.41 and 76.

⁸⁵ McGregor Tan Research, ‘*Monitoring the Development of Energy Retail Competition – Business*’, dated January 2006, p.37 and 65.

Most respondents that had not taken out a market contract noted that they were happy with their current retailer.⁸⁶ Around 4 to 12 per cent of residential customers cited other reasons including insufficient information, they could not be bothered, they didn't like contracts or the fact that they had not been approached by a retailer.⁸⁷ The other main reasons put forward by small business customers were inadequate potential savings, insufficient information, waiting for better offers, hadn't got around to it and don't like contracts. Around 6 to 17 per cent of small business customers cited one or more of these factors.⁸⁸ It is interesting to note that inadequate potential savings was cited by higher proportions of small business customers in metropolitan Adelaide at 16 per cent.

When asked to rate various factors in terms of their importance in the decision to switch retailers, most residential and small business respondents considered price, supply and the level of customer service to be very important. None of the customer groups surveyed considered having both contracts with the one supplier to be important.⁸⁹ This appears to accord with the fact that only half of all residential respondents and 29 per cent of small business respondents with both electricity and gas supplies had the same retailer for both energy sources.⁹⁰

Conclusion

As expected, the primary factor that drives all types of customers to switch is price. Quality and consistency of supply and customer service are also important factors. The convenience of having both contracts with the same supplier does not appear to be an important factor in the decision to switch, although may have a slightly higher level of importance for small business gas customers.

6.2.3.3. Cost of Switching

While there has been a relatively high level of switching to date from standing to market contracts, it can be expected that over time the level of switching will decrease due to the fact that a larger proportion of customers will already be on lower priced market contracts with a term of up to three years, which may include penalties for early termination.

⁸⁶ This was the main reason put forward by residential customers (53 per cent for electricity and 50 per cent for gas respectively) as well as small business customers (38 per cent for electricity and 66 per cent for gas respectively).

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p.42 and 77 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.38 and 66.

⁸⁷ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p.42 and 77.

⁸⁸ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.38 and 66.

⁸⁹ On a scale of 1 to 5, Price was given an average rating of 4.6 to 4.7 by all respondents, Supply was given an average rating of 4.3 to 4.5, Customer Service was given an average rating of 4 to 4.3 and having both contracts with the one supplier was given an average rating of 2.8 to 3.3. McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p.47 and 81 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.42 and 69.

⁹⁰ McGregor Tan Research, *'Computer Tabulations – Residents (a)'*, 2006, confidential supporting data to *'Monitoring the Development of Energy Retail Competition – Residents'*, dated January 2006, p. 46 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.40.

Having assessed the offers provided by retailers, early termination fees for current offers appear to range from around \$48 to \$125, depending on the contract and the time at which the contract is terminated as shown in Appendix G. We note that a number of the market contracts currently offered at a discount to the standing contract do not appear to have a fixed term or any associated early termination fees. We therefore do not consider early termination fees to be a significant impediment to customer switching between retailers in the near future.

6.3. Summary of Market Conduct

In sum, our assessment of the conduct of market participants in both the electricity and gas retail market in South Australia suggests that both retailers and customers are acting in a manner that is broadly consistent with an effectively competitive market. In particular:

- § retailers are actively making market offers to customers, with an increasing number (more than half of all small electricity customers and over a third of all residential gas customers) having received an offer of a market contract since the implementation of FRC;
- § although some retailers are not currently complying with the requirements of the Commission's Energy Price Disclosure Code, almost all retailers have published fact sheets on their website and a number of retailers allow customers to obtain an online quote;
- § despite the increase in the proportion of respondents to the Commission's survey that indicated they had encountered high pressure selling from retailers, potentially bordering on harassment, the number of contacts to the EISOA actually fell over the 2005/06 year (a period where there was around seven month overlap between July 2005 and January 2006). The number of competitive contacts represented only a very low percentage of all small energy customers (.12 per cent) and small customers that had switched to market contracts over the period (0.37 per cent);
- § the vast majority of small customers are aware that they are able to choose their energy retailer;
- § while only a few customers appear willing to contact retailers themselves or look for information regarding market offers, most that do find information regarding offers easy to find;
- § even though a significant proportion of customers that look for information on market offers themselves do not consider these offers easy to understand and compare, most consider the information they do obtain to be sufficient to make an informed choice and considered the information they did obtain to be important in their decision to switch; and
- § a large proportion of customers, particularly residential customers, are switching to market contracts with both the incumbent and new entrant retailers over time.

While the views and conduct of retailers and customers is encouraging, there are a few areas that represent potential cause for concern.

First, retailers do not appear to be exerting much effort in attracting small business gas customers. Only 16 per cent of small business respondents to the Commission's survey had received an offer of a contract from a gas retailer over 2005, down from 18 per cent in the previous year. This is the only customer group for whom the proportion of respondents that had received an offer actually decreased over this time period.

The relative lack of competition for these customers is further supported by the analysis of market share and switching data. Only 10 per cent of all small business gas customers in South Australia had switched to market contracts by December 2006, with only 7 per cent having switched to contracts with new entrant retailers. The level of switching also decreased over the last year, with the rate of switching having fallen to only 2 per cent in 2006. The main reason given by those small business gas customers for not switching to a market contract is that there was insufficient information available, they were waiting for a better offer, they didn't want to be locked into a contract and that the potential savings were inadequate. As noted in section 5.6 above, retailers may not have an interest in attracting these customers if they consider them to be too small a group to justify the expenditure that would be required to identify who they are and actively market their offers.

On the whole, retailers also do not appear to be complying with their requirements under the Commission's Energy Price Disclosure Code. Some retailers have not published price fact sheets on their website and, of those that have, a number of these are out of date, either specifying contracts that are no longer available or an estimated annual bill based on rates which no longer apply to that contract. While lack of compliance with the Code does not necessarily hinder competition, particularly when only a small number (less than 15 per cent) of customers actually look for information on market contracts themselves, it does make it more difficult for customers that do look for information to compare offers between retailers. As noted in section 6.2.2.3, the proportion of respondents that had looked for information on electricity market contracts and found this information easy to understand and compare was only moderate at around 50 – 55 per cent.

7. Market Performance

Market performance is the outcome of the competitive process. In this section we consider a number of measures of market performance, including the extent to which:

- § retailers are currently offering market contracts at rates below the standing contract and whether the discounts provided under market contracts relative to the standing contract have increased or decreased over time;
- § retailers are offering market contracts with different price and non-price features;
- § retailers are improving various performance measures over time; and
- § low income customers have benefited from market contracts.

7.1. Availability of Market Offers at a Discount to the Standing Contract

One of the primary measures of market performance is the extent to which retailers are offering market contracts at rates below those offered under standing contracts. So long as the margin contained in the standing contract allows retailers to cover their fixed costs plus a rate of return above the weighted average cost of capital, it would be reasonable to observe retailers offering market contracts at rates below the standard contract in an effectively competitive market.

For the purpose of this review we have assessed the estimated annual charge calculated by retailers under each of their market contracts for residential customers with a moderate level of energy usage. We have also assessed the change in the range of discounts offered by each retailer under market contracts relative to the standard contract since the introduction of FRC.

In addition to the above, we have also compared the average quarterly energy bill for all residential and small business customers on standing and market contracts and the average charge per unit of energy consumed by these customers since the beginning of FRC in South Australia. We note that the conclusions that can be drawn from this analysis are limited for the purpose of assessing the benefit that customers on market contracts have derived relative to standing contract customers since the implementation of FRC. This analysis is set out in Appendix G.

7.1.1. Electricity market contracts

The estimated annual electricity charge for residential customers with a medium level of electricity usage (5,000 MWh) and off-peak electricity usage of 1.5MWh under the market contracts currently offered by each retailer in South Australia is set out in table 7.1 below.

Market contracts are listed by retailer from lowest to highest cost and the estimated annual charge excludes any additional charges and rebates, although we have noted where such charges and rebates apply. A more detailed summary of all additional costs and benefits associated with each market contract is set out in Appendix H.

Table 7.1
Estimated Annual Bill Under Electricity Market Contracts as at March 2007

	Estimated Annual Electricity Bill		Savings Relative to Standing Contract (%)	
	Peak	Off-Peak	Peak	Off-Peak
	5,000 MWh	1,500 MWh	5,000 MWh	1,500 MWh
<u>Standing Contract</u>				
AGL Standing Contract	\$1,064	\$115		
<u>Market Contracts</u>				
AGL				
AGL Freedom 5%^{N1}	\$1,018	\$109	4%	5%
AGL Freedom ¹	\$1,064	\$115	0%	0%
AGL Advantage ^{1,2}	\$1,064	\$115	0%	0%
Aurora Energy				
Aurora Standard Contract¹	\$970	\$165	9%	(44%)
Country Energy				
Country Energy Premium³	\$985	\$114	7%	1%
EnergyAustralia				
EnergyAustralia Maxisaver	\$1,001	\$108	6%	6%
EnergyAustralia RAA Saver⁴	\$1,001	\$108	6%	6%
EnergyAustralia EasySaver	\$1,011	\$109	5%	5%
EnergyAustralia Green Saver 2	\$1,043	\$113	2%	2%
EnergyAustralia RAA Green Saver	\$1,043	\$113	2%	2%
EnergyAustralia Green	\$1,064	\$115	0%	0%
EnergyAustralia Green Saver Premium ²	\$1,064	\$115	0%	0%
EnergyAustralia Qantas Frequent Flyer ⁴	\$1,064	\$115	0%	0%
EnergyAustralia Qantas Frequent Flyer Green Saver	\$1,064	\$115	0%	0%
Momentum Energy				
Momentum Energy Residential Anytime^{2,5}	\$949	\$112	11%	2%
Origin Energy				
Origin HomeChoice	\$1,011	\$109	5%	5%
Origin HomeSupply ¹	\$1,065	\$115	0%	0%

Table 7.1 (Cont)
Estimated Annual Bill Under Electricity Market Contracts as at March 2007

	Estimated Annual Electricity Bill		Savings Relative to Standing Contract (%)	
	Peak	Off-Peak	Peak	Off-Peak
	5,000 MWh	1,500 MWh	5,000 MWh	1,500 MWh
Powerdirect				
Powerdirect Basic Market Contract ⁴	\$940	\$104	12%	9%
Red Energy				
Red Energy Market Contract ⁵	\$1,041	\$113	2%	2%
SA Electricity				
SA Market Electricity Contract	\$1,044	\$115	2%	0%
TRUenergy				
TRUenergy At Home ²	\$1,004	\$115	6%	3%
TRUenergy Go For More ⁵	\$1,022	\$110	4%	4%
TRUenergy Go Easy ⁵	\$1,064	\$115	0%	0%

Source: See Appendix E for source details

Notes: (1) Account establishment fee is payable (2) Loyalty rebate payable (3) Entry rebate payable (4) Direct debit rebate payable (5) Prompt payment discount payable.

We note that a number of energy retailers have a number of other market offers available that incorporate higher charges for the use of renewable energy sources which are not included in table 7.1 above.

Table 7.1 shows that all electricity retailers have a market contract that is offered at a discount to the standing contract, where the discount offered ranges from 1 per cent to 12 per cent from the AGL standing contract (these contracts are highlighted). Generally, those contracts offered at a discount from the standing contract for peak consumption also have discounted rates for off-peak consumption and the percentage discount is consistent over different consumption levels. We note that the potential savings that may be achieved under these contracts may be greater than that outlined above due to the inclusion of rebates and other benefits such as loyalty rebates, entry rebates or rebates for prompt payment or payment by direct debit. These additional fees and rebates are outlined in more detail in Appendix H.

Our assessment of the estimated bill under the contracts offered by each retailer over time suggests that discounts to the standing contract have been offered from the beginning of FRC. While AGL have only recently begun to offer market contracts at rates at a significant discount to their standing contract (excluding other price and non-price benefits), other retailers such as Origin and TRUenergy have offered discounts of up to 12 per cent

since at least 2004. With the exception of AGL, there has been no discernable trend in the discount provided over time by each retailer.

While all retailers offer at least one contract at a discount to the standing contract, we note that four retailers (AGL, EnergyAustralia, Origin and TRUenergy) also have a number of contracts available at rates equal to the standing offer contract. Some of these contracts incorporate other benefits of value to customers such as the use of renewable energy sources, however, a number of these do not. For example the AGL Freedom, AGL Advantage, Origin HomeSupply and TRUenergy Go Easy contracts do not appear to offer customers any additional benefits over these retailer's lower cost market contracts.⁹¹ It is unclear from the information provided whether these retailers only make their lower cost market contracts available to particular customer classes.

Details of electricity market contracts made available to small business customers are not as transparent as those for residential customers since they are not required to be published by retailers under the Commission's Energy Price Disclosure Code. However, information provided by some retailers as part of this review suggests that a variety of market contracts are available to small business customers with different rates and rate structures.

7.1.2. Gas market contracts

The estimated annual gas charge for residential customers with a medium level of gas usage (24GJ) under each market contract offered in South Australia is set out in table 7.2 below. Again, market contracts are listed by retailer from lowest to highest cost. Those gas contracts which are offered only in conjunction with electricity, ie, dual fuel contracts, are specified. The estimated annual charge under each contract excludes additional charges such as account establishment fees or rebates, although we have noted where such charges and rebates apply. A more detailed summary of all additional costs and benefits associated with each market contract is set out in Appendix H.

As was the case for electricity, all gas retailers offer at least one market contract at a discount to Origin's standing contract for supply to metropolitan Adelaide, where the discount ranges from 2 per cent to 6 per cent (these contracts are highlighted). Again, the discount provided is generally constant across consumption levels. Again, there is no discernable trend in the discounts provided over time. We note that the potential savings that may be achieved under these contracts may be greater than this due to the inclusion of rebates and other benefits. Most of the gas contracts offered at a discount to Origin's standing contract are for dual fuel contracts only. For example, AGL's Freedom 5% gas offer is only made in conjunction with its electricity offer as are all of EnergyAustralia's gas offers. Origin and TRUenergy each only offer one stand-alone gas contract at a discount to the standing contract.

Our assessment of the estimated bill under the contracts offered by each retailer over time suggests that discounts to the standing contract have been offered from the beginning of FRC, although the discounts have not been as substantial for gas as they have for electricity.

⁹¹ Note that there are two AGL Advantage contracts that are available. Only one of these includes a loyalty payment of \$100 over three years or \$150 if the customer takes a dual fuel contract.

Table 7.2
Estimated Annual Bill Under Gas Market Contracts as at March 2007

	Estimated Annual Gas Bill (24GJ)	Savings Relative to Standing Contract (%)
<u>Standing Contract</u>		
Origin Standing Contract	\$596	
<u>Market Contracts</u>		
AGL		
AGL Freedom 5% (Dual Fuel)^{N1}	\$574	4%
AGL Freedom ^{N1}	\$596	0%
AGL Advantage ^{N1}	\$596	0%
EnergyAustralia		
EnergyAustralia Maxisaver (Dual Fuel)	\$560	6%
EnergyAustralia RAA Saver (Dual Fuel)^{N5}	\$560	6%
EnergyAustralia EasySaver (Dual Fuel)	\$566	5%
EnergyAustralia Green Saver 2 (Dual Fuel)	\$584	2%
EnergyAustralia RAA Green Saver (Dual Fuel)	\$584	2%
EnergyAustralia Green (Dual Fuel)	\$596	0%
EnergyAustralia Green Saver Premium (Dual Fuel) ^{N2}	\$596	0%
EnergyAustralia Qantas Frequent Flyer (Dual Fuel) ^{N5}	\$596	0%
EnergyAustralia Qantas Frequent Flyer Green Saver (Dual Fuel)	\$596	0%
Origin Energy		
Origin HomeChoice	\$584	2%
Origin GreenEnergy Home (Dual Fuel)	\$584	2%
Origin One Month Free (Dual Fuel)	\$596	0%
Origin ChoicePlus Magazine Offer (Dual Fuel)	\$596	0%
TRUenergy		
TRUenergy Go For More^{N7}	\$578	3%
TRUenergy At Home ^{N2}	\$596	0%
TRUenergy Go Easy ^{N7}	\$596	0%

Source: See Appendix E for source Notes: (N1) Account establishment fee is payable (N2) Loyalty rebate payable (N3) Green Spirit charges equal to 99c per week. This has been incorporated into the peak consumption component but not the off-peak consumption component (N4) Entry rebate payable (N5) Direct debit rebate payable.

While all retailers have at least one market offer at a discount to the standing contract, they also have a number of contracts available at rates equal to the standing offer contract. As was the case for electricity, it is unclear from the information provided whether these retailers make their lower cost market contracts available to all customer classes.

On the basis of information supplied by AGL and TRUenergy it appears that a number of market contracts are available to small business gas customers with various fixed discounts from the standard product offering. However, these contracts are only available to customers in metropolitan Adelaide. We have not conducted a detailed analysis of these contracts due to the lack of available data.

Conclusion

All retailers of electricity and/or gas in South Australia offer at least one market contract at a discount to the standing contract, although discounted gas offers are often only available for customers that take out dual fuel contracts. Some retailers continue to offer contracts at rates equal to the standing contract with no additional associated benefits. It is unclear from the information provided whether these contracts are the only type of contracts that are available to particular customer classes, eg, customers that have previously defaulted or that are on instalment plans. If so, this would suggest that these customers may not obtain any significant benefits from moving to market contracts.

7.2. Availability of Differentiated Market Contracts with Alternative Price and Non-Price Features

In addition to discounts from the standing offer contract, competition between retailers may be evidenced by the development offers that vary in terms of their price or non-price features. In an effectively competitive market, retailers will have an incentive to differentiate their products from that of other retailers in order to attract customers and will be responsive to the observed preferences of customers.

In the sections below we assess both the price and non-price benefits offered under market contracts to South Australian residential customers. For the purpose of this analysis we consider price benefits to include one-off or periodic rebates from the customer's electricity bill. Conversely, we consider non-price benefits to include payments or rebates for expenditure that is not directly related to the customer's energy bill or the offer of other non-monetary benefits that are of value to customers. We also consider customer views on the variety of offers available and the extent of product innovation over the last year.

7.2.1. Price Benefits

A summary of the price features offered by each retailer under market contracts for residential customers is set out in table 7.3 below. A summary of the features of all contracts offered by each retailer is set out in more detail in Appendix H.

The type of price features offered by retailers include loyalty rebates, entry or sign-up rebates, rebates for paying bills on time and rebates for paying by direct debit. Not all retailers provide each of these types of price benefits. It is interesting to note that those

retailers with more than one market offer generally only apply price benefits to only one or two of those offers. For example:

- § AGL only applies loyalty credits to its Advantage contract and not to its Freedom contract (note AGL also has a price fact sheet for its Advantage contract with no loyalty credit applied); and
- § Energy Australia only applies the \$25 rebate for paying bills on time to two of the 9 offers listed in tables 7.1 and 7.2 above and only applies a direct debit discount to one of these contracts.

Table 7.3
Additional Price Benefits Offered under Market Contracts

Retailer	Price Feature
AGL	AGL Advantage provides for loyalty credits over the three year contract term: \$100 for electricity only contract, \$50 for gas only contract and \$150 for electricity and gas contract.
Aurora Energy	No additional price discounts provided
Country Energy	\$60 entry rebate and loyalty card discounts
EnergyAustralia	RAA Green Saver and Green Saver Premium allow for a \$25 rebate if all bills are paid on time over the previous 12 month period. RAA Saver account allows for a direct debit rebate of 2.74c per day, which equates to around \$10 per annum.
Momentum Energy	10% discount provided for payment by the due date and loyalty rebate available
Origin Energy	One month free electricity under the One Month Free and One Month Free GreenEarth dual fuel contracts. GreenEarth contribution of \$2 per week waived if the customer takes out the GreenEnergy Home dual fuel contract.
Powerdirect	\$20 one-off rebate for direct debit
Red Energy	5% discount provided for payment by the due date under a contract with no fixed term, increased to 7% for a 2 year market contract.
South Australia Electricity	No Price Discounts provided
TRUenergy	Loyalty rebate payable under the At Home contract. 3% discount provided for payment by the due date under the Go Fore More and Go Easy contracts.

Source: See Appendix E for source details

Note that in addition to price benefits, some contracts include additional charges for establishing an account and for exiting a contract or for terminating the contract before the expiry of the contract. For example:

- § AGL, Aurora Energy and Origin Energy each charge an account establishment fee of between \$19.36 and \$55;
- § Aurora Energy, Country Energy, South Australia Electricity and TRUenergy each charge an exit fee of between \$50 and \$95; and
- § AGL, Energy Australia, Powerdirect and Red Energy each charge early termination fees in the range of \$25 to \$125 depending on when the contract is terminated.

We note that a range of price benefits are also offered to small business customers although these are often not specified on retailer websites. Those retailers that do publish some information regarding price benefits under market offers to small business customers include Origin Energy (10 per cent discount from standard business rates), Red Energy (5 per cent discount for paying by the due date and TRUenergy (3 – 10 per cent discount off electricity and gas bills and a further 3 per cent discount for paying by the due date for some plans).

7.2.2. Non-Price Features

Non-price benefits range from the offer of green energy options, flexible payment options, single billing for dual fuel customers, and the offer of specific monetary benefits or tangible goods. A summary of the specific non-price benefits offered by each retailer under market contracts for residential customers is set out in table 7.4 below. A summary of the features of all contracts offered by each retailer is set out in more detail in Appendix G.

Table 7.4
Non-Price Benefits Offered under Market Contracts

Retailer	Non-Price Benefit
AGL	\$50 Voucher with \$200 minimum spend at an AGL shop or \$400 minimum spend at an AGL Energy shop for all AGL contracts
Aurora Energy	No specific additional non-price benefits noted on website
Country Energy	No specific additional non-price benefits although fact sheet notes that switching incentives may be included in the offer in the form of material or goods.
EnergyAustralia	<p>Discount on membership renewal fees for Royal Automobile Association of South Australia, valued at \$40 in Year 1 and \$30 in years 2 and 3 for both the RAA Saver and RAA Green Saver contracts.</p> <p>Under the Qantas Frequent Flyer electricity only contract customers received 7,500 Qantas frequent flyer points plus an additional 1,000 points if paying by direct debit or make payment from a credit card account. If customers sign up for electricity and gas, they receive 15,000 frequent flyer points. The points may be transferred to another nominated Qantas frequent flyer member.</p> <p>Under the Qantas Frequent Flyer Green Saver contract customers receive 2,500 Qantas frequent flyer points if they contract for electricity only and 5,000 points if they contract for both electricity and gas. All customers receive one point for every dollar spent on their electricity or gas. Electricity only customers receive 1,000 points per annum for paying bills on time whereas electricity and gas customers receive 2,000 points per annum for prompt payment.</p>
Momentum Energy	No specific additional non-price benefits noted on website
Origin Energy	<p>Free magazine for 2 years under the ChoicePlus and ChoicePlus GreenEarth dual fuel contracts.</p> <p>Free energy efficiency pack provided under the GreenEnergy Home dual fuel contract.</p>
Powerdirect	\$20 per customer referred or transferred
Red Energy	No specific additional non-price benefits noted on website
South Australia Electricity	Monthly prize draw of a holiday travel gift voucher valued at \$2,000 which is fully transferable but not redeemable for cash
TRUenergy	<p>Coles Myer gift vouchers under the Go For More and At Home contracts.</p> <p>DVD offered if customers sign up for both fuels under the Go For More and Go Green market contracts.</p> <p>Bill smoothing for dual fuel customers.</p>

Source: See Appendix E for source details

We note that some non-price benefits are also made available to small business customers although these are much less widely publicised than offers to residential customers.

7.2.3. Customer Views on Innovation

In both its 2004 and 2006 customer surveys, the Commission asked respondents whether, in their opinion, the offers made by retailers were more innovative compared to a year ago and whether there was a greater variety of offers compared to a year ago.⁹²

There was a reasonably high level of agreement among both residential and small business respondents that there were a greater variety of offers around January 2006 compared to those that were available at the beginning of 2005. In terms of these offers being more innovative compared to a year ago, there was a mixed response, with respondents on average neither strongly agreeing nor disagreeing that this was the case.⁹³

Conclusion

Retailers offer a range of price benefits to customers under market contracts, although such benefits are often attached to only one or two contracts. There are also a wide range of non-price benefits offered under market contracts. These are often in the form of rebates payable for expenditure on particular items other than customer's energy bill but also include tangible gifts, prize draws and rebates paid as a reward for customer referrals.

Most retailers also appear to offer a range of green energy options that include different types of renewable energy sources, eg, wind and solar, and different degrees of renewable energy production. These offers are mostly made at a premium to the standing contract, although some retailers are starting to offer some green energy options at no additional cost to the customer. The development of these renewable energy offers suggests that customer's value the environmental benefits associated with renewable energy supplies and that retailers have responded to this via the development of these green energy options.

7.3. Retailer Performance and Customer Satisfaction

Another potential indicator of the effectiveness of competition is the extent to which retailers have improved performance in relation to customer management over time. Retailers report on a number of measures of performance to the Commission on a quarterly basis, including the level of complaints received and the level of responsiveness to telephone and written enquiries. The performance of each retailer in relation to these measures over the period 2003 to 2006 is set out in table 7.5 below.

⁹² Respondents were asked to rate, on a scale of 1 to 5, where 5 is strongly agree and 1 is strongly disagree, their level of agreement with these statements. It is generally considered that an average rating of 3.5 represents a reasonably high level of agreement, 4.0 a very high level of agreement, and 4.5 or above an extremely high level of agreement.

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, q. 54.

⁹³ Residential respondents gave the question regarding the variety of offers a rating of 3.7, which was unchanged from 2004, and small business respondents gave this a rating of 3.8, up from 3.5 in 2004. Residential respondents gave the question regarding the innovation of offers a rating of 3.3, up from 3.1 in 2004. Small business respondents also gave this a rating of 3.3, up from 3.0 in 2004.

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p. 95 and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.77.

Table 7.5
Retailer Performance, 2003 - 2006

	AGL	Country Energy	Energy Australia	Origin Energy	Power-direct	TRU energy
Electricity						
Average Complaints per 100 Customers						
2003	0.46	N/A	N/A	4.58	N/A	10.19
2004	0.48	N/A	13.64	2.71	5.24	1.66
2005	0.65	1.95	1.18	1.01	1.53	0.71
2006	0.64	1.17	1.02	0.86	1.85	1.39
Percentage of Calls Answered in 30 Seconds						
2003	79%	N/A	N/A	69%	N/A	71%
2004	83%	N/A	56%	73%	70%	83%
2005	87%	86%	81%	75%	83%	81%
Percentage of Written Enquiries Answered in 5 Days						
2003	95%	N/A	N/A	100%	N/A	100%
2004	98%	N/A	66%	94%	97%	88%
2005	99%	100%	N/A	95%	95%	92%
Gas						
Average Complaints per 100 Customers						
2004	0.34	N/A	3.78	0.49	N/A	0.33
2005	0.71	N/A	1.16	0.37	N/A	0.18
2006	0.53	N/A	0.18	0.30	N/A	0.44
Percentage of Calls Answered in 30 Seconds						
2004	67%	N/A	N/A	80%	N/A	85%
2005	80%	N/A	82%	62%	N/A	76%
Percentage of Written Enquiries Answered in 5 Days						
2004	95%	N/A	N/A	91%	N/A	100%
2005	99%	N/A	55%	95%	N/A	90%

Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

The table shows that the performance of retailers in relation to all measures has generally improved over time. With the exception of AGL, all of the retailers outlined above had fewer complaints per customer over 2005 and 2006 than at the time of entry in 2003 and 2004. The drop off in the rate of complaints occurred over all complaint types: billing, marketing, transfer and other complaints. Although the number of complaints received by

AGL in relation to electricity supplies as a proportion of its customer base increased over the period, the rate of complaints to AGL was substantially lower than that for other retailers. The increase in the rate of complaints to AGL is likely to be due to both the fall in the number of AGL's customers as well as the increase in the number of transfers over time.⁹⁴

Retailer's responsiveness to telephone enquiries also appears to have improved over time, at least for electricity enquiries. The percentage of telephone enquiries answered within 30 seconds in relation to electricity supplies increased for all retailers over the period from rates between 69 to 79 percent to rates between 75 to 87 per cent.⁹⁵ By contrast, the percentage of telephone enquiries answered within 30 seconds in relation to gas supplies decreased over 2004 to 2005 for both Origin Energy and TRUenergy from rates of around 80 to 85 per cent to rates of around 62 to 76 per cent respectively. It is unclear why this would be the case.

The timeliness of retailer responsiveness to written enquiries varied between retailers, although was generally at high levels with most retailers responding to more than 90 per cent of written enquiries within 5 days.

The performance of retailers in relation to telephone and written enquiries appears to accord with customer survey results. In its 2006 customer surveys, the Commission asked respondents whether they had contacted their retailer within the previous 12 months, and if so, how satisfied they were with the timeliness of the response and the assistance provided.⁹⁶ Only 27 per cent of residential respondents and 26 per cent of small business respondents had contacted their retailer in the previous 12 months. There was a reasonably high level of satisfaction among residential customers with respondents rating their level of satisfaction with timeliness of retailer's response at 3.7 and the assistance provided at 3.8 out of 5.⁹⁷ On average, small business respondents were less satisfied with both the timeliness of retailer's response and the assistance provided, giving these a rating of 3.1 and 3.5 respectively.⁹⁸ This may reflect a lower degree of priority given to small business customers by retailers, or alternatively, it could reflect differential attitudes between residential and small business customers as to what constitutes a 'timely' response.

⁹⁴ The average number of complaints per 100 customers for each retailer is comparable with that of Victorian retailers, although though we note that retailer performance varied considerably in Victoria between 0.25 and 8.3 for the year ended 30 June 2006. See ESC, *'Energy Retail Businesses: Comparative Performance Report for the 2005 – 06 Financial Year'*, November 2006, p.44.

⁹⁵ These performance rates are similar to that of Victorian retailers. See ESC, *'Energy Retail Businesses: Comparative Performance Report for the 2005 – 06 Financial Year'*, November 2006, p.40.

⁹⁶ Respondents were asked to rate their level of satisfaction on a scale of 1 to 5, where 5 is very satisfied and 1 is not at all satisfied.

McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, and *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, q. 57.

⁹⁷ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 99.

⁹⁸ McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Business'*, dated January 2006, p.79 - 80.

7.4. Impact of Competition on Financially Disadvantaged Groups

As part of this review it is necessary to consider the extent to which the benefits derived from FRC are shared between customer groups, particularly financially disadvantaged customers. Low-income customers or those receiving financial assistance may be less attractive to retailers, particularly if the risk of default by these customers is higher than that for other customer groups. Retailers may therefore be less willing to offer contracts to these customers, where they can be identified. Alternatively, retailers may choose to offer products that meet the needs of financially disadvantaged customers through the offer of flexible energy payment plans. Access to contracts that allow for flexible payment arrangements will help to reduce the number of disconnections due to non-payment

This section considers a range of indicators specific to the outcomes of FRC for low income or financially disadvantaged customers. First, we consider whether there are any differences in the views, experiences or behaviour of low income customers that may suggest there are issues specific to this customer group. Second, we consider the change number and distribution of customers on financial assistance and instalment plans and the trend in the number of disconnections for non-payment.

7.4.1. Conduct and views of low-income customers

In both its 2004 and 2006 customer surveys the Commission identified respondents that could be classified as low income customers. These customers were classified as those that:

- § were single, with a gross household income of \$20,000 per annum or less;
- § lived with a partner or spouse, with a gross household income of \$25,000 per annum or less;
- § were single adults with a dependant child or children, with a gross household income of \$30,000 per annum or less; or
- § lived in a household with two or more adults with dependant children, with a gross household income of \$35,000 per annum or less.

The Commission also identified those customers that received an energy concession. We note that low-income customers likely comprise a subset of energy concession customers. In December 2006 around 30 per cent of all South Australian energy customers were concession recipients.⁹⁹

The results of the 2006 customer survey showed that while low income customers were less aware than others of their ability to choose their energy retailer, they were no more likely

⁹⁹ Concession recipients represented a higher proportion of all survey respondents at 39 per cent. McGregor Tan Research, *'Monitoring the Development of Energy Retail Competition – Residents'*, dated February 2006, p. 104.

than other customers to name AGL as their current retailer for electricity, and were in fact more likely to name AGL as opposed to Origin as their current retailer for gas.¹⁰⁰

The proportion of low income customers that had been contacted by an energy retailer with an offer of a contract was around the same as that for other customers, as was the case for concession recipients.¹⁰¹ With the exception of Origin, there was no discernable difference in the retailers from whom electricity offers were made, suggesting that most retailers either do not attempt to restrict their offers to higher-income customers, or they are unable to effectively carry out such a strategy. In the case of gas, a higher proportion of low-income customers named AGL, and a lower proportion named Origin, as a retailer from whom an offer was made.¹⁰²

There was no discernable difference between low-income or concession holders and other customers of the ease of understanding either the contracts that had been offered to them or the information they found themselves regarding market offers.¹⁰³ These customers were less likely than other customers to look for information regarding market contracts and placed less importance on this information in their decision to switch electricity retailers.

It is interesting to note that both the low-income customers surveyed and those receiving energy concessions were more likely to have switched to an electricity market contract than other customers, although this difference was not statistically significant for low-income customers. Concession customers were also more likely than other customers to have

¹⁰⁰ As noted earlier, low-income customers were more likely than other customers to be of the view that they are obliged to purchase electricity from their current retailer (21%). However, of those low-income customers surveyed, only 64% named AGL as their current retailer for electricity, compared with 61% for other customers. A similar proportion of low-income and other customers named TRU-energy, EnergyAustralia and Powerdirect as their current electricity retailer.

Of all low income gas customers, 29% named AGL as their current retailer for gas, compared to only 16% for other customers. Low income customers were less likely than other customers to name Origin as their gas supplier (51% compared to 64%) and were equally likely to name TRUenergy and EnergyAustralia.

McGregor Tan Research, '*Computer Tabulations – Residents (b)*', 2006, confidential supporting data to '*Monitoring the Development of Energy Retail Competition – Residents*', dated January 2006, p. 10 and 63.

¹⁰¹ 49% of low income customers had been contacted by an electricity retailer, compared to 53 per cent of other customers. For gas, the proportions were 33% and 35% respectively.

McGregor Tan Research, '*Computer Tabulations – Residents (b)*', 2006, confidential supporting data to '*Monitoring the Development of Energy Retail Competition – Residents*', dated January 2006, pp. 15 and 67.

¹⁰² The proportion of low-income respondents that received an offer of an electricity contract from Origin was low compared to other customers at 15 and 25 per cent respectively. The proportion of concession recipients that had been contacted by Origin was 14 per cent compared to 27 per cent for non-concession holders.

McGregor Tan Research, '*Computer Tabulations – Residents (a)*', 2006, p. 73 and 301 and '*Computer Tabulations – Residents (b)*', 2006, pp. 16, and 67 confidential supporting data to '*Monitoring the Development of Energy Retail Competition – Residents*', dated January 2006.

¹⁰³ On the whole, low income earners were slightly less likely to have looked for information themselves, were slightly more likely to have considered the information in respect of gas to be insufficient to make an informed choice and consider the information obtained in regard to electricity to be less important than other customers in their decision to switch. We note that these results were not marked as being statistically significant.

McGregor Tan Research, '*Computer Tabulations – Residents (a)*', 2006, p. 82, 200, 236, 241, 246, 319, 443, 470 and 475 and '*Computer Tabulations – Residents (b)*', 2006, pp. 18, 45, 52, 54, 55, 70, 98, 103, 105 and 106 confidential supporting data to '*Monitoring the Development of Energy Retail Competition – Residents*', dated January 2006.

switched to a gas market contract, primarily with AGL.¹⁰⁴ On the whole, a greater proportion of low-income and concession customers said that they would be unlikely to switch within the next year, although this result must be considered in light of the larger proportion of these customers that had already switched.¹⁰⁵

Of those customers that did switch, price/cost was considered the most important factor by all customer groups, although consistency of supply rated more highly among low-income and concession customers for both electricity and gas.¹⁰⁶ For those customers that did not switch, low-income and concession recipients were more likely to note that they were happy with their current retailer.¹⁰⁷

7.4.2. Trends in financial assistance, instalment plans, payment defaults and disconnections for non-payment

As noted above, in addition to offering energy plans below standing contract rates, one of the ways in which both incumbents and new entrant retailers can assist low income or financially disadvantaged customers is to offer these customers contracts with extended payment terms, with the potential for payments to be made in instalments.

Under the Energy Retail Code, retailers are required to offer instalment plans, where an instalment plan is defined as:

“an arrangement between a retailer and a small customer for the customer to pay arrears and continued usage on their account, according to an agreed payment schedule and capacity to pay. It does not include customers using a payment plan as a matter of convenience or for flexible budgeting purposes.”

The Commission also defines an instalment plan as one that involves at least three payments in order to differentiate between customers in financial hardship from those using extended or flexible payment plans for convenience.

The percentage of residential customers with financial assistance and those on instalment plans for each retailer for the years ended 31 December 2004 to 2006 is set out in table 7.6 below.

¹⁰⁴ 43% of low-income customers said they had switched to an electricity market contract compared to 39% for other customers. Low income and other customers were equally likely to have taken out a market contract with a gas retailer (32% of respondents). 46% of concession recipients said they had switched to an electricity market contract and 36% to a gas market contract compared to 37% and 30% for other customers respectively.

McGregor Tan Research, ‘Computer Tabulations – Residents (a)’, 2006, p. 106 and 343 and ‘Computer Tabulations – Residents (b)’, 2006, pp. 24, and 76 confidential supporting data to ‘Monitoring the Development of Energy Retail Competition – Residents’, dated January 2006.

¹⁰⁵ McGregor Tan Research, ‘Computer Tabulations – Residents (a)’, 2006, p. 159 and 402 and ‘Computer Tabulations – Residents (b)’, 2006, pp. 35 and 88 confidential supporting data to ‘Monitoring the Development of Energy Retail Competition – Residents’, dated January 2006.

¹⁰⁶ McGregor Tan Research, ‘Computer Tabulations – Residents (a)’, 2006, p. 133 and 370 and ‘Computer Tabulations – Residents (b)’, 2006, pp. 29 and 81, confidential supporting data to ‘Monitoring the Development of Energy Retail Competition – Residents’, dated January 2006.

¹⁰⁷ McGregor Tan Research, ‘Computer Tabulations – Residents (a)’, 2006, p. 134 and 387 and ‘Computer Tabulations – Residents (b)’, 2006, pp. 31 and 83, confidential supporting data to ‘Monitoring the Development of Energy Retail Competition – Residents’, dated January 2006.

Table 7.6
Customers with Financial Assistance, on Instalment Plans and that were
Disconnected for Non-Payment, 2003 – 2006

	AGL	Country Energy	Energy Australia	Origin Energy	Power-direct	TRU energy	Total
Financial Assistance							
Percentage of Residential Customers with Financial Assistance							
2004	29.90%	n/a	55.82%	11.46%	29.24%	11.57%	28.43%
2005	30.44%	n/a	43.06%	21.21%	51.92%	10.86%	28.56%
2006	31.32%	46.30%	30.66%	20.93%	62.71%	31.63%	30.67%
Instalment Plans							
Percentage of Residential Electricity Customers on Instalment Plans							
2004	5.37%	n/a	0.64%	1.22%	0.52%	2.11%	5.00%
2005	1.33%	1.69%	0.70%	1.86%	0.47%	3.00%	1.50%
2006	1.65%	1.01%	0.65%	2.66%	0.35%	4.99%	2.04%
Percentage of Residential Gas Customers on Instalment Plans							
2004	0.00%	n/a	2.24%	0.75%	n/a	0.84%	0.74%
2005	0.31%	n/a	0.87%	0.70%	n/a	1.37%	0.70%
2006	0.68%	n/a	0.65%	1.03%	n/a	3.14%	1.17%
Disconnections for Non-Payment							
Disconnections for Non-Payment per 100 Residential Electricity Customers							
2004	2.14	0	0.23	0.07	0.00	0.18	1.94
2005	1.26	0	0.13	0.19	0.03	0.44	1.03
2006	1.29	0	0.20	0.24	0.03	0.63	0.98
Disconnections for Non-Payment per 100 Residential Gas Customers							
2004	0	n/a	0	0.83	n/a	0	0.77
2005	0	n/a	0.07	1.11	n/a	0.17	0.89
2006	0	n/a	0.22	0.77	n/a	0.58	0.60

Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

The table shows that a relatively high proportion of residential customers received financial assistance in the year to December 2006 at around 30 per cent, up slightly from the previous two years. Customers receiving financial assistance were spread between retailers, with new entrant retailers Country Energy and Powerdirect having a much higher proportion of these customers and Origin energy having a much smaller share of these customers as a percentage of its total customer base.

The proportion of residential customers on instalment plans for both electricity and gas is relatively low when compared to those that receive financial assistance. We note, however, that it is possible that a larger number of customers are on flexible payment plans that are not technically considered instalment plans, and are therefore not captured in the above data.¹⁰⁸

The proportion of customers on instalment plans for both electricity and gas appears to have increased since the 2005 year. In its last monitoring report, the Commission suggested that care should be exercised in drawing conclusions on trends in relation to this statistic, as it has been liaising with retailers in an effort to improve consistency in the reporting of this indicator.¹⁰⁹

Even if the data do suggest that an increasing number of customers are either opting or are forced to move to instalment plans, this is not necessarily an indication that competition is not effective for these customers. As noted by the Commission, the increase in instalment plans could be considered a favourable trend given the assistance such plans provide in preventing financially disadvantaged customers from being disconnected. The number of financially disadvantaged customers is ultimately outside the control of retailers and is more likely dependant on wider economic factors such as unemployment and wage movements. Evidence that retailers are responding to an increased level of financial hardship among customers may therefore suggest that these customers have benefited from increased competition in the energy retail market.

An assessment of disconnection for non-payment shows that the number of disconnections per 100 customers has fallen as more customers move to instalment plans.¹¹⁰ The number of disconnections for non-payment fell by 5 per cent for electricity and 3 per cent for gas over 2006. While in no way conclusive, the statistics may suggest that the move toward increased use of instalment plans has had a beneficial impact on disconnection rates.

It is interesting to note that the rate of electricity disconnections in South Australia is significantly higher than that in neighbouring Victoria and New South Wales. In its latest monitoring report, the Commission notes that the average number of electricity disconnections per 100 customers was 0.98 in New South Wales and 0.54 in Victoria in the year to 30 June 2005.¹¹¹ The disconnection rate for Victoria fell further to 0.22 per 100 customers for the year ended 30 June 2006.¹¹²

¹⁰⁸ The proportion of small business customers on instalment plans is considerably lower than that for residential customers and has therefore not been reported separately above.

¹⁰⁹ ESCOSA, *'Performance of South Australian Energy Retail Market; 2005/06 Annual Performance Report'*, November 2006, p.28.

¹¹⁰ Note that the Commission currently assesses a number of other disconnection statistics including residential disconnections and reconnections for non-payment in the same name and address in the previous 24 months, disconnections and reconnections in the same name and address of concession recipients and disconnection of customers on an instalment plan in the previous 24 months. These indicators have been reported by retailers since 1 July 2006, although there is insufficient data to conduct any analysis of these indicators here.

¹¹¹ ESCOSA, *'Performance of South Australian Energy Retail Market; 2005/06 Annual Performance Report'*, November 2006, p.35.

¹¹² ESC, *'Energy Retail Businesses: Comparative Performance Report for the 2005 – 06 Financial Year'*, November 2006, p.23.

As noted by the Commission it is unclear why South Australia's rate of disconnections is high relative to other states, particularly given that data published by the EIOSA does not suggest that there are an inordinate number of complaints specifically in relation to disconnections. Similarly, there does not appear to have been any issues with non-compliance on the part of retailers with the disconnection provisions of the Energy Retail Code. Ultimately, differences in disconnection rates between states may be the result of a number of factors over which retailers and regulators have little control including differences in economic conditions and differences in the support systems for financially disadvantaged customers, such as the energy or other concession thresholds or the type of concessions available in each state. Differences in disconnection rates between retailers in any one year or a single retailer over time may also be due to factors specific to individual retailers. For example, information deficiencies may result in a lag between the time at which a disconnection should and does occur and the subsequent over or under-reporting of disconnections due to events that occurred in each period. This suggests that it is difficult to draw conclusions about the impact that competition has had on customer disconnections without assessing the broad range of factors that influence disconnection rates.

7.5. Summary of Market Performance

The analysis of market performance suggests that electricity retailers are offering products that are consistent with a competitive market outcome, at rates below the standing offer contract and with features and benefits that are responsive to customer preferences.

All electricity retailers in South Australia offer a contract that is at a discount to the AGL standing contract, where the discount provided ranges from 2 to 12 per cent for a customer with a mid-range annual peak consumption of 5,000 MWh. Recent new entrants Aurora, Country Energy, Momentum Energy and Powerdirect appear to offer the most significant discounts between 6 to 12 per cent, with more established retailers offering discounts of up to 6 per cent. Further discounts are provided under a number of contracts for paying bills by the due date or paying by direct debit which leads to further reductions in the average bill for customers, although we note only a few contracts attract these discounts.

While lengthy contract terms may have been a feature of market contracts at the implementation of FRC, a number of electricity market contracts that are currently on offer at a discount to the standing contract appear to be for no fixed term.¹¹³ Some of these contracts require customers to pay a one-off establishment fee, although a number of these do not.

Exit or early termination fees appear to be a feature of some market contracts, including both those with no fixed term and those with a term of two to three years. These fees range from \$25 to \$125 depending on when the contracted is terminated and are generally higher in the early years of fixed term contracts. While these fees increase the cost of customer switching prior to the contract exit date, they are often associated with the provision of related benefits such as loyalty rebates and discounts for non-energy related expenditure at

¹¹³ Under the Commission's Energy Price Disclosure Code retailers are not required to specify the term of contracts. For some contracts it is not possible to determine the contract term on the basis of the fact sheets published by retailers.

the time the contract was entered into. We note that a few market contracts are available at a discount to the standing contract for no fixed term and without any penalty for exit, such as the AGL Freedom 5% and the EnergyAustralia Easy Saver contract. Those customers that do not wish to be locked into a contract can therefore still obtain electricity supplies at a relatively competitive price under these contracts.

Most electricity retailers offer non-price benefits to induce customers to switch. These benefits range from vouchers for expenditure on items other than the customers electricity bill, discounts from membership renewal fees, frequent flyer points and discounts for customer referrals. These benefits are offered not only under those contracts with rates equal to the AGL standing contract, but also under those contracts offered at a discount to the standing contract. While these benefits do not reduce the customers' energy bill they do have a monetary value and are likely to play an important role in customers' decisions to switch.

In addition to the above non-price benefits, most retailers have developed at least one "green" energy option which allows customers to derive a proportion of their total energy consumption from renewable energy sources. Some retailers have developed a relatively broad range of green energy options, which specify either the proportion of the customer's energy consumption to be derived from renewable sources and/or the type of renewable energy source from which energy will be derived. Most of these contracts are offered at a premium to the standing contract, suggesting that some consumers are willing to pay more for a product with positive externalities. Some retailers have recently started to offer some green energy options at rates equal to the standing contract which may suggest that competition for those customers that wish to make some positive contribution to the environment but are still price sensitive is becoming more intense.

Market contracts for gas supplies appear to be less competitive than that for electricity. Only two retailers, Origin and TRUenergy provide gas-only market contracts at a discount to the standing contract, where the discount is in the region of 2 – 3 per cent. At least one of these appears to be for a fixed term of three years with penalties imposed for early termination. The other two gas retailers only offer gas market contracts as dual fuel contracts. The discounts provided under these contracts are in the range of 2 to 6 per cent, although these discounts may not be as beneficial as those provided under the aforementioned gas-only contracts if the customer can source a significantly cheaper electricity supplies from an alternate retailer.

Given that AGL and EnergyAustralia only offer gas under dual fuel contracts, the price and non-price benefits offered by these retailers are largely the same as that offered under electricity-only contracts, with incremental benefits for the addition of gas. Origin and TRUenergy have introduced additional benefits under their dual fuel contracts including one month's free energy, a 2 year magazine subscription and a DVD offer.

We note that the gas market contracts assessed appear to be for supply to Adelaide only. We have not conducted a more detailed assessment of the contracts that may be available to gas customer in rural and regional areas of South Australia but note that only Origin and Energy Australia appear to service these customers.

In addition to competing on price, retailers have also improved their performance in relation to a number of measures of customer service over the last three years. With the exception of AGL, the number of complaints made in relation to electricity and gas supplies has generally fallen over time and retailer response to telephone enquiries has improved, at least in relation to electricity supplies.

Market outcomes for low-income customers also appear to be improving. Low income customers appear to be taking advantage of market offers. They are just as likely to have switched to market contracts as other customers and are no more likely to have switched to a market contract with the incumbent retailer. In fact, low-income gas customers are more likely than other customers to have switched to AGL as opposed to a market contract with Origin.

The switching behaviour of low-income customers revealed in the Commission's customer surveys is supported by data provided by retailers which indicate that customers receiving financial assistance are spread between retailers. Concession recipients comprise around 30 per cent of the customer base of the more established retailers AGL, EnergyAustralia and TRUenergy and a much higher proportion of the customer base of new entrant retailers Country Energy and Powerdirect. Origin Energy is the only retailer with a much lower share of these customers, although its share of these customers is growing over time.

8. Conclusion

This report has considered the degree to which competition in energy retail markets for small customers in South Australia can now be considered effective. Importantly, this assessment has been undertaken in the context of a transition from a service that has a long history of monopoly provision to and beyond the opening up of the market to full retail competition. Although it may be many years before market outcomes are not influenced in any way by this history, the assessment of the effectiveness of competition must strike a balance between the implications of history for incumbent service providers and the fact that competition and choice are forward looking concepts.

The term ‘effective competition’ refers to the degree of rivalry between market players that is sufficient to ensure that no one producer, or group of producers, has sufficient market power to be able to earn significant durable above-normal profits through giving less or charging more. While effective competition does not require outcomes to be consistent with the hypothetical ideal of perfect competition, in the case of energy retail markets that were once served by regulated monopolies, it could be expected that effective competition would be characterised by:

- § growth in the number and market share of new entrant retailers over time, which suggests that barriers to entry and/or expansion are sufficiently low to encourage entry where profitable opportunities for supply exist;
- § evidence of rivalry between retailers through the offer of contracts at rates lower than the regulated standing contract and/or the offer of differentiated products with various price and non-price features that change over time in response to customer preferences; and
- § evidence that customers are responding to the offers made by retailers.

Our analysis of the outcomes observed in the South Australian electricity retail market for small customers suggest that this market is now effectively competitive. A total of nine retailers have entered this market in the four years since the introduction of FRC, suggesting that barriers to entry are relatively low. Over this period these retailers have managed to capture at least 36 per cent of all residential and 25 per cent of all small business customers. Given that four of these retailers only entered the market over the year to December 2006, we expect that the market share of new entrant retailers will continue to increase in the coming years, as they work on expanding their customer base in both metropolitan Adelaide and other regional areas.

Our assessment of market conduct suggests that most small customers are aware of their ability to choose their own retailer, although very few appear to be willing to contact retailers on their own accord or look for information regarding market offers that are available to them. While such apathy on the part of customers may in some circumstances suggest that competition may not be particularly effective, such behaviour must be always considered in light of actual switching data. Customer switching from standing to electricity market contracts has been relatively high over the last five years with around 60 per cent of residential and 35 per cent of all small business customers having switched to market contracts. Customer switching appears to have been led primarily through retailer

marketing activity, with over half of all small customers having been contacted by an electricity retailer with a market offer since the implementation of FRC.

The entry of new retailers has led to pricing pressure in the market, with all retailers now offering market contracts for residential customers at discounted rates to the standing contract. While there has been no discernable trend in the extent of discount provided by each retailer over time, the discounts currently on offer are in the range of 2 to 12 per cent from the standing contract. These discounts are not limited to those customers with high energy usage, but are available to customers at all consumption levels, including those with off-peak consumption. There is also evidence that retailers are attempting to differentiate their products through the offer of various price and non-price contract features such as discounts for prompt payment or payment by direct debit as well as discounts or rebates for non-energy related expenditure. For most market contracts the actual monetary savings or total benefits available are therefore greater than just the upfront discount from the standing contract rates.

The market rates available for small business electricity customers are not as transparent as that for residential customers since the amounts payable under these contracts are not required to be published by retailers under the Commission's Energy Price Disclosure Code. However, information provided by retailers in the course of this review suggest that there are a variety of market contracts available to small business customers at varying rates and with different price and non-price benefits.

Looking forward, there is little reason to suggest that competition between retailers for both residential and small business electricity customers will not continue to grow, with more customers moving to market contracts over time. The one factor identified by retailers as a potential concern for future competition was the trend toward increased vertical integration, in combination with the risk of increased concentration among generators. While access to competitive electricity supplies and adequate hedging products was not, on the whole, considered a significant barrier to entry or expansion, some retailers did raise concerns that further integration may lead to a reduction in the availability of hedging products and ultimately place non-vertically integrated retailers at a disadvantage to their integrated counterparts. We note that the ACCC is aware of this concern and will consider the impact of any future acquisitions on the ability of non-vertically integrated retailers to compete in the market when conducting merger assessments.

Our analysis of outcomes in the South Australian gas retail market for small customers suggests that it is well on the way to being effectively competitive, albeit with some limited areas of exception. It is important to recall that the introduction of FRC in the gas retail market followed that in electricity by around one year. On that basis alone, it could be expected that the transition to effective competition would not be as well advanced.

Notwithstanding this less demanding expectation, our analysis suggests that competition for small retail customers in the principal, metropolitan Adelaide segment of the gas market is well established, and likely to be effective. A fewer number of retailers (four) are competing in this market. However, new entrants have managed to capture 35 per cent of the residential market, in around two and half years. As for electricity, this is an impressive rate of net switching when assessed against the performance of other energy retail markets

where competition has been introduced. Nearly half of all residential customers (47 per cent) have moved to market contracts.

The rate of switching to new entrant retailers has been markedly less for small business gas retail customers. However, given the experience of the residential segment of this market, there is no reason to believe that this slower rate of change arises from the existence of barriers to entry, and so the potential for competing retailers to act as a constraint on pricing decisions of the incumbent. The existence of price discounts from the standing offer tariff, and the innovation in non-price contract terms are both consistent with that experienced in the electricity retail market, and supportive of a conclusion that competition is well on the way to being effectively competitive.

The principal exception to this broad conclusion is the development of competition in the regional segment of the gas retail market. The competitive pressure in this segment appears less intense. The most likely explanation appears to be that the incumbent controls a substantial portion of the transportation capacity for pipeline laterals running off the MAPS. The extent to which this 'feature' of the regional market segment is one that could be expected given the balance of need for and availability of transport capacity along these laterals, and the precise terms on which they are contracted is not clear. It is also difficult to draw a firm conclusion on the extent to which this problem can be expected to reduce over time. Perhaps more importantly, however, there is no evidence to suggest that this issue has hindered the development of competition in the more substantial metropolitan Adelaide segment of the market.

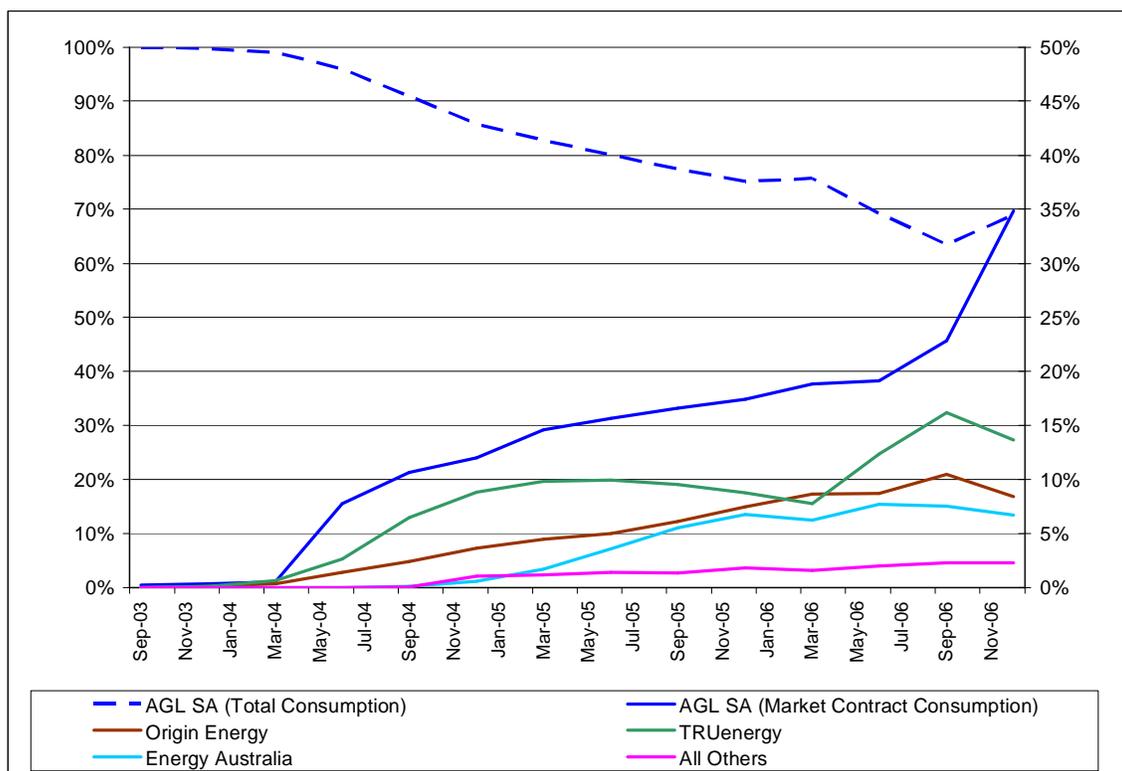
Appendix A. Market Shares

The market share of all South Australian electricity and gas retailers for residential and small business customers based on consumption of energy is set out in sections A.1 and A.2 below.

A.1. Electricity Market Shares

The market share of all South Australian electricity retailers for residential and small business customers for the period September 2003 to December 2006 is shown in figures A.1 and A.2 below. Note that for ease of illustration, the total market share of the incumbent retailer, represented by a dashed line, is measured against the axis on the left hand side of each figure which has a scale of 0 – 100 percent. The market share of all new entrants and the market share of the incumbent based on market contracts only, denoted by the unbroken lines, are measured against the secondary axis on the right hand side of the diagram, which has a scale of 0 – 50 per cent.

Figure A.1
Market Share of SA Electricity Retailers for Residential Customers
based on Consumption, September 2003 - December 2006

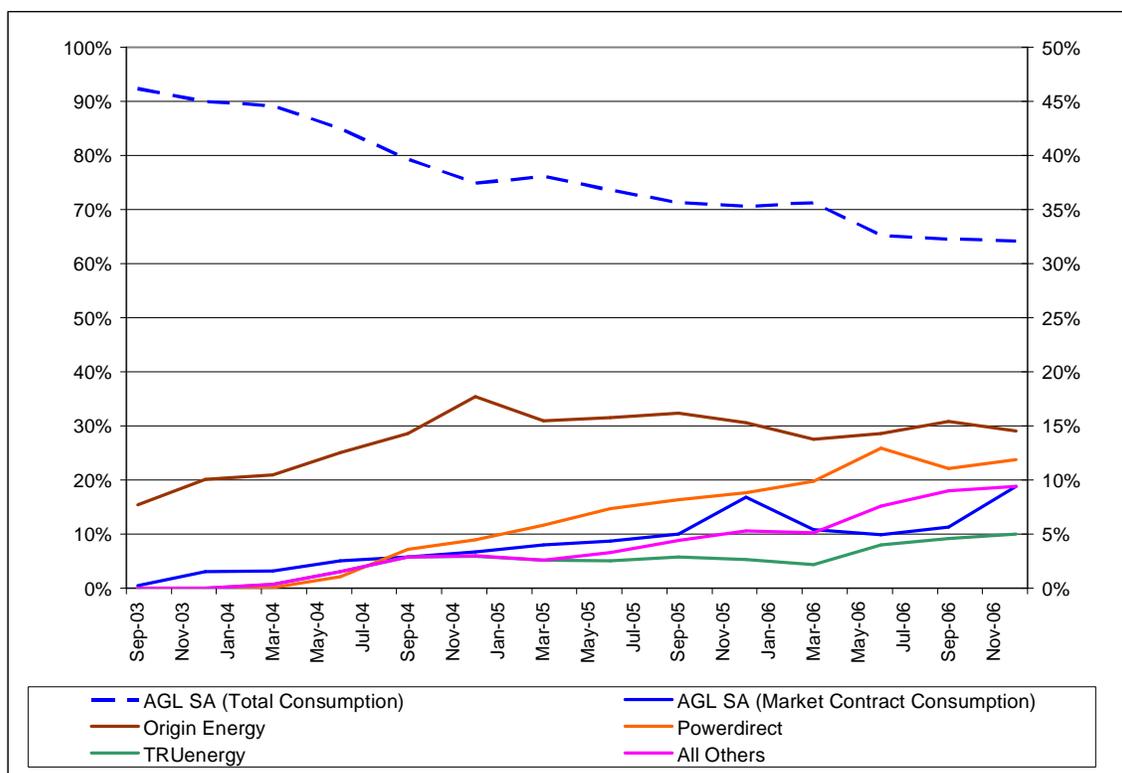


Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

AGL's market share for residential electricity customers has declined significantly since the introduction of FRC from close to 100 per cent in September 2003 to approximately 69 per cent in December 2006. The majority of electricity sold by AGL is to standing contract customers, which still account for 34 per cent of all residential electricity consumption.

AGL has a higher share than other retailers of electricity sales to residential customers on market contracts, although we note that TRUenergy, Origin Energy and EnergyAustralia each currently account for between 7 and 14 per cent of all electricity sales to these customers.

Figure A.2
Market Share of SA Electricity Retailers for Small Business Customers
based on Consumption, September 2003 - December 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

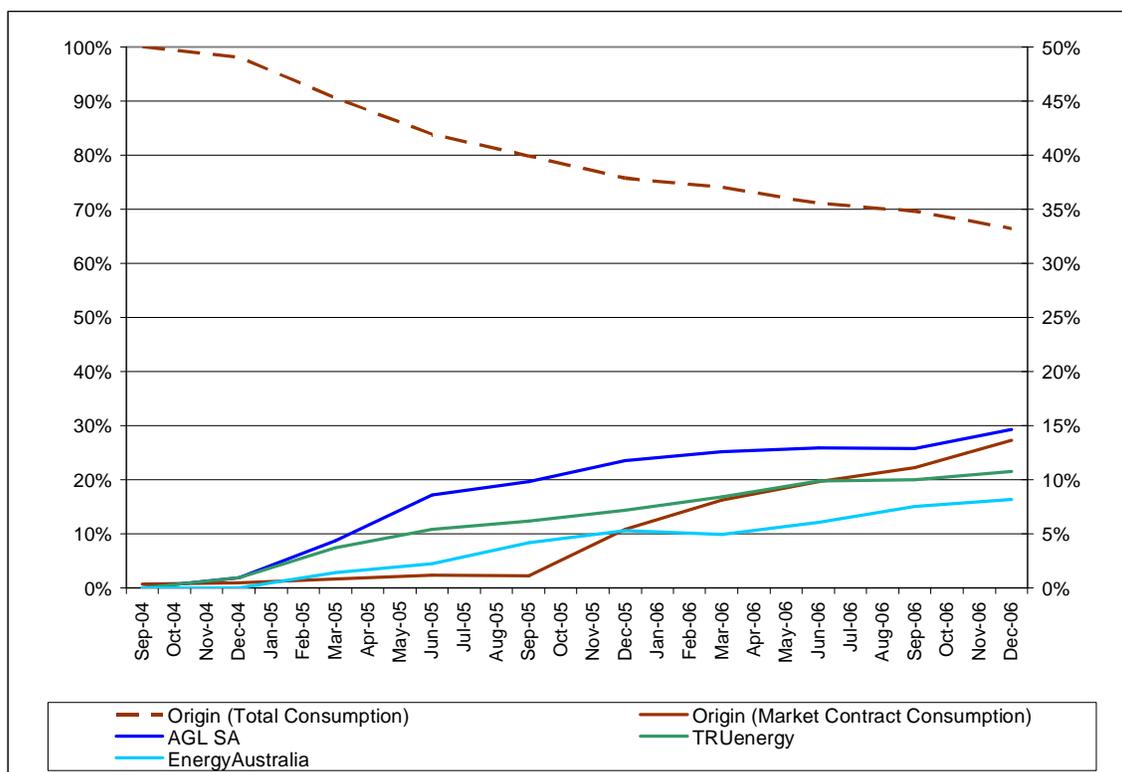
AGL's market share for electricity sales to small business customers has also declined significantly over the last three years to approximately 64 per cent as at December 2006. The majority of electricity sales to small business customers (55 per cent) are to standing contract customers.

AGL's share of sales to the remaining small business electricity customers under market contracts is considerably lower than that for residential customers at 21 per cent. Origin has a higher market share than AGL for sales to these customers at around 32 per cent (or 15 per cent of all small business electricity consumption as shown above) and Powerdirect has a market share of 26 per cent for sales to these customers (or 12 per cent of all small business electricity consumption as shown above).

A.2. Gas Market Shares

As is the case for electricity, the market share of gas standing contract retailer, Origin Energy, has decreased since the introduction of FRC in 2004, although to a much lesser extent as shown in figures A.3 and A.4 below.

Figure A.3
Market Share of SA Electricity Retailers for Residential Customers
based on Revenue, September 2003 - December 2006

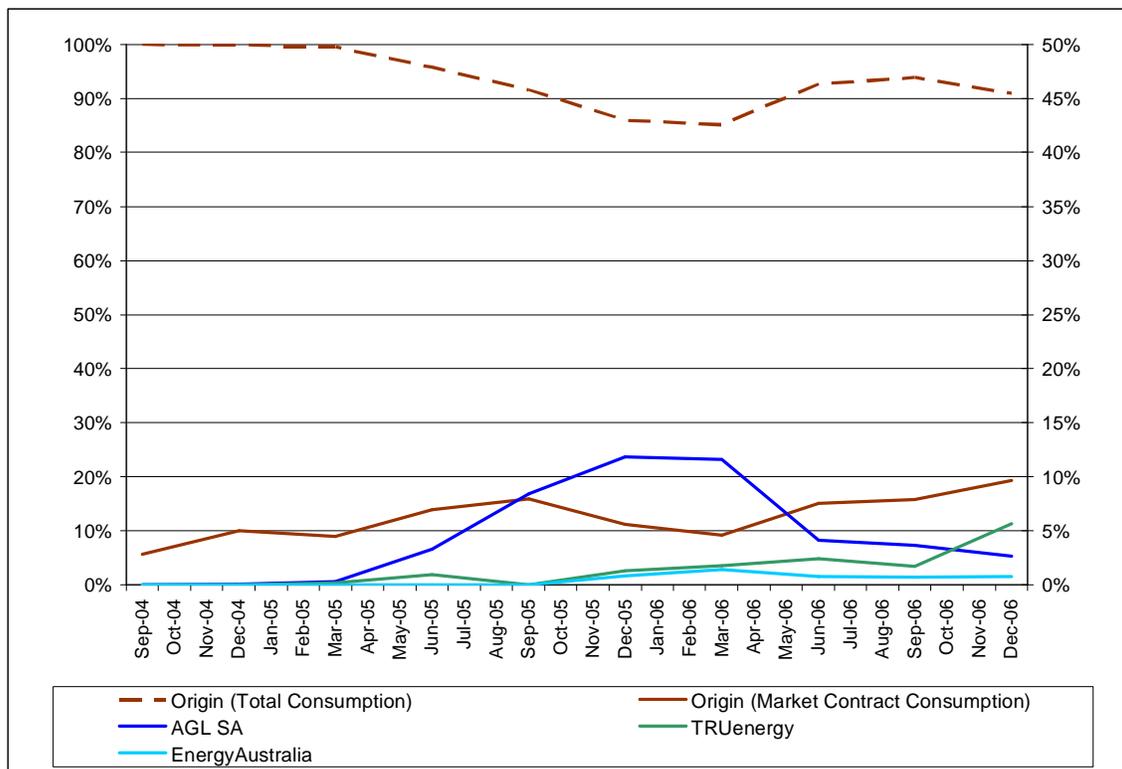


Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

Origin's market share for residential gas customers has fallen from close to 100 per cent in September 2004 to 66 per cent in December 2006. Just over half (53 per cent) of all gas sales to residential customers are to standing contract customers. AGL has a higher share than other retailers of sales to those residential gas customers on market contracts at 31 per cent (or 15 per cent of all residential gas consumption as shown above) although Origin, TRUenergy and Energy Australia are not far behind at 29 per cent, 23 per cent and 17 per cent respectively (equal to 14 per cent, 11 per cent and 8 per cent of all residential gas consumption as shown above).

We note that Origin only began to increase its share of sales to residential gas customers under market contracts in September 2005. The increase in its share of sales to these customers has been significant relative to that of other gas retailers over the period September 2005 to December 2006.

Figure A.4
Market Share of SA Electricity Retailers for Small Business Customers
based on Revenue, September 2003 - December 2006



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

Origins' share of sales to small business gas customers has also fallen over the period to December 2006 but by a much smaller amount than its share of sales to residential gas customers. The majority (81 per cent) of small business gas sales are to standing contract customers.

Of those sales to customers on market contracts, Origin has the highest share at 51 per cent (equal to only 10 per cent of all small business gas consumption as shown above). TRUenergy has a market share 30 per cent of sales to these customers (equal to 6 per cent of all small business gas consumption) and AGL and EnergyAustralia each have between 4 and 14 per cent share (equal to 3 per cent and 1 per cent of all small business gas consumption respectively as shown above).

Summary of Market Shares

In sum, the market shares of incumbent retailers AGL and Origin and other new entrant retailers for each type of small energy customer in South Australia as at 31 December 2006 were as follows:

§ Market shares based on customer numbers:

- residential electricity customers – AGL has 64 per cent (41 per cent on standing contracts and 23 per cent on market contracts) and new entrant retailers 36 per cent;
- small business electricity customers - AGL has 75 per cent (66 per cent on standing contracts and 9 per cent on market contracts) and new entrant retailers 15 per cent;
- residential gas customers – Origin has 65 per cent (53 per cent on standing contracts and 12 per cent on market contracts) and new entrant retailers 35 per cent;
- small business gas customers - Origin has 97 per cent (90 per cent on standing contracts and 7 per cent on market contracts) and new entrant retailers 3 per cent.

§ Market shares based on consumption:

- residential electricity consumption – AGL has 69 per cent (34 per cent to standing contract customers and 35 per cent to customers on market contracts) and new entrant retailers 31 per cent;
- small business electricity consumption - AGL has 64 per cent (55 per cent to standing contract customers and 9 per cent to customers on market contracts) and new entrant retailers 36 per cent;
- residential gas consumption – Origin has 66 per cent (13 per cent to standing contract customers and 53 per cent to customers on market contracts) and new entrant retailers 34 per cent;
- small business gas consumption - Origin has 91 per cent (81 per cent on standing contracts and 10 per cent on market contracts) and new entrant retailers 9 per cent.

Appendix B. Market Concentration

Market concentration refers to the extent to which market shares are spread evenly between suppliers. Market concentration is often measured by the Herfindahl-Hirschman Index (HHI), which is computed as the sum of squares of the market shares of each supplier. A market characterised by a perfect monopoly has a HHI of 10,000.

While there is no generally accepted view as to what precise level HHI is indicative of a highly competitive or uncompetitive market, competition authorities have developed benchmark levels which they use as a guide to assessing whether the level of concentration in a market is sufficient to warrant further investigation of potential competition concerns. For example, the US Department of Justice (DOJ) considers markets with a HHI of below 1,000 to be unconcentrated, between 1,000 and 1,800 to be moderately concentrated and above 1,800 to be highly concentrated.¹¹⁴ For the purpose of determining whether an increase market concentration due the merger of two firms has the potential to reduce competition in a market, the DOJ presumes that any merger that increases the HHI by more than 100 points above 1,800 will likely create or enhance market power or facilitate its exercise.¹¹⁵

The ACCC also gives further consideration to transactions which result in:¹¹⁶

- § a post-merger combined market share of the four largest firms (or fewer) of 75 per cent or more, where the merged firm will supply at least 15 per cent of the relevant market; or
- § the merged firm having a market share of more than 40 per cent.

Calculated in terms of HHI, the ACCC will consider mergers that result in a post-merger HHI of 1,425 to 1,600 or more to have the potential to create competition concerns.

The HHI of the South Australian electricity and gas retail markets for residential and small business customers over the period 2004 to 2006 is set out in table B.1 below. The HHI is calculated for total customers and customers on market contracts only and is derived using market share calculations based on both customer numbers and relative consumption levels.

Table B.1 shows that the electricity and gas retail sub-markets for residential and small business customers are all still highly concentrated. Even when measured on the basis of market contracts only, the HHI for each sub-market is significantly higher than the thresholds set by both the DOJ and the ACCC for the assessment of mergers.

We note that high market concentration is to be expected in markets that have only recently opened up to competition and in those characterised by economies of scale. What is

¹¹⁴ US Department of Justice and the Federal Trade Commission, *'Horizontal Merger Guidelines'*, Issued 2 April 1992, revised 8 April 1997, p.15.

¹¹⁵ US Department of Justice and the Federal Trade Commission, *'Horizontal Merger Guidelines'*, Issued 2 April 1992, revised 8 April 1997, p.16.

¹¹⁶ Australian Competition and Consumer Commission (ACCC), *'Merger Guidelines'*, June 1999, p.44

important to note for the purpose of this assessment is that, with the exception of the small business gas sub-market, market concentration is falling over time as new entrants expand their market share.

**Table B.1
Market Concentration (HHI) Based, 2004 - 2006**

Customer Segment	Electricity			Gas		
	2004	2005	2006	2004	2005	2006
HHI Based on Total Customers						
Residential	7,090	5,488	4,428	8,170	5,766	4,665
Small Business	7,555	6,545	5,763	9,879	8,905	8,564
HHI Based on Market Contracts Customers Only						
Residential	3,298	2,685	2,570	4,204	2,994	2,568
Small Business	4,468	2,626	2,163	4,170	3,179	2,705
HHI Based on Total Consumption						
Residential	7,455	5,831	5,058	9,622	5,953	4,808
Small Business	5,942	5,304	4,511	9,981	7,534	8,303
HHI Based on Consumption of Market Contracts Customers Only						
Residential	3,457	2,719	3,495	3,549	2,813	2,616
Small Business	4,341	2,769	2,341	9,628	4,526	3,773

Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data

Appendix C. Retailer Survey

CONFIDENTIAL

Essential Services Commission of South Australia

Monitoring the Development of Retail Competition in South Australia

Retailer Survey Questionnaire: 2007

Name of Retailer:

Contact: Name **Phone Number**

Confidentiality

The Commission understands that some of the information requested in this questionnaire may be considered commercially sensitive. Any information received from this survey will be either suitably masked or presented as percentile information, so as to preserve anonymity. However, any information provided to the Commission that is considered particularly sensitive should be clearly marked as such.

Survey Questions

Please note that a small electricity customer (either business or residential) is defined as a customer consuming less than 160MWh p.a. and a small gas customer is defined as a customer consuming less than 1TJ p.a. (through a single connection point).

1. Participation

Small Business

Did you offer market contracts for the retailing of electricity and/or gas to the following categories of SA small business at any time during the 2005-06 financial year? (Please tick relevant boxes below).

	Electricity		Gas	
Metropolitan Adelaide	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Rural & Regional South Australia				
Barossa Valley	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Yorke Peninsula	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Mt Gambier	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Whyalla	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Port Pirie	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Riverland	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>

Other (please specify) Yes No Yes No
 Have you or do you intend to offer market contracts for the retailing of electricity and/or gas to the following categories of SA small business at any time during the 2006-07 financial year? (Please tick relevant boxes below)

	Electricity		Gas	
Metropolitan Adelaide	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Rural & Regional South Australia				
Barossa Valley	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Yorke Peninsula	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Mt Gambier	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Whyalla	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Port Pirie	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Riverland	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Other (please specify)	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>

Residential

Did you offer market contracts for the retailing of electricity and/or gas to the following SA residential categories at any time during the 2005-06 financial year? (Please tick relevant boxes below)

	Electricity		Gas	
Metropolitan Adelaide	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Rural & Regional South Australia				
Barossa Valley	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Yorke Peninsula	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Mt Gambier	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Whyalla	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Port Pirie	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Riverland	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Other (please specify)	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>

Have you or do you intend to offer market contracts for the retailing of electricity and/or gas to the following SA residential categories at any time during the 2006-07 financial year? (Please tick relevant boxes below)

	Electricity		Gas	
Metropolitan Adelaide	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Rural & Regional South Australia				
Barossa Valley	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Yorke Peninsula	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Mt Gambier	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Whyalla	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Port Pirie	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Riverland	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>
Other (please specify)	Yes <input type="checkbox"/>	No <input type="checkbox"/>	Yes <input type="checkbox"/>	No <input type="checkbox"/>

2. Barriers to Entry

The Commission is interested to identify the existence of any barriers to entry or expansion, which may impede potential new entrant retailers or limit their expansion in the South Australian retail market.

This question is being asked of both South Australian licensed retailers and a number of interstate licensed retailers that do not currently have a South Australian retail licence. For those licence holders already servicing the small customer market, please answer the question by reference to those issues that were seen as barriers at the time of entering the market, or remain issues of concern by reference to potential expansion in the market.

For each Barrier to Entry or Expansion category, only one response should be circled, with the graduated rating scale defined as follows: 1 = *strongly believe it is not an issue*; 2 = *believe it is not an issue*; 3 = *neutral*; 4 = *believe it is an issue*; 5 = *strongly believe it is an issue*.

<u>Category of Barrier</u>	<u>Electricity</u>					<u>Gas</u>				
	Not an Issue		Major Issue			Not an Issue		Major Issue		
Structural Barriers										
Access to energy supply at reasonable cost	1	2	3	4	5	1	2	3	4	5
Access to risk mitigation products (eg, hedging)	1	2	3	4	5	1	2	3	4	5
Access to adequate transmission and distribution services	1	2	3	4	5	1	2	3	4	5
Regulatory Barriers										
Extent of state regulation (eg, customer protection)	1	2	3	4	5	1	2	3	4	5
Regulatory differences between jurisdictions	1	2	3	4	5	1	2	3	4	5
Regulatory uncertainty	1	2	3	4	5	1	2	3	4	5
Standing offer price regulation	1	2	3	4	5	1	2	3	4	5
Incumbency Advantages										
Retailer brand awareness	1	2	3	4	5	1	2	3	4	5
Customer inertia	1	2	3	4	5	1	2	3	4	5
Access to sufficient customer data to make offers	1	2	3	4	5	1	2	3	4	5
Customer transfer process	1	2	3	4	5	1	2	3	4	5
Exit or termination fees for some customer contracts	1	2	3	4	5	1	2	3	4	5

For any comments in relation to the issues raised above, or additional barriers to entry or expansion not listed above, please use the box below, or provide separate attachments.

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2.1 Barriers to Entry and Expansion in the South Australian Electricity Market

Is there sufficient availability of competitively priced hedging products to manage electricity price variability? If not, what specific problems have you encountered?

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Is there any aspect of the timeliness and/or the process for customer transfers that impedes your ability to compete for small electricity customers? If so, what?

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Is there any aspect of the arrangements for access to metering data and/or the ownership of meters that impedes your ability to compete for small electricity customers? If so, what?

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Would the introduction of smart or advanced metering infrastructure¹¹⁷ enhance your ability to compete for small electricity customers? If so, how?

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2.2 Barriers to Entry and Expansion in the South Australian Gas Market

Have you ever encountered problems in acquiring wholesale gas for supply to South Australia? If so, what specific problems have you encountered (eg, firmness of available capacity, supply from specific locations, timing of supply, negotiating terms and conditions of supply)?

¹¹⁷ Meters that allow the time of use to be measured, and which may possess two way communications infrastructure.

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Have you ever encountered problems in negotiating access to transmission or distribution pipeline capacity for the supply of gas to South Australia? If so, what specific problems have you encountered (eg, supply to specific locations, negotiating terms and conditions of carriage)?

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Is there any aspect of the timeliness and/or the process for customer transfers that impedes your ability to compete for small gas customers? If so, what?

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Is there any aspect of the arrangements for access to metering data and/or the ownership of meters that impedes your ability to compete for small gas customers? If so, what?

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Have you encountered any problems in offering dual fuel products to South Australian customers? To what extent are these problems location specific?

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Please direct any enquiries on this request to Amber Miller, ESCOSA, (08) 8463 6656.

Questionnaires to be returned to ESCOSA by 14 March 2007

Postal Address – GPO Box 2605, ADELAIDE SA 5001

Fax Number - (08) 8463 319

Email – amber.miller@escosa.sa.gov.au

Appendix D. McGregor Tan Customer Surveys

Following the establishment of FRC of the South Australian electricity retail market in January 2003, the Commission engaged McGregor Tan Research to conduct a number of surveys of small customers in September 2003, August 2004 and February 2006. These surveys comprised both residential households and small businesses in Adelaide and regional areas of South Australia. A copy of these surveys and their results can be found on the Commission's website at www.escosa.sa.gov.au/site/page.cfm?u=105&c=46.

The intention of the surveys was to monitor changes from the initial survey as to how competition had developed in the electricity and gas retail markets in South Australia. More specifically, the research aimed to determine the following:

- § Awareness of choice of retailer;
- § Current retailers used;
- § The degree to which consumers were receiving offers from electricity retailers and understood those offers;
- § The extent to which information was available to consumers;
- § The degree to which consumers were approaching electricity retailers;
- § The degree to which consumers were transferring between electricity retailers;
- § The uptake of market contracts and the reasons why consumers do or do not switch to market contracts;
- § The likelihood of taking up market contracts in the future;
- § Evidence of the development of innovative products by retailers; and
- § Experience of misleading or deceptive behaviour by retailers.

In its August 2004 surveys McGregor Tan Research conducted 1,201 telephone interviews with residential customers, of which 800 were from Adelaide and 401 from regional South Australia. It also conducted telephone interviews with 406 small business customers, of which 250 were from Adelaide and 156 from regional South Australia.

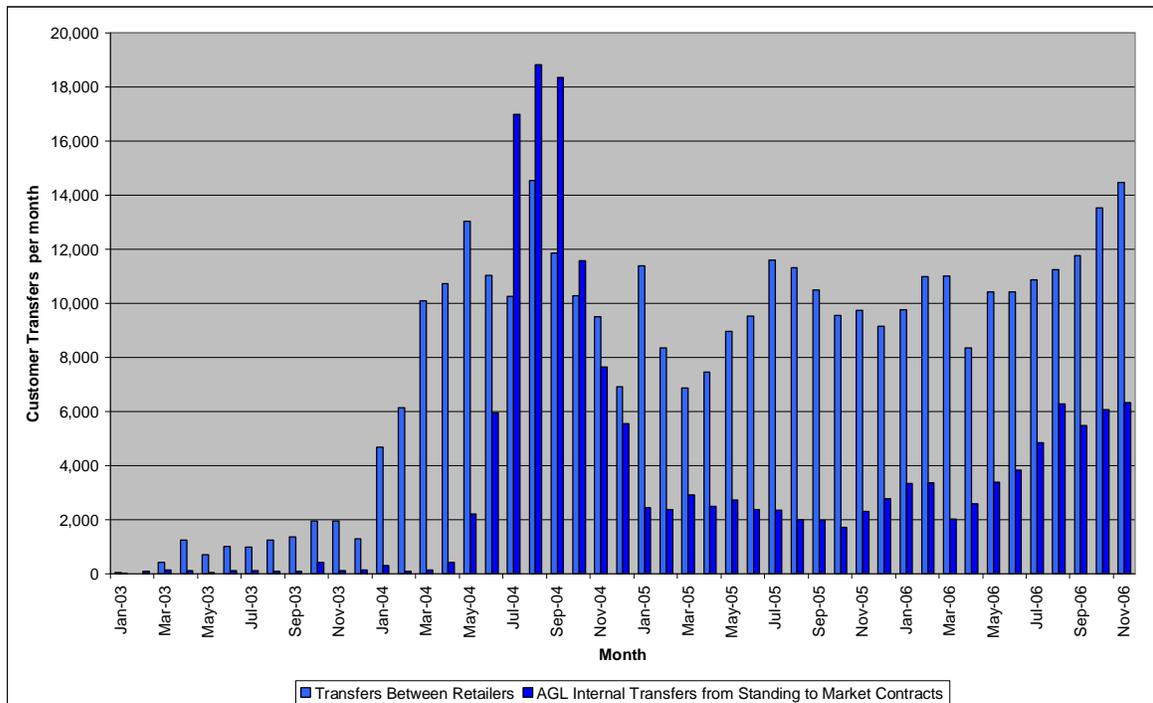
In its February 2006 surveys McGregor Tan Research conducted 1,211 telephone interviews with residential customers, of which 808 were from Adelaide and 403 from regional South Australia. It also conducted telephone interviews with 410 small business customers, of which 253 were from Adelaide and 157 from regional South Australia.

McGregor Tan notes that the same size for residential customers allows for a level of accuracy of plus or minus 3 per cent at a confidence interval of 95 per cent, although this level of accuracy is lower for the smaller sample sizes. The sample size for small business customers allows for a lower level of accuracy of plus or minus 5 per cent at a confidence interval of 95 per cent.

Appendix E. Gross Switching

Figure E.1 below shows the total number of electricity customer transfers each month for the period January 2003 to November 2006 as well as the number of AGL small customer internal transfers from standing to market contracts.

Figure E.1
SA Electricity Transfers, January 2003 - November 2006



Source: NEMMCO and AGL data. Transfers between retailers are calculated as total transfers, less transfers that are recorded as errors less AGL move-in transfers.

As shown in figure E.1, the level of customer switching between retailers in the electricity market was relatively low in the first year after the introduction of FRC at around 2,000 transfers or less per month. This was followed by a rapid increase in monthly switching in the first half of 2004, both between retailers and within AGL from standing to market contracts.

Over the period June 2004 to November 2006, the number of transfers between retailers fluctuated from approximately 7,000 to just over 14,000 per month. This equates to an average annualised switch rate of around 15 per cent of all electricity connections, where the term 'switch rate' is defined as instances of customer switching as a proportion of total connections and includes move-ins and instances of multiple switching. We note that due to the inclusion of move-ins and multiple switching the average annualised switch rate does **not** imply that on average, 15 per cent of all customers switched their electricity supplier over the relevant period.

Over this period:

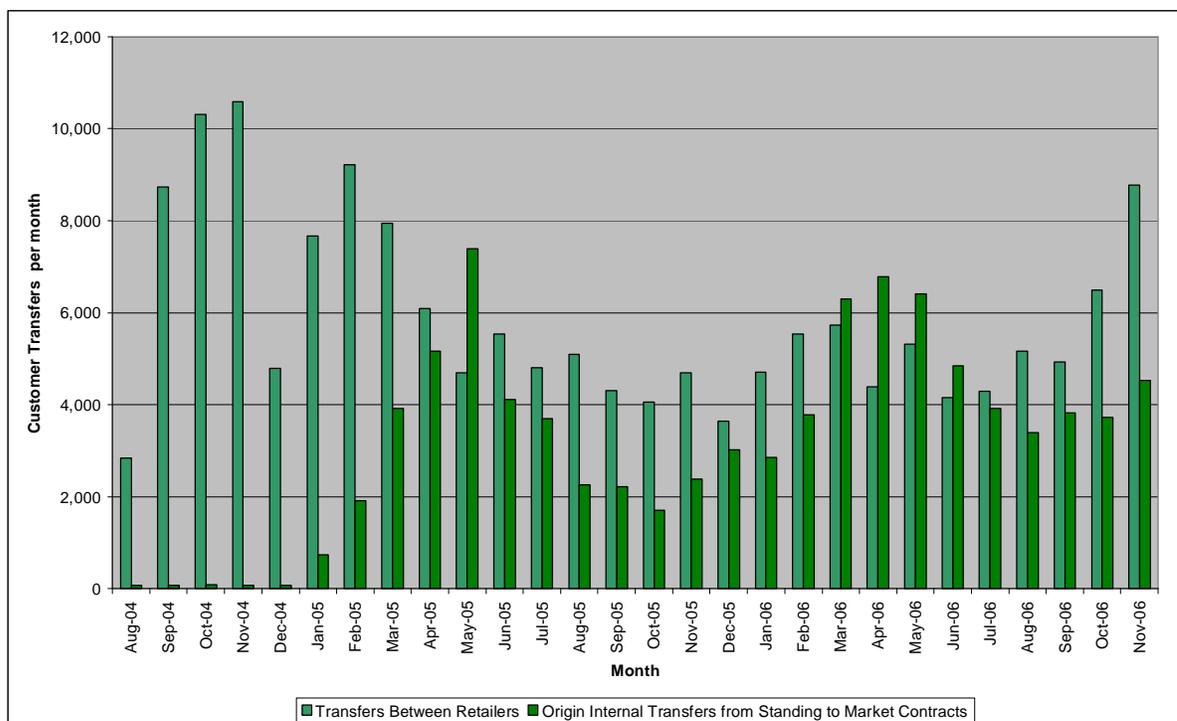
§ move-ins accounted for between 2 and 18 per cent of all customer transfers between retailers per month (12 per cent on average) - it is not possible to assess whether these 'move-ins' were due to customers changing retailer or customers transferring in order to remain with their current retailer;

§ instances of multiple switching:

- from new entrant (Tier 2) retailers to the incumbent (Tier 1) retailer AGL averaged 1,805 per month (from July 2005 only); and
- from new entrant (Tier 2) to other new entrant (Tier 1) retailers averaged 2,375 per month (from July 2005 only).

Gas transfers show a different trend than that for electricity as shown in figure E.2 below.

Figure E.2
SA Gas Transfers, July 2004 - November 2006



Source: NEMMCO and AGL data.

The number of gas transfers between retailers reached a peak of 10,952 in November 2004, only five months after the introduction of FRC. Since that time the number of monthly transfers has fluctuated from around 3,500 to just over 9,000, with an average annualised switch rate of around 16 – 18 per cent. The number of Origin internal transfers from standing to market contracts has also fluctuated from 70 to almost 7,500 per month over the same period.

Compared to other countries, the level of gross switching in South Australia has been relatively high for both electricity and gas. A recent study conducted by First Data Utilities of switching rates between energy providers in more than 30 countries suggests that few countries have gross switching rates in excess of 15 per cent.¹¹⁸ First Data Utilities classifies countries into four categories:

- § Hot markets – over 15 over cent of customer switching per year;
- § Active market – between 5 and 15 per cent of customer switching per year;
- § Slow market – between 1 and 5 per cent of customer switching per year; and
- § Dormant market – less than 1 per cent of customers switching per year.

Over the 2005 year, Great Britain and Victoria were ranked first equally as the hottest retail markets in the world based on the percentage of customers that had switched utility providers. Utility customers in these two markets switched supplier during 2005 at rates exceeding 20 per cent per year.

¹¹⁸ See www.firstdatautilities.com/customer-switching/press_releases/WorldsHottestEnergyMarkets2006.html

Appendix F. Characteristics of Standing Contract Customers

In its 2006 customer surveys, the Commission identified those respondents that had not taken out a market contract. While some customers are likely to have answered this question incorrectly, on the whole, those customers that indicated they had not taken out a market contract likely represent a good proxy of those customers that are still on standing contracts.

In this appendix, we identify the general characteristics of standing contract customers by assessing the responses of those customers that indicated they had not accepted an offer of a contract from either an electricity or gas retailer.

- § Received an offer of a contract from a retailer – standing contract customers are less likely than market contract customers to have received an offer of a market contract;
- § Gender – there is no substantial difference in the proportion of males and females on either electricity or gas standing contracts;
- § Age – those over the age of 40 are more likely to have switched to an electricity market contract, and those over 55 are more likely to have switched to gas market contracts;
- § Occupation – professionals/executives, white collar and blue collar workers are more likely to be on standing contracts than retirees of customers with home duties;
- § Employment – those in paid work are more likely than those not in paid work to be on a standing offer contract;
- § Household structure – those in single or shared household structures are more likely to be on electricity standing contracts;
- § Electricity pension – those **not** receiving an energy concession are more likely to remain on standing contracts;
- § Income – those customers **not** classified as low income customers are more likely to be on electricity standing contracts. There is no substantial difference in the proportion of low-income and non-low income customers on gas standing contracts;
- § Location – customers in regional areas are more likely than those in metropolitan Adelaide to be on standing contracts for both electricity and gas.

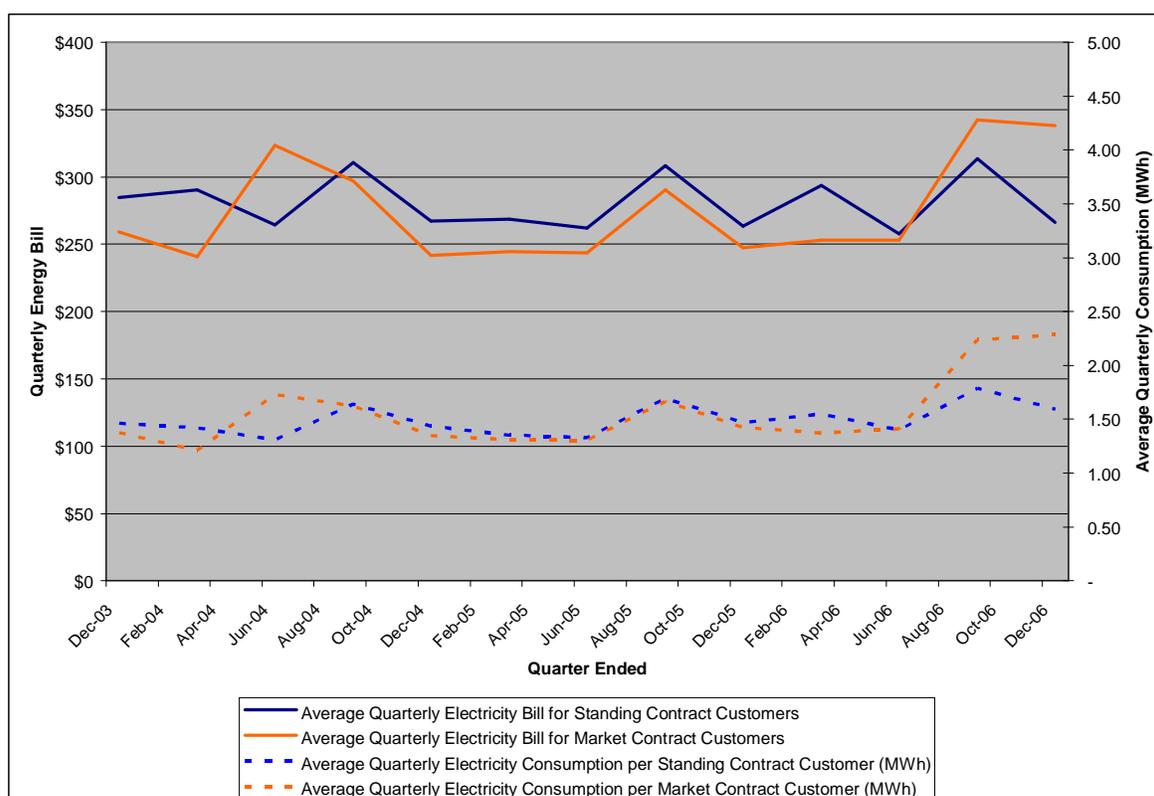
Appendix G. Average Prices and Bills for Standing and Market Contract Customers, 2003 – 2006

This Appendix outlines changes in the average quarterly electricity bill and the average electricity prices price paid by residential and small business customers under standing and market contracts over the period September 2003 to December 2006.

G.1. Residential Electricity Customers

Figure G.1 below show the movement in the average quarterly electricity bill for residential customers under standing and market contracts over the period September 2003 to December 2006 and the average quarterly consumption of these customers over that period.

Figure G.1
Average Quarterly Electricity Bill for Residential Customers, 2003 – 2006 (\$Dec 06)



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** (1) The average bill per customer is calculated as average revenue divided by the average number of customers per quarter, uplifted by the change in the All Groups CPI for Adelaide (2) The change in the methodology used to report customer numbers under the Commission's Guideline No. 2 in June 2006 may have an impact on the calculation of the average quarterly energy bill per customer for the last two quarters of 2006.

Figure G.1 shows that the average real quarterly electricity bill for residential customers on both standing and market contracts has fluctuated over the period between around \$250 and \$310 for standing contract customers and between \$240 and \$340 for market contract customers. As shown in the graph, fluctuations in the average real quarterly bill for both standing and market contract customers is largely affected by fluctuations in quarterly consumption. On the whole, however, there has been no substantial increase or decrease in the real average quarterly bill of either customer class over the period.

We note that differences in the consumption level of standing and market contract customers does impact the calculation of the average real quarterly bill for each and thus means that the two are not perfectly comparable. Despite the fact that the average quarterly bill for market contract customers was, on average 7 per cent below that of standing contract customers over the 18 month period from July 2004 to December 2005, at a time where there was little difference in the average consumption of each, this does not imply that on average market customers were “better off” under market contracts. This is because even the small variance in average consumption level of standing and market contract customers would result in a 5 – 6 per cent difference in the average quarterly bill of each if they both purchased electricity under the same contract.

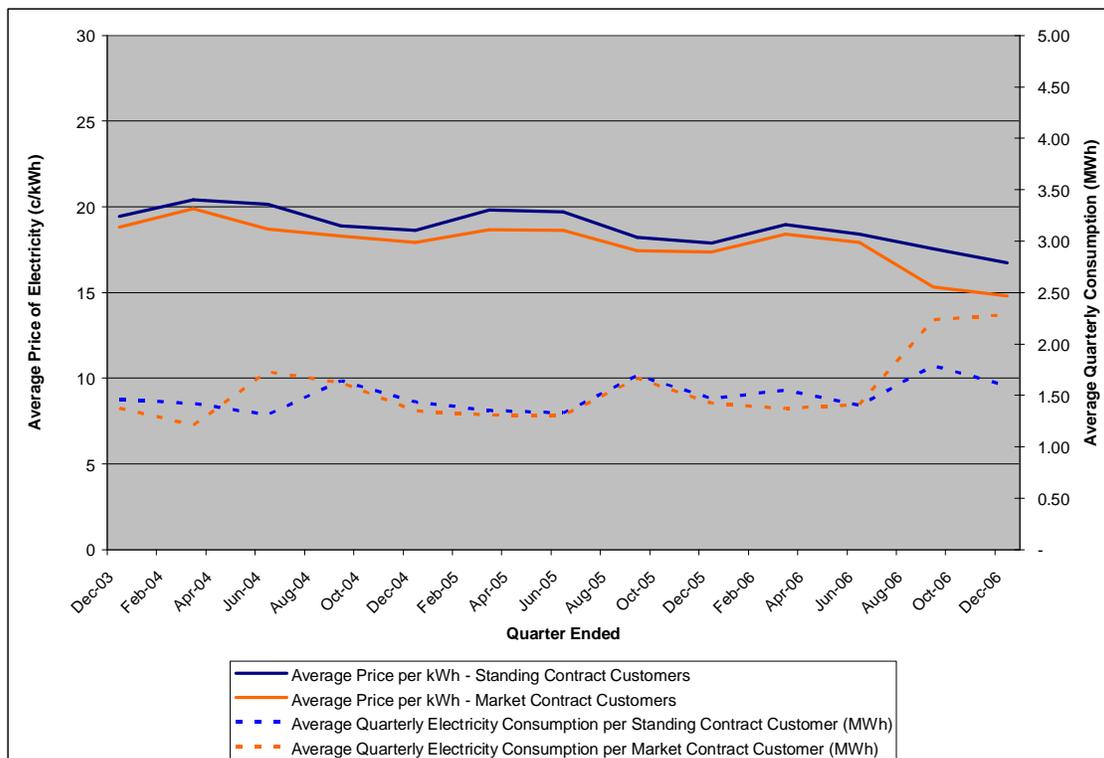
For example, the average quarterly peak consumption of residential market contract customers over the period July 2004 to December 2005 was 1,447kWh. The difference in the average quarterly consumption of standing and market contract customers over that period ranged from a minimum of 20kWh per to a maximum of 86kWh. The estimated quarterly electricity bill of a standing contract customer with an average quarterly peak consumption of 1,450kWh would have been \$303 (in current dollars) as at 30 June 2005. The estimated bill of a customer with quarterly peak consumption of 1,536kWh (being the average consumption of 1,450kWh plus the maximum variance of 86kWh) under the same contract at that time would have been \$319, which is 5 per cent higher than the aforementioned bill.

Given the impact that variances in consumption and potential differences in the consumption profile of standing and market contract customers has on the determination of the average annual bill of each, it is not possible to draw any firm conclusions about the impact of FRC based on this analysis.

A comparison of changes in the average real price of electricity for these two customer types over time also reveals little about the impact of FRC for residential electricity customers. Figure G.2 below shows the average price per kWh paid by standing and market contract customers in real terms over the period September 2003 to December 2006 as well as the average quarterly consumption of each.

The figure shows that the average real electricity price paid by residential customers on market contracts was consistently below that for standing contract customers over the entire period. Average consumption of market contracts customers was also generally below that of standing contract customers over the period.

Figure G.2
Average Real Electricity Price per kWh for Residential Customers, 2003 – 2006 (\$Dec 06)



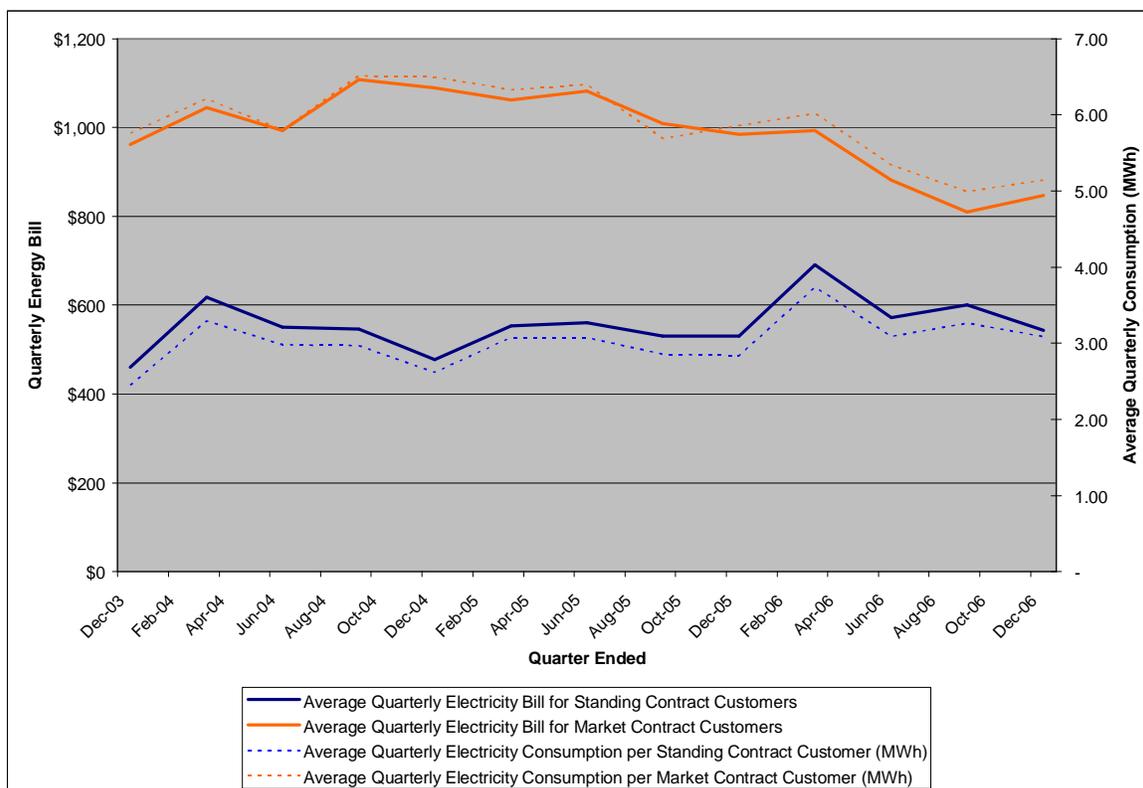
Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** (1) The average bill per customer is calculated as average revenue divided by the average number of customers per quarter, uplifted by the change in the All Groups CPI for Adelaide (2) The change in the methodology used to report customer numbers under the Commission's Guideline No. 2 in June 2006 may have an impact on the calculation of the average quarterly energy bill per customer for the last two quarters of 2006.

While the average cost of electricity will generally fall with increased consumption, suggesting that rates under market contracts were at a substantial discount to standing contract over the period, it is not possible to determine the extent of any benefit derived by market contract customers without further information on the consumption profile of these customers. Differences in peak and off peak consumption and in the variability of consumption between standing and market contract customers would have an impact on such an assessment.

G.2. Small Business Electricity Customers

Figure G.3 below show the movement in the average quarterly electricity bill for small business customers under standing and market contracts over the period September 2003 to December 2006 and the average quarterly consumption of these customers over that period.

Figure G.3
Average Quarterly Electricity Bill for Residential Customers,
2003 – 2006 (\$Dec 06)

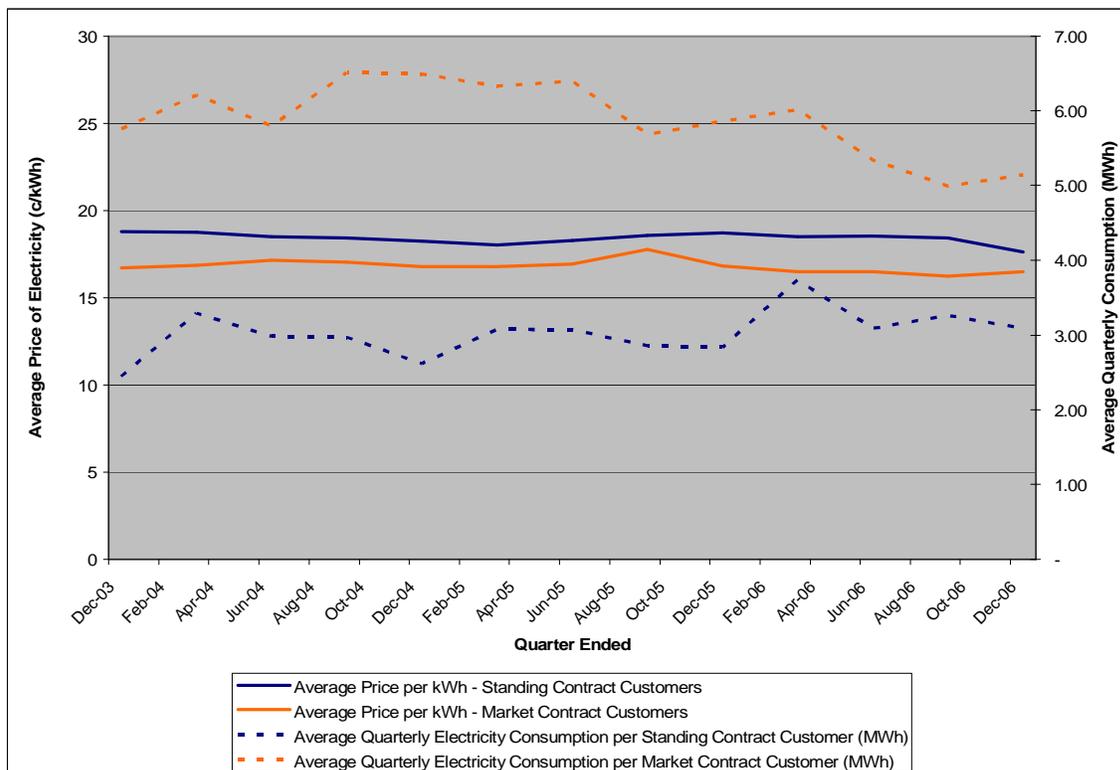


Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** (1) The average bill per customer is calculated as average revenue divided by the average number of customers per quarter, uplifted by the change in the All Groups CPI for Adelaide (2) The change in the methodology used to report customer numbers under the Commission's Guideline No. 2 in June 2006 may have an impact on the calculation of the average quarterly energy bill per customer for the last two quarters of 2006.

The figure shows that the average bill of market contract customers was substantially higher than that of standing contract customers, which is largely due to the fact that the average consumption of these customers was around twice that of standing contract customers.

The average real price of electricity for these two customer types over time is set out in figure G.4 below. The figure shows that the average price paid by small business customers on market contracts was below that paid by standing contract customers over the entire period.

Figure G.4
Average Quarterly Electricity Bill for Residential Customers,
2003 – 2006 (\$Dec 06)



Source: Information supplied by ESCOSA based on Guideline 2 Reporting Data **Notes:** (1) The average bill per customer is calculated as average revenue divided by the average number of customers per quarter, uplifted by the change in the All Groups CPI for Adelaide (2) The change in the methodology used to report customer numbers under the Commission's Guideline No. 2 in June 2006 may have an impact on the calculation of the average quarterly energy bill per customer for the last two quarters of 2006.

Appendix H. Summary of Market Offers

A summary of the price and non-price features of all market contacts currently on offer are set out in table H.1 below.

**Table H.1
Price Features of Market Contracts for Residential Customers as at March 2007**

Market Contract	Discount from Standing Contract	Term (Years)	Additional Costs		Additional Benefits				
			Account Establish Fees	Exit Fees	Entry Rebate	Loyalty Rebate	Direct Debit Rebate	Prompt Payment Discount	Other Non-Price Benefits
AGL^{S1}									
AGL Freedom 5%	4%	û	\$37.84 or \$19.36 for CC holders	û	û	û	û	û	\$50 Voucher with \$200 minimum spend at AGL shop or \$400 minimum spend at AGL Energy shop.
AGL Freedom	0%	û	\$37.84 or \$19.36 for CC holders	û	û	û	û	û	\$50 Voucher with \$200 minimum spend at AGL shop or \$400 minimum spend at AGL Energy shop.
AGL Advantage	0%	3 Years	\$37.84 or \$19.36 for CC holders	\$75	û	\$100 over 3 Years for electricity only, \$50 for gas and \$150 for electricity and gas	û	û	\$50 Voucher with \$200 minimum spend at AGL shop or \$400 minimum spend at AGL Energy shop.
AGL Advantage	0%	3 Years	\$37.84 or \$19.36 for CC holders	\$75	û	û	û	û	\$50 Voucher with \$200 minimum spend at AGL shop or \$400 minimum spend at AGL Energy shop.
Aurora Energy^{S2}									
Aurora Standard Contract ^{N1}	9%	û	\$55	\$55 after 3 mth trial period	û	û	û	û	û

Table H.1 (Cont)
Price Features of Market Contracts for Residential Customers as at March 2007

Market Contract	Discount from Standing Contract	Term (Years)	Additional Costs		Additional Benefits				
			Account Establish Fees	Exit Fees	Entry Rebate	Loyalty Rebate	Direct Debit Rebate	Prompt Payment Discount	Other Non-Price Benefits
Country Energy^{S3}									
Country Energy Premium	7%	û	û	\$95	\$60	Loyalty Card Discounts	û	û	No specific additional non-price benefits although fact sheet notes that switching incentives may be included in the offer in the form of material or goods.
EnergyAustralia^{S4}									
Maxisaver	6%	2 Years	û	Y1 \$125, Y2 \$50	û	û	û	û	û
RAA Saver	6%	3 Years	û	Y1 \$75, Y2 \$50, Y3 \$25	û	û	2.74c/day	û	Discount on membership renewal fees for Royal Automobile Association of South Australia, valued at \$30 in Year 1 and \$20 in years 2 and 3. Discount increased to \$40 in Year 1 and \$30 in years 2 and 3 under dual fuel offer.
EasySaver	5%	û	û	û	û	û	û	û	û
Green Saver 2	2%	2 Years	û	Y1 \$125, Y2 \$50	û	û	û	û	û
RAA Green Saver	2%	3 Years	û	û	û	û	û	\$25 per annum if all bills in previous 12 months paid on time	Discount on membership renewal fees for Royal Automobile Association of South Australia, valued at \$30 in Year 1 and \$20 in years 2 and 3. Discount increased to \$40 in Year 1 and \$30 in years 2 and 3 under dual fuel offer.

Table H.1 (Cont)
Price Features of Market Contracts for Residential Customers as at March 2007

Market Contract	Discount from Standing Contract	Term (Years)	Additional Costs		Additional Benefits				
			Account Establish Fees	Exit Fees	Entry Rebate	Loyalty Rebate	Direct Debit Rebate	Prompt Payment Discount	Other Non-Price Benefits
EnergyAustralia^{S4}									
Green	0%	0	0	0	0	0	0	0	0
Green Saver Premium	0%	0	0	0	0	0	0	\$25 per annum if all bills in previous 12 months paid on time	0
Qantas FF	0%	3 Years	0	Y1 \$125, Y2 \$50, Y3 \$25	0	0	0	0	7,500 Qantas FF points for entering a contract for electricity only or 15,000 for electricity and gas. An additional 1,000 points is provided if paying by Direct Debit.
Qantas FF Green Saver	0%	3 Years	0	Y1 \$125, Y2 \$50, Y3 \$25	0	0	0	0	2,500 Qantas FF points for entering a contract for electricity only or 5,000 for electricity and gas. All customers receive one point for every dollar spent on their electricity or gas bill. Electricity only customers receive 1,000 points per annum for paying bills on time whereas electricity and gas customers receive 2,000 points per annum for prompt payment.

Table H.1 (Cont)
Price Features of Market Contracts for Residential Customers as at March 2007

Market Contract	Discount from Standing Contract	Term (Years)	Additional Costs		Additional Benefits				
			Account Establish Fees	Exit Fees	Entry Rebate	Loyalty Rebate	Direct Debit Rebate	Prompt Payment Discount	Other Non-Price Benefits
Momentum Energy^{S5}									
Residential Anytime	11%	Unclear	û	û	û	Yes, although details not clear	û	10% off Bill	û
Origin Energy^{S6}									
HomeChoice (Elec or Gas only)	5% (Elec) 2% (Gas)	Unclear	\$28.60	Unclear	û	û	û	û	û
GreenEarth Home (Dual Fuel)	2% (Gas)	Unclear	\$28.60	Unclear	û	û	û	û	\$2 GreenEarth contribution waived for first year of contract. Free energy efficiency pack
HomeSupply (Gas Only)	0%	Unclear	\$28.60	Unclear	û	û	û	û	û
One Month Free (Dual Fuel)	0%	Unclear	\$28.60	Unclear	û	û	û	û	One month free electricity
Origin ChoicePlus Magazine Offer (Dual Fuel)	0%	Unclear	\$28.60	Unclear	û	û	û	û	2 year magazine subscription
Powerdirect^{S7}									
Basic Market Contract	12%	Unclear	û	\$48	û	û	\$20 one-off	û	\$20 per customer referred as part of Business Referral Program

Table H.1 (Cont)
Price Features of Market Contracts for Residential Customers as at March 2007

Market Contract	Discount from Standing Contract	Term (Years)	Additional Costs		Additional Benefits					
			Account Establish Fees	Exit Fees	Entry Rebate	Loyalty Rebate	Direct Debit Rebate	Prompt Payment Discount	Other Non-Price Benefits	
Red Energy ^{S8}										
Red Energy Market Contract	2%	No term or 2 year contract	û	Y1 \$90, Y2 \$45 for 2 yr contract	û	û	û	5% no fixed term or 7% 2 year term	û	
SA Electricity ^{S9}										
SA Market Electricity Contract	2%	û	û	\$75	û	û	û	û	Monthly prize draw of holiday gift voucher valued at \$2,000	
TRUenergy ^{S10}										
Go For More	4% (Elec) /3% (Gas)	Likely 3 years	û	Y1 \$90, Y2 \$70, Y3 \$50	û	û	û	3%	Coles Myer gift vouchers. DVD offered is customers sign up for both fuels. Bill smoothing for dual fuel customers.	
At Home	6% (Elec)	Likely 3 years	û	Y1 \$90, Y2 \$70, Y3 \$50	û	Y1 \$25, Y2 \$30, Y3 \$35	û	û	Coles Myer gift vouchers. Bill smoothing for dual fuel customers	
Go Easy	0%	Unclear	û	û	û	û	û	3%	Bill smoothing for dual fuel customers	

Source: (S1) AGL SA offer fact sheets at www.agl.com.au. AGL also has "Greenspirit" which can be incorporated with the AGL Freedom or AGL Freedom 5% offers. Greenspirit involves an additional charge of 99c per week or approximately \$51.62 per annum (S2) Information provided by Aurora Energy (S3) Country Energy SA offer fact sheets at www.countryenergy.com.au. Country energy also has a range of green options for an additional charge ranging from \$1.50 to \$4.40 per week (S4) Rates for EnergyAustralia supplied by the Commission. Energy Australia's Green options have been included in this analysis as these contracts do not appear to be the simple addition of a green energy charge on top of another basic market contract (S5) Rates for Momentum Energy supplied by the Commission and additional costs and benefits from website at www.momentumenergy.com.au (S6) Information provided by Origin Energy. Origin Energy also have a number of higher priced GreenEarth options (S7) Powerdirect SA offer fact sheets as at 11 July 2006 at www.powerdirect.com.au (S8) Red Energy fact sheet at www.redenergy.com.au (S9) Rates for South Australia Electricity supplied by the Commission and additional costs and benefits from its website at www.saelectricity.com.au (S10) Information provided by TRUenergy. TRUenergy also has a number of green energy option available at an additional charge ranging from \$0 to 5.775c per kWh.

NERA

Economic Consulting

NERA Economic Consulting
Darling Park Tower 3
201 Sussex Street
Sydney NSW 2000
Tel: +61 2 8864 6500
Fax: +61 2 8864 6549
www.nera.com

NERA Australia Pty Ltd, ABN 34 092 959 665