

WACOSS Submission to the Office of Energy's Electricity Supplier of Last Resort Discussion Paper



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Western Australian
Council of Social Service Inc

*Ways to make
a difference*

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INTRODUCTION

The Western Australian Council of Social Service Incorporated (WACOSS) is the peak body of the community service sector across Western Australia. Since 1956, WACOSS has been developing and strengthening the non-government community services sector's capacity to assist all Western Australians. With over 298 members, WACOSS has strong relationships with the social services sector and seeks to represent their interests, and those of the disadvantaged individuals and families they assist at a service level. Given this relationship, WACOSS is in a unique position to comment on issues in our society that socially impact upon members of the community experiencing disadvantage.

WACOSS is respected within both government and non-government arenas as being an authoritative voice for consumers with regard to energy market reform in Western Australia. WACOSS has developed a strong network with utility policy workers across Australia, which provides us with information and expert opinion on these issues.

In January 2005, WACOSS commenced the Consumer Utilities Project. Building upon the utility policy work WACOSS had undertaken over the previous four years the Consumer Utilities Project works with consumers and representative organisations to achieve better outcomes in the provision of essential services.

WACOSS has direct access to the issues of disadvantaged consumers who are living on low incomes through our Consumer Reference Group, which includes representatives from the Emergency Relief sector, Unions, Financial Counsellors and Community Legal Centres. These agencies provide us with policy information and direction in relation to our work and look to us to represent the interests of their clients with regard to utility issues. We have taken on this role due to the level and severity of the utility issues being raised by community agencies and the absence of any other resourced body in Western Australia representing these issues.

WACOSS is pleased to provide a response to the Office of Energy's discussion paper on Electricity Supplier of Last Resort (SOLR) Regulations. The impacts on consumers of the withdrawal of a supplier from the market are potentially significant. SOLR and Last Resort Supply Plans (LRSP) are one way in which consumers of an essential service may be protected in the case of a volatile or failing market.

EXECUTIVE SUMMARY

The electricity market in Western Australia is currently undergoing a significant process of reform. This reform has the potential to greatly affect small-use customers who are not subject to full retail competition in the electricity market. As Western Australia is outside of the National Energy Market (NEM), there are significant opportunities to gain from the experiences of markets in other states which have undergone greater processes of deregulation.

The Office of Energy's Discussion Paper

Mitigating the potential effects of market failure and negative impacts on consumers is an important aspect of essential service market regulation. To this end, the Office of Energy states that it is progressing regulation in the area of Suppliers of Last Resort (SOLR) as a part of its mandate. In the context of electricity, SOLRs provide services in situations where the incumbent supplier has failed and exited the market. Electricity providers in this situation are also referred to often as ROLRs (Retailer of Last Resort) in the Eastern States of Australia or POLRs (Provider of Last Resort) in the United States.

As Western Australia does not have full retail contestability in the electricity market, WACOSS questions the necessity of progressing SOLR regulations prior to the further investigation into the effects of events triggering Last Resort Supply Plans (otherwise known as SOLR events) on small-use consumers, or indeed, the consideration of implementing greater levels of contestability in Western Australia. The need for careful consideration in this area is further highlighted by the recent exit of Energy One from the Queensland retail energy market, triggering a Retailer of Last Resort (ROLR) event. Energy One cited low profitability and high wholesale electricity prices as being major causes of their exit from the market.

The Office of Energy does not make it clear in their discussion paper whether the proposed changes to SOLR regulation are intended to improve the circumstances of all small use customers or just those who are currently contestable, by virtue of their higher than average consumption. For the purposes of this paper, WACOSS makes the assumption that SOLR events as referred to in the Office's discussion paper are occurring within the context of the contestability of the small use retail electricity market.

Price Caps

Governments across Australia have instituted regulated price caps for the sale of electricity for smaller-use consumers. These caps are adopted to protect electricity consumers in markets which are not yet mature, or in areas of lower profitability and are intended to be set at such a level so as to not cause hardship or detriment to consumers. The imposition of SOLR fees (including a profit margin) in addition to the regulated tariff, on consumers of a failed supplier, has the potential to significantly impact on already vulnerable consumers.

Benefits for SOLRs for Business

SOLRs have a responsibility to ensure that the interests of consumers are protected under Last Resort Supply Plans (LRSP). This general principle is reflected in the past

recommendations of the Victorian Essential Services Commission¹. Additionally, it should also be recognised that despite short-term marginal costs, SOLRs are likely to enjoy positive growth by way of increased clientele as a result of a SOLR event and therefore should not seek to gain short-term profit from consumers who have not exercised market choice in the selection of the SOLR.

The WACOSS Position

WACOSS asserts that any privatization of state-owned electricity retail businesses is not in the public interest. Additionally, WACOSS continues to believe that retail contestability in the small use electricity market poses significant risks to small use electricity consumers, especially those living on lower incomes or facing hardship. Because of this, the incumbent state-owned retail electricity provider should be automatically appointed as the SOLR in the case of an LRSP being triggered. For the purposes of this paper, however, references and recommendations regarding SOLRs are intended to denote whichever supplier has been appointed in that role by the relevant authority.

Due to time constraints WACOSS has only commented on the sections of the Office's Issues Paper that were considered to be the most relevant (part 1). Absence of comment on any section of the Issues Paper should not be taken as support for or opposition to any proposal by the Office of Energy to amend or alter the existing regulations.

For further information regarding this submission or the work of the WACOSS Consumer Utilities Project, please contact Aden Barker at aden@wacoss.org.au or (08) 9420 7222.

¹ Essential Services Commission of Victoria (ESC), 'Energy Retailer of Last Resort: Issues Paper', October 2004, p. 2

WACOSS RECOMMENDATIONS

RECOMMENDATION 1

That in the case of a SOLR event, all SOLR customers are automatically supplied with the relevant standard-form contract for their SOLR service.

RECOMMENDATION 2

That standard form contracts to be implemented, or offered in the case of a SOLR event be pre-approved by the relevant authority, containing specific information regarding any additional fees and charges to be paid by the SOLR customer.

RECOMMENDATION 3

That further reform and 'progression' of Supplier of Last Resort and associated regulation be suspended until such a time as there has been a transparent, publicly accessible investigation into the appropriateness and likely effects of competition in the West Australian retail electricity market.

RECOMMENDATION 4

That there be further clarity in the Office's recommendation regarding the use of vesting contracts by Suppliers of Last Resort.

RECOMMENDATION 5

That vesting contract formally held by the failed supplier be made available to the SOLR by regulation and that the SOLR adopt these contracts in cases where an available vesting contract is able to supply SOLR customers electricity at a cheaper price than available elsewhere

RECOMMENDATION 6

That full cost recovery (including the cost of additional generation and administration costs) not be incorporated into any fee applied to a SOLR customer. In incorporating the additional cost of electricity generation, the application of a SOLR fee effectively by-passes existing uniform capped tariff regimes.

RECOMMENDATION 7

That the Office of Energy specify the length of time for which SOLRs may claim costs within any proposed SOLR fee regime.

RECOMMENDATION 8

That SOLRs not be allowed to incorporate a profit margin into any proposed SOLR fee. The incorporation of profit into any proposed fee ignores the fact that SOLRs benefit significantly from an increased client based in the case of a SOLR event.

RECOMMENDATION 9

That the Office of Energy present a range of options regarding SOLR service pricing and the application of any proposed SOLR fee to customers.

RECOMMENDATION 10

That in the event SOLRs are allowed to apply an additional specified SOLR fee to SOLR customers, that there should be a cap on such fees, set by government.

1. Contracts and Prices for Small Use Customers under SOLR Arrangements

1.1 *The SOLR will be obliged to supply small use customers under a standard form contract, consistent with the Electricity Industry (Customer Contracts) Regulations 2005 ("Customer Contract Regulations").*

Standard Form Contracts

WACOSS recognises that customer contracts are a vital mechanism for the protection of essential service consumers in an increasingly deregulated market. Standard Form Contracts have the capacity to provide a direct interface between the retailer and customer – setting-out the rights and obligations of each. These contracts are also intended to be the mechanism for the delivery of certain consumer protections, outlined in the relevant regulation.

Because of the role of Standard Form Contracts in delivering consumer protection, it is important that they be accessible and that they provide adequate, easily understood information to customers, ensuring that they are made aware of their rights in addition to their obligations. Details of how to access information additional to that contained within the contract should also be easily accessible with relevant regulation referred to directly within the body of the contract.

RECOMMENDATION 1

That in the case of a SOLR event, all SOLR customers are automatically supplied with the relevant standard-form contract for their SOLR service.

RECOMMENDATION 2

That standard form contracts to be implemented, or offered in the case of a SOLR event be pre-approved by the relevant authority, containing specific information regarding any additional fees and charges to be paid by the SOLR customer.

1.2 *The SOLR will use best endeavours to source the cheapest electricity supply for small use customers, including utilising the Vesting Contract arrangements wherever possible, if the SOLR is party to the Vesting Contract.*

Electricity Reform Should Protect Consumers

Electricity is an essential service. Because of this, it is vital that its provision should continue unhindered in the case of a licensee failing. The desire to ensure that no consumer is worse off in a competitive market is also a principle which should underlie any possible future move towards greater levels of competition in the retail energy market² in Western Australia. This sentiment was recently expressed by a range of consumer groups in their submission to the Retail Policy Working Group, Department of

² Centre for Credit & Consumer Law, 'Submission to the Energy Competition Committee: Electricity Full Retail Competition Proposed Policy Positions', Griffith University, 7 April 2006, p. 7

Industry, Tourism and Resources in regards to the proposed National Electricity Market rules³.

Given the necessity for further reform to consider the needs and best interests of smaller consumers, in addition to industry, WACOSS questions the appropriateness of reviewing and 'progressing' the current SOLR regulations at a time when greater, publicly transparent examination of increased levels of competition in the retail energy sector has yet to occur. Additionally, the need for further study and consultation is highlighted by the recent collapse of a retail energy provider in Queensland and the subsequently triggered ROLR event which affected thousands of customers⁴.

Power at the Best Possible Price

In the event that a SOLR event does occur and a supplier is required to locate additional generation capacity from an energy generation company, it is vital that this additional capacity be located at the best possible price. It is unclear within the body of the discussion paper as to whether the vesting contracts referred to may be those already held by the SOLR, or the vesting contracts previously held by the failed service provider.

Whilst the Office's discussion paper refers to the likelihood that the SOLR will seek to negotiate with the failed provider's former energy generating companies, WACOSS recommends that in cases where a supplier fails, their vesting contracts should be made available for transfer to the SOLR by regulation, if they offer the lowest possible price. The SOLR should be required by regulation to source electricity at the lowest-cost possible. Having the option of transferring existing vesting contracts to the SOLR may both lower the costs involved in obtaining additional generational capacity as well as reducing the degree of volatility in the wholesale electricity market⁵. This may be particularly important as the exit of a provider from the market can be seen to be most likely at a time of increased market volatility and high wholesale prices⁶.

WACOSS is concerned that even in situations where vesting contracts are available to the SOLR and able to supply electricity at a cheaper price than other markets or contracts, that the SOLR may choose to buy electricity at a higher price to hedge against the possibility of some SOLR customers leaving the SOLR for other suppliers after only a short period of time. Because of this, WACOSS believes that the regulation should mandate that the SOLR must make best endeavour to purchase electricity at the lowest possible price.

RECOMMENDATION 3

That further reform and 'progression' of Supplier of Last Resort and associated regulation be suspended until such a time as there has been a transparent, publicly accessible investigation into the appropriateness and likely effects of competition in the West Australian retail electricity market.

³ National Consumers Roundtable on Energy et. Al., 'Response to RPWG NEM Rules Composite Paper', August 2007, p. 35

⁴ Energy One, Details listed on Energy One Homepage, <http://www.energyone.com.au/>, Accessed 07.08.2007.

⁵ ESC, op. cit., p. 9

⁶ Ibid, p. 29

RECOMMENDATION 4

That there be further clarity in the Office's recommendation regarding the use of vesting contracts by Suppliers of Last Resort.

RECOMMENDATION 5

That vesting contract formally held by the failed supplier be made available to the SOLR by regulation and that the SOLR adopt these contracts in cases where an available vesting contract is able to supply SOLR customers electricity at a cheaper price than available elsewhere

1.3 *As required under the standard form contract, the SOLR will supply small use customers at the regulated tariffs under the Energy Operators (Electricity Retail Corporation) (Charges) By Laws 2006 in the SWIS, or under the Energy Operators (Regional Power Corporation) (Charges) By Laws 2006 outside of the SWIS. However, the SOLR may recover any costs (including wholesale electricity costs) that are above that covered by the regulated tariff under a "last resort supply fee" (equivalent to fee described in section 7 of the Gas SOLR Regulations).*

Uniform Regulated Tariffs

Regulated tariffs have been set in place in various jurisdictions at different points in time to protect consumers from the unpredictability of the wholesale electricity market and ensure the continued access of supply by groups that may not be able to participate in a less regulated market by virtue of their relative vulnerability or perceived risk they pose to suppliers.

WACOSS challenges the appropriateness of full cost recovery of administration and other costs via a fee in the case of a SOLR event. Uniform tariff caps have been set by the Government in order to protect the needs of consumers. While not actually changing the uniform tariff cap, the imposition of additional SOLR fees effectively does this by proxy. This situation becomes abundantly clear when considering that a portion of the SOLR fee may actually be the increased real cost of obtaining electricity supply.

The Duration of the SOLR Fee

Whilst the Office's discussion paper refers to a SOLR fee, it is not specified as to whether this fee can only be applied on one occasion. Additionally, the discussion paper does not clarify as to what period the additional costs can be claimed for. Whilst there may be some 'one-off' administration and other costs involved in acquiring SOLR customers, there may be additional, ongoing costs. In the interest of clarity and fairness it is important that this period of cost capture in any possible fee to SOLR customers be better defined by the Office.

The Significant Benefits to Providers of Being the SOLR

Further to the National Consumers Roundtable response to the RPWG Composite Paper, WACOSS firmly believes that consumers should not be disadvantaged by SOLR events

which are effectively beyond their control and should therefore be protected by regulation⁷. Aside from the initial administrative cost of acquiring new customers, SOLRs are likely to experience significant economic benefit as a result of receiving a possibly large quantity of new customers without the attendant costs of advertising and sales⁸. Given this likelihood, it is unreasonable that SOLRs then be able to incorporate an additional profit margin into the SOLR fee as suggested by the Office of Energy in the Issues Paper.

The extent to which being a SOLR can provide business benefit has been demonstrated elsewhere where providers have actually had to outbid each other in a competitive process to achieve SOLR status⁹. The benefit may also be particularly evident in cases where there are no or few other suppliers in a given area. Such a situations raises other concerns regarding consumer disadvantage¹⁰.

The SOLR Fee

WACOSS notes that there are many possible ways in which the cost to customers may be apportioned in the case of a SOLR event, only one of which has been presented by the Office of Energy. The Victorian Essential Services Commission presented several different options in their Issues Paper on *Energy Retailers of Last Resort*, including the possibility that additional funds charged over the cost of provision of electricity be refunded to the customer¹¹.

Given the essential nature of electricity and other forms of energy, it is unavoidable that many consumers will be distressed at the collapse of their electricity provider and any resultant associated costs. Because of this, it is important that there be caps, in addition to the recommended level of transparency in any future SOLR fees and charges. The existence of a cap, set at a conservative figure, will provide a level of security and predictability for both customers of a failed energy business and providers. The need for caps has also been identified by the Victorian Essential Service Commission¹².

RECOMMENDATION 6

That full cost recovery (including the cost of additional generation and administration costs) not be incorporated into any fee applied to a SOLR customer. In incorporating the additional cost of electricity generation, the application of a SOLR fee effectively by-passes existing uniform capped tariff regimes.

RECOMMENDATION 7

That the Office of Energy specify the length of time for which SOLRs may claim costs within any proposed SOLR fee regime.

⁷ National Consumers Roundtable on Energy et. al., p. 35

⁸ ESC, op. cit., p. 33

⁹ Bowman, D., Coghill, D. & Hodge, G., 'Protecting Utility Consumers form Market Failure', Monash University, February 2004, p. 17

¹⁰ Ibid. p. 4

¹¹ ESC, op. cit., p. 26

¹² Ibid. p. 32

RECOMMENDATION 8

That SOLRs not be allowed to incorporate a profit margin into any proposed SOLR fee. The incorporation of profit into any proposed fee ignores the fact that SOLRs benefit significantly from an increased client based in the case of a SOLR event.

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CONCLUSION

Last Resort Supply Plans and the appointment of Suppliers of Last Resort are important in ensuring the continued supply of electricity to consumers in situations where a supplier has ceased trading because of business failure or the withdrawal of their operating license. Electricity is an essential service and as such, its continued, uninterrupted supply without detriment to consumers should be a focus for regulation. WACOSS submits that without the appropriate regulation in place, markets sometimes have relatively little incentive to act in a socially responsible manner¹³.

The proposed SOLR fee and lack of additional detail regarding the purchasing of supply by a SOLR both have the potential to impact negatively on consumers who have already been disadvantaged by the withdrawal of their supplier from the market. Given the current non-contestable nature of the small use electricity market, it is inappropriate that further progression regarding SOLR regulation be conducted until such a time as electricity market deregulation has been fully studied in the West Australian context and been open to public consultation in a transparent manner.

Western Australia has a unique opportunity to take advantage of the experiences of other jurisdictions regarding the appropriate regulation of essential service markets. Given events in the Eastern States wholesale energy market and the recent collapse and subsequent withdrawal from the market of an energy retailer, WACOSS recommends that further progression of SOLR regulation be suspended until such time as the impacts of SOLR events on consumers have been properly studied.

¹³ Bowman et. Al., p. 41

REFERENCES

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