



Review of the Effectiveness of Competition in Electricity and Gas Markets in South Australia - Second Draft Report

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OVERVIEW

- Purpose of the Second Draft Report
- Background to the Commission's draft advice
- The Commission's draft advice
- Consultation process and next steps
- Specific issues for discussion
- Questions

SOUTH AUSTRALIAN RETAIL REVIEW

- Under the AEMA, the AEMC is required to:
 - Assess whether competition is effective in electricity and gas retailing in South Australia
 - If competition is effective, provide advice to the SA Government and Ministerial Council on Energy on ways to phase out retail price regulation
 - If competition is not effective, provide advice identifying ways to develop effective competition

PURPOSE OF SECOND DRAFT REPORT

- The Commission's First Final Report was published on 19 September 2008
- First Final Report confirmed the Commission's preliminary finding that competition is effective in electricity and gas retailing in South Australia, although relatively more intense in electricity than in gas
- Second Draft Report outlines the Commission's draft advice on ways to phase out retail price regulation in South Australia

BACKGROUND TO DRAFT ADVICE

- First Final Report found that competitive has been effective in keeping prices in line with costs and margins at or below competitive levels
- Energy sector entering a period of transition:
 - tightening supply/demand balance in SA
 - increasing wholesale energy costs
 - introduction of new climate change policies
- This is likely to lead to increases in input costs and an erosion of retail margins
- Effective competition will continue so long as standing contract prices can adjust flexibly to provide competitive margins
- Price regulation is unnecessary and can impose costs where competition is effective
- With rising input costs, continuation of retail price regulation risks the viability of retailers and the supply reliability of consumers

COMMISSION'S DRAFT ADVICE: OVERVIEW

- Key recommendations
- Features of the Commission's recommended price oversight framework
- Options for additional oversight of the regional gas supply
- Reasoning for the Commission's draft advice
- Consequential amendments following the removal of retail price regulation
- South Australia's compliance with the AEMA

KEY RECOMMENDATIONS

- The existing framework for regulating retail prices should be replaced by a transparent price monitoring framework
- Regulation of standing contract prices should cease by no later than the expiration of the current price determinations for electricity and gas
- Under the model recommended by the Commission:
 - cost-reflective prices will be set by the competitive retail market
 - ESCOSA will undertake transparent price monitoring and reporting
 - SA Government has a conditional reserve pricing power to re-impose price controls if competition deteriorates
 - non-price consumer protection arrangements continue
- The framework recommended by the Commission should be introduced for a period of at least three years following the removal of price regulation

FEATURES OF RECOMMENDED FRAMEWORK

- **Standing Contract Prices**

- Obligations to agree to sell electricity and to sell and supply gas will apply to the FRMP for existing connections and to the standing contract retailer for new connections
- All retailers set and amend own standing contract prices

- **Price Disclosure Requirements**

- The Energy Price Disclosure Code will be extended to standing contracts and default contracts
- Retailers must publish a notice in a local newspaper prior to changing their standing contract or default contract price

FEATURES OF RECOMMENDED FRAMEWORK cont'

- **Monitoring by ESCOSA**

- ESCOSA monitors and publishes information about trends in standing contract and default contract prices
- Options for additional oversight of regional gas supply

- **Price Monitoring Reports**

- ESCOSA to publish half yearly price monitoring reports, outlining as a minimum:
 - Trends of each retailer's standing contract and default contract prices
 - Changes in the pricing structure for standing contract and default contract prices

FEATURES OF RECOMMENDED FRAMEWORK cont'

- **Reserve pricing power**
 - Conditional statutory power that can be exercised by the SA Government to re-introduce retail price regulation should be included in the Electricity Act and Gas Act
 - Reserve pricing power can only be exercised if a review by the AEMC finds competition is not effective and price regulation is the appropriate policy response
- **Additional AEMC Competition Reviews**
 - Mechanism to enable the SA Government to request the AEMC to conduct an accelerated review of competition at short notice
- **Periodic Review of Framework**
 - AEMC to undertake review of price monitoring framework within three years of implementation

ADDITIONAL GAS PRICING OVERSIGHT

- **Structural limitations in regional gas supply**
 - First Final Report identified constraints in access to transmission haulage capacity that are affecting the ability of retailers to expand into regional areas
 - Some structural issues will be resolved in the short to medium term, with the expiry of Origin's legacy contracts for firm transmission haulage on some MAPS laterals
- **Ensuring access to competitive offers**
 - Origin's market offers available to regional customers currently provide the same level of discounting as Origin's market offers available in Adelaide
 - However, additional oversight of the regional gas supply may ensure regional gas customers can continue to access competitively priced market offers

ADDITIONAL GAS OVERSIGHT PRICING cont'

Options for additional oversight role

- **ESCOSA could:**
 - report on any price differences between comparable gas market contracts offered by Origin in regional SA and metropolitan Adelaide in its half-yearly price monitoring reports; and/or
 - require Origin to report on requests for access to the SESA Pipeline and the outcomes of those requests

REASONING FOR DRAFT ADVICE

- The proposed price monitoring regime allows the flexibility of market-determined prices whilst maintaining oversight of standing contract and default contract prices, and the ability to re-introduce retail price regulation if competition deteriorates
- **Competition is effective:** Effective competition has kept prices in line with costs and margins at or below competitive levels
- **Changes in costs/prices:** Prospective increases in costs/prices would be better handled by the competitive market than by a regulator
- **Price monitoring:** Monitoring provides a prudent transparent oversight of market pricing performance

REASONING FOR DRAFT ADVICE cont'

- **Power to re-regulate:** Conditional reserve pricing power can be exercised by the SA Government if competition deteriorates, following a competition review by the AEMC
- **Retailers' incentives:** Rivalry of competitors and threats of re-regulation provides incentives for retailers to price competitively
- **Viability of retail energy sector and supply reliability:** Cost reflective pricing necessary to ensure incentive to enter retail market is maintained in light of future cost pressures
- **Comprehensive consumer protection framework:** Will continue to apply under the Commission's recommended price monitoring regime

RECOMMENDED CONSEQUENTIAL AMENDMENTS

- The Commission has considered how the replacement of direct retail price regulation with a price monitoring framework will affect existing non-price protections for customers
- The Commission has made some proposals to allow non-price protections to better operate in an environment without direct retail price regulation.
- These suggestions include:
 - the obligation to agree to sell electricity and to sell and supply gas should apply to the FRMP for existing connections and to the standing contract retailer for new connections
 - each retailer should determine its own default contract prices: default contract prices should not be fixed by ESCOSA or by the Electricity Pricing Order

RECOMMENDED CONSEQUENTIAL AMENDMENTS cont'

- a Retailer of Last Resort (RoLR) scheme for gas should be introduced at the earliest opportunity
- ESCOSA should consider whether the reference in the RoLR Guideline to linking the variable element of price should continue to refer to the standing contract price
- the SA Government could consider undertaking a consumer awareness and education campaign as part of the transition to phasing out retail price regulation

COMPLIANCE WITH THE AEMA

- The AEMA requires the Commission to assess whether community service obligations (CSOs) are transparently funded and do not materially impede competition
- There are currently four CSO programs in place in SA:
 - a customer concession scheme for energy
 - the Emergency Electricity Payment Scheme
 - funding assistance
 - the Country Equalisation Scheme

COMPLIANCE WITH THE AEMA cont'

- The Commission found that SA's CSOs are transparently funded.
- There is currently no evidence that SA's CSOs have an anti-competitive effect on energy retailing, including the Country Equalisation Scheme.
- The Commission invites comments from stakeholders in their submission

CONSULTATION & NEXT STEPS

**Submissions on the Second Draft Report are due
4 pm, Monday 17 November 2008**

- The Commission welcomes views on all matters relevant to its draft advice
- The Commission is also seeking views on a range of specific issues, which are outlined in the following slides
- Second Final Report will be published in mid-December 2008
- SA Government to consider and respond to the Commission's final advice, to be published in the Second Final Report

SPECIFIC ISSUES FOR DISCUSSION

Stakeholder views are sought on the following issues:

- **Price oversight of default contracts**

- What are the potential costs and benefits of monitoring default contract prices?
- Do default contract prices need to be monitored, noting that these prices may be set by reference to retailers' standing contract prices?
- Are there any other comments on the price monitoring regime design or operation?

SPECIFIC ISSUES FOR DISCUSSION cont'

- **Extension of the Energy Price Disclosure Code to standing contract and default contract prices**
 - What are the potential costs and benefits of extending the Code to standing contract and default contract prices?
 - Should market contract prices remain subject to the Code during the initial three years of the framework?
 - Are there any other comments on the Commission's price disclosure proposals?

SPECIFIC ISSUES FOR DISCUSSION cont'

- **Proposal for ESCOSA to monitor and report on any price differences between comparable gas market contracts in regional SA and metropolitan Adelaide**
 - What are the potential costs and benefits of this additional price monitoring role for regional gas market contracts?
 - Given that Origin's regional gas market offers currently provide the same discounts as market offers available in Adelaide, is this additional pricing oversight necessary?

SPECIFIC ISSUES FOR DISCUSSION cont'

- **Proposal for ESCOSA to establish and maintain a register of Origin's negotiations for access to the SESA Pipeline**
 - What are the potential costs and benefits of this register?
 - What type of information should be reported on by Origin under this register?
 - Should the information in the register be publicly available?
 - Should ESCOSA be required to report on the outcomes of requests for access in its half-yearly price monitoring reports?

SPECIFIC ISSUES FOR DISCUSSION cont'

- **Impact of the Country Equalisation Scheme on the development of retail electricity competition**
 - What are the costs and benefits of Scheme?
 - Given that competition is effective for electricity retailing, is the Scheme necessary?

QUESTIONS

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- **Questions from the floor**