Australian Energy Market Commission

REVIEW

FINAL REPORT

2014 Retail Competition Review

Reference: RPR0002
Final Report

Inquiries

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

E: aemc@aemc.gov.au
T: (02) 8296 7800
F: (02) 8296 7899

Reference: RPR0002

Citation

AEMC, 2014 Retail Competition Review, Final Report, 22 August 2014, Sydney.

About the AEMC

The AEMC reports to the Council of Australian Governments (COAG) through the COAG Energy Council. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the COAG Energy Council.

Executive Summary

Retail energy markets across the national electricity market (NEM) are evolving and maturing. As jurisdictional governments implement reforms to promote competition, customers have access to greater choice of both retailer and energy plan. Customers who shop around and take advantage of these choices are saving on their energy bills.

Increased rivalry among retailers is expected to increase the types of energy products and services available to customers. Customers that are equipped with the information and tools they need to compare offers should benefit from these developments.

Markets are dynamic: conditions change as the costs of inputs and technologies change, innovation occurs, firms enter and exit the market and customer preferences change. Markets provide the mechanism for retailers to discover what customers want and for customers to discover the service and price combinations that retailers are offering. Competition is an iterative process that drives retailers to attract and retain customers and for customers to seek out the best deal that meets their needs.

The Australian Energy Market Commission (AEMC or Commission) has been asked by the COAG Energy Council to assess annually the state of competition in electricity and natural gas retail markets for small customers in the NEM. This report sets out our findings from the first of these reviews.

Overview of findings

The Commission has found that the state of competition in energy markets for small customers varies across the NEM reflecting the different pace of market reforms across jurisdictions. The state of competition also varies between electricity and gas markets due to differences in size, structural and market design features.

In electricity, competition has led to greater choice of retailers and plans in Victoria, South Australia, New South Wales and South East Queensland. Effective competition is yet to emerge in electricity markets in the Australian Capital Territory, Tasmania and regional Queensland.

In gas, competition has been more tempered as gas is a secondary consideration for most customers and a less attractive value proposition for some retailers. Structural and market design features have led to significant differences in market outcomes between and within states.

While reforms are progressing at different paces across NEM jurisdictions, a number of common themes have emerged.

Customer activity and outcomes

Customers surveyed for this review expressed a high level of interest in energy market issues and many are interested in looking for a better deal. Most were unaware of the extent of choice available and some customers are less engaged, particularly in relation to retail gas markets.

Many customers are shopping around, generally in response to a price rise or bill shock. Other customers do not expect that the potential savings will be worth the effort. Customers are seeking better and simpler information from trusted sources to help them make more informed decisions about their energy plans. Yet across the NEM there was very low awareness of the availability of price comparator websites, particularly those maintained by governments or regulators, which can simplify the search process and identify potential savings.

Customers appear to be broadly satisfied with services provided by their retailer, although this seems to be more related to reliability of supply than retailers' customer service. Qualitative research suggests customers are more negative about energy retailers in general than they are about their own retailer and there is a high level of mistrust of the industry.

Retailers are responding to customer concerns with measures such as ceasing door knocking and providing simpler information. However, there is still a role for government to support customers by providing an independent, trusted source of information and encouraging customers to become 'energy shoppers' that regularly seek out better deals. This is a change in mindset for some customers away from treating energy like the government supplied, regulated monopoly it used to be and more like other goods that involve exercising choice regularly.

Customers that are currently on higher priced standing offers could particularly benefit from shopping around for a better deal. This includes customers that are on concessions, as the benefits of these concessions can be eroded by higher prices. These customers should be encouraged and supported to investigate their energy options.

The AEMC published a consumer engagement blueprint in 2013 that provided recommendations of relevance to all jurisdictions on how to increase the confidence of customers to shop around for a better deal. This included increasing awareness of existing information and tools, such as independent comparator websites, and making these tools user-friendly.

Some groups of customers have additional challenges in accessing information and assessing their options. This is particularly the case for customers who do not have the confidence or the technology to access online resources. The blueprint provided specific advice on how to tailor information and tools for different people in the community, including these types of customers.

Impediments to entry and rivalry between retailers

New retailers have entered the electricity market in most jurisdictions over the last few years. Second tier retailers have begun winning customers from incumbent retailers. At the same time, incumbent retailers have been actively competing with each other. Retailers primarily attract customers by offering discounts and other incentives.

While new retailers have entered some gas markets, impediments appear higher than for electricity, particularly in areas with small customer bases. Similarly, rivalry has been more limited than in electricity. New retailers are winning market share but product differentiation is generally lower than for electricity.

Despite some reforms aimed at achieving a common approach to retail markets, jurisdictional differences remain. These can impede expansion by retailers across multiple jurisdictions by increasing compliance costs, which will ultimately be passed through to customers.

Future developments

Enabling technology, such as smart meters and smart appliances, combined with regulatory reforms are creating new opportunities for customers and retailers alike and will change the traditional way in which energy is supplied and consumed.

These developments have the potential to increase competition, drive product innovation and lower bills. They also have the potential to make energy markets more complicated for customers.

In this increasingly complex environment, it is critical that customers are able to compare options and make choices that meet their needs. They must be aware of, and have access to, effective tools and information to support their decisions, with the right protections and access to assistance if required.

While innovative new products and services may provide an incentive for customers to shop around, there is also a possibility that switching rates may decrease as a result of:

- moderating prices - price rises have been a key driver to encourage customers to shop around;
- retailers moving away from door knocking and cold calling;
- greater use of retention strategies to avoid losing customers; and
- maturing markets.

Retailers anticipate a number of other issues will influence the level of competition in the future. These include the removal of price regulation in South East Queensland and

New South Wales,[1] changes in wholesale market conditions, industry consolidation and additional competition from new entry.

Recommendations

The Commission recommends that jurisdictions:

- consider options for raising awareness of the tools available for comparing energy offers to improve customer confidence in the market;
- ensure concession schemes are delivering on their intended purpose in an efficient and targeted way;
- continue to harmonise regulatory arrangements across jurisdictions to minimise costs, including implementing the National Energy Customer Framework; and
- remove energy retail price regulation where competition is effective.

The remainder of this Executive Summary sets out our approach to conducting this review, followed by key findings for each jurisdiction.

Approach to this review

In order to assess the state of competition in NEM electricity and gas markets, the Commission considered five competitive market indicators:

- the level of customer activity in the market;
- barriers to retailers entering, expanding or exiting the market;
- the degree of independent rivalry;
- customer outcomes; and
- retailer outcomes.

Each of these indicators provides a useful check on the state of the market. However, it is important to note that an adverse finding for a single indicator is not necessarily indicative of a systemic problem with the way in which the market functions. It is the combination of all these indicators that determine the state of competition in a market.

The Commission drew from a number of sources to assess the competitive indicators, including: submissions to our approach paper; qualitative and quantitative customer research; retailer interviews and surveys; and data provided by retailers, Ombudsmen, jurisdictional regulators, the Australian Energy Regulator and the Australian Energy Market Operator.

1 Price regulation has already been removed in Victoria and South Australia.

The Commission published an approach paper in January 2014. Issues raised in submissions to this paper are set out in Appendix C. We will consult in the latter half of 2014 on ways to refine our approach for future annual reviews.

South East Queensland

Competition is effective in the South East Queensland electricity market and is delivering customers a choice of retailers and plans.

Most customers have chosen market offers and many are actively investigating their options and switching plans or retailers. While there was high awareness that customers could choose their retailer, awareness of the extent of choice in the market was low.

The majority of customers are satisfied with their retailer, though there appears to be a general mistrust of energy retailers, particularly smaller retailers. Some customers would like greater choice in the market which may occur if rivalry between retailers increases following the removal of electricity retail price regulation.

Competition between the ten electricity retailers has been less intense in recent years but remains effective. Retailers attribute this to lower profitability and perceived risks associated with the regulated price freeze and the methodology used to determine prices. Rivalry is expected to increase once price regulation is removed. This will further improve conditions for current retailers to compete to expand their customer base and for new retailers to enter the market.

Rivalry appears lower in the retail gas market than the electricity market, with just two gas retailers competing. Switching rates are lower than for electricity, with fewer gas options to choose from. Additional retailers have not entered the gas market primarily due to the small size of the market, with low penetration of gas pipelines to households and small businesses and a low level of average gas demand. Competition is not expected to increase over the next few years for this reason, coupled with issues securing competitively priced gas in the wholesale market.

Based on the findings of this review, the Commission considers there is sufficient competition in the South East Queensland electricity market for customers to benefit from removal of retail price regulation. Combined with a customer engagement strategy, this can be expected to promote further competition in the market to deliver innovation, greater choice and competitive prices in South East Queensland. We understand the Queensland Government is currently developing its customer engagement strategy.

Regional Queensland

Competition in regional Queensland's retail electricity market is not effective due to the way the uniform tariff policy is applied. This policy allows all customers in the same class in Queensland to have access to the same price through subsidies paid to the incumbent retailer, Ergon Energy. These subsidies make it difficult for other retailers to profitably enter the market and offer a competitive price.

The Queensland Government is currently considering ways to improve competition in regional Queensland. This includes alternative options for giving effect to the uniform tariff policy. If new retailers enter the market, an information and awareness campaign will be important to raise customer awareness and understanding of their options.

Low penetration and use of gas has impeded entry by gas retailers. While gas customers in Toowoomba and Oakey have access to two competing gas retailers, customers in Wide Bay-Burnett, Gladstone and Rockhampton only have access to one retailer. Competition is unlikely to develop further in these regions due to the small size of the customer base and the regional specific economies of scale associated with gas retailing, as well as broader conditions in the wholesale gas market.

New South Wales

Competition is effective in New South Wales electricity and natural gas retail markets, although less so in certain regional areas for gas. With the removal of price regulation on 1 July 2014, the New South Wales electricity market will continue to mature as retailer activity increases along with technology developments, allowing innovative products and services to emerge.

Many customers are actively investigating options and there are high switching rates for electricity and gas driven by price concerns. Despite these high switching rates, New South Wales has a relatively high proportion of customers on regulated offers in both the electricity and gas markets. Some customers are less engaged and are not interested in looking for a better deal, primarily because they are satisfied with their existing deal or they perceive little difference between the options available.

Retailers consider entry into the retail electricity and gas markets reasonably easy. Expansion was considered more difficult, primarily due to retail price regulation in both markets (noting that retailer interviews took place prior to price deregulation being announced), as well as upstream issues in the gas market. However, second tier electricity retailers appear to have had some success expanding over the last two years, which suggests that barriers to expansion are relatively low.

In the last two years just one second tier retailer has started supplying gas to customers in the Sydney area, which suggests that the barriers to entry in this market are higher than they are in the Victorian gas retail market where two second tier retailers have entered over the same period.

There is rivalry in the retail electricity market despite the high market concentration, with increasing activity of second tiers. There are now 14 active electricity retailers and an increasing proportion of switches involve customers moving from the larger retailers to second tier retailers. Retailers are differentiating their market offers based on discounts and non-price incentives. The level of differentiation is expected to further increase with the removal of retail price regulation. Rivalry appears weaker for retail gas, particularly in some regional areas where there is only one retailer operating.

Competition can be expected to continue to evolve now that price regulation has been removed. The full impact of this policy decision is unlikely to be evident over the short term as it will take time for retailers and customers to respond to new opportunities. Some retailers consider there is potential for activity in New South Wales to overtake Victoria as customers become more engaged and further new entry occurs. This is consistent with retailer views that New South Wales is an attractive market in terms of size and regulatory and policy stability, particularly now that price regulation has been removed.

In the retail gas market, competition is providing choices for the majority of small customers in New South Wales. Prices in this market continue to be regulated, which could deter further entry and expansion. However, the overriding issues affecting retailer entry are likely to be the ability of retailers to access transmission pipelines and the ability of retailers to obtain competitively priced gas in the wholesale market.

Australian Capital Territory

Effective competition is yet to emerge for small customers in the Australian Capital Territory in electricity or gas retail markets. The incumbent retailer continues to dominate the market and other retailers do not expect this to change in the near future.

The Australian Capital Territory has a very low proportion of customers on market offers and low customer switching rates, which appears to be due to the limited choices available and low customer awareness that they can choose their retailer or plan.

Many customers surveyed were very satisfied with their retailer, but many also want greater choice of retailer and plan. Residents have a choice between two retailers and a small number of market offers available to customers that are very similar. The key point of difference between electricity offers is the discount offered by the incumbent retailer for ‘bundling’ multiple services such as mobile phone, landline and internet.

Retailers consider entry into the electricity and gas retail markets to be difficult and expansion even more difficult, citing the incumbent retailer’s dominance in the market and the relatively small customer base as significant barriers. The way in which retail price regulation is applied was also raised as a key impediment for entry or expansion in the electricity market.

The AEMC recommended a series of changes to improve competition as part of the Australian Capital Territory competition review in 2011. The AEMC also recommended changes to the way in which prices are regulated as part of our advice on best practice retail price regulation methodology. These recommendations still apply.

Victoria

Competition is effective for small customers in the Victorian retail electricity and gas markets. Victoria is the preferred market for retailers to develop new products and services, given the higher levels of customer engagement and the additional options for innovation that the widespread availability of smart meters provides.

Customers in Victoria are the most active of all NEM jurisdictions. Most customers have chosen market offers, many are actively investigating their options and Victoria has the highest level of switching between plans and retailers. As with all jurisdictions, some customers are not interested in looking for a better deal, primarily because they are satisfied with their existing retailer. Most customers surveyed were satisfied with the level of choice in the market, the quality of service and the value for money provided by retailers.

Retailers consider there are fewer impediments to entry or expansion in the gas or electricity market than in other jurisdictions. There is evidence of strong rivalry between the 16 electricity and eight gas retailers through a high level of retailer product differentiation and marketing activity. Second tier retailers are very active and are winning electricity customers from the three incumbent retailers. Six electricity retailers and three gas retailers indicated they are planning to expand in the next five years. Two retailers indicated they are in the process of entering the gas market.

Retailers did not expect conditions in the Victorian retail gas market to materially change in the near future. Some retailers noted that while Victoria is relatively well-placed in terms of its close proximity to large gas reserves, retail customers may still feel the effect of the tightening demand and supply conditions in the wholesale gas market through higher retail gas prices.

Based on analysis undertaken as part of the AEMC’s 2013 Residential Electricity Price Trends review, estimated gross retailer margins in February and September 2013 appeared higher in Victoria then in other jurisdictions. However, it is unclear whether these results are due to under-estimating wholesale energy costs and/or operational costs. Some retailers interviewed for this review highlighted higher wholesale energy and operational costs in Victoria as the reason for higher estimated gross margins, specifically driven by customer protection obligations, costs associated with the roll-out of smart metres and higher switching rates. However, these retailers did not provide evidence of the magnitude of these costs.

The requirement to provide a standing offer may create an artificial benchmark for retailers' pricing strategies and can make it difficult for customers to compare offers. This issue may warrant further investigation.

Approximately one quarter of Victorian customers are on standing offers and these customers may be encouraged to switch if they were aware of the savings they could make by switching to a cheaper market offer. We have recommended that all jurisdictions, including Victoria, promote awareness of the information and tools available to help customers compare offers and find a better deal. This includes increasing awareness of independent price comparator websites.

South Australia

Competition in the South Australian retail electricity and natural gas markets is effective, although less so for gas customers in regional areas. While price regulation was removed at the beginning of 2013, competition in the retail electricity market has been influenced by AGL's agreement with the South Australian Government to freeze prices for two years. This agreement is in place until the end of 2014 and consequently may continue to influence competition in the short term.

South Australia has the highest proportion of customers on market offers for electricity and gas of all NEM jurisdictions. The majority of customers are aware that they can choose their energy retailer and plan, many are actively investigating options and there are high switching rates for electricity and gas. Many customers are satisfied with the level of choice in the market and with their current retailer, although some perceive little difference between the choices available and some, particularly among the small businesses surveyed, were not interested in looking for a better deal.

Retailers consider entry, exit and expansion relatively easy in the South Australian energy retail markets. Four existing electricity retailers are planning to expand in the next five years. There are five vertically integrated retailers competing in South Australia. Some retailers considered it to be difficult to expand in the electricity market without having interests in generation assets.

Retailers consider entry into the gas market can be more difficult in regional areas because of the small customer base in these areas and constraints on the availability of capacity on some regional pipelines.

Despite a high level of market concentration, there is strong rivalry in retail electricity and gas markets. Thirteen retailers currently compete for electricity customers and three smaller second tier retailers are considering entry into the electricity market over the next five years. Five retailers are competing for gas customers and two of these are planning to expand over the next five years. Second tier retailers are becoming more active and are winning market share. Rivalry appears weaker for retail gas in regional areas.

Competition is expected to continue to evolve as the South Australian energy markets mature. Some retailers consider that South Australia has the potential to overtake Victoria as the most competitive electricity market in Australia, as customers become more engaged and further new entry by retailers occurs. To take full advantage of the offers available, customers may benefit from greater awareness of Energy Made Easy as an independent source of information to help them compare plans.

Competition is less intense but still effective for the majority of customers in the retail gas market. Gas market structure issues continue to impede entry into regional areas. Only two retailers compete outside of Adelaide and the incumbent retailer has close to a 100 per cent market share in some regional locations. Competition in the gas market is not expected to change considerably in the near future as a result of tight wholesale conditions and lack of uncontracted capacity on the South East Australian Gas Pipeline.

Tasmania

The Tasmanian electricity market is undergoing a period of change with the introduction of full retail competition for residential and smaller business customers from 1 July 2014. The completion of this final tranche of full retail competition is a good step towards promoting competition in the small customer electricity market. The Tasmanian Government is also implementing a number of changes to the wholesale market arrangements in Tasmania to try and encourage retailers to enter the market as part of the broader implementation of full retail competition.

Based on interviews and survey responses by retailers to this review, the outlook for competition in the small customer market is unclear at this stage. One small second tier retailer indicated it may consider entry in the small business segment and another may consider entry into the residential segment over the next five years. Neither retailer had firm plans to do so. Smaller retailers considered that there are risks associated with entry, primarily around the wholesale supply arrangements and the size of the customer base. At the time of interviews, larger retailers stated that they did not have plans to enter the Tasmanian retail market.

If new retailers enter the electricity market, it will be important to increase customer awareness of their ability to choose between retailers and plans. At the same time, customers could be informed of the information and tools available to them to support their choice.

While there is greater competition in gas, it is also somewhat limited. Customers have a choice of two retailers; however the Commission understands that there is limited switching between the two. No retailers appear to be considering entry into the gas market in the short term, primarily due to the very low penetration of gas distribution pipelines.

Table 1 Queensland summary of indicators

	South East Queensland	
	Electricity	**Gas**
Customer activity	70% of customers are on market offers	75% of all Queensland gas customers are on market offers
	17% of small customers changed their retailer in 2013	11% of small customers changed their retailer in 2013
	91% of residential customers and 93% of business customers surveyed were aware they could choose their retailer	88% of residential customers surveyed were aware they could choose their retailer (business sample not statistically significant)
	30% of residential customers and 27% of business customers surveyed actively investigated energy offers in the past 12 months	
	62% of residential customers and 64% of business customers surveyed were currently, or interested in, looking for a better deal	
Barriers to entry, exit and expansion	Retailers considered the market relatively difficult to enter and expand in, however impediments are likely to reduce if price regulation is removed	Retailers consider access to and/or the price of gas, the size of the market and the market design issues impeding entry
Independent rivalry	While the market share of the two incumbents remains high, there are ten retailers in the market; 30% of switches are from the two incumbent retailers to second tier retailers; and there is a moderate degree of product differentiation	Rivalry appears relatively weak, with only two retailers competing and fewer offers available than in electricity
Customer outcomes	65% of residential customers and 66% of business customers surveyed were somewhat or very satisfied with their current electricity retailer	78% of residential customers surveyed were somewhat or very satisfied with their current gas retailer (business sample not statistically significant)
	74% of residential customers and 88% of business customers surveyed were either somewhat or very satisfied with the switching process	73% of residential customers surveyed were either somewhat or very satisfied with the switching process (business sample not statistically significant)
	48% of residential customers and 53% of business customers surveyed were either somewhat or very satisfied with the level of market choice	
Retailer outcomes	Profitability has varied over the last few years. Retailers rated profitability the same as in New South Wales and South Australia.	Retailers rated profitability the same as for electricity and the same as in New South Wales and South Australia

Regional Queensland		
	Electricity	**Gas**
Customer activity	Virtually no customers are on market offers	75% of all Queensland gas customers are on market offers
Barriers to entry, exit and expansion	The main impediment to entry is the way in which the uniform tariff policy is given effect, which the Queensland Government is currently reviewing	The size of the market and access to and/or the price of gas are key impediments to entry and expansion.
Independent rivalry	There is no rivalry as there is only a single retailer	There is no rivalry as there is only a single retailer
Customer outcomes	Customer satisfaction appears high, but this may be due to lack of engagement and fewer complaints as a result of no marketing activity and switching	No separate information available
Retailer outcomes	The incumbent retailer currently receives a subsidy to compensate it for losses No other retailer can access this subsidy and so cannot profitably compete.	Limited information available

Table 2 New South Wales summary of indicators

	Electricity	Gas
Customer activity	60% of customers are on market offers	70% of customers are on market offers
	18% of customers changed their retailer in 2013	17% of customers changed their retailer in 2013
	90% of residential and 86% business customers surveyed were aware they could choose their retailer	85% of residential customers surveyed were aware they could choose their retailer
	27% of residential customer and 41% business customers surveyed actively investigated offers in the past 12 months	
	55% of residential and 69% business customers surveyed were either currently looking or interested in looking for a better deal	
Barriers to entry, exit and expansion	Retailers rated this market as being neither easy nor difficult to enter and expansion as slightly difficult, however impediments are likely to reduce following the New South Wales Government's announcement that it will remove retail price regulation	Retailers considered this market harder to enter than Victoria as a result of: access to and/or the price of gas; retail price regulation; market design issues; difficulty accessing transportation; and low gas penetration and average consumption
Independent rivalry	While the market share of the two incumbents remains high, there are 14 retailers in the market. Almost 30% of switches are from the two incumbent retailers to second tier retailers. There is limited product differentiation.	Only two retailers operate in the market. There is limited product differentiation
Customer outcomes	69% of residential customers and 66% of business customers surveyed were somewhat or very satisfied with their current electricity retailer	78% of residential customers surveyed were somewhat or very satisfied with their current gas retailer
	77% of residential customers and 81% of business customers surveyed were either somewhat or very satisfied with the switching process	79% of residential customers surveyed were either somewhat or very satisfied with the switching process
	47% of residential customers and 54% of business customers were either somewhat or very satisfied with the level of market choice	
Retailer outcomes	Based on evidence available, the market appears sufficiently profitable to promote effective competition	Based on evidence available, the market appears sufficiently profitable to promote effective competition

Table 3 Australian Capital Territory summary of indicators

	Electricity	Gas
Customer activity	19% of customers are on market offers	20% of customers are on market offers
	2% of small customers changed their retailer in 2013	Switching data not available
	57% of residential customers and 63% of business customers surveyed were aware they could choose their retailer	36% of customers surveyed were aware they could choose their retailer
	10% of residential customers and 6% of business customers surveyed actively investigated offers in the past 12 months	
	58% of residential customers and 43% of business customers surveyed were currently, or interested in, looking for a better deal	
Barriers to entry, exit and expansion	Retailers considered entry into this market to be relatively difficult and expansion even more difficult	Retailers considered entry into this market to be relatively difficult and expansion even more difficult
Independent rivalry	Rivalry appears very limited; the market remains highly concentrated; and there is limited product differentiation.	Rivalry appears very limited; the market remains highly concentrated; and there is limited product differentiation.
Customer outcomes	73% of residential customers and 75% of business customers surveyed were somewhat or very satisfied with their current electricity retailer	69% of residential customers surveyed were somewhat or very satisfied with their current gas retailer
	80% of residential customers surveyed were either somewhat or very satisfied with the switching process. (Business sample not statistically significant)	(Samples not statistically significant)
	33% of residential and 38% of business customers surveyed were somewhat or very satisfied with the level of market choice	
Retailer outcomes	Profitability for new entrants appears low and insufficient to support effective competition	Limited information is available on profitability, but retailers rated it as relatively low

Table 4 Victoria summary of indicators

	Electricity	Gas
Customer activity	75% of customers are on market offers	75% of customers are on market offers
	28% of small customers changed their retailer in 2013	27% of small customers changed their retailer in 2013
	95% of residential customers and 89% of business customers surveyed were aware they could choose their retailer	95% of residential customers and 91% of business customers surveyed were aware they could choose their retailer
	39% of residential customers and 57% of business customers surveyed actively investigated energy offers in the past 12 months	
	59% of residential customers and 67% of business customers surveyed were either currently looking or interested in looking for a better deal	
Barriers to entry, exit and expansion	Retailers considered entry and expansion in the Victorian market to be relatively easy	Retailers considered the Victorian market more conducive to entry and expansion than other markets due to its design
Independent rivalry	There is a high degree of rivalry, with 16 retailers competing. Approximately 30% of switches are from the three incumbents to second tier retailers. There is a high degree of product differentiation.	There is a high degree of rivalry, with 8 retailers competing There is less product differentiation in gas than in electricity
Customer outcomes	63% of residential customers and 67% of business customers surveyed were somewhat or very satisfied with their current electricity retailer	67% of residential customers and 64% of business customers surveyed were somewhat or very satisfied with their current gas retailer
	76% of residential customers and 70% of business customers surveyed were either somewhat or very satisfied with the switching process	76% of residential customers and 59% of business customers surveyed were either somewhat or very satisfied with the switching process
	57% of residential and 64% of business customers surveyed were either somewhat or very satisfied with the level of market choice	
Retailer outcomes	Gross retail margins appear higher in Victoria than elsewhere, but it is not clear what is driving this. Retailers rated profitability as moderate, and more profitable than other jurisdictions.	Retailers rated profitability as lower than the Victorian electricity market but consistent with South Australia and New South Wales

Table 5 South Australia summary of indicators

	Electricity	Gas
Customer activity	83% of customers are on market offers	81% of customers are on market offers
	28% of small customers changed their retailer in 2013	17% of small customers changed their retailer in 2013
	92% of all customers surveyed knew they could choose their retailer	89% of residential customers were aware they could choose their retailers
	30% of residential customers and 37% of small business customers surveyed actively investigated offers in the past 12 months	
	51% of residential customers and 56% of small business customers surveyed were either currently looking or interested in looking for a better deal	
Barriers to entry, exit and expansion	Retailers considered the market relatively easy to enter, but some retailers raised concerns about the ability to access hedging instruments	Retailers considered this market harder to enter than Victoria as a result of access to and/or the price of gas, difficulty obtaining access to transportation and market design issues
Independent rivalry	There is strong rivalry in retail in the electricity market despite the high market concentration, with 13 retailers competing. Approximately 30% of switches are from the three incumbents to second tier retailers. There is a moderate degree of product differentiation.	There is strong rivalry in the retail gas market despite the high market concentration, with 5 retailers competing. Rivalry appears weaker for retail gas in regional areas. There is less product differentiation than in electricity.
Customer outcomes	65% of residential customers and 68% of business customers surveyed were somewhat or very satisfied with their current electricity retailer	67% of residential customers and 63% of business customers surveyed were somewhat or very satisfied with their current gas retailer
	73% of residential customers and 62% of business customers surveyed were either somewhat or very satisfied with the switching process	66% of residential customers surveyed were either somewhat or very satisfied with the switching process
	56% of residential customers and 51% of business customers were either somewhat or very satisfied with the level of market choice	
Retailer outcomes	Retailers rated the electricity market as somewhat profitable, consistent with their rating for New South Wales. Based on evidence available, it appears sufficiently profitable to promote effective competition.	There is limited information on profitability, but retailers suggest it is similarly profitable to electricity. Based on evidence available, it appears sufficiently profitable to promote effective competition.

Table 6 Tasmania summary of indicators

	Electricity	Gas
Customer activity	Very limited	Appears limited
Barriers to entry, exit and expansion	In general, retailers expect it will be challenging to enter this market.	Retailers consider there are a number of significant factors discouraging entry into this market
Independent rivalry	Very limited	Appears limited
Customer outcomes	Based on available evidence, satisfaction appears high.	Based on available evidence, satisfaction appears high.
Retailer outcomes	Retailers rate profitability as low	Limited information available

Contents

1 Introduction 1

1.1 Scope of the review 1

1.2 Purpose of the report and next steps 2

1.3 Sources of information 3

1.4 Structure of the report 4

2 Assessment Framework 5

2.1 Introduction 5

2.2 Market definition 5

2.3 How do we measure effective competition? 7

2.4 Methodology 8

2.5 Customer activity in the market 10

2.6 Barriers to entry, exit or expansion 12

2.7 Independent rivalry 13

2.8 Customer outcomes 14

2.9 Retailer outcomes 15

2.10 Drawing these indicators together 16

3 Overview and Main Findings 17

3.1 Past - a brief history of the reform agenda 18

3.2 Present - state of competition in retail energy markets 19

3.3 Future - developments affecting retail competition 42

4 South East Queensland 47

5 Regional Queensland 79

6 New South Wales 91

7 Australian Capital Territory 122

8 Victoria 146

9 South Australia 185

10 Tasmania 213

A Abbreviations 227

B Concessions and hardship 229

C Summary of submissions to the AEMC's Approach Paper 236

D Solar arrangements 261

D Active retailers in NEM jurisdictions 265

F Victorian retail consumer protections 266

1 Introduction

This is the first time the Australian Energy Market Commission (AEMC) has assessed the state of retail energy competition in all national electricity market (NEM) jurisdictions as part of a single, annual competition review. This reflects a new approach agreed by the COAG Energy Council (formerly the Standing Council on Energy and Resources) in December 2012.

The AEMC is responsible under the Australian Energy Market Agreement (AEMA) for assessing the state of competition in electricity and natural gas retail markets. These reviews provide advice to governments to support a commitment made by all jurisdictions under the AEMA to remove retail energy price regulation where effective competition can be demonstrated. Separate competition reviews were completed for Victoria and South Australia in 2008, the Australian Capital Territory in 2011 and New South Wales in 2013.

This 2014 review considers competition in all Australian states and territories with the exception of Western Australia and the Northern Territory, which are not part of the NEM. As part of this review, the AEMC has had a particular focus on South East Queensland. This is the first time the AEMC has reviewed competition in Queensland and our advice is to support the Queensland Government's decision on whether to remove retail price regulation in South East Queensland from July 2015.[2]

1.1 Scope of the review

The terms of reference was provided from the COAG Energy Council to the AEMC on 13 January 2014. It is a standing terms of reference that applies to this year's review as well as future annual reviews.[3] The scope of these reviews is set out in the terms of reference and in the amended AEMA.

The AEMA requires the AEMC to assess the effectiveness of competition in accordance with guidance issued by Energy Ministers for the purpose of jurisdictional decisions on the retention, removal or reintroduction of retail energy price controls.

The terms of reference require the AEMC to consider a set of criteria in assessing the effectiveness of competition across and within NEM jurisdictions. These criteria were developed by the Ministerial Council on Energy (MCE)[4] and have been factors in all AEMC retail reviews to date. Consistent with the AEMC's approach to the

---

2 Queensland Government, *Queensland Government response to the Interdepartmental Committee on Electricity Sector Reform*, 16 June 2013.

3 The terms of reference are available on the project page (project code "RPR0002") on the AEMC's website: www.aemc.gov.au.

4 The MCE is referenced in the AEMC's governing legislation and is a legally enduring body comprised of the Federal, State and Territory Ministers responsible for energy. On 1 July 2011 the MCE was amalgamated with the Ministerial Council on Mineral and Petroleum Resources. The amalgamated council is now called the COAG Energy Council.

New South Wales competition review, we have incorporated these criteria into our assessment framework, which considers the following competitive market indicators:

1. customer activity;
2. barriers to entry, exit or expansion;
3. independent rivalry;
4. customer outcomes; and
5. retailer outcomes.

Our approach to assessing these indicators is discussed further in Chapter 2.

As part of our assessment of the retailer outcome indicator, we have had a particular focus on Victoria. The 2013 AEMC Residential Electricity Price Trends report found that the competitive market cost component of customer bills (which includes the retail and wholesale components) appears to be higher in Victoria than in other jurisdictions with market offers. This 2014 competition review has further considered this issue, which is discussed in Chapter 8.

1.2 Purpose of the report and next steps

Final report

This report sets out the Commission's findings on the state of retail energy competition in NEM jurisdictions. It was provided to the COAG Energy Council ten days prior to publishing as required under the Terms of Reference.

The report is accompanied by two consultant reports that provide further details on retailer and customer research undertaken for this review.[5]

Further advice

The terms of reference require the AEMC to advise Energy Ministers whether there are any jurisdictions to which we could usefully provide further advice on possible ways to transition to price deregulation. If requested by Energy Ministers, there may be scope for the AEMC to provide more detailed advice on this or other issues raised.

Future competition reviews

This review will be repeated on an annual basis in accordance with the standing terms of reference issued by the COAG Energy Council. We welcome stakeholder feedback

5 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014; and Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014.

on ways to refine the approach for future years and will be publishing a draft approach paper for stakeholder comment ahead of next year's competition review. Stakeholders will be notified at the start of this consultation process through the AEMC weekly stakeholder email and through an announcement on our website.[6]

1.3 Sources of information

The AEMC drew from publicly available data to inform our analysis, as discussed in Chapter 2. Additionally, we received information from stakeholders through submissions, meetings, and data requests. We also engaged consultants to collect quantitative and qualitative information.

The AEMC would like to thank all stakeholders who provided input to this review. In particular, we would like to thank those stakeholders who provided extensive data to support our analysis of the criteria set out in our terms of reference. This included data from energy retailers, the Australian Energy Market Operator, the Australian Energy Regulator, Ombudsmen and jurisdictional regulators.

Submissions

The Commission initiated this review on 17 January 2014 by releasing an Approach Paper with a series of questions to inform our analysis. Stakeholders were invited to respond to these questions and provide more general views on the current state of competition in each jurisdiction.

In response, the Commission received 18 submissions from a range of stakeholders including consumer advocacy groups, retailers, distributors, and government bodies. A summary of stakeholder submissions and the Commission's response is provided in Appendix C.

Stakeholder meetings

The time frame for this review did not provide sufficient time to publish a draft report and seek stakeholder comment on the Commission's draft findings.

Instead, we invited any interested stakeholders to contact the AEMC to discuss the review. The AEMC met with a range of stakeholders throughout the review process, including consumer groups, retailers, Ombudsmen, pricing regulators, members of the financial sector, and jurisdictional governments.

6 Please visit www.aemc.gov.au if you would like to 'subscribe for updates' to receive our weekly email with updates on all of the AEMC's rule changes and reviews.

Consultants

Additionally, energy customers and energy retailers were involved in this review through research undertaken by our consultants. The following consultants were engaged to inform our analysis:

- **Customer research**: Newgate Research was engaged to undertake customer research through qualitative deliberative forums and quantitative surveys.
- **Retailer research**: K Lowe Consulting and Farrier Swier Consulting jointly conducted interviews and surveys with electricity and gas retailers in each of the jurisdictions.

Chapter 2 provides further detail on how the findings of this work have been incorporated into our assessment of competition. The report produced by Newgate Research, and the report by K Lowe Consulting and Farrier Swier Consulting, set out the methodology and detailed findings of this research and are available on our website.[7]

1.4 Structure of the report

Our assessment framework and methodology are set out in Chapter 2, providing details on our information sources and the competitive indicators we have used to measure the five assessment criteria. This chapter also sets out key limitations of the data used and should be read in conjunction with Chapters 4-10 on specific jurisdictions.

Our analysis revealed a number of common trends across most jurisdictions. These are discussed in Chapter 3 (Overview and Main Findings) which provides context for the discussion in the subsequent jurisdiction-specific chapters.

Findings are set out in individual chapters for each NEM jurisdiction, with the exception of Queensland where our assessment of South East Queensland and regional Queensland has been split into two separate chapters.

Our appendices provide additional detail on stakeholder submissions, jurisdictional concession and hardship policies, jurisdictional solar subsidy arrangements and the energy retailers that operate in each jurisdiction.

[7] Project code RPR0002, www.aemc.gov.au.

2 Assessment Framework

This chapter explains the analytical framework that underpins the Commission's assessment of the effectiveness of competition for this review. National Electricity Market (NEM) jurisdictions are at different stages of promoting competition in energy retail markets. Consequently care needs to be taken when comparing outcomes across jurisdictions and concluding whether one jurisdiction is "more" competitive than another. For this review we have used a range of competitive market indicators to consider the state of competition in electricity and gas retail markets in each jurisdiction.

2.1 Introduction

Markets are dynamic: conditions change as the cost of inputs and technologies change, demand levels vary, innovation occurs, firms enter and exit the market and customer preferences change. Markets provide the mechanism for retailers to discover what customers want and for customers to discover the price and service combinations that retailers are offering. Higher retailer returns reward innovation and strong customer service, and also drive new entry which in turn creates further incentives for differentiation and cost reduction. This is a continuous, iterative process and one that does not always happen smoothly.

Many of the metrics used in typical competition assessments can change over time depending on external conditions, the stage of the business cycle or the maturity of the market. For example, while we would expect switching rates to be high as markets are opened to competition and customers test out new retailers, over time these rates should reduce once customers establish their preferences. Technology developments and other innovations may then spur increased customer activity for a period of time. Consequently it is important to consider these metrics over a period of time and in the broader context of the maturity of each market.

2.2 Market definition

In order to carry out a competition assessment, it is useful to define the market or markets to be considered. For this review we have done this in relation to two general areas – the product market and the geographic market. This market definition may change over time as jurisdictions harmonise their retail energy frameworks and markets continue to develop.

The terms of reference require the AEMC to focus on small electricity and natural gas customers in NEM jurisdictions.

For the purpose of this review we have considered each jurisdiction as a single geographic market with two product markets: an electricity retail market and a gas retail market. Residential and small business customers are considered to be part of the same product market. This market definition was adopted for the New South Wales competition review in 2013, based on our analysis of the available data.[8]

The key exception is Queensland where we looked at two geographic regions. The first is South East Queensland, where a number of retailers are currently operating and where the Queensland Government is considering removing retail price regulation in 2015. The second is the remainder of Queensland ("regional Queensland"), where retail competition is permitted but there is only one retailer at present. This distinction is appropriate as customers in these regions have fundamentally different experiences: those in South East Queensland have a choice of retailer, whereas those in regional Queensland only have access to one.

South East Queensland is defined by the Energex distribution network, which broadly covers Brisbane, Ipswich, Gold Coast and Sunshine Coast. Regional Queensland is defined by the Ergon distribution network, which covers the remainder of Queensland.

This definition was broadly supported in submissions to the Approach Paper for this review.[9] One exception was Envestra, who considered that regional gas markets should be considered a separate market from urban gas markets.[10] The Public Interest Advocacy Centre also considered the AEMC should assess rural areas separate from regional areas.[11]

We agree that different customer segments can experience different levels of competition. For this reason, while we have presented our analysis on the basis of the above market definition, we have also specifically considered:

- the extent to which there are differences between urban and regional areas within jurisdictions; and
- whether there are any differences between residential and small business customers.

In this report we highlight any instances where experiences do diverge between these customers and, if so, what factors may be driving these differences. We have not systematically considered differences between regional and rural areas. However, we note that the consumer surveys (discussed below) were geographically representative of the NEM population and therefore captured rural customers as well as regional and urban customers.

8 See the AEMC's *Review of Competition in the Retail Electricity and Natural Gas Markets in NSW* for further detail on why we considered this market definition to be appropriate.

9 See, for example, submissions to the Approach Paper from AGL, Alinta, Origin Energy and the Council of the Aging Queensland.

10 Envestra, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p3.

11 Public Interest Advocacy Centre, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p4.

2.3 How do we measure effective competition?

Effective competition requires effective participation of customers and retailers. Our assessment has considered whether customers are aware, informed and engaged, and whether retailers are competing to provide the products customers want.

It is difficult to identify a single objective measure that can capture the dynamic nature of retail energy markets. Rather, we have examined a number of different indicators that highlight both the behaviour of retailers and the responses of customers. The Commission has been guided by the terms of reference for this review, which require the Commission to consider, where practicable, and subject to data availability and resourcing constraints:[12]

1. customer switching behaviour;
2. ability of suppliers to enter the market;
3. independent rivalry within the market;
4. differentiated products and services;
5. price and profit margins; and
6. the exercise of choice by customers.

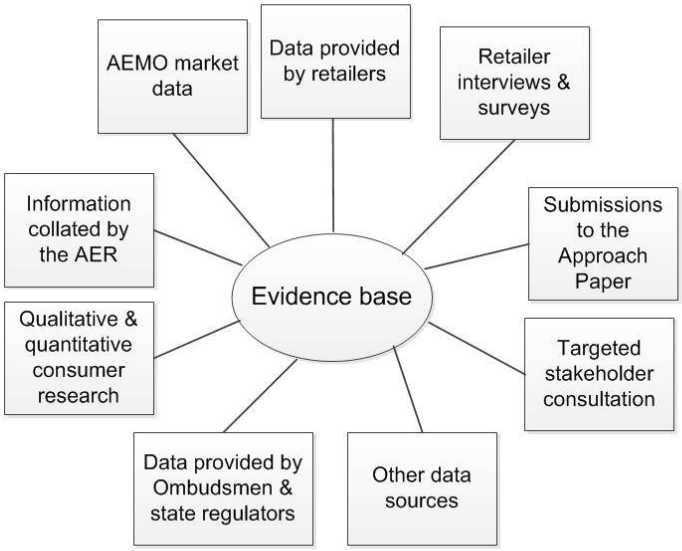
We have drawn on these criteria and refined them to focus our assessment on whether retail markets in NEM jurisdictions are providing outcomes that are consistent with effective competition. This approach is consistent with the New South Wales review completed in 2013. The criteria used in this review are therefore:

- the level of customer activity in the market;
- barriers to retailers entering, expanding or exiting the market;
- the degree of independent rivalry;
- customer outcomes; and
- retailer outcomes.

Together, these are referred to as the "competitive market indicators" (or "indicators"). We have used these indicators to structure our assessment of competition in Chapters 4 through 10. We have drawn from a number of sources to assess these indicators, combining both quantitative and qualitative information, as captured in Figure 2.1.

12 COAG Energy Council, Terms of Reference - *AEMC reviews of retail energy market competition*, 2014, p2.

Figure 2.1 Summary of information sources



Before describing how we have used the evidence base to assess these indicators, the next section describes our methodology for obtaining data on these indicators and the limitations of some of that data.

2.4 Methodology

2.4.1 Consumer research

The AEMC engaged Newgate Research to conduct quantitative and qualitative research on small electricity and gas customers' experiences of retail energy markets in the NEM.

A quantitative survey was conducted with 1,833 residential customers and 380 small business customers across South East Queensland, New South Wales, the Australian Capital Territory, Victoria and South Australia. The survey was not conducted in regional Queensland or Tasmania as the vast majority of small electricity customers in these areas were with their incumbent retailer at the time the survey was undertaken and therefore had limited experiences of a competitive electricity market.[13]

This survey was complemented with a series of qualitative forums held in the capital city and a regional centre in South East Queensland, Victoria and South Australia, as well as Canberra. Qualitative research was not conducted in New South Wales as similar research was completed in 2013 for the New South Wales retail review. The purpose of the qualitative research was to explore in greater detail consumers' experiences in energy retail markets. Each forum comprised between 14 and 32

13 We note that in Tasmania all gas customers have been contestable for some time, and that approximately 40 per cent of customers are not with the incumbent gas retailers. However, given the very limited gas penetration in Tasmania it would be difficult to obtain a statistically significant sample.

participants and a total of 162 participated in this research. The forums lasted for approximately 3.5 hours. Participants in these forums were recruited such that a broad mix of the community was represented, consistent with the demographic profile of each location.

Additional detail on the methodology used to undertake this research is available in a report prepared by Newgate Research.[14]

2.4.2 Retailer interviews and survey

The AEMC engaged K Lowe Consulting and Farrier Swier Consulting to conduct a series of interviews with retailers, the Energy Retailer's Association of Australia and the Energy Supply Association of Australia. The purpose of these interviews was to elicit retailers' views and experiences in operating in energy markets across the NEM. These interviews were supplemented by a survey.

Of the 23 organisations that were asked to participate in the interview and survey process, 14 agreed to be interviewed, 13 agreed to complete the electricity survey and seven completed the gas survey. Some organisations participated in both and others participated in either the survey or the interview. Overall, 17 of the 23 organisations participated.

2.4.3 Data provided by retailers

We requested information from retailers to provide additional evidence on the level of customer engagement in energy retail markets. This included:

- the number of small customers on regulated/standing offers versus market offers;
- the number of small customers that changed their plan with the same retailer; and
- the proportion of customers on a retailer's best offer.

In addition, we asked for information to inform our analysis of why competitive market costs in Victoria may be higher than in other jurisdictions. This issue is discussed further in Chapter 8.

Participation in this data collection was mixed and some of the retailers that participated were not able to provide information on all issues. In some instances retailers' systems did not allow them to extract the information we requested and they instead provided an estimate. Consequently, while the information provided was considered in our analysis, we have not relied on it to draw conclusions.

14 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014.

2.4.4 Submissions on the Approach Paper for this review

Eighteen submissions were received in response to the Approach Paper. These submissions represent a range of stakeholder views, including consumer groups, retailers, regulators, government and a gas distributor.

We have drawn on these submissions as part of our analysis. Appendix C provides a summary of issues raised in the submissions and, where relevant, our response.

2.4.5 AEMO market data

The Australian Energy Market Operator (AEMO) provided the AEMC with detailed electricity and gas data on customer transfers by retailer. For electricity this data goes back to 2009 for all jurisdictions. For gas we have access to a more limited historical data set, going back to October 2012. This data is further discussed in section 2.5.2.

2.4.6 Timing

Where possible we have looked at historical time series. Where we have been unable to consider a time series due to data limitations we have focussed, where possible, on the 2013 calendar year. Some data was only available over financial years, in which case this is stated.

2.5 Customer activity in the market

A desirable outcome of a competitive market is that customers are aware of the choices available to them and are able to act on those choices. By shopping around to receive lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service customers demand. Customer activity is an important indicator of whether competition is effective. Customer awareness, understanding and behaviour have been considered as part of this indicator.

2.5.1 Customer awareness and understanding

We assessed customers' awareness and understanding of energy markets primarily through quantitative and qualitative research on:

- the extent to which customers are aware of:
  - their ability to choose between energy retailers and plans;
  - the number and names of companies they could choose from; and
  - the existence of comparator sites.
- their understanding of energy plans and bills.

We also considered the proportion of customers on market offers versus standing or regulated offers. This metric must be interpreted with care. There will likely always be a segment of “sticky” customers for whom looking for a better deal and switching retailers is not a high priority. The AEMC is primarily concerned with ensuring those consumers who would like to switch retailers or change their energy plan understand that they can and are able to access the right information to choose an energy plan that suits their needs.

2.5.2 Customers investigating options and switching

The level of customer activity was informed by quantitative and qualitative consumer research on how and why customers participate in the market and whether there are any issues preventing customers from shopping around. This included considering the extent to which customers investigate their options and switch retailers or plans, as well as reasons for investigating and switching.

In order to investigate the extent to which customers switch retailers, we also considered market data from AEMO on switching rates. There are some issues when analysing switching data, including:

- The data on switches between retailers also does not capture unique switches[15] and so may overestimate the proportion of energy customers that switch if a smaller group of customers change retailer multiple times.
- The gross data includes some switches that do not represent a decision by customers to change retailer, such as: when switches occur in error; where a new meter has been installed; or where a customer moves house. We present two switching rates for electricity: a gross rate, which is consistent with the monthly switching data published by AEMO; and a second rate net of new meter “switches” and move-in “switches”. The net rate may underestimate switching with customer switching being somewhere between the net and gross rate. The gas data is unadjusted.
- The definition of “small electricity customer” has changed in some jurisdictions since the systems for capturing this information were implemented. Consequently in those jurisdictions where “small customer” is not defined as consuming less than 160MWh per annum, this data will overestimate the actual proportion of small customers that switch retailer.

We also attempted to capture the proportion of customers that switch plans with the same retailer, drawing on the customer survey and data or estimates provided by some retailers.

Switching rates were carefully interpreted in conjunction with other indicators as we note that high or low rates are not necessarily a sign of a well-functioning market.

15 If a customer switches multiple times, each switch is counted. For example, it is not possible to distinguish between one customer switching twice or two customers switching once each.

2.6 Barriers to entry, exit or expansion

Identifying any significant barriers to entry, exit and expansion is an important element of an assessment of competition. This involves analysing whether new retailers can freely enter the market and whether incumbent retailers can exit or expand within the market. Under these conditions, there are competitive pressures on existing retailers to charge prices commensurate with efficient costs and to improve their products and services. An effectively competitive market will generally have no significant barriers to entry, exit or expansion.

Our analysis of this market indicator primarily drew on information provided in retailer interviews and surveys and included consideration of:

- any evidence of entry, exit or expansion by retailers over the last two years;
- the impact of price regulation, where applicable;
- for electricity, a retailer's ability to manage spot price risk, either physically (through vertical integration with a generator) or financially (through contracting with a generator or via financial markets);
- for gas, the complex nature of the arrangements for obtaining and transporting gas, as well as the ability to access gas pipelines;
- the size and geographic spread of the market;
- the need for credit support, which is required by parties such as the Australian Energy Market Operator, generators, financial intermediaries and electricity networks;
- economies of scale, whereby larger retailers can spread fixed costs over a larger customer base;
- economics of scope, where a retailer can spread fixed costs over more than one product;
- whether any exit costs exist;
- the influence of branding, particularly in markets dominated by the incumbent retailer(s); and
- impediments to expanding across jurisdictions, including differences in:
    - the adoption of the National Energy Customer Framework;
    - energy efficiency schemes and feed-in tariff schemes;
    - customer protection frameworks; and
    - other regulatory requirements.

We also specifically considered whether there were any impediments to retailing in rural and regional areas.

Part of our assessment of whether retailers could obtain competitively priced hedging products involved examining contract market liquidity and the impact of vertical integration on this market.

For a new entrant retailer without generation assets, the most common strategy to manage price and volume risk is to enter financial contracts with generators and/or intermediaries that lock in the future price of electricity.[16] These contracts are known as derivatives and can be traded bilaterally in over the counter (OTC) markets or publicly on the Australian Securities Exchange (ASX).[17]

The effectiveness of derivatives as a risk management tool depends upon retailers being able to purchase these products at competitive prices, when required. One measure of the performance of OTC and exchange traded markets is the degree of liquidity. This provides an indication of how easily retailers can obtain these products by considering the number of trades that occur compared to the amount of energy sold.

While data on the number of exchange-traded derivatives is readily available from the ASX, it is more difficult to obtain information on OTC contracts, since these are bilaterally negotiated. The Australian Financial Markets Association publishes an annual report on Australian financial markets, which provides some information. However the data on electricity OTC contracts is based on a voluntary survey. Not all retailers participate in this survey and the rate of response varies from year to year. Consequently, while we can be confident that in any given year the number of OTC trades is at least as high as reported, we cannot compare data between years.

One factor that can influence market liquidity is the extent of vertical integration. If retailers adopt a strategy of building a portfolio of generation interests, the requirement to enter the market for hedge contracts may decrease. To the extent a retailer's generation assets match the energy required for its retail customers, there is unlikely to be a commercial need to offer generation contracts in the market. This could negatively impact entry and expansion conditions for retailers without generation interests, such as smaller retailers that may require more tailored hedging products.

2.7 Independent rivalry

Independent rivalry reflects the extent to which retailers are competing to attract or retain customers. Rivalry between retailers helps to drive discounting and product innovation. An effectively competitive market will generally have a high level of independent rivalry. Rivalry can be measured by, for example, the number of retailers

16 Price risk results from volatility of the spot price; whereas volume risk arises when the customer load exceeds the retailer's contracted load.

17 For an explanation of these markets, see: AEMC, *NEM Financial Market Resilience*, Issues Paper, 8 June 2012.

participating in the market; market share and concentration of the market; the degree of differentiation between service and product offerings; and aggressiveness or defensiveness of marketing strategies.

The specific components of this market indicator that we considered are set out below.

2.7.1 Market share and concentration

The Herfindahl-Hirschman Index (HHI) is a measure of market concentration. The HHI is calculated by summing the squares of the percentage market share of each retailer. A score of 10,000 indicates a pure monopoly and an extremely competitive market has an HHI close to zero. We calculated a HHI for each jurisdiction based on market share data for calendar year 2013, provided by AEMO.[18] The Australian Competition and Consumer Commission uses a score of 2000 as a threshold when considering the level of competition for merger assessments.[19]

2.7.2 Switching between first and second tier retailers

To determine whether retailers are actively competing to attract new customers, we looked at the level of switching over time between larger, incumbent retailers and second tier retailers. This included considering how active second tier retailers are in the market and whether these smaller retailers are able to gain or maintain market share. Switching between second tier retailers is a particularly useful metric as it indicates that customers are not necessarily biased towards larger incumbent retailers and that these retailers are competing between themselves as well as with incumbents.

2.7.3 Product differentiation and the number of market offers available

We looked at the number of market offers available and the ways in which offers differ to test whether and how retailers are competing by differentiating their brand and their products and services. This involved surveying the range of offers advertised as at 31 March 2014 in each NEM jurisdiction. While a static assessment of offers available at one point in time has some limitations, it can provide a useful snapshot of the type of differentiation occurring in a market.

In retailer interviews, retailers were also asked how they try to differentiate their products and brand and about the extent of product differentiation and innovation in each jurisdiction in the NEM.

2.8 Customer outcomes

High levels of customer awareness and high switching rates by themselves do not provide a full picture of whether there is competition in a market. In effectively

18 The data used for the HHI calculation includes Australian Power and Gas as a separate retailer from AGL since its acquisition took place in late 2013.

19 See ACCC, Merger guidelines, November 2008, p37.

competitive markets, customers are generally satisfied with the service and range of products available to them. We note, however, that customer complaints can also be a sign that customers are starting to engage in the market, particularly as the market transitions from a monopoly provider to competition.

To measure satisfaction, as part of the customer research we asked customers about their satisfaction with:

- the level of choice in the market;
- retailers;
- the switching process; and
- value for money.

In addition, we examined the nature and frequency of customer complaints to, or issues raised with, retailers and Ombudsmen.

In this report, “complaint” refers to a single expression of dissatisfaction with an electricity or gas retailer. Multiple issues may be raised in a single complaint. Depending on the data available, we have either presented the number of complaints or the number of issues raised. When the number of complaints is referred to, the issues breakdown is by the main issue raised during each complaint. These distinctions should be considered in comparing different complaint figures.

2.9 Retailer outcomes

Profit margins can provide an indication of the level of competition in a market. If profit margins are persistently very high, retailers may be earning profits in excess of the efficient cost of supply and so the market may not be sufficiently competitive to maintain downward pressure on prices. On the other hand, if profit margins are persistently very low then new retailers may be deterred from entering the market if they cannot earn a reasonable return on their investment.

Over time, as firms enter and exit, the market will evolve and mature, and retailer margins can be expected to vary with the business cycle. Periods of temporarily elevated margins stimulate new entry and give customers incentives to seek out lower-price suppliers and/or to reduce consumption. Periods of depressed margins put pressure on suppliers to exit the market and/or to seek cost efficiencies.

Estimates of retailer margins are sensitive to a number of assumptions used in the calculation, including the time period over which the analysis is conducted, the representative retail tariff used, the annual consumption of an ‘average’ consumer, how wholesale energy costs are estimated and the operational costs assumed for retailers. Changes in these assumptions can have material effects on the results and care should be taken when interpreting the numbers and forming conclusions.

Our analysis of this market indicator primarily drew on information provided in retailer interviews and surveys and the AEMC's 2013 Residential Electricity Price Trends report. Where prices are regulated, we considered the profit margins factored into the regulated prices in those jurisdictions and whether there was sufficient headroom to promote competition.

Further discussion on the nature of profit margins in competitive markets is contained in Chapter 3. There is also additional discussion in Chapter 8, where we explored possible reasons for competitive market costs appearing higher in Victoria than other jurisdictions in the AEMC's 2013 Residential Electricity Price Trends report.

2.10 Drawing these indicators together

As discussed above, markets evolve over time as regulations change, technology advances and consumers become better informed and engaged. These changes encourage entry and/or exit by retailers as they vie to offer customers new products, lower prices or improved services while making a reasonable return on their investments over time.

Each of the indicators discussed above provide a useful check on the state of the market. However, it is important to note that an adverse finding for a single indicator is not necessarily indicative of a systemic problem with the way in which the market functions. For example, in a well-functioning market we would expect retail margins to fluctuate. Similarly, we would expect to see periods of retailer entry followed by consolidation, and for consumer satisfaction to change as retailers search for ways to improve their services.

For this reason, it is important to consider the competitive market indicators as contributing one piece to the broader picture. It is the combination of all these indicators that determines the state of competition in a market.

3 Overview and Main Findings

Box 3.1: Key findings

- The state of competition varies across the NEM as retail markets have evolved at different rates. Electricity and gas markets also differ.
- Customers are interested in energy issues but some are less engaged, particularly in the retail gas market. There is an opportunity to encourage customers to shop around for a better deal by increasing awareness of the information and tools available to simplify the process.
- Governments provide concessions to certain customers to help them meet their energy expenditure. The benefits of these schemes may be eroded by higher prices if a customer is on a standing offer and does not have sufficient information or support to find a better deal.
- In electricity, competition has led to more choice of retailers and plans in Victoria, South Australia, New South Wales and South East Queensland. Competition is yet to emerge in small customer electricity retail markets in the Australian Capital Territory, Tasmania and regional Queensland.
- In gas, competition has been more tempered as gas is a secondary consideration for most customers and retailers. Structural and market design features have led to significant differences in market outcomes between and within states. In markets with low customer numbers and low average demand, some retailers expect competition to stagnate or decline as upstream market conditions lead to increased gas prices.
- Despite some reforms aimed at achieving a common approach to retail markets, jurisdictional differences remain. These can impede expansion by retailers across multiple jurisdictions by increasing compliance costs, which will ultimately be passed through to customers.
- The Commission recommends that jurisdictions:
  - consider options for raising awareness of the tools available for comparing offers to improve customer confidence in the market;
  - ensure concession schemes are delivering on their intended purpose in an efficient and targeted way; and
  - continue to harmonise regulatory arrangements across jurisdictions to minimise costs, including implementing the National Energy Customer Framework; and
  - remove energy retail price regulation where competition is effective.

This chapter provides an overview of common themes and findings across jurisdictions in the national electricity market (NEM). Details of our research results, analysis and findings for each jurisdiction are set out in subsequent chapters. This chapter sets out:

- a brief history of the Council of Australian Government's reform agenda;
- the present state of jurisdictional energy retail markets; and
- possible future market developments affecting retail competition.

3.1 Past - a brief history of the reform agenda

Prior to the commencement of the market reforms for electricity and gas, small customers had no choice regarding their preferred energy retail supplier. All customers were supplied from the incumbent retailer for their region. Reforms to these arrangements began with the introduction of full retail competition, whereby new retailers were permitted to enter the market and compete with the incumbent supplier. This generally occurred in a staged fashion, with larger customers being able to choose their energy supplier before mass market customers (ie small business and residential customers). All NEM jurisdictions have now introduced full retail competition for all customers.

The next phase of reform has been to remove retail price regulation. Price regulation was maintained as an additional protection for customers following full retail competition on the basis that it would take some time for competition to develop. Consequently customers would not immediately see the benefits of competition in terms of price and service offerings. As competition increases, price regulation can hinder further market development.[20] Consequently jurisdictions agreed to phase out retail price regulation where effective retail competition can be demonstrated.

The purpose of these reforms has been to improve outcomes for energy customers through increased competition. As markets evolve, competitive pressures should result in:

- prices that trend to the efficient cost of supplying a service;
- a quality of service that matches customers' expectations; and
- a choice of products and services that match customers' preferences.

These outcomes are achieved through multiple retailers competing to attract and retain customers by offering them innovative new products and services and lower prices. Where these outcomes are achieved, there is no need for regulatory intervention. It is important to note that there can be different degrees of competition. Consequently while some markets may appear to be "more competitive" than others, this does not

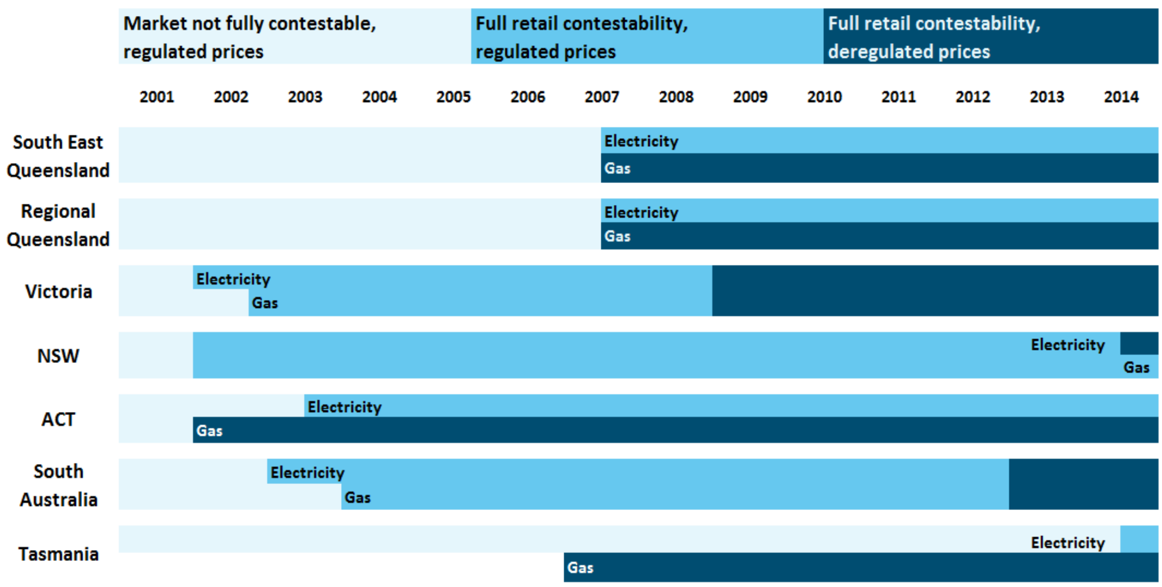
---

20 See AEMC, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, Final Report, 3 October 2013, Sydney, p59, for a summary of the benefits and costs of price regulation.

mean that a market characterised by fewer retailers, lower levels of customer engagement or more limited product differentiation compared to another market is not competitive. Rather, it may simply be at a different stage of market maturity.

Jurisdictions are at different stages along the reform path as shown in Figure 3.1. Victoria, for example, has had full retail competition for both electricity and gas customers since 2002 and prices in that market have been set by retailers since 2009. Tasmania has only recently introduced full retail competition for residential customers. Jurisdictions also differ based on the extent to which their energy markets have been privatised. Different market characteristics, such as the size of the customer base and average consumption levels, can also impact the extent of competition in a market. Consequently it is difficult to meaningfully compare outcomes across all jurisdictions.

Figure 3.1 Stages of energy retail market reform



3.2 Present - state of competition in retail energy markets

Introducing competition in electricity retail markets has led to more choice of retailers and plans in Victoria, South Australia, New South Wales and South East Queensland. While most retailers entered Victoria first and some continue to only operate in that jurisdiction, many retailers have expanded into other markets. Customers surveyed in these jurisdictions have a consistently high awareness of their ability to choose their retailer and many customers surveyed were more likely to have changed their electricity retailer in the last five years than other service providers such as insurance and telecommunications.

Competition is yet to emerge for small customers in electricity markets in the Australian Capital Territory, Tasmania and regional Queensland, where regulatory arrangements have impeded entry by new retailers.[21] Customers surveyed in the

21 In the Australian Capital Territory, the way in which the regulated price is set makes it difficult for new retailers to profitably enter the market. In Tasmania, full retail competition has only recently

Australian Capital Territory were generally less aware of their ability to choose their retailer and were less satisfied with the level of choice available compared to those in Victoria, South Australia, New South Wales and South East Queensland. Customer research was not conducted in Tasmania or regional Queensland where most mass market customers have not been able to choose an alternative retailer because there is currently no alternative to the incumbent retailer.

Competition in natural gas retail markets, while still broadly effective, has been more tempered. Gas is a secondary consideration for most customers and is a less attractive value proposition for many retailers. Structural and market design features in gas markets, such as the size of the customer base, contract carriage versus market carriage models and the ability to source and transport gas have led to significant differences in market outcomes between and within states. Limited penetration of natural gas distribution networks and small customer bases in Queensland and Tasmania and some regional areas has impeded the development of competition. In contrast, the high penetration of gas in Victoria, the design of the Declared Wholesale Gas Market, and the transportation model in Victoria, have prompted eight retailers to participate in the gas retail market.

Energy retail markets are currently characterised by an increased pace of change, falling demand and uncertainty about the future of gas, the carbon price, renewable policy and consumer policy. Some of these issues are discussed in more detail in section 3.3.

The remainder of this section sets out our findings on:

- customer activity in the market;
- customer outcomes;
- market conditions and outcomes for electricity retailers;
- market conditions and outcomes for gas retailers; and
- areas where differences between jurisdictions may be impeding retailer expansion across the NEM.

3.2.1 Customer activity in the market

Over the last few years there has been an increasing focus on customer engagement across the energy industry. The first of the AEMC's strategic priorities is to strengthen consumer participation and to continue to promote competitive retail markets:

been introduced for residential customers and smaller businesses, so it will take some time for entry to occur. In regional Queensland, the way in which a uniform tariff policy is given effect makes it difficult for retailers other than the incumbent to profitably compete. These issues are discussed in detail in the jurisdictional-specific chapters.

> "Effective consumer participation can contribute to more efficient markets and help consumers manage how much they spend on energy. Competitive retail markets promote choice and value for consumers, by providing incentives for retailers to minimise costs and prices, and to offer a range of tariffs. This priority aims to empower consumers to participate in regulatory processes, voice their demand for energy services and choose options right for them."[22]

A range of opportunities for consumer participation in policy and regulatory processes have been, or are currently being, developed. For example, the Australian Energy Regulator has established a consumer reference group and a Consumer Challenge Panel. These are intended to help consumer representative groups provide input into regulatory processes and incorporate the interests of consumers into decisions that ultimately impact outcomes for customers in the retail market.

At the household and small business level, customers want better and simpler information from trusted sources to help them make more informed decisions about their energy providers. While many customers are shopping around, generally in response to a price rise or bill shock, other customers do not expect the potential savings will be worth the effort.

This section discusses the extent of customer activity in the NEM and sets out some of the triggers for, and barriers to, shopping around for a better deal.

Customers are shopping around but want better information

Customers surveyed for this review[23] have a high level of interest in energy issues and are very concerned about future energy prices, most likely triggered by electricity price increases over the last few years. Most are aware that they can choose their energy provider. However, many struggle to compare options when searching for alternative energy plans.[24]

> "It's all too confusing. It's like phone companies. It's all different but there's no base. (Maroochydore)"

> "It's like comparing apples and oranges (Adelaide)"

Despite some challenges with comparing offers, switching rates in Victoria, South Australia, New South Wales and South East Queensland are generally high compared to other industries and countries.[25] Customers surveyed in these jurisdictions were

---

22 AEMC, *Strategic Priorities for Energy Market Development*, October 2013, p6.

23 As discussed in Chapter 2, quantitative research was conducted in South East Queensland, New South Wales, Australian Capital Territory, Victoria and South Australia. Qualitative research was also conducted in each of these jurisdictions except for New South Wales.

24 Newgate Research, C*onsumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p98,161.

25 VasaaETT, Utility Customer Switching Research Project, *World Energy Retail Market Switching Analysis and Rankings*, November 2012, p18.

more likely to have changed their electricity retailer or plan than for other providers of services such as mobile phones, internet, banking and insurance.

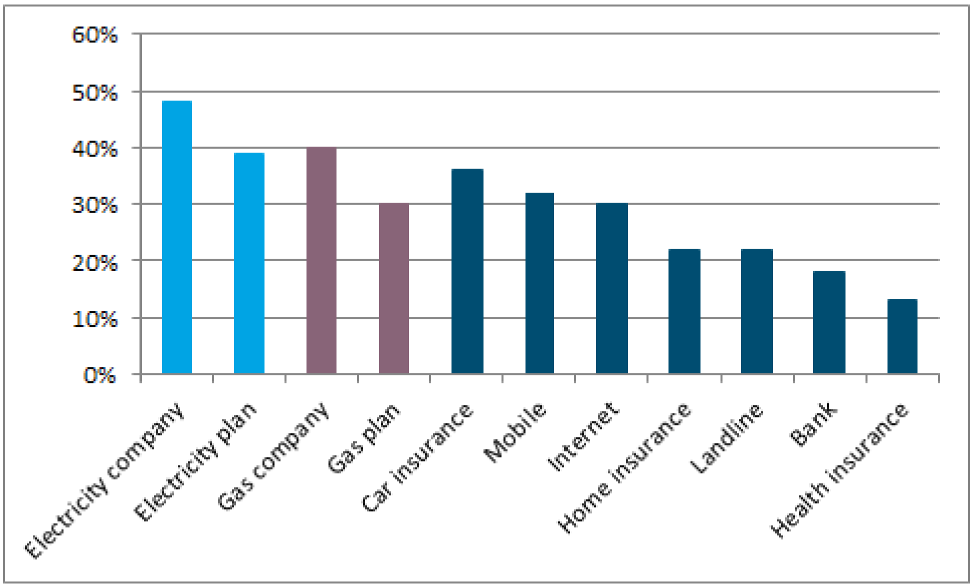
> "(Switching) was easy and I'd do it again (Murray Bridge, Lower income)"

> "The tools are there, it is up to the consumer to do the research (Ballarat, Income unidentified)"

> "I'm always moving from one supplier to another to try to save money (Murray Bridge, Higher income)"

Figure 3.2 shows the proportion of customers surveyed across the NEM (excluding Tasmania and regional Queensland) that have switched various service providers at least once in the last five years.

Figure 3.2 Proportion of customers surveyed that have switched provider or plan at least once in the last 5 years



Source: Data from Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p32. AEMC analysis.

Around three in ten customers surveyed had actively investigated different offers or options in the last 12 months. This rose to four in ten customers in Victoria, where price regulation was removed in 2009, and was as low as one in ten in the Australian Capital Territory, where retailer choice is limited and many customers are not aware they can switch.

An increase in customer activity is expected following an increase or change in the nature of the choices available as customers test out new options. As the market evolves, this level of activity may reduce in line with other, more established service industries.

Triggers for, and barriers to, shopping around

The majority of customers surveyed changed retailer primarily to obtain a better price. This is consistent with retailer experiences which suggest that customers switch in response to bill shock, substantial price increases, direct approaches from retailers and media focus on rising prices. Some retailers considered that poor customer service and billing practices are unlikely to prompt a switch, but make customers more amendable to switching if approached.[26] Very few customers surveyed cited poor customer service as the main reason for switching, however discussion at the forums suggest poor customer service is an underlying issue for some customers.

While many customers are shopping around, some appear to be less interested in changing provider. Around half of customers surveyed were not interested in switching retailer or plan in the next 12 months.

Not all customers will choose an active role. Some customers consider any savings would not be worth the time and effort required to research, compare and choose an offer, and they want to "set and forget".[27]

> “I'm just lazy, complacent about it (Ballarat, income unidentified)”
>
> “The bill comes, it seems fine, I can afford it so I pay it (Adelaide, lower income)
>
> “Other priorities in life, not having the time (Murray Bridge, higher income)”

Other customers were not aware of the potential savings they could make and did not perceive differences between the retailers or prices available.[28]

> “The value of the offers isn't big enough. It's not worth my energy and time (Maroochydore, income unidentified)”
>
> “There's lots of choice but prices are practically the same (Adelaide, income unidentified)”
>
> “There isn't enough price difference to switch - if it's 3 per cent don't bother, but if it was 15 per cent I might (Ballarat, income unidentified)”

These customers may be more likely to switch if they had an easy way of comparing offers from a credible information source. Over sixty per cent of survey respondents were not aware of, or could not name, a price comparator website. Awareness of the

26 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014 p73.

27 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014 p41,p95, p96.

28 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p41, p117, p173.

government comparator website was very low. Qualitative research suggests that the likelihood of switching is directly related to the perceived savings that can be made and customer confidence in being able to access easy to understand and credible, independent information about the different offers available. Knowing that they can save money by shopping around and that tools are available to support their choice should help customers engage more confidently in the market.

Some customers are also confused about their options if they have solar panels. Some participants in the customer forums expressed concern that they would lose their feed-in tariff if they switched retailer. This was particularly the case in Queensland, although a higher proportion of surveyed customers in New South Wales named having solar panels as the main barrier to switching (six per cent compared to two per cent in South East Queensland).

In addition to the factors discussed above, retailers considered the following could also impede switching:[29]

- limited awareness of ability to switch and low levels of interest;
- perceived complexity of contract terms and conditions, prices, discounts, exit fees and other fees and penalties;
- misconceptions about the role of the government in energy retail markets and the protections afforded by standing contracts;
- exit fees; and
- the time taken to transfer.

The Queensland Consumer Association also considered transfers between retailers should be "more consumer friendly" and quicker.[30] On the other hand, AGL and EnergyAustralia submitted that there are no significant barriers that prevent customers from switching retailer or plan.[31]

Most retailers considered that all customers have the same level of access to competitive offers. The majority of retailers operate in both urban and regional areas. However, they acknowledged that some groups, such as those with special needs, non-English speaking customers and the elderly, may have less ability to take advantage of these offers. Retailers also noted that while they would prefer to take on credit worthy

29 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014 p74.

30 Queensland Consumer Association, submission to the *2014 Retail Competition Review*, Approach Paper, p2.

31 AGL, submission to the *2014 Retail Competition Review*, Approach Paper, p2; and EnergyAustralia, submission to the *2014 Retail Competition Review*, Approach Paper, p3.

customers that pay on time, the costs associated with running credit checks is costly so this type of segmentation is not widespread.[32]

Some of these impediments to switching plan or retailer are already being addressed by retailers themselves, as discussed below. Further, the AEMC has made recommendations on improving the switching experience for customers (see Box 3.2) and how to better inform customers, particularly segments of the community that may require additional support (see Box 3.3).

Box 3.2: AEMC recommendations to improve the switching experience

The AEMC recently conducted a review of electricity customer switching arrangements in the NEM.[33] We found that, generally, most customers are able to switch retailers efficiently. However, some customers experience lengthy or inaccurate transfers. Knowledge of bad experiences may spread and so could undermine confidence in the retail market over time.

A number of recommendations were made to improve the timing and accuracy of customer transfers, including:

- allow estimated meter reads to be used for in-situ customer transfers between retailers, where the customer consents;
- develop standards to improve the accuracy of the data used in the customer transfer process;
- require the Australian Energy Regulator to publicly report on timing and accuracy of customer transfers;
- require the Australian Energy Market Operator to periodically review the effectiveness of the customer transfer system; and
- require retailers to resolve erroneous customer transfers in a timely manner.

We recommended that the COAG Energy Council propose rule changes to the AEMC to give effect to these recommendations. The Council noted that officials are currently reviewing the report and recommendations.[34]

Gas tends to be a lower involvement product than electricity and switching decisions by gas customers are often linked to electricity switching decisions. Ten per cent of customers surveyed across the NEM cited the main reason for switching gas retailer as wanting to have gas and electricity with the same retailer. Gas switching rates are

32 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, report for the AEMC, June 2014 pp57-58.

33 AEMC, *Review of Electricity Customer Switching*, Final Report, 10 April 2014.

34 COAG Energy Council, Meeting Communique, 1 May 2014, p4.

typically lower than for electricity, but still similar to other industries as shown in Figure 3.2 above. This is likely due to gas bills typically being lower than electricity and gas customers having seen more moderate price rises to date.

Some “sticky” customers may never become active shoppers in the energy retail market because their energy bills are not sufficiently high for them to expend their time searching for a better offer. However there are many customers interested in finding a better deal. Greater support is required for these customers as discussed in the next section.

3.2.2 Customer outcomes

Customers appear to be broadly satisfied with services provided by their own retailer. However, customers that participated in the qualitative research appeared less satisfied with the energy industry overall. Mistrust of retailers was high, probably due to a mix of price rises and the negative consequences of door knocking to obtain customers.

While retailers appear to be responding to customer concerns, more can be done to support customers by providing an independent, trusted source of information, informing customers of their rights and responsibilities and ensuring customers in need have access to an effective concession scheme.

This section first provides an overview of customer views of the retail market and provides examples of how retailers are beginning to respond to customer concerns. It then highlights where governments continue to play an important role, namely in providing a source of independent information and ensuring that customer protection frameworks, including concession schemes, are appropriate and effective.

Both satisfaction and mistrust appear high

A common theme in the customer research forums was 'better the devil you know', signalling a high level of mistrust of energy retailers. While most customers were at least somewhat satisfied with their own retailer, they were more negative about energy companies in general. Satisfaction with their own retailer appeared to be more related to reliability of supply than customer service from retailers. Further, some customers that participated in the research forums appeared to be satisfied with their retailer either because they had not heard from them or because they were not dissatisfied with them.[35]

> “I pay for what I get. I'm not happy or dissatisfied. They provide a service; it's a necessary evil. I don't have anything to complain about. It's not exceptional service - they don't do anything out of the ordinary but they haven't stuffed me around (Melbourne, middle income)”

35 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p55, p114, and p225.

> "The less I hear from my electricity company the happier I am (Adelaide, Income unidentified)"

> "I have no reason not to be satisfied (Canberra, lower income)"

Although mistrust of energy companies was not raised as a key barrier to investigating offers or switching, it was raised as an important underlying issue in the forums.[36]

> "[My retailer is] the best of a bad bunch (Melbourne, Small business)"

> "There's no real policing over it. There's an inherent distrust. I think in the back of my mind they're screwing me, I'm angry whenever the bill turns up (Murray Bridge, lower income)"

> "I don't think it matters who you go with, you're going to have a bad experience at some point (Adelaide, higher income)"

Retailers are increasingly responding to customer concerns

Retailers have recently made a number of changes that suggest they are responding to some customer concerns. For example:

- In 2013 AGL, EnergyAustralia and Origin Energy ceased doorknocking residential customers.
- Origin Energy has recently announced it will stop cold calling residential customers and will no longer charge exit fees. Many second tier retailers already do not charge exit fees.
- Some retailers are developing campaigns that attempt to better explain their products and address customer criticism of poor service, such as EnergyAustralia's "Perfect Plan" and Origin Energy's "The change you've been waiting for".
- Many retailers are attempting to simplify their offers to reduce complexity and make it easier for customers to choose.

AGL noted that "being able to provide customers with useful, high quality information is a form of product innovation and product differentiation that is being increasingly embraced by energy retailers".[37]

The reduction in door knocking had been noticed and appreciated by some customers in Victoria that participated in the forums.[38]

---

36 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p61,97,113.

37 AGL, submission to the *2014 Retail Competition Review*, Approach Paper, pp1-2.

38 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p44.

This action by retailers suggests that the market is evolving such that customers are now better positioned to start driving improved outcomes and products that better suit their needs and preferences, without the need for regulatory intervention.

Some retailers agree that customer preferences have played a significant role in introducing some products,[39] such as those that enable customers to manage their bills[40] and fixed price products.[41] Some retailers use focus groups and test the market before introducing new products.

Other retailers said customer preferences have little influence over their products. One retailer said this was because it is difficult to identify precisely what customers want since energy is a low involvement product. Another considered that changes to the regulatory framework meant that retailers had become "more regulatory driven than customer driven."[42]

There is a role for government in providing independent information

While on balance retailers appear to be responding to customer concerns and preferences, there is still a role for government in supporting customers, particularly while there remains a level of mistrust of retailers. Customers are currently sceptical about information provided by retailers and also commercial comparator websites. In contrast, there was significant support for an independent government run website that could be used to compare offers.

In our 2013 review of competition in New South Wales we found that half of the customers surveyed would be quite or very likely to switch if they knew that there was a free, independent government website where they could compare energy plans.[43] Qualitative research conducted in other jurisdictions in 2014 suggests that customers in other states would be similarly more confident in choosing an offer if they know they can obtain information from an independent source.

> "There are so many comparison websites that have a hidden agenda (Melbourne, income unidentified)"
>
> "I don't really believe the comparison companies - they have their own clients and they would just mention those offers (Maroochydore, looked but didn't switch)"

---

39 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p53.

40 For example, My AGL Monthly Bill and Origin's EasiPay.

41 EnergyAustralia and Origin Energy offer fixed price gas and electricity products.

42 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p53.

43 AEMC, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, Supplementary Report: Increasing consumer engagement, 31 October 2013, Sydney, p19.

“It is nice to know there is a government run one [comparator website] (Murray Bridge, higher income)”

Greater promotion of Energy Made Easy,[44] or the equivalent jurisdictional switching site, could therefore go a long way to improving customer confidence in the market. This could be combined with a government information and education campaign to encourage customers to shop around regularly, inform them of their rights and address common misperceptions that may be a barrier to switching. This is consistent with advice provided to the New South Wales Government last year and a summary of this advice, contained in our 'consumer engagement blueprint',[45] is set out in Box 3.3.

While the blueprint was based on research conducted in New South Wales, the findings and recommendations are relevant to other jurisdictions that also share the challenge of providing customers with the information they need to shop around.

Importantly, the blueprint recommends ways to support customers that may not be captured by mass marketing or that may require additional support to choose a plan that suits their needs. For example, the blueprint acknowledges that not all customers have the same level of access, confidence or skills to use the internet, and so provides suggestions on how these customers can be assisted.

In interviews for this review, some retailers expressed support for both government comparator websites[46] and a role for government in educating customers.[47] Some retailers considered governments should address the following specific issues to encourage switching:

- raising the level of customer awareness of their ability to change retailer in South East Queensland when price regulation is removed;
- inform customers in New South Wales that their choice of retailer is not constrained by the distribution network in which they are located; and
- educate customers on standing contracts and financial assistance providers about the benefits of moving onto a market contract.

---

44 Energy Made Easy was first launched in July 2012 following consultation with a wide range of stakeholders. In late 2012 the website was tested for usability with a range of users. In response to feedback from key stakeholders, including consumer groups, industry and participants in usability testing, the Australian Energy Regulator will be relaunching Energy Made Easy in the second half of 2014. The enhanced website will make it easier for consumers to compare offers. Changes are also being made to simplify the process for retailers to input their offers, and to incorporate complex time of use tariff offerings.

45 AEMC 2013, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales, Supplementary Report: Increasing consumer engagement*, 31 October 2013, Sydney.

46 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p59.

47 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p72.

Box 3.3: Empowering consumers: A blueprint for informing and empowering small consumers in energy markets

In 2013 the AEMC, in collaboration with consumer groups, energy retailers and communication and research experts, developed a consumer engagement blueprint to empower consumers and make it easier for them to compare offers. Our advice was based on extensive consumer research that found:

- many consumers are confused about their options and how to compare available offers;
- consumers don't know what their rights and protections are;
- there's a mistrust of retailers and the prices they offer; and
- consumers aren't aware that they could save money.

The blueprint provides possible strategies to overcome barriers that prevent more participation in energy retail markets and that meet the needs of specific groups in the community. The aim of the blueprint is to empower consumers so that they have the right information and support to choose an energy plan that suits their needs.

Our proposals had three limbs:

- **Inform consumers**. Consumers need to know that:
  - they can choose between plans and retailers and could save money;
  - there's an independent website that will give them comparisons and a helpline that will assist in finding the right deal for them;
  - they have rights and protections when they enter a new agreement; and
  - the energy supply to their home won't be affected by changing retailer.
- **Make it easy for them to choose**. We recommended refining Energy Made Easy and the Australian Energy Regulator's 1800 helpline service. We also recommended refinements to the price fact sheets that retailers are required to provide.
- **Use a variety of ways to reach consumers**. In addition to mass media, we recommended distributing informative leaflets in multiple languages to places where people go such as local councils, community based organisations and Centrelink. We also recommended targeted media to reach different segments of the community and providing information packs and training to community organisations.

The Australian Competition and Consumer Commission has named energy consumer issues as one of its priorities. A particular area of focus for investigation and enforcement concerns misleading discount claims relating to the promotion of discounts and savings off energy use and/or supply charges under those plans. The ACCC instituted proceedings in December 2013 and May 2014 against two retailers regarding these issues.[48]

Consumer protections and concessions

Electricity is an essential service and gas is also seen as essential by customers in some jurisdictions where it is used for cooking, heating and hot water. In recognition of this, protections are in place to ensure that consumers have access to an energy supply.

The National Energy Customer Framework (NECF) harmonises state-based regulatory frameworks (excluding retail price regulation and community service obligations) into a single set of national rules governing the distribution and retail of energy. As discussed further below, some jurisdictions are yet to adopt the NECF and those that have adopted it have generally done so subject to some changes.

The NECF regulates the sale and supply of electricity and gas to retail customers. It contains a range of energy-specific consumer protections and includes a number of obligations on retailers such as quality of information on bills, marketing regulation, and mandatory hardship programs which require every retailer to help customers in financial trouble.

In addition to protections governing the supply of energy, governments have in place a number of concession schemes to help certain sections of the community in meeting their energy expenditure. Generally these concessions apply to customers such as pensioners, those with certain medical conditions and low income households and involve a contribution towards meeting a customer's energy bill. The eligibility criteria and quantum of the concession varies between jurisdictions. A full list is set out in Appendix B.

In the AEMC's Power of choice review we recommended that governments review the effectiveness of concession schemes to ensure they are appropriately targeting those customers in need. A similar recommendation was made in our New South Wales review. We note that the Independent Pricing and Regulatory Tribunal (IPART) has also recommended the New South Wales Government conduct a review to ensure that affordability measures "target the most vulnerable customers in a comprehensive, complementary and cost-effective manner".[49]

There would also be benefits in governments encouraging and assisting consumers who are entitled to concession schemes to review their energy plans. There is a risk that the benefits of a concession could be eroded by higher prices if a customer remains

48 ACCC Media Releases 5 December 2013 and 8 May 2014; R Sims, 'CEDA conference: Looking forward to 2014', 21 February 2014, CEDA conference, Sydney.

49 IPART, submission to *2014 Retail Competition Review*, Approach Paper, 26 February 2014, p2.

on higher-priced plan. By ensuring these customers are on an appropriate energy plan consistent with their energy needs, governments may better achieve the objectives of these schemes. This will ensure that any government assistance is providing maximum benefit for these consumers and maximise the efficient use of government resources.

3.2.3 Market conditions and outcomes for electricity retailers

Most jurisdictions have seen new retailers enter the electricity market over the last five years. Despite this, some impediments to entry and expansion remain. The significance of these impediments varies between jurisdictions, but there are some common issues.

As second tier retailers have entered the market they have begun winning customers from incumbent retailers. Incumbent retailers have also been actively competing amongst themselves. Retailers primarily attract customers by offering discounts and other non-price incentives. Product differentiation has been somewhat limited to date in most jurisdictions, partly because of technology limitations. This is beginning to change.

This section summarises some of the impediments that remain to retailers entering electricity retail markets. It then sets out the ways in which retailers compete to acquire and retain customers, before providing a discussion on retailer outcomes. Conditions in the gas market are discussed in the subsequent section, followed by observations on different approaches between jurisdictions that may impede retailer expansion.

Entry has occurred in most jurisdictions but some impediments remain

Competition has provided, to varying extents, more choice of electricity retailers and plans in Victoria, South Australia, New South Wales and South East Queensland. Only one retailer competes with the incumbent in the Australian Capital Territory market for residential customers. In regional Queensland entry has been impeded by the way in which a uniform tariff policy is given effect. In Tasmania retail competition has only recently opened up for residential and smaller business customers.

Three new electricity retailers have entered the NEM since 2012, all in Victoria. Existing retailers have expanded into some other jurisdictions. This suggests that while there may be some impediments to entry, these are not insurmountable in most electricity retail markets.

Between 10 and 16 retailers now compete to provide electricity to small customers in Victoria, South Australia, New South Wales and South East Queensland. While markets tend to be dominated by AGL, EnergyAustralia and Origin Energy, second tier retailers are gaining market share.

It is worth noting that an increase in the number of competitors would be expected following, or just prior to, deregulation as new businesses enter and experiment with different business models. Not all retailers will be successful and some will subsequently exit the market. Others may enter with the intention of building up a customer base then selling it to a competitor. Therefore the number of retailers can be expected to fluctuate for some time as markets continue to evolve and mature.

Retailers, particularly second tier retailers, consider that some impediments to entry and expansion remain to varying degrees across jurisdictions. These include:

- **Price regulation**. In jurisdictions that continue to regulate retail electricity prices, this is cited as the main barrier to entry and expansion. Despite this, over ten retailers have been competing in South East Queensland and New South Wales (prior to price regulation being removed). The manner in which price regulation is currently applied in the Australian Capital Territory is seen by some retailers as inhibiting entry.

- **Hedging products**. Retailers' ability to access competitively priced wholesale supply and hedging products was also identified as a key concern for some retailers, although views were mixed on how significant this issue is. Larger, vertically integrated retailers considered hedging markets to be sufficiently liquid to allow retailers to hedge their loads. Smaller retailers considered there have been some constraints on the availability of competitively priced hedging products in some jurisdictions.

  > “Whilst liquidity in the standard wholesale market and futures products remains reasonable, there are now very few entities left in the market with the motivation to market products, which allow a small retailer to reduce their cost to serve
  >
  > ...I have problems with the futures market because there is insufficient liquidity in some parts of the futures market, the product mix isn't right, information flows are poor and the minimum transaction level is too high.[50]”

- **Credit support arrangements**. Smaller retailers noted that the prudential arrangements and credit support required by parties such as the Australian Energy Market Operator, generators, financial intermediaries, the ASX and electricity networks can be a significant impediment to entry and expansion, because they “involve a significant capital outlay and tie up growth capital”.[51] Alinta also raised this as an issue in their submission,[52] while AGL submitted that credit support arrangements are not an issue.[53] We note that these costs are generally scalable, that is, they are relatively low for smaller retailers and increase as they grow. The Commission therefore considers that these

---

50 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p35.

51 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p37.

52 Alinta, submission to *2014 Retail Competition Review*, Approach Paper, p4.

53 AGL, submission to *2014 Retail Competition Review*, Approach Paper, p4.

requirements, which are necessary to safeguard the integrity of the NEM, do not constitute an insurmountable barrier to entry or expansion.

- **Policy and regulatory risk**. Retailers considered that a perception of high policy and/or regulatory risk can affect a retailer's confidence in that market and, in turn, its decision to enter or actively compete in that market. Perceived policy and/or regulatory risk was considered to vary across jurisdictions.

Most retailers that participated in interviews considered that there are no barriers to retailing electricity in regional and rural areas. This is consistent with most retailers offering electricity across each jurisdiction in which they compete. However, some retailers noted that there may be some impediments to retailing outside of major urban areas, including higher customer acquisition costs and brand loyalty.[54]

Retailers held conflicting views on the importance of economies of scale.[55] Views were not dependent on the size of the retailer. Some retailers considered economies of scale are associated with the costs of call centres and IT systems. Some also considered there is a minimum load a retailer requires to enter into appropriate hedging arrangements. Others considered many costs can be outsourced and generators can provide flexible hedging cover for small players.

Similarly, retailers held mixed views on the importance of economies of scope.[56] Some considered retailing electricity and gas provides an important source of efficiency in terms of acquisition costs and is particularly important in jurisdictions with high gas penetration. Others considered dual fuel offerings are simply a form of product differentiation which does not give rise to cost efficiencies.

Larger retailers with generation interests did not consider that vertical integration was required to compete in electricity retail markets, noting that retailers with no generation interests are currently competing. Smaller retailers (including small gentailers) claimed that it is becoming increasingly important to have generation interests due to increased concentration of ownership in the wholesale market. These retailers also noted generation interests were particularly important in jurisdictions that are affected by congestion on inter-regional transmission lines. A small and a large gentailer considered vertical integration is more important if a retailer wants to expand beyond a certain scale.

No retailers raised any impediments to exit.

---

54 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p39.

55 Economies of scale exist in electricity retailing where the average cost of serving a customer declines as the size of the customer base increases, since a larger customer base allows a retailer to spread its fixed costs across a greater number of customers.

56 Economies of scope may exist where a retailer that can spread its fixed costs over more than one product (eg, electricity and gas) has an advantage over retailers that only offer one product.

Product differentiation and innovation is occurring within limits

Product differentiation and innovation varies across jurisdictions. Retailers primarily compete on price and non-price inducements such as discounts and sign-up gifts. However, as discussed further in section 3.3.1, innovation is increasing as technology advancements enable new products and services to be developed. Retailers also consider the removal of price regulation has allowed alternative tariff structures to develop in Victoria.

Electricity is currently sold to residential and business customers on a single fuel, dual fuel and multi-utility (such as gas, electricity and internet) basis. Terms and conditions can vary substantially across retailers, as can the price and non-price inducements that retailers use to attract and/or retain customers.

Retailers have noted that prices specified in a "standing offer contract"[57] will typically be based on either:

- the regulated retail price in those jurisdictions that are still subject to price regulation; or
- the retailer's own estimate of the cost of supply (subject to any effective cap from a voluntary pricing agreement) in those jurisdictions that no longer regulate price.

In relation to "market offers"[58], retailers tend to adopt a benchmark rate for usage and supply charges and then apply a discount to that rate. The benchmarks are typically based on the standing offer contract price. In some instances individual retailers have adopted a higher benchmark price than the regulated price for their market offers, which they then discount from.

With a few exceptions, smaller retailers tend to offer only a single “best offer” product, whereas larger retailers (including larger second tier retailers) offer a number of different plans with varying contract lengths, fixed benefits periods and gradations of price and non-price inducements. Some smaller retailers consider the proliferation of offers from larger retailers contributes to consumer confusions, while large retailers state they offer more tailored plans to meet diverse needs.

Retailers use a number of measures to differentiate their products and brands, such as: offering one simple product; offering a range of ‘tailored’ products; customer service; information provision; and affiliation with airline or shopping loyalty schemes. Some retailers also offer feed-in tariffs for customers with solar panels in addition to the

57 Standing offer contracts are basic electricity and gas contracts with terms and conditions that are prescribed by law.

58 Market offers, or market retail contracts are electricity and gas contracts that include minimum terms and conditions prescribed by law. The terms and conditions of market retail contracts generally vary from standing offer contracts. Prices under market retail contracts are set by energy retailers. (www.energymadeeasy.gov.au)

government or regulator specified rate[59] and flexible pricing (time of use tariffs) to customers with interval or smart meters.

Retention strategies appear to be becoming increasingly important and a source of rivalry and competitive tension, particularly for larger retailers. Strategies include:[60]

- customer service-related activities such as online self-service and first call resolution designed to minimise the interaction customers need to have with their retailer;
- cross-selling, value adding and reward schemes, designed to make customers more "sticky";
- measures designed to minimise bill shock such as bill smoothing;
- offering customers that are nearing the end of their fixed benefit period or fixed term contract a new competitive product; and
- contacting customers that have indicated they intend to switch and offering them a higher discount to stay ("save calls").

One retailer noted that smaller retailers offering no lock-in contracts are less likely to have recourse to such retention strategies. This is because they "need to have a high level of customer satisfaction, service and to offer the best prices at all times"[61] since their customers have already demonstrated a willingness to switch.

Retailers generally consider that retention strategies have been effective and that a greater degree of competition is now occurring around retention. However, discretionary strategies, such as save calls and targeted reward campaigns, tend to be biased towards more "valuable" customers with a good credit history and high consumption.

Retailers consider the roll-out of smart meters in other jurisdictions and changes in technology will pave the way for further innovation, although they cautioned that unnecessary regulation could prevent customers from benefiting.[62] One retailer suggested that non-price forms of rivalry, like customer service and bundling, are likely to become more important in the future.[63]

59 Appendix C provides further detail on solar arrangements in each NEM jurisdiction.

60 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, report for the AEMC, June 2014, p62.

61 Ibid, p61.

62 Ibid, p56.

63 Ibid, p64.

Retailer outcomes

The AEMC's 2013 Residential Electricity Price Trends review found that the average gross retailer margin for Victoria was higher than in other states. This analysis was based on February and September 2013 best market offers provided by retailers. The gross margin was between 34 per cent and 37 per cent of total wholesale costs for Victorian retailers, while for other jurisdictions the gross margin was between 11 per cent and 18 per cent.[64] We note this analysis was conducted at two points across a short period of time and may not represent a trend. It also does not take account of retailers' operating costs.

Box 3.4: Defining "margins"

Retailer outcomes are generally measured in terms of 'gross' and 'net' retailer margins.

Gross retailer margin is defined as the difference between an energy retailers' revenue and total wholesale costs of supply. It is commonly calculated by subtracting estimates of wholesale energy costs, environmental policy costs and network costs from a nominated tariff. This could be a standing offer, average market offer or lowest available offer at a point in time. Gross margin does not account for retailers' costs of running the business (operational costs). Net retailer margin is similar to gross retailer margin, but retailers' operational costs are also subtracted from the nominated tariff.

Both gross and net retailer margin are presented as a percentage of a retailer's costs. For instance, a ten per cent gross margin implies that a retailer is earning revenue that is ten per cent greater than its total wholesale costs of supply.

Estimates of gross and net margins are sensitive to a number of assumptions, including the time period of analysis, the retail tariffs used to calculate the margins, the annual consumption of an 'average' customer, how wholesale costs are estimated and the operational costs assumed for retailers. Changes in these assumptions can have material effects on the results and therefore care needs to be taken when interpreting the numbers and forming conclusions.

Retailers that participated in interviews observed that electricity retail margins can differ in the following ways:[65]

- across retailers, depending on their operating and hedging costs;
- across jurisdictions, depending on:
  - whether prices are regulated and, if so, how;

64 AEMC, *2013 Residential Electricity Price Trends*, 13 December 2013, Sydney, p94.

65 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, report for the AEMC, June 2014, pp81-82.

- whether there are any other voluntary pricing arrangements in place that may influence prices;
- the risks associated with operating in a jurisdiction, which can differ depending on conditions in the wholesale market, the nature of demand and the extent to which risks can be hedged; and
- the level of competition;

- within a jurisdiction and across customers, depending on:
  - the distribution network in which customers are located;
  - the type of customer being supplied; and
  - the volume of electricity consumed by a customer and their load profile; and
- depending on the time of year in which profit margins are measured.

Over time, as firms enter and exit, the market will evolve and mature, and retailer margins can be expected to vary with the business cycle. Periods of temporarily elevated margins stimulate new entry and give customers incentives to seek out lower-price suppliers and/or to reduce consumption; periods of depressed margins put pressure on suppliers to exit the market and/or to seek cost efficiencies. An analysis of retailer margins therefore needs to be carried out over a sufficiently long period to understand the profitability of the industry through multiple business cycles and changes in market conditions.

When examining the competitiveness of a market, one of the most important indicators is whether firms are entering and competing and/or whether there is a legitimate threat of new entry. If this is the case, then competitive pressure can be expected to lead to efficient outcomes for customers. Intervening in a competitive market based on short term, inconclusive evidence can reduce the effectiveness of competition and may result in higher prices for customers.

3.2.4 Market conditions and outcomes for gas retailers

Competition in natural gas retail markets has been more tempered than in electricity. While new retailers have entered some markets, impediments appear higher than for new electricity retailers, particularly in areas with small customer bases. Similarly, rivalry has been more limited than in electricity. New retailers have won market share, but product differentiation is fairly low. This section elaborates on some of the impediments that gas retailers face and how they compete to win and retain customers.

Market characteristics limit entry into some gas retail markets

There are fewer retailers and offers in the gas retail market than in electricity. Between one and eight retailers now compete to provide gas to small customers across NEM jurisdictions. Gas markets tend to be dominated by the incumbent retailer. Despite this, retailers are competing in some areas to attract and retain customers.

Retailing gas constitutes a very different proposition than retailing electricity because the upstream supply and transportation arrangements are fundamentally different. Combined with a typically smaller customer base, we would therefore expect fewer retailers to enter the market than in electricity.

Structural and market design features in gas markets have also led to significant differences in market outcomes between and within jurisdictions.

The main issues that retailers face in retail gas markets that may impede entry are:

- **The complex and bilateral nature of gas supply arrangements**. This is one of the more significant factors that smaller retailers considered could deter entry. This is because retailers must enter into bilateral contracts for wholesale supply, transportation, pipeline storage, underground storage, liquefied natural gas (LNG) storage and other risk management products. In addition, retailers must contend with different market arrangements between jurisdictions, as discussed further below.

- **The small size of some markets**. Tasmania, Queensland and the Australian Capital Territory and regional and rural areas in some other jurisdictions have small customer bases. This can be because of small populations and/or limited gas penetration. The size of a market will not, in and of itself, usually constitute a barrier to entry. However, if the costs of supplying that market are largely fixed or sunk (ie there are economies of scale associated with supply), then the size of the market may place a cap on the number of retailers that can enter and effectively compete in the market.

- **Access to some transmission and distribution pipelines**. The cost of expanding the capacity of a pipeline can be significant and so entry can be deterred where pipelines are fully, or close to fully, contracted.[66]

- **Access to and/or the price paid for, the wholesale gas supply**. The development of LNG facilities in Queensland is starting to affect entry and expansion decisions by retailers. The price paid for gas is now substantially higher than it has been historically, particularly in Queensland. There is also considerable uncertainty

66 Retailers noted that the SEA Gas Pipeline, which enables gas to be supplied from Victoria to South Australia, and the Eastern Gas Pipeline, which enables gas to be supplied from Victoria to New South Wales, are currently in this position. A number of regional pipelines in South Australia, New South Wales, Queensland and Victoria (outside the Declared Wholesale Gas Market) also have capacity issues.

over how conditions in the wholesale market will develop. This uncertainty may deter entry and expansion.

Differences in the design of balancing markets and transportation carriage models across jurisdictions have influenced the ease with which gas retailers can expand across multiple jurisdictions. Retailers noted that the Victorian Declared Wholesale Gas Market (DWGM) is more conductive to entry by small retailers than other markets. This is because, unlike the short term trading markets (STTM) in Brisbane, Adelaide and Sydney, retailers do not need to enter into gas transportation agreements and they can purchase gas from a more liquid market while building up their customer base.

On the other hand, larger retailers did not consider market design issues as having a strong influence on whether a retailer decides to participate in a market.

Low gas penetration, pipeline capacity and a small customer base have limited the ability of retailers to enter and compete in regional and rural areas. Of the seven retailers that responded to the retailer survey, five stated that it can be more difficult to enter and expand in rural and regional areas of New South Wales, Queensland, South Australia, and outside the DWGM in Victoria.[67] In addition to market characteristics, brand loyalty and higher customer acquisition costs were cited as factors that may deter entry in these areas.

Economies of scale were generally seen as more important in gas than electricity because the price structures specified in gas supply and transportation contracts are predominantly fixed. Further, economies of scale tend to be regional or jurisdictional-specific given the fixed costs associated with transporting gas to particular locations.[68]

Retailers held mixed views on the importance of economies of scope. With the exception of Tas Gas, there are no pure gas retailers operating in NEM jurisdictions, suggesting that economies of scope are more important in gas than electricity retailing.

Retailer views on the significance of exit costs in deterring entry were also mixed. Some claimed that exit costs are an important consideration because of take or pay commitments in gas supply contracts and capacity based charges in transportation contracts. Others noted that while supply and transportation contracts can be an impediment, retailers could on-sell gas or transportation contracts or novate their contracts to another player in the market.

Product differentiation and innovation is more limited in gas than electricity

Similar to electricity, gas retailers primarily compete based on prices and discounting to attract customers. They use a similar variety of factors to differentiate themselves,

67 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p46.

68 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p47.

including contract terms and conditions, discounts, rebates and other non-price inducements.

Only one of the eight gas retailers interviewed currently markets gas as a separate product. The others market gas as part of either a dual fuel or multi-utility offering.[69]

Innovation has been more limited than in electricity. Retailers attribute this to:[70]

- gas customers being less engaged than electricity customers; and
- a lack of scope to differentiate products due to the widespread use of accumulation meters that limit innovation.

Most retailers did not expect innovation to occur in retail gas products. However, one gas retailer indicated it was looking into installing smart gas meters.

3.2.5 Different approaches between jurisdictions can impede expansion

Jurisdictions are moving towards a common approach to retail market frameworks. Despite a number of reforms to achieve this, some differences remain. These differences can impede expansion by retailers across multiple jurisdictions by presenting additional hurdles that must be addressed. This makes it more costly for retailers to comply with multiple requirements, in terms of compliance costs and system changes, which are ultimately passed through to customers. Examples of areas where jurisdictional differences remain include:

- **Continued price regulation in some jurisdictions**. The Australian Energy Market Agreement (AEMA) sets out a common agreement to remove retail price regulation where effective competition can be demonstrated. South Australia and New South Wales have joined Victoria in removing electricity retail price regulation, although New South Wales has retained gas retail price regulation. The Queensland Government intends to remove retail price regulation on 1 July 2015, subject to a number of criteria being met. The Australian Capital Territory and Tasmania have not signalled an intention to remove retail price regulation in the near future.

- **Differences in customer protection frameworks**. The NECF reforms are intended to drive national consistency in the rights and responsibilities of retailers and customers across the NEM. In the last two years, four jurisdictions have implemented the NECF and the Queensland Government has signalled its intention to do so. Some jurisdictions are yet to adopt the legislation and, where it has been adopted, it was done so subject to jurisdictional derogations.[71] This

69 Note that although these retailers may not *market* gas separately, this is not to say that they will not *sell* gas separately.

70 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p57.

71 See www.aemc.gov.au for a comparison of the NECF and jurisdictional derogations.

can undermine the intent of a harmonised scheme and the benefits of harmonisation may not be fully captured.

- **Multiple, jurisdictional-specific environmental schemes**. At a federal level, retailers are currently required to comply with the carbon pricing mechanism (noting this may be removed) and the renewable energy target (noting this is currently under review). At the jurisdictional level, multiple solar feed-in tariff and energy efficiency schemes have been introduced. Feed-in tariff schemes vary between jurisdictions depending on the level of the tariff and whether it is a gross tariff or net tariff.[72] Energy efficiency schemes have been introduced by the Australian Capital Territory, New South Wales, South Australian and Victorian governments, although the Victorian government has recently announced its scheme will close at the end of 2015[73].

- **Differences in customer concession schemes**. Each jurisdiction administers its own concession schemes. Under the AEMA jurisdictions agreed that community service obligations and a number of other functions would remain the responsibility of individual jurisdictions.[74] Appendix B sets out a summary of concession schemes.

The Commission supports continued moves towards national consistency where this achieves reduced compliance and system costs for retailers and where these savings are reflected in lower costs to customers.

3.3 Future - developments affecting retail competition

3.3.1 Technology changes are challenging the traditional energy retail model

Energy has traditionally been a low involvement product for end-use customers. Enabling technology and regulatory reforms are creating new opportunities for customers and retailers alike and will change the way in which energy has traditionally been supplied and consumed. Retail energy services now extend beyond simply the essential service of sale and supply of electricity: they are evolving to include the supply of information, energy and network management services.

Customers are set to benefit, but may need additional support

Advances in technology have the potential to expand the range of products and services available to customers. Enabling technology such as smart meters and smart appliances can provide opportunities for customers to better understand and manage their electricity use and their bills.

72 A gross tariff provides a payment for every kWh of energy produced by a rooftop solar generation system, while a net feed in tariff provides a payment only for energy exported to the grid.

73 See www.energyandresources.vic.gov.au .

74 Australian Energy Market Agreement, cl.14.7.

Retailers are already taking advantage of technology to develop innovative new services and products. For example, the following has been observed in Victoria where smart meters are more prevalent:

- Retailers and networks have developed web portals that allow customers to monitor their usage.
- Powershop, a new entrant into the Victorian retail market, allows customers to purchase electricity in blocks of varying sizes and costs to be used straight away or in the future. Their rates change monthly to reflect changes in wholesale costs.
- Origin is offering customers the ability to install an electric vehicle charging unit in their garage through an alliance with ChargePoint. They also have a specific tariff for electric vehicle charging.
- AGL has announced it is investigating offering on-bill financing to assist customers with the purchase of appliances such as air conditioning, heating and hot water.

Combined with changes to the way in which distribution services are priced, these developments will also provide customers with the incentives to consider and take up new products and other energy management services such as direct load control, distributed generation such as solar panels, and energy efficiency.

Changes in customer participation and advances in technology are increasing the scope for competition in energy retailing by providing greater opportunities for rivalry through product differentiation. Niche players are entering the market, creating a new source of competition for traditional retailers. These companies are able to target specific customers groups, such as those with solar panels or high energy use appliances, such as pool pumps or air conditioning.

Third parties are able to bundle products and services to offer a range of value add energy services to customers. For example, third party energy services companies are offering contracts to customers whereby solar panels are installed at a premise at no upfront cost and the customer agrees to purchase energy generated from those panels for fixed period of time.[75] Similarly, Ergon Energy and Energex introduced an incentive based program to actively encourage customers to manage air conditioning and pool pump loads.

75 Some retailers raised concerns about solar panel leasing companies that enter into power purchase agreements with small customers being granted an exemption from authorisation under the National Energy Retail Law by the Australian Energy Regulator. This exemption means that such companies are not subject to the same consumer protection provisions, risks and other regulatory requirements as other retailers are. Some retailers consider this exemption will expose small customers to a greater level of risk and create an uneven playing field. See K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, pp91-92. The AEMC recommended the NECF is amended to include a framework which governs third parties providing energy services to residential and small business customers as part of its Power of Choice review.

Better consumption information can also help customers use price comparison sites more effectively to access competing offers from different electricity retailers. In turn, as customers change plans or retailers, this should provide the right signals to retailers to develop the products and services that customers want.

These developments have the potential to increase competition, product innovation and lower bills. For customers to benefit it is critical that they are able to compare increasingly complex options and make choices that best meet their needs. They must be aware of and have access to effective tools and information to support their decisions, with the right protections and access to assistance if required.

The AEMC's Power of Choice review sets out recommendations for supporting market conditions that facilitate efficient demand side participation.[76] Many of these recommendations are already being progressed. These recommendations, combined with those from the AEMC's consumer engagement blueprint, could provide effective support to all customers.

As markets evolve, we should see increased differentiation as retailers develop different products and services to suit a range of customer preferences. This includes customers who want to be active in managing their energy use and maximise their savings, as well as customers that want less involvement and would rather "set and forget". We are starting to see evidence of this differentiation and can expect more as the market further evolves.

3.3.2 Other changes affecting electricity retail competition

Retailers interviewed for this review cited a number of other factors that may impact competition in retail electricity markets going forward. These include:

- **Retail price regulation**. Retailers were broadly optimistic that the Queensland Government will remove retail price regulation in South East Queensland and that competition would increase as a result. There is no expectation amongst retailers that price regulation will be removed in the Australian Capital Territory or Tasmania in the foreseeable future. Consequently the state of competition is not expected to change significantly in these jurisdictions.

- **Wholesale market conditions**. A number of non-vertically integrated retailers noted that if further consolidation occurs in wholesale electricity markets it could affect their ability to access cost reflective hedging products and, in turn, their ability to compete.

- **Industry consolidation**. A large number of retailers noted the potential for some consolidation to occur over the next five years. One large retailer suggested that the next transaction of this nature was more likely to involve larger second tier retailers and that, if this occurred, it could result in the creation of a fourth big player in the market.

76 For further information see www.aemc.gov.au.

- **Additional competition from new entry**. While some consolidation is expected, retailers also consider there is potential for new entry, including new types of players, in both gas and electricity. For example, Macquarie Bank was granted an electricity retailer authorisation on 11 April 2014, although it intends to only supply large customers at this stage.[77]

There is also a possibility that switching rates may decrease as a result of:

- moderating electricity prices, which to date have been a key driver encouraging customers to shop around;
- retailers moving away from door knocking and cold calling;
- greater use of retention strategies to avoid losing customers; and
- maturing markets.

3.3.3 Changes in the natural gas market may be driven by LNG developments

Entry and expansion in gas retail markets is expected to become more difficult given conditions in the upstream market.

The LNG developments and tightening conditions in the wholesale gas market are expected to:[78]

- result in a significant increase in wholesale gas prices;
- adversely affect the ability of some retailers to access competitively priced gas;
- limit the supply options available to retailers in New South Wales and South Australia; and
- give rise to some additional pricing risks for retailers if the prices specified in their gas supply contracts are linked to an international oil price benchmark.

These factors, and more generally the uncertainty as to the way in which the LNG developments will impact gas retail markets, may reduce retailers' appetites to enter and expand in the next few years, particularly outside of the Victorian DWGM for reasons discussed in section 3.2.4. As, one retailer observed:[79]

> "We expect LNG to disrupt and distort the market for a while and it is possible the retail market may stagnate, with potential new entrants deciding just to wait and see what happens until things settle down."

77 Macquarie Bank Limited, *Energy Retail Authorisation Application*, February 2014, p5.

78 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p92.

79 Ibid, p93.

Tighter demand and supply conditions are starting to lead to gas prices rises for small customers.[80] As has occurred in electricity, rising gas prices could drive increased customer engagement in the retail gas market. Customers may be more disposed to seek ways to reduce their gas bill, through reducing their demand as well as shopping around for better deals.

80 The New South Wales Independent Pricing and Regulatory Tribunal has recently approved price increases by AGL, ActewAGL and Origin Energy. The main reason for these increases relate to wholesale gas prices now being influenced by international prices following the development of facilities in Queensland to export LNG. IPART, *Changes in regulated retail gas prices from 1 July 2014*, Gas - Final Report, June 2014, p5.

4 South East Queensland

Box 4.1: Key findings

- Competition is effective in the South East Queensland electricity market and is delivering customers a choice of retailers and plans. While competition has been less intense in recent years, rivalry can be expected to increase once price regulation is removed.
  - Customers are increasingly taking advantage of the choices available to them. In 2013, seven in ten electricity customers were on market offers, three in ten energy customers shopped around for a better deal and close to two in ten changed retailer. Others found a better deal with their existing retailer.
  - Ten retailers are currently competing to acquire and retain electricity customers by offering discounts and other incentives. Four electricity retailers are intending to expand in the next five years and at least two retailers have indicated they may enter the market if price regulation is removed.
  - The majority of customers surveyed are generally satisfied with the quality of service they receive. However, customers are seeking more transparent and meaningful information that helps them to understand their options and easily compare offers.
- A targeted engagement strategy could help to improve customer awareness and understanding of the options available and provide the information and tools to help customers find a retailer and plan that suits their needs.
- For the gas market, competition remains limited with two retailers operating in the market.
  - Fewer retailers have entered this market primarily due to the small size of the market, with low penetration of gas pipelines to households and small businesses and a low level of average gas demand for heating or cooking.
  - Competition is not expected to increase over the next few years due to size of the market and difficulties for retailers to secure competitively priced gas in the wholesale market.

4.1 Overview

This is the first time the AEMC has reviewed competition in Queensland's retail energy markets. This chapter focusses on the state of competition in South East Queensland and Chapter 5 discusses competition in regional Queensland.[81]

The Commission's assessment of competition against the five criteria set out in Chapter 2 has found that competition is effective in the electricity market, but less effective in the gas market with only two retailers competing. This difference primarily relates to structural differences between the electricity and gas market, with the electricity market being one of the largest in the national electricity market (NEM) and the gas market one of the smallest.[82]

The findings for the South East Queensland electricity market can be summarised as follows:

- **Customer activity:** Most customers have chosen market offers and many are actively investigating their options and switching plans or retailers. While there was high awareness that customers could choose their retailer, there is lower awareness of the number of retailers and plans to choose from and limited understanding of the options available. Customers could therefore benefit from a targeted customer engagement strategy.

- **Barriers to entry, exit and expansion:** Retailers consider retail price regulation is the key issue deterring entry and expansion in the electricity market and expect market conditions to improve considerably following the planned removal of electricity retail price regulation. The key issues that may limit entry into the gas market are the small size of the retail gas market and conditions in the wholesale market.

- **Independent rivalry:** There is evidence of rivalry between the ten electricity retailers active in the market with retailers differentiating their offers and second tier retailers attracting customers away from the incumbents. Further retailer activity and product differentiation in the electricity market may occur in time with the planned removal of price regulation. Rivalry appears weaker in the gas retail market with just two retailers currently competing for customers.

- **Customer satisfaction:** The majority of customers are satisfied with their electricity retailers, though there appears to be a general mistrust of energy retailers, particularly smaller retailers. Some customers would like greater choice in the market which may occur if rivalry between retailers increases following the planned removal of electricity retail price regulation.

---

81 Discussion of the South East Queensland gas market in this chapter also applies to Toowoomba and Oakey, which are in the regional Queensland electricity market but can be considered part of the South East Queensland gas market as they are served by the same pipelines.

82 The Queensland electricity market has approximately 1.3 million customers. The gas market has approximately 175,000 customers and total residential demand for the state equates to 3 per cent of that in Victoria. Most of these gas and electricity customers are located in South East Queensland.

- **Retailer outcomes:** The profitability of electricity retailing has reportedly varied over the last few years, largely driven by the impacts of the price freeze and the methodology used to determine the regulated price.

Based on the findings of this review, the Commission considers there is sufficient competition in the South East Queensland electricity market for customers to benefit from removal of retail price regulation. This can be expected to promote further competition in the market to deliver innovation, greater choice and competitive prices in South East Queensland.

The Commission does not expect a material improvement in the level of competition in the gas market due to the small size of the market and the tightening demand and supply conditions in the wholesale gas market.

4.2 History and market characteristics

Full retail competition was introduced in retail electricity and gas markets in Queensland in July 2007. At this time, retail price regulation was removed for gas but retailers are required to offer standard contracts with regulated terms and conditions. Regulated retail prices were retained for electricity.

In May 2014, the Queensland Government introduced legislation into parliament to replace electricity retail price regulation with market monitoring in South East Queensland.[83]

The Commission understands that the Queensland Government intends to remove electricity retail price regulation and commence market monitoring on 1 July 2015, subject to the certain preconditions being met, including:

- ensuring there is sufficient competition in South East Queensland;
- implementing appropriate customer support mechanisms, which we understand includes adopting the National Energy Customer Framework (NECF);
- improving customer engagement in the market;
- establishing an effective regulatory framework; and
- ensuring a viable methodology to determine regulated retail electricity prices in regional Queensland.[84]

The AEMC has conducted detailed analysis for South East Queensland as an input to the Queensland Government's decision on the first precondition above.

83 Hon. MF McArdle (Minister for Energy and Water Supply) speech transcript 20 May 2014, http://www.parliament.qld.gov.au/documents/tableOffice/BillMaterial/140520/Electricity.pdf

84 As these are currently based on regulated prices in South East Queensland.

4.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

Our analysis of this criterion considers the findings of a customer survey and qualitative forums performed by Newgate Research and data provided to the AEMC on customer switching.[85] This analysis suggests the following:

- **Most customers have chosen market offers**. Approximately 70 per cent of electricity customers and 75 per cent of gas customers are on market offers.[86]
- **The majority of customers are aware that they can choose their plan and retailer**, though more can be done to increase awareness and understanding of the range of choices.
- **Many customers are investigating their options and choosing between different market offers**. Switching rates for electricity and gas have been declining in recent years but remain at reasonably high levels relative to other jurisdictions and industries. Price is the main trigger driving customers to consider different market offers. However, some customers are not interested in looking for a better deal, primarily because they are satisfied with their existing deal.

The Commission considers that customer activity in the market could further increase after price regulation is removed if retailers step up their marketing activities, as expected. A government-led customer engagement strategy could also improve customer confidence and awareness of the benefits of regularly shopping around.

4.3.1 Customer awareness and understanding

For customers to actively participate in the market, they first need to be aware of their choices. There was a high level of awareness among South East Queensland survey respondents that they have a choice between multiple retailers and plans in the market.

Close to 90 per cent of small customers surveyed were aware that they could choose their electricity and gas retailers, but most were unaware of how much choice they had. Residential customers surveyed considerably underestimated the number of electricity retailers and overestimated the number of gas retailers in the market. Many could not name more than two or three retailers during the forums, with Origin Energy and AGL the most commonly cited.

---

85 See Chapter 2 for further discussion on our methodology.

86 Electricity data for South East Queensland from the AER. Gas data provided to the AEMC by gas retailers for the whole of Queensland. Most of these gas customers are in South East Queensland.

Three quarters of the residential customers surveyed were aware that they could choose from a range of different energy plans and slightly more reported being confident that they understood the different offers and options available. Qualitative research found that actual knowledge of the different features of energy plans and bill components is somewhat limited.

The Queensland Council of Social Services (QCOSS) submitted to this review that a low level of knowledge is not limited to low income and vulnerable customers, but extends to many residential customers.[87] The findings of Newgate Research's qualitative forums appear to support this view, where knowledge levels were similar among most forum participants regardless of their income.

> “There’s a lot more choices than I realised there was. (Brisbane, Small Business)”

> “I’m surprised at how little I know. I can’t believe how many providers there are. (Maroochydore, higher income)”

> “Never heard of those discount plans! Where are they hiding all this information? (Brisbane, higher income)”

In forum discussions, less than half were aware that each retailer offered a range of different types of plans, price structures, discounts, contract lengths and contract terms. A key message was that energy offers were hard to compare because they were all presented differently and in ways that were hard to understand.

In comparison with the forum participants in other jurisdictions, there was a strong sense in South East Queensland that you would pay almost the same price with all retailers. There were also higher levels of mistrust of retailers in these forums than in other jurisdictions. The interaction between these customer perceptions and switching behaviour is further discussed below.

4.3.2 Customers investigating options and switching

For a market to be effectively competitive, it is not sufficient for customers simply to be aware of their ability to choose their retailer. They also need to have the right information and tools to investigate their options and switch plan or retailer where they may receive a lower price or better service.

Evidence suggests that a considerable proportion of the South East Queensland market are investigating their options and switching plans or retailers.

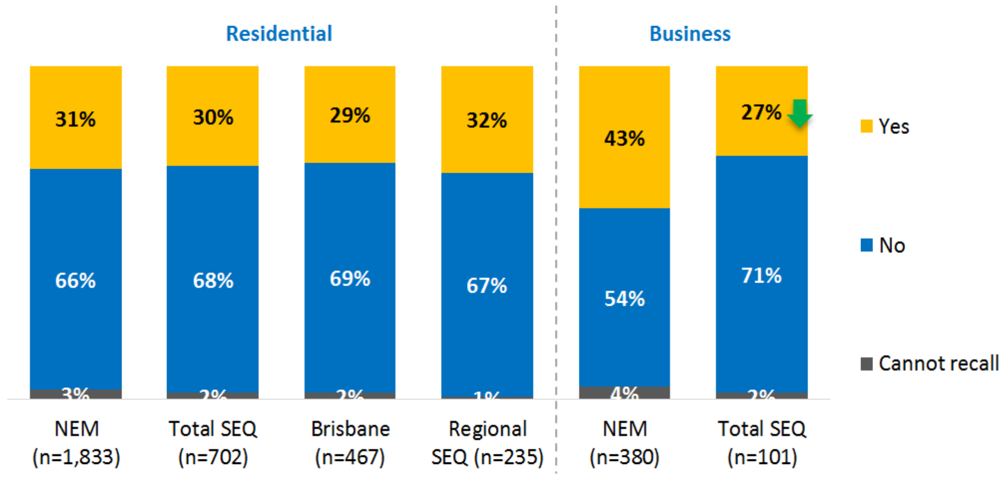
Figure 4.1 shows the proportion of customers that actively investigated options over the last 12 months. The arrow indicates a result that is statistically different from the NEM average at the 95 per cent confidence level. Thirty per cent of residential customers surveyed in South East Queensland investigated energy options in the past

87 Queensland Council of Social Services (QCOSS), submission to the 2014 Retail Competition Review, Approach Paper, 28 February 2014, p 6.

12 months, which is consistent with the NEM average. Approximately 83 per cent of those who investigated decided to switch their plan.

Considerably fewer small businesses in South East Queensland investigated their options relative to the NEM average.

Figure 4.1 Customers who actively investigated offers or options in past 12 months



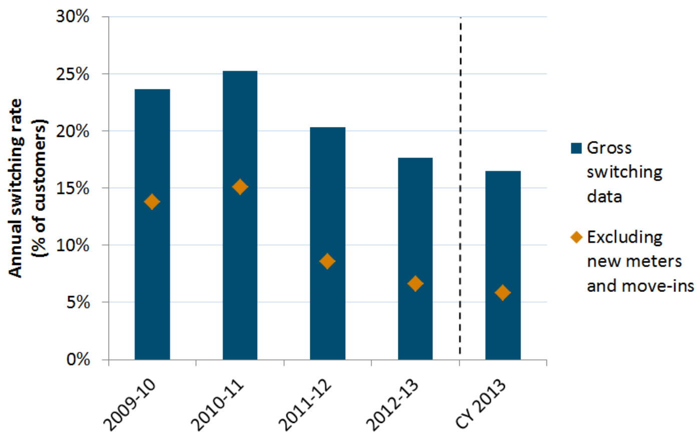
Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p164. Survey question: In the past 12 months, have you actively investigated different offers or options that you could potentially switch to? Customers surveyed: All.

Over half of the residential customers surveyed reported they had switched electricity retailer or plan in the last five years, with an average of around two switches during that time. This is higher than the reported switching rates for service providers of car insurance, phone, internet, banking, home insurance or health insurance. Small business switching rates were close to the NEM average of 56 per cent, with 50 per cent of small businesses in South East Queensland changing electricity plan or retailer in the last five years.

Fewer customers switched their retailer or plan for gas than for electricity. Approximately 33 per cent of customers in South East Queensland gas customers reported they had switched their gas retailer or plan in the last five years, which is less than the NEM average of 49 per cent.

Figure 4.2 shows customer switching rates using data on customer transfers between retailers each year. This type of data should be interpreted with caution, as discussed in Chapter 2, but can provide an indication of the level of customer activity in a market. Consistent with the survey results, this data illustrates relatively high customer switching between retailers. Although switching reached its lowest levels of the last four years in 2013 at 17 per cent, this switching rate is relatively high and is comparable to rates in New South Wales and South Australia.

Figure 4.2 History of electricity customer switching rates

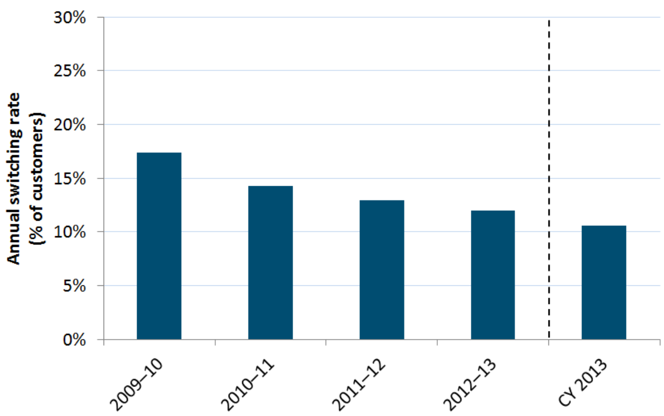


Source: AEMO data, AEMC analysis.

The decline in electricity switching from 2011-12 appears to coincide with lower retailer marketing activity in this region. Retailers have suggested that a series of unfavourable regulated pricing determinations, as well as a price freeze in 2012-13, have reduced their incentive to actively market in South East Queensland. This is discussed further in section 4.3.1. The reduced marketing activity was evident in Newgate Research's customer survey where fewer people in South East Queensland reported being directly approached by a retailer than in all other jurisdictions except the Australian Capital Territory.

For gas, Figure 4.3 shows that actual gross switching rates are slightly below electricity with an average of 11 per cent in 2013 for Queensland customers, most of which are in South East Queensland. This state-wide switching rate may understate the level of switching in the South East Queensland gas market due to the close link between electricity and gas switching rates and the higher rate of electricity switching in South East Queensland relative to the rest of Queensland.

Figure 4.3 History of gas customer switching rate – whole of Queensland



Source: AER, *State of the Energy Market 2013*, 2013 and AER Retail Statistics[88].

88 http://www.aer.gov.au/Industry-information/industry-statistics/retail

Similar to electricity switching, the gas switching rate has been declining over the last three years. Findings from retailer interviews and customer research suggest that gas is a secondary consideration for most customers and that gas switching decisions appear to be linked to electricity switching decisions, with many choosing to bundle their gas and electricity with the same retailer.

Switching data for electricity and gas does not capture customers who have actively investigated their options and either chosen to remain on their existing plan or have chosen to switch plans with their existing retailer. Data provided by retailers suggests that up to 20 per cent of customers changed their electricity plan and 16 per cent of customers changed their gas plan with their existing retailer in 2013.[89]

Price appears to be the key driver for switching behaviour

Customer surveys suggest the key reason for switching energy retailer or plan in all NEM jurisdictions was to obtain a better price. Of the South East Queensland customers who switched electricity retailer or plan, 61 per cent of residents and 77 per cent of businesses stated that price was the main reason they switched. Similarly for gas, just over 50 per cent of South East Queensland residents who switched gas retailer or plan did so for price reasons.

This is consistent with survey results that also showed that switching was higher among residential customers with electricity bills of $700 or more a quarter than those with lower bills. Forum discussions revealed that concern about rising prices either made customers more receptive to approaches from energy retailers or more motivated to investigate options independently.

> "I've been trying to remember why I changed. Bills kept going up. People were coming round all the time. Bills went down but then I was getting late fees that weren't right and when I rang up they didn't help. A young fellow came round and mentioned discounts that I was entitled to and said I'd get a better deal. (Maroochydore, lower income)"

> "I heard of others getting good deals so was curious to find out what might be available for us. (Maroochydore, looked but didn't switch)"

> "I listen out all the time to what friends tell me and to anyone who knocks on my door. If I hear of a better offer I'll change again. (Maroochydore, switched)"

A distant second to price, 11 per cent of respondents cited moving house as being their main reason for changing electricity retailer or plan and seventeen per cent for gas. The third most common reason to switch was poor customer service for electricity customers, with seven per cent of residents and six per cent of small businesses citing this as the main reason for switching electricity plans. This was also the main reason for ten per cent of gas switchers.

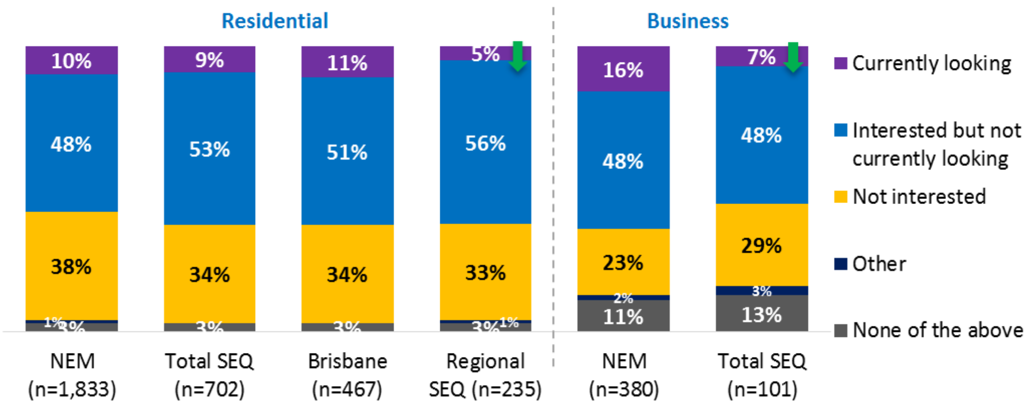
89 Some retailers cautioned that these estimates are indicative only.

Some customers are less engaged

Most customers surveyed expressed an interest in energy issues, energy prices and investigating their energy options. While many are interested in shopping around, there is a considerable proportion of customers who are less engaged.

As shown in Figure 4.4, fewer small business customers and residential customers outside of Brisbane were currently looking for a better deal compared to the NEM average. Close to one third of residential customers surveyed in South East Queensland said they had no interest in looking for a better deal.

Figure 4.4 Interest in looking for a better deal



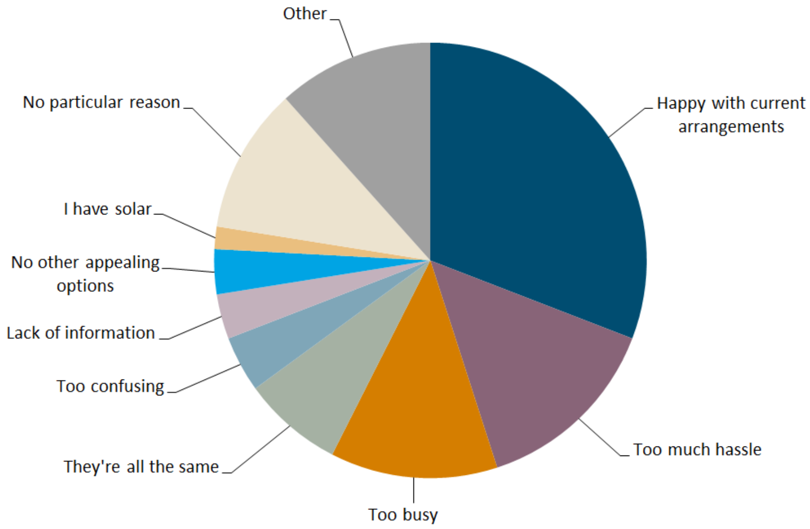
Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p183. Survey question: When it comes to your household's energy company, which of the following statements is most applicable to your household? Customers surveyed: All.

For many, this disinterest in shopping around may reflect satisfaction with their existing arrangements, which was the most common reason cited by customers for not investigating options or changing retailer or plan. For others, it could reflect perceptions about the lack of appealing alternatives in the market or general disengagement. For example, 17 per cent cited "too much hassle, couldn't be bothered, too lazy" as their key reason and 15 per cent stated it was because they were "too busy, don't have time".

It is possible some will not want to investigate deals or switch in the next twelve months if they have already recently done so. Close to a third of residential customers surveyed had already investigated options in the last twelve months. Similarly, close to a third of residential customers were not interested in going through this process in the next twelve months.

Figure 4.5 shows the most common reasons cited by customers in South East Queensland who had not investigated options in the last 12 months or had not switched retailer or plan in the last five years.

Figure 4.5 Most common reasons for not investigating or switching



Source: Data from Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p171. Survey question: Are there any reasons why you haven't investigated different options or why you haven't changed your energy company or plan in the last few years? Customer could select multiple responses. Customers surveyed: Residential customers who hadn't investigated options or changed their energy company.

The overarching barrier to customer participation identified in forums was a sense that it was not worth the time to investigate and switch as the savings on electricity bills would be minimal. This view is somewhat supported by advice from retailers about lower discounting in South East Queensland than other jurisdictions. AEMC analysis of the offers available to residential customers also suggests that the potential savings from switching plans in 2012-13 may not have been sufficient to motivate some customers to investigate their options and switch. This is summarised in Box 4.2.

Box 4.2: Potential savings from moving off a standing offer to a market offer

The AEMC's 2013 Residential Electricity Price Trends report found that the average residential customer in South East Queensland may have saved around five per cent per annum (or approximately $60 a year) by switching from a standing offer to a market offer in 2012-13. This does not capture the full savings which could be made by switching to the lowest advertised market offer or by negotiating with retailers to obtain lower prices than those advertised.

There are tools available to help simplify the process for customers to investigate their energy options and identify potential savings from switching plans. This includes the Queensland Competition Authority (QCA)'s price comparator website, which is currently available to customers in South East Queensland. However, there was very low awareness of this website among the customers surveyed.

Just one per cent of residents and none of the businesses surveyed mentioned this website without prompting. When prompted, 12 per cent of residents and 19 per cent of small business customers said they had heard of the site. The possible benefits of promoting greater awareness of the price comparator website are discussed further in section 4.8.2.

Forum discussions also revealed higher levels of mistrust of energy companies than in other NEM jurisdictions, particularly in relation to second tier retailers. This was driven by personal experiences with billing issues or door knockers and experiences of deceptive practices spread by word-of-mouth.

> "I'd want someone who is financially reliable. The bigger players have more clout with generators. (Maroochydore, investigated but didn't switch)."

> "I don't trust them. They have to earn my trust. A referral would be good. (Brisbane, switched)."

Another concern that was raised more frequently in South East Queensland forums was the solar feed-in tariff customers currently receive. Some customers on high legacy solar feed-in tariffs were concerned they would lose their current rate if they switched plan or retailer.

These customers were not aware that they do not lose their existing government solar rate by moving retailers. Some retailers provide an additional feed-in tariff as a 'top-up' above the Government's rate. Solar feed-in tariffs would therefore only act as a barrier to switching if the customer's existing retailer is offering a considerably higher top-up rate than other retailers.

4.4 Retailer barriers to entry, exit and expansion

The ability of retailers to enter, exit or expand within a market is another important indicator of the state of competition. Low barriers to entry and expansion place competitive pressure on retailers due to the threat of new entrants or other incumbents attracting away customers. These competitive pressures should lead to retailers charging prices that are commensurate with their costs and providing customers with the products and service that they demand.

Our analysis of this criterion considers key findings from retailer interviews and surveys conducted by consultants engaged for this review, K Lowe Consulting and Farrier Swier Consulting.[90] Eight of the 10 energy retailers that are currently active in South East Queensland agreed to participate in the retailer interview and/or the survey process.[91]

One of the key issues that these retailers were asked to provide their opinion on in the interview and survey was the ease with which entry and expansion can occur in gas

90 For full details refer to K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014.

91 As at December 2013, AGL owned Australian Power & Gas and Powerdirect and these are treated as one retailer for our analysis of competition in the market.

and electricity retail markets in South East Queensland. The responses to these questions revealed the following about the two markets:

- **Electricity retail market** - Entry and expansion in the electricity market is currently perceived to be relatively difficult by retailers. Current or future impediments cited by retailers include retail price regulation, the Queensland Government's freeze on standard domestic tariffs in 2012-13, the delayed implementation of the NECF and a number of non-regulatory barriers. If retail price regulation is removed, some retailers are expected to expand their marketing activities and at least two retailers have indicated they may enter the market.

- **Gas retail market** – Entry and expansion in the gas market is also perceived to be relatively difficult by retailers. Impediments cited by retailers were the small size of the market and the tightening demand and supply conditions in the wholesale gas market, which have been triggered by the development of LNG facilities in Queensland.

4.4.1 Changes to regulatory settings could foster greater competition in electricity

Two of the more significant factors that retailers claim have deterred entry and expansion in the South East Queensland retail electricity market over the last two years are:

- **The price freeze that was applied to the standard domestic tariff (Tariff 11) by the Queensland Government in 2012-13**. Retailers claimed that this action prompted a number of retailers to stop actively marketing and some prospective entrants to defer their plans to enter the market. Retailers also claimed that the price freeze led to an increase in the perceived degree of regulatory risk in Queensland, which has further discouraged entry and expansion in this market.

- **Retail price regulation and the manner in which it has recently been applied by the QCA**. According to retailers, the QCA's 2012-13 and 2013-14 determinations were 'biased on the low side' and have had a deleterious effect on retailer activity and discouraged both entry and expansion. The QCA's 2014-15 draft determination has been viewed more positively by retailers, with a number stating that entry and expansion conditions should start to improve if the position adopted in the draft determination is maintained in the final determination.

As discussed in section 4.2.2, the claim by retailers that the price freeze and pricing decisions by the QCA have adversely affected retailer activity in South East Queensland is consistent with the downward trend in customer switching. With respect to the retailers' claims regarding the regulatory settings, we note that two retailers entered the market in 2013 and this suggests the regulatory settings have not been sufficient deterrents for all retailers.[92] We are unable, however, to determine whether more retailers would have entered or expanded if the regulatory settings had been more conducive to entry over the last two years.

The Commission understands from interviews that retailers are broadly optimistic that conditions will start to improve if the Queensland Government follows through on its plan to remove retail price regulation by 1 July 2015. This optimism is reflected in the responses retailers provided to the retailer survey on plans to enter or expand post deregulation, which is discussed further in section 4.7.1.

Changes to the current regulatory settings in South East Queensland could therefore encourage a greater level of entry and expansion going forward and, in so doing, foster a greater degree of competition in this market.

The final observation that retailers made about regulatory barriers in Queensland is that the delayed implementation of the NECF has made it more difficult for retailers operating in other adoptive jurisdictions to enter the South East Queensland market. While there was a general expectation among retailers that the Queensland Government will implement the NECF, concerns have been raised about the potential for a large number of jurisdictional derogations to be adopted and for this to add to the costs faced by retailers operating across multiple jurisdictions. This issue is discussed in further detail in Chapter 3.

4.4.2 Non-regulatory barriers appear to be relatively low for electricity retailers

Through the interview and survey process, retailers identified two other potential impediments to entry and expansion in the South East Queensland retail electricity market. These were credit support requirements and brand loyalty. Some retailers also noted that while access to competitively priced hedging instruments in Queensland has not been a problem to date, this could change in the future if the Queensland Government decides to privatise its generation assets. The views expressed by retailers about each of these potential impediments are outlined below.

4.4.3 Credit support requirements

A number of the smaller retailers that participated in the interview and survey process claimed that the prudential arrangements and credit support required by the Australian Energy Market Operator (AEMO), electricity networks and hedging counterparties (eg generators, financial intermediaries or the Australian Securities Exchange (ASX)) acted as impediments to entry and expansion because they 'involve a significant capital outlay' and 'tie up growth capital'. The effect of prudential and credit support requirements on new entrants and small players was also raised by Alinta Energy and AGL in their respective submissions to the review.[93]

92 The two retailers that entered in 2013 were Diamond Energy and Simply Energy.

93 See for example, submissions to the *2014 Review of Retail Competition*, Approach Paper, 28 February 2014, Alinta Energy, p4 and AGL p4.

Prudential and credit support requirements are not unique to South East Queensland. In each of the competition reviews that have been conducted to date the Commission has considered whether compliance with these requirements is likely to constrain entry or expansion.

As noted in these other reviews, the Commission understands that retailers are required to commit a proportion of their working capital to satisfy prudential and credit support requirements and that the financing costs associated with maintaining a working capital facility may be higher for newer entrants because they don't have a credit history or credit rating. However, the Commission is also aware that:

- the prudential and credit support requirements are scalable, which means that smaller retailers face a lower cost than larger retailers; and
- there has been no suggestion by existing or prospective retailers that these requirements have prevented an efficient new entrant retailer from either entering the market or deciding to expand.

The Commission therefore considers that these requirements, which are necessary to safeguard the integrity of the NEM, do not constitute an insurmountable barrier to entry or expansion.

Brand loyalty

Another potential impediment to entry and expansion that a second tier retailer cited was brand loyalty to the incumbent retailers, Origin Energy and AGL.

While the observation that there is a relatively high degree of brand loyalty in South East Queensland is broadly consistent with the market share and switching data the Commission has examined, there are signs that AGL's and Origin Energy's market share is gradually eroding and that second tier retailers have had some success in capturing customers (see section 4.5). Brand loyalty therefore does not appear to constitute an insurmountable barrier to entry or expansion in this market.

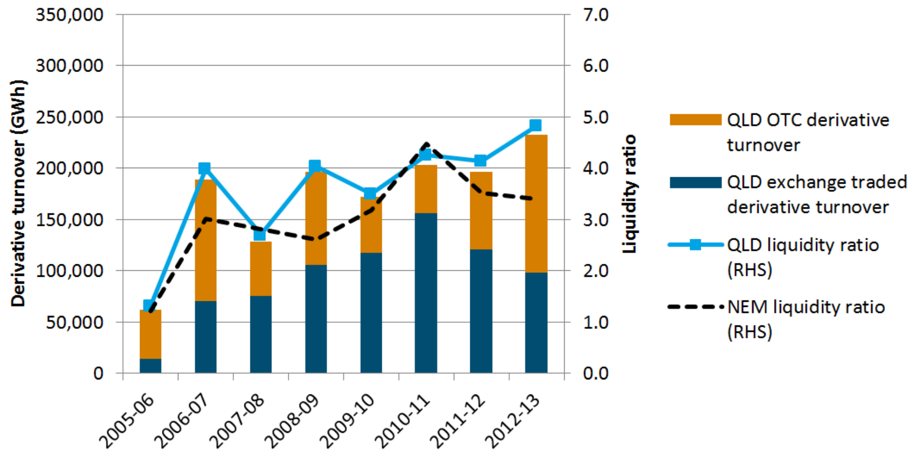
Access to hedging instruments and wholesale market conditions

Recent estimates published by the Australian Energy Regulator (AER) indicate that the Queensland Government owned generators, CS Energy and Stanwell, currently control about 65 per cent of the generation capacity in Queensland. The largest electricity retailers in South East Queensland, Origin Energy and AGL, collectively control just 12 per cent. Retailers claim to have had little difficulty accessing competitively priced hedging instruments to date. This is likely due to the lower levels of vertical integration in Queensland than most other jurisdictions and one of the more liquid futures markets in the NEM, as shown in Figure 4.6.[94]

---

94 Section 2.6 sets out why this data should be interpreted with caution.

Figure 4.6 Annual electricity futures turnover and liquidity ratios



Source: ASX Energy and AEMO data; AEMC analysis.

While access to competitively priced hedging instruments has not been a problem to date, the Commission understands that a number of retailers have expressed concerns about the potential for this to change in the future if the Queensland Government decides to privatise CS Energy and Stanwell and to sell the assets to retailers.

One small retailer claimed it is becoming increasingly important for retailers to hedge their exposure in Queensland because the wholesale market in Queensland is becoming more akin to South Australia in terms of the propensity for price separation with a degree of price volatility during these periods. The same retailer went on to note that if CS Energy and Stanwell were sold to retailers, then non-vertically integrated retailers could experience difficulties securing competitively priced hedging instruments, which could have broader reaching implications for the South East Queensland retail market.

At the time of the interviews, the Queensland Government had not announced its plans to seek a mandate to privatise CS Energy and Stanwell at the next election.[95] If the sale of these assets proceeds, the Commission considers it would be possible to structure the sale in a way that promotes competitive market outcomes.

4.4.4 The size of the gas market and wholesale market conditions may limit entry

Unlike electricity, the retail gas market in South East Queensland is not subject to retail price regulation and was not subject to the 2012-13 price freeze. The only impediments to entry and expansion that retailers cited were therefore non-regulatory in nature.

95 Subject to seeking a mandate at the next election, the Queensland Government has proposed selling the generation and coal assets of Stanwell Corporation Limited and CS Energy Limited, when market conditions are suitable. See the Queensland Government's *The Strongest & Smartest Choice: Queensland's Plan for Secure Finances and a Strong Economy*, June 2014, pp. 27 and 32.

One of the more significant non-regulatory factors that retailers claimed is deterring entry into the South East Queensland retail gas market is the size of the market, which is estimated to be about three per cent of the size of the Victorian market.[96] The size of a market will not, in and of itself, usually constitute a barrier to entry. However, if the costs of supplying that market are largely fixed or sunk (ie there are economies of scale associated with supply), then the size of the market may place a cap on the number of retailers that can enter and effectively compete in the market.

The Commission is aware from the work that was done as part of the gas market scoping study[97]and from information provided by retailers through the interviews and survey, that the costs faced by retailers can exhibit these types of characteristics. It is therefore not surprising, given the nature of the costs faced by retailers and the relatively small volume of gas consumed by small customers in South East Queensland, that there has been limited entry into this market to date, or that only one retailer has indicated it is considering entry into this market over the next five years.[98]

The other factor that may be affecting entry into this market is the development of LNG facilities in Gladstone. During the interviews a number of retailers noted that these developments, which are due to come online in late 2014 and 2015, are placing upward pressure on wholesale gas prices in Queensland and making it ‘extremely difficult’ to secure competitively priced gas in Queensland. These observations are consistent with those made by other buyers in Queensland[99] and are not surprising given that a large proportion of the certified reserves in the region have already been dedicated to the LNG projects and that LNG proponents have been competing with domestic buyers to secure gas for their facilities.[100]

Looking forward, the latest demand and supply projections developed by AEMO suggest that conditions in the wholesale gas market will remain relatively tight in the short to medium term and that shortfalls in supply could be observed in Queensland from as early as 2014 if supply and transportation constraints are not alleviated. The difficulties that buyers in Queensland have experienced accessing competitively priced gas is expected therefore to continue to act as an impediment to entry into the South East Queensland gas retail market in the short to medium term.

96 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p22.

97 K Lowe Consulting, *Gas Market Scoping Study*, a report for the AEMC, July 2013, pp42-45.

98 The Commission understands that the only second tier retailer that has entered this market in the last five years is Australian Power and Gas, but following AGL’s acquisition of Australian Power and Gas in late 2013 there are now just two retailers supplying South East Queensland.

99 See for example, Department of Energy and Water Supply, *Gas Market Review Queensland*, 2012, p38 and The Australian, *Clash looms as supply contracts unsecured*, 19 January 2013.

100 K Lowe Consulting, *Gas Market Scoping Study*, a report for the AEMC, July 2013, p23 and p31.

4.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

Our analysis of this criterion considered findings from retailer interviews and advertised market offers, which suggest the following:

- **Second tier retailers are gaining market share**. While the market share of the two incumbents remains high, there are now ten active electricity retailers and almost one third of switches involve customer transfers from the "big two" incumbent retailers[101] to second tier retailers.

- **Retailers are differentiating their market offers** based on tariff structure, discounts, contract duration and non-price incentives. The level of differentiation is expected to further increase with the removal of retail price regulation

- **Rivalry appears weaker in the gas market** with only two retailers competing and fewer offers available.

4.5.1 Market share and concentration

There are ten active energy retailers currently competing in the small customer market, two of which offer gas as well as electricity.[102] South East Queensland has a high level of market concentration with the Herfindahl-Hirschman Index (HHI) for the retail electricity and retail gas markets at 4083 and 4872, respectively.[103] The market share of the two incumbent electricity retailers, Origin Energy and AGL, has been gradually eroding but remains high at approximately 82 per cent.

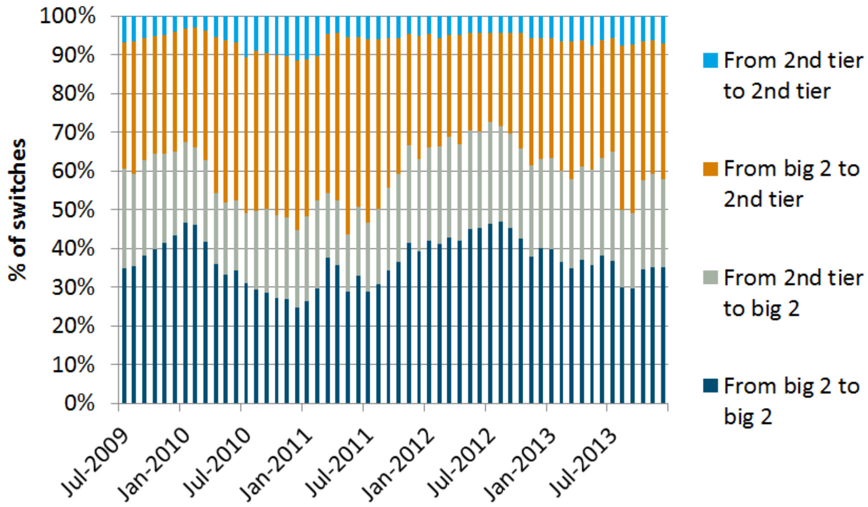
Figure 4.7 shows that, of the electricity switching that occurred in the last half of 2013, close to one third occurred between the big two retailers. Importantly, a similar proportion of switching occurred from the big two to second tier retailers. Switching between the big two retailers has been declining since August 2012 with second tier retailers attracting customers away from the big two. There was a slight jump in switches from the big two to second tier retailers in mid-2013, which appears to follow the One Big Switch campaign in Queensland.

101 The big two retailers in South East Queensland are Origin Energy and AGL, who have the vast majority of electricity customers and all gas customers in this region.

102 AGL acquired Australian Power and Gas in 2013 and also owns Powerdirect. These retailers are treated as one for the purpose of this competition review.

103 The Australian Competition and Consumer Commission uses a score of 2000 as a threshold when considering the level of competition for merger assessments.

Figure 4.7 Proportion of switches between different sized retailers



Source: AEMO data, AEMC analysis.

Rivalry in the gas market is not as strong as in the electricity market, with only two retailers that offer gas in South East Queensland. Switching occurred between the two retailers, with one retailer making moderate net gains while the other made moderate net losses overall.

As at August 2013, Origin Energy had almost 60 per cent and AGL had just over 40 per cent of the whole Queensland market.[104] Competitive conditions in the gas market are unlikely to change in the short term for reasons discussed in section 4.4.

4.5.2 Product differentiation

Retailers interviewed stated that product differentiation in South East Queensland is lower than in Victoria and attribute this to the small number of advanced meters in South East Queensland and the lack of incentives to innovate in the presence of retail price regulation. Our analysis of offers advertised in South East Queensland indicates there is a moderate level of product differentiation in terms of tariff structures, discounts and contract types.

In addition to the features discussed below, retailers also differentiate their brand through service quality such as call centre operation hours, information provision, policies on hardship and complaints, policies on door knocking and cold calling, online account access and, in some cases, shopfronts for customers to visit and discuss their options.

---

104 AER, *State of the Energy Market*, 2013, p122.

Standard offers

There is no differentiation between standard electricity offers as all retailers are required to offer these contracts and the associated prices are regulated.

Gas retailers are also required to offer a standard contract, but the price is not regulated. The standard gas offers for residential customers from the two retailers are differentiated with different fixed charges, inclining block levels, and inclining block tariffs.

Electricity market offers

As at 31 March 2014, there were 25 market offers available for residential electricity customers in South East Queensland.[105] Many of these offers are very similar in terms of their tariff structures, discounts, contract types and other features.

Table 4.1 summaries their key differences to provide examples of how retailers are differentiating electricity offers to residential customers in this region.

The AEMC's survey and analysis of the offers available found that there is less discounting than in states without retail price regulation, with some market offers being identical to the regulated offer and the highest discount rate being 11 per cent off usage.

The range of offers available and the level of product differentiation was the same for urban and regional customers in South East Queensland and broadly similar for residential and small business customers.

Gas market offers

Consistent with other NEM jurisdictions there is less differentiation in gas offers in South East Queensland with just two retailers offering gas products. Unlike the electricity offers available, these retailers are offering gas products with inclining block tariffs. There were conditional discounts available for residential gas customers of up to five per cent off usage.

Discounts of one to two per cent are available for small business customers, which are smaller discounts relative to those on offer for residential customers. Many of the offers surveyed for small business customers did not have a fixed term.

---

105 The Queensland Competition Authority price comparator website showed more than 25 offers, however most of these additional offers differed solely in terms of the amount of GreenPower available and have not been included in this count. GreenPower is identified as one of the ways retailers differentiate their products in Table 4.1. This approach was taken to be consistent with other NEM jurisdictions where offers are presented on price comparator websites as one unique offer with the option to select the level of GreenPower.

Table 4.1 Differences in electricity offers in Brisbane as at 31 March 2014

Areas of difference between offers *(high number of offers: >30; moderate: 15-30; low: 0-15)*	
Time of use tariffs	Moderate number of offers available with a low level of differentiation between them. There were slight variations only between the supply, peak, off peak and shoulder charges on offer. There was also slight variation in the supply charge.
Other tariffs	Low number of offers with a low level of difference. These offers did not have any structural differences - all had a supply charge and standard peak price.
Discounts	Moderate number of offers with low level of difference. Unconditional discounts ranged from 3 - 5 per cent off usage. Conditional discount options range from 1 - 11 per cent off usage. Options include discounts for: • paying on time; and • paying by direct debit. Minor discounts only (1-3 per cent) were available for customers who did not want to commit to a fixed term but would pay by direct debit.
Contract duration	Moderate level of difference between offers. High number of offers without a fixed term. Fixed term contracts ranged from 1 – 3 years.
Non-price incentives	Low number of offers with low level of difference. Options include: • Bonus sign up rebates from $20-30 • Bonus $20 rebate for signing up to direct debit • 10,000 frequent flyer points on sign up, 6 points per $1 spent on bill • Ability to purchase renewable energy certificate equivalent to proportion of electricity consumption (GreenPower)
Solar feed-in tariff	Low range of difference in terms of offers tailored to customers with solar panels. As at 1 July 2014, retailers in South East Queensland offered solar feed-in tariffs of 6 to 12 c per kWh.[106]

106 In March 2014, information on solar offers was not available on the QCA price comparator website. More information on solar arrangements is provided in Appendix D.

4.6 Customer outcomes

Effective competition is characterised by how well the process of markets promote the long term interest of customers, including satisfaction with the level of choice available, the quality of service and the value for money provided by retailers. Our analysis of this criterion considered the findings of customer surveys and data on customer complaints, which suggest the following:

- **Many customers want greater choice**. Close to one fifth of customers were somewhat or very dissatisfied with the level of choice in the market, with many perceiving little difference between the current options available.
- **Most customers are satisfied with their current retailer**, but there appears to be a general mistrust of energy retailers.
- **Most customers are very satisfied with the quality of service and value for money** provided by retailers, giving particularly high ratings for gas retailers.
- **The number of customer issues reported by retailers grew in 2012-13**, which may be largely due to complaints associated with new billing systems. The number of complaints to the Ombudsman did not materially increase over the same period.

4.6.1 Satisfaction with the level of choice

The degree of customer satisfaction with the level of choice in South East Queensland is slightly lower than in most other jurisdictions, with 48 per cent satisfied, 18 per cent dissatisfied and the remainder being neutral or undecided. However, discussions in the forums suggested that the issue is complex and actual satisfaction may be lower.

A number of customers in forums saw little evidence of competition or of how greater choice was delivering lower prices or better service.

> "It's only there if you really push them. They're not really competing with each other. They're not actively fighting each other. You have to ring them. (Maroochydore, higher income)"

> "There is a slight bit of difference in the offers, but not enough. (Brisbane, small business)"

Some stated the level of choice may improve as competition improves and with the removal of regulation.

> "It's not a truly competitive market until you remove all the regulations. (Brisbane, income unidentified)"

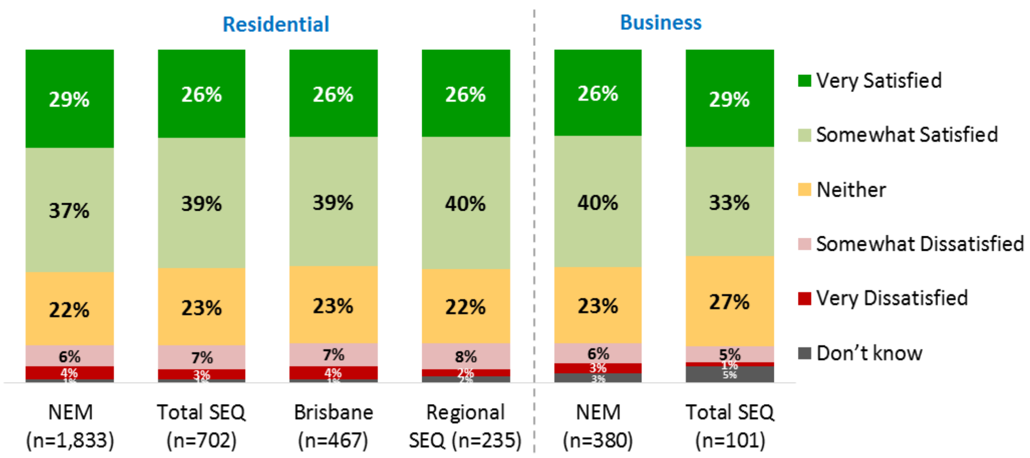
“Competition would increase once the next stage comes along. Then it would be true competition. Truer competition than having part of it set by the government. (Maroochydore, income unidentified).”

Many forum participants commented that they find it hard to get information they trust and it is difficult to compare offers. Many participants believed that greater awareness of choice through promoting the independent comparison website would assist in improving competitiveness, but they noted that investigating alternative plans would only be worthwhile once real savings are available.

4.6.2 Satisfaction with retailers

The majority of customers were satisfied with their retailer in all NEM jurisdictions surveyed, with 65 per cent of South East Queensland customers somewhat or very satisfied with their electricity retailer as shown in Figure 4.8.

Figure 4.8 Satisfaction with current electricity retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p186. Survey question: How satisfied are you with your current electricity company? Customers surveyed: All.

Approximately ten per cent of residential customers and six per cent of business customers surveyed were either somewhat or very dissatisfied with their electricity retailer. Submissions from Queensland consumer groups to the AEMC's review highlighted a range of customer service issues experienced by their stakeholders. This included (but was not limited to) long call centre waiting times, difficulties understanding the call centre operator, retailers requiring that certain transactions only be performed online and a range of billing issues.[107] In the Newgate Research forum discussions, similar issues were raised and dissatisfaction generally related to billing issues, concerns about rising prices, or poor customer service.

107 Queensland Council of Social Services (QCOSS), submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, pp18-19 and COTA Queensland, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p3.

While most customers surveyed were at least 'somewhat' satisfied with their retailer, the forum discussions suggest that satisfaction often relates to an absence of negative issues with their retailer rather than a positive experience. Most customers in forums appeared relatively ambivalent towards their retailer, but satisfaction was generally higher among those customers with solar panels. There appeared to be widespread dissatisfaction with rising electricity prices and mistrust of the way retailers price their services, market and communicate to customers.

Satisfaction was higher for gas retailers, with 78 per cent somewhat or very satisfied. In forum discussions, gas customers were happy to have access to gas, had never experienced service issues and felt it was well priced.

The overall quality of service for electricity and gas was largely perceived as good or excellent by survey respondents. Customers in regional South East Queensland rated the quality of service even higher than customers in Brisbane.

Value for money was rated at least fair overall and close to half of residential and business customers considered electricity value for money good or excellent. However, 15 per cent of residential customers and nine per cent of business customers rated electricity value for money as poor.

It is likely that value for money ratings primarily relate to higher electricity bills in recent years. Price increases have been experienced by customers on market and regulated contracts. For regulated contracts, part of the increase in 2013-14 is due to the end of the tariff 11 price freeze.

The largest driver of price increases for regulated and market contracts in 2012-13 was increasing regulated network costs which made up an estimated 52 per cent of the average market offer price in 2012-13. Environmental policies, including the carbon pricing mechanism, the renewable energy target, the Queensland Solar Bonus scheme and the Queensland gas scheme, constituted an estimated 20 per cent of electricity price over this same period.[108] A full discussion of the drivers of price movements and trends in electricity prices is available in the AEMC's annual residential pricing trends report.

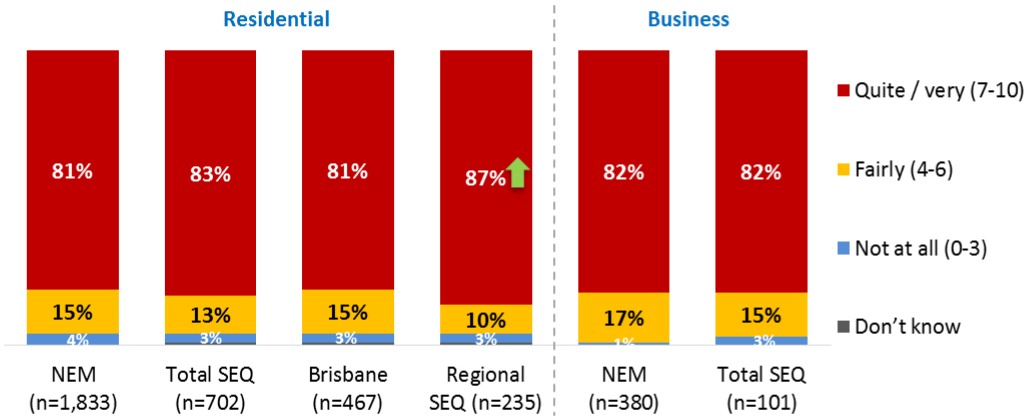
Figure 4.9 shows that approximately 80 per cent of customers surveyed in South East Queensland stated that they were 'quite' or 'very' concerned about future electricity prices. This is broadly consistent with the NEM average.[109] There were even higher levels of concern among residential customers outside of Brisbane.

---

108 AEMC, *2013 Residential Electricity Price Trends*, 13 December 2013, pp48-50.

109 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p153.

Figure 4.9 Level of concern about future energy prices



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p153. Survey question: How concerned are you about future energy prices? Customers surveyed: All.

For South East Queensland customers with high and middle incomes on market contracts, annual electricity bills are estimated to represent approximately 0.5-1.3 per cent of the annual disposable income. For low income customers on market contracts, annual electricity bills represent approximately 3.3-4 per cent of annual disposable income, depending on whether the customer receives a concession.[110]

Pensioners, seniors and veterans can be eligible for concessions through Electricity Rebates, Reticulated Natural Gas Rebates or the Home Energy Emergency Assistance Scheme. Concessions are also available to customers with medical issues through the Medical Cooling and Heating Electricity Concession Scheme and the Electricity Life Support Concession Scheme. These energy-related concession schemes are paid as lump sum, irrespective of consumption levels and are discussed in Appendix B.

The Queensland Government accepted an independent panel's recommendation in 2012 to develop a clear and effective hardship and concessions framework informed by public consultation.[111] This is consistent with the AEMC's Power of Choice recommendations for all jurisdictions to review their concession schemes.

Complaints to retailers

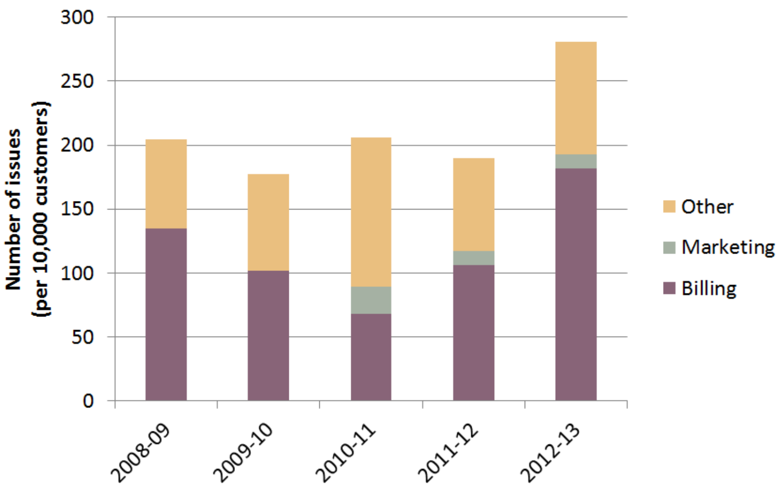
When a customer makes a complaint, multiple issues may be raised. As shown in Figure 4.10, the number of issues raised with electricity retailers in 2012-13 was higher than in any of the previous four years. This is consistent with trends in other jurisdictions. Billing was the most common issue in most years since 2008-09, making

110 This AER analysis is based on average annual electricity consumption of 5,000 kWh for low income customers and 6,800 kWh for middle and high income customers. Concessions included the Electricity Rebate and the Reticulated Natural Gas Rebate. AER, *Annual report on the performance of the retail energy market 2012-13*, 2013, p61.

111 Interdepartmental Committee on Electricity Sector Reform, *Report to government*, May 2013, p95.

up 65 per cent of the issues raised with electricity retailers in South East Queensland in 2012-13.

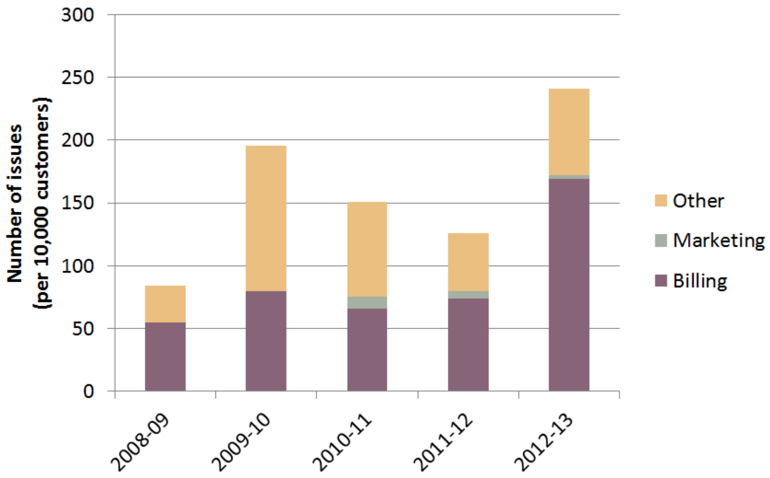
Figure 4.10 Electricity complaints to retailers - number of issues raised



Source: Complaints data from the Queensland Competition Authority (QCA), customer numbers from AEMO, AEMC analysis.

The number of issues customers raised with gas retailers in Queensland in 2012-13 was only slightly lower than for electricity, when adjusted for market size. Similar to electricity, the number of issues raised in 2012-13 was higher than in the previous four years (see Figure 4.11). In 2012-13, there was a 92 per cent increase on the previous year, largely driven by billing issues which increased by 129 per cent. The sharp increase in billing issues is likely related to difficulties with the new billing systems of a number of retailers.[112]

Figure 4.11 Gas complaints to retailers - number of issues raised



Source: Complaints data from the QCA, customer numbers from AEMO and ESAA *Electricity Gas Australia* reports, AEMC analysis.

112 Energy and Water Ombudsman Queensland, *Annual Report 2012-13*, 2013, p13.

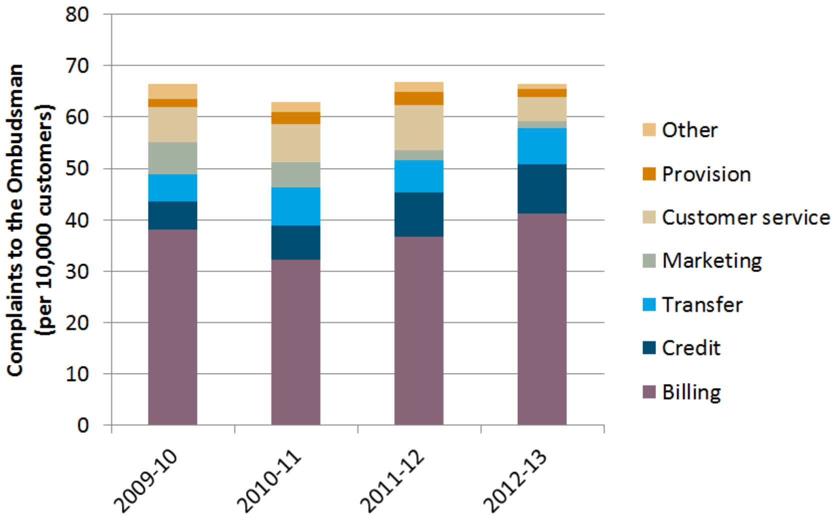
Complaints to the Ombudsman

The number of complaints made to the Energy and Water Ombudsman in Queensland (EWOQ) about electricity retailers in South East Queensland was similar in 2012-13 to previous years (see Figure 4.12).[113] Note that issues raised with EWOQ include referrals back to retailers, which are also captured in complaints to retailers described above.

The number of complaints in 2012-13 equates to 66 people per 10,000 customers. It is difficult to accurately compare this figure to some of the other NEM jurisdictions. In some other jurisdictions, the number of issues raised has been recorded, rather than the number of complaints (there may be more than one issue per complaint).

Over 60 per cent of complaints were related to billing issues and 14 per cent of complaints were related to credit issues. Credit issues were from customers who experience difficulty in paying their bill. High bills, errors and delays account for the majority of electricity billing issues, with high bills alone accounting for 30 per cent of billing issues. According to EWOQ, "Complaints about high bills sometimes disguise the real reason for calling EWOQ – the customer simply cannot afford to pay their bill. We continued to assist many customers in negotiating payment plans and accessing hardship programs this year."[114]

Figure 4.12 Electricity complaints to the Ombudsman – number of complaints – South East Queensland



Source: Complaints data from EWOQ, *Annual Report 2012-13*, customer numbers from AEMO, AEMC analysis.

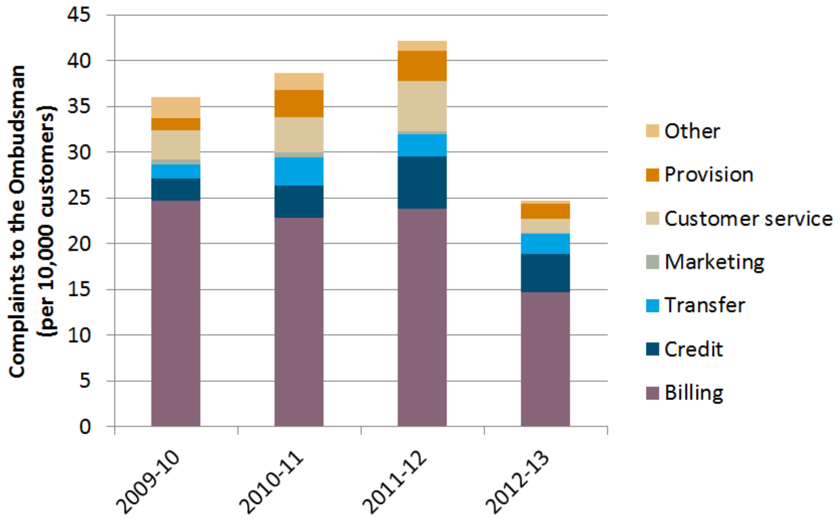
Twenty-five gas complaints per 10,000 customers were registered by EWOQ in 2012-13, over half of which concerned billing issues (see Figure 4.13). This was the lowest

113 Data on complaints to EWOQ excludes cases which were out of jurisdiction or not complaints. Complaints regarding Ergon Energy have been removed.

114 Energy and Water Ombudsman Queensland, *Annual Report 2012-13*, 2013, p5.

number of gas complaints to the Ombudsman in the last four years. Gas complaints to EWOQ decreased by around 40 per cent between 2011-12 and 2012-13 and billing complaints decreased by 38 per cent. There was also a drop in complaints categorised as customer service complaints due to a change to EWOQ's categorisation of complaints.

Figure 4.13 Gas complaints to the Ombudsman – number of complaints – whole of Queensland



Source: Complaints data from EWOQ, *Annual Report 2012-13*, customer numbers from AEMO and ESAA *Electricity Gas Australia* reports, AEMC analysis.

4.7 Retailer outcomes

Profit margins can provide an indication of the level of competition in a market. However, they can also be expected to fluctuate over time. Consequently it is important to carry out analysis of retailer margins over a sufficiently long time period. It is also important to consider the results of such analysis in the context of other competitive indicators. While retail margins have not been estimated for the purpose of this review, we make a number of observations on retailer outcomes drawing from retailer interviews and pricing determinations by the jurisdictional regulator.

The profitability of electricity retailing in South East Queensland has varied over the last few years, largely driven by the impacts of the price freeze and the methodology used by the QCA to determine the regulated price. Two retailers have entered the South East Queensland market in the last two years, suggesting that retail margins are, or are expected to be, sufficient to support new entry. Consistent with this, the QCA's 2014-15 pricing determination was viewed more favourably by retailers.

Retailers interviewed for this review noted that the price freeze and subsequent regulatory decision by the QCA had:[115]

- adversely affected the profitability of retailing in South East Queensland, with one retailer stating that the price freeze resulted in '20 per cent of the gross margin being removed in some areas'; and
- 'forced' one Queensland based retailer to move into other jurisdictions to remain commercially viable.

One retailer considered the effects of the QCA's regulatory decision are still impacting the market, stating:[116]

> "In our view there is not sufficient headroom in South East Queensland to be actively retailing at present."

Origin Energy estimated that the decision to freeze prices reduced its electricity gross profit by $58 million,[117] while the impact on AGL was around $30 million.[118] Australian Power & Gas stopped actively seeking new customers as a result of the decision.[119]

Retailers that participated in the survey rated profitability in Queensland at a similar level to NSW and South Australia.

The QCA's recent 2014-15 draft determination was viewed more favourably by retailers that participated in interviews. While some retailers continue to hold concerns about the QCA's approach to calculating the energy cost allowances, the larger retailers were generally supportive of the magnitude of the retail margin and headroom allowance.

Origin Energy's annual report for 2012-13 noted that "the 2014 financial year Queensland tariff determination recovers some of the adverse impact of wholesale cost increases not recovered in the 2013 financial year."[120] This suggests that, while profitability may have reduced in 2012-13, it is expected to pick up.

The Queensland Government's intention to remove retail price regulation in 2015, subject to a number of conditions, may also improve conditions for retailers going forward.

115 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p20.

116 Ibid, p20.

117 Origin Energy, United States Roadshow, March 2013, p15.

118 AGL, FY13 Interim Results presentation, 27 February 2013, p4.

119 APG, Investor Update, March 2013, p7.

120 Origin Energy, Annual Report 2013, p3.

There is limited available information on the profitability of gas, particularly due to the confidential nature of wholesale gas contracts and the lack of publicly available reference data. We note that retailer survey participants rated gas profitability in South East Queensland the same as for electricity profitability, although comparisons should be treated with caution as a different set of retailers participated in each survey

4.8 Future developments

Competitive conditions in the South East Queensland market are likely to improve once price regulation is removed. Retailers are reportedly poised to enter the market or expand their current efforts once this regulatory risk is reduced. The level of product differentiation is currently modest with customers perceiving little difference between the choices available, but greater retailer rivalry is expected to bring more choices to customers in future. It will be important for customers to be aware of and have access to the right information and tools to exercise their choice in a more competitive market.

4.8.1 Competition is likely to further improve if price regulation is removed

The main issue affecting competition in the South East Queensland electricity retail market is the intended removal of retail price regulation. This is likely to further improve competition between retailers and result in greater innovation, increased product choice and competitive pricing for customers.

The retailers interviewed seemed broadly optimistic that South East Queensland will remove electricity retail price regulation and noted that this would lead to greater competition. Survey responses from retailers suggest that two small retailers are considering entry while four existing second tier retailers are planning to expand over the next five years, subject to price regulation being removed.

Interviews with retailers also revealed that there are at least two other second tier retailers currently supplying commercial and industrial customers in Queensland that could readily move into the small customer segment if entry conditions were amenable.

Some retailers cautioned that even once price regulation was removed it could take time before there is a demonstrable increase in competition. They considered that the level of customer engagement is low and that work is required to improve awareness, particularly following the price freeze.

4.8.2 Customers must be aware of, and have access to, trusted information

Customer research suggests that all NEM jurisdictions face a similar challenge in providing customers with the information they need to compare offers and choose an energy plan. There is an opportunity in all jurisdictions, including South East Queensland, to increase the confidence of customers to shop around for a better energy deal.

As discussed in this chapter, customer research in South East Queensland suggests:

- most customers are unaware of the extent of choice available or perceive little difference between the choices;
- very few customers understand the details of the offers available and find it difficult to compare different offers; and
- many customers are not interested in shopping around for a better offer because of the perceived time and effort involved in doing so.

These findings are consistent with research conducted in New South Wales in 2013 to inform a consumer engagement blueprint for the New South Wales government. This blueprint is discussed in Chapter 3 and is broadly applicable to South East Queensland. It provides advice on how to inform and empower customers to choose an energy plan that suits their needs.

Much of what customers want exists, such as an independent comparison website like those offered by the QCA in South East Queensland and the AER in NECF states.[121] These websites can help to address the key issues highlighted above by increasing awareness of the extent of choice available, making it easier to compare "apples with apples", and reducing the time and effort involved in shopping around. However, research shows there is very low awareness of these websites.

Customers surveyed strongly favoured online information on different plans, but approximately 70 per cent were unaware of any comparator websites and just one per cent was aware of the QCA website without prompting. Forum participants stated that greater awareness of an independent price comparator website would make them more likely to investigate their options.

> "The comparison website is a good start. Getting to the apples to apples comparison. (Maroochydore, higher income)"
>
> "The time commitment to find the best deal is one of the major barriers so anything that makes it easier would be good. (Brisbane, switched)"
>
> "It's extremely good and I recommend people look at it because they don't have an axe to grind and they don't take a commission if people look at it and get a better price. (Brisbane, lower income)"

It is important that customers are aware of the availability of government comparator websites in all NEM jurisdictions and that these tools are user-friendly.[122] This is

---

121 Queensland customers will have access to the AER's comparator website, Energy Made Easy, once Queensland adopts the National Energy Customer Framework.

122 We note that the submission from QCOSS highlighted a number of issues with the QCA price comparator website that it considers reduce the useability of the site. Submissions to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, Queensland Council of Social Service (QCOSS), pp7-8.

particularly important for South East Queensland where more choices are expected to become available following the removal of electricity retail price regulation.

All customers should be encouraged to reassess their energy needs and shop around regularly to take advantage of new offers or move to more suitable plans as their needs change. However, as highlighted in submissions to this review and in research conducted for the NSW competition review, some groups of customers have additional challenges in accessing information and assessing their options. This is particularly the case for customers who do not have the confidence or the technology to access online resources.[123] The blueprint developed for NSW provides specific advice on how to tailor information and tools for different people in the community, including these types of customers.

We understand that the Queensland Government is currently working to improve engagement to help customers benefit from discounts and improved products in a competitive market. This includes publicly consulting on options to increase customer engagement in the electricity sector and develop an effective customer engagement strategy.[124]

A government-run information and education campaign can help raise customer awareness of their options and improve customer confidence and willingness to become "energy shoppers".

Qualitative research suggests that additional, targeted messages may be required for customers with solar panels who may be uncertain about their ability to switch retailer and retain their feed-in tariff. Targeted messages may also be required for small businesses as survey data suggested significantly fewer small businesses are interested in looking for a better deal, investigating their options or switching.

4.8.3 Wholesale electricity market conditions

In section 4.4.2, we found that electricity wholesale market conditions are currently favourable. However, some retailers considered that the potential privatisation of generation assets, combined with increased spot price volatility, could influence retailers' ability to obtain hedging cover. These retailers noted that if the Queensland Government divests its generation assets it should give careful consideration to how it sells the assets and who it sells the assets to in order to promote the best competitive market outcome.

---

123 Submissions to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, QCOSS, p7; COTA Queensland, p2; and South Australian Council of Social Services, pp4-5.

124 Queensland Government response to the Interdepartmental Committee on Electricity Sector Reform p10. Available at: http://www.dews.qld.gov.au/__data/assets/pdf_file/0007/78568/queensland-government-response-to-idc-report.pdf.

4.8.4 Gas market conditions

The key issues currently limiting competition in gas markets appear to be largely structural, primarily due to limited penetration of and demand for reticulated natural gas. As with other states, influences on competition in the gas retail market are likely to be dominated by changes in the wholesale market. Queensland is expected to feel these effects more acutely than other jurisdictions given its proximity to the LNG developments. This is because the transportation costs associated with supplying gas from other jurisdictions, particularly Victoria, are likely to be high.[125] Given this environment, competition is unlikely to change significantly going forward.

Retailers did not provide many comments on the outlook for competition in the Queensland retail gas market over the next few years. One retailer noted that it was "considering" entry over the next five years but had no firm plans to do so.

125 There are also other hurdles that would need to be overcome to supply gas from Victoria to Queensland, including the limited physical interconnection between some pipelines and having to rely on an 'as available' backhaul transportation service unless the predominant flow of gas changes.

5 Regional Queensland

Box 5.1: Key findings

- Competition in regional Queensland is not effective in the electricity retail market due to the uniform tariff policy that allows all Queensland customers in the same class to have access to the same price. This policy provides subsidies to the incumbent retailer, Ergon Energy, and makes it difficult for other retailers to enter the market at a competitive price.
  - Almost all small electricity customers in regional Queensland are on a regulated offer with Ergon Energy.
  - No other retailers have plans to enter the regional Queensland market while the uniform tariff policy is in place.
- The Queensland Government is considering options for changing the way in which the uniform tariff policy is applied to encourage retail competition. Changes are essential for providing the right conditions for competition to develop.
- An information campaign will also be important to raise customer awareness and understanding of their options.
- While gas customers in Toowoomba and Oakey have access to two competing gas retailers, customers in Wide Bay-Burnett, Gladstone and Rockhampton only have access to one retailer.
- Competition is unlikely to develop further in these areas due to the small size of the customer base in these regions and the regional specific economies of scale associated with gas retailing.

5.1 Overview

The Commission's assessment of competition against the five criteria set out in Chapter 2 has found that competition is not currently effective in the electricity and gas markets. The findings for the regional Queensland retail market can be summarised as follows:

- **Customer activity**: Almost all customers remain on standing offers.
- **Barriers to entry, exit and expansion**: Due to the way in which the Uniform Tariff Policy (UTP) is given effect, electricity retailers are not able to profitably enter the regional electricity market and compete. Low penetration and use of gas has impeded entry by gas retailers.
- **Independent rivalry**: There is no rivalry in either the electricity or gas markets since only one retailer currently operates in each of these markets.

- **Customer satisfaction**: Customer complaints appear low, however this may reflect limited, or no, retailer marketing activity and a clack of customer engagement.
- **Retailer outcomes**: The incumbent electricity retailer currently receives a subsidy to compensate it for incurring net costs as a result of the UTP. No other retailer is eligible for this subsidy and so cannot profitably operate.

5.2 History and market characteristics

Full retail competition for small customers of electricity and natural gas was introduced in regional Queensland in July 2007, at the same time as for South East Queensland. Regulated prices were retained for electricity but not for gas customers.

There are currently just under 700,000 small electricity customers in regional Queensland, compared to 1.3 million in South East Queensland. Regional Queensland's electricity customers are spread out over a much larger area. Ergon Energy's network covers over one million square kilometres[126], compared to Energex's 25,000 square kilometres.[127]

The Queensland Government has a uniform tariff policy (UTP) that ensures all Queensland customers in the same class have access to the same price. The Government has acknowledged that this arrangement is impacting competition in regional Queensland as discussed in section 5.4.1.

Queensland is considering the introduction of the National Energy Customer Framework (NECF), subject to a set of conditions which are outlined in section 4.2. If introduced, the NECF will apply to electricity and gas customers.

The only areas in regional Queensland where reticulated gas is currently available are Gladstone, Rockhampton, the Wide Bay-Burnett region (Bundaberg, Maryborough and Hervey Bay), Toowoomba and Oakey (less than five per cent penetration for residential customers).[128]

As discussed in Chapter 2, we have used the Energex and Ergon electricity distribution network areas to define the bounds of South East Queensland and regional Queensland, respectively. However, this definition is less applicable in the gas market. While Toowoomba and Oakey fall into the Ergon distribution network, gas customers in these areas are supplied from the same pipeline as customers in South East Queensland (the Roma to Brisbane pipeline).

---

126 See www.ergon.com.au.

127 See www.energex.com.au.

128 Reticulated liquefied petroleum gas (LPG) is also available in some areas, including parts of Rockhampton, Townsville and Cairns. Competition in the LPG market is outside the scope of this review. There are two small distribution networks in Roma and Dalby which are owned and operated by their respective local governments. These customers do not have a choice of their retailer.

Consequently, gas customers in Toowoomba and Oakey have access to the same offers as customers in South East Queensland. For this reason the discussion in this chapter on the gas retail market focuses on customers in Gladstone, Rockhampton and the Wide Bay-Burnett region.

We note that the Queensland Competition Authority (QCA) completed a review of competition in the small customer retail gas market in 2008 which found that customers in regional areas (excluding Toowoomba and Oakey) were unable to access or negotiate retail contracts from a competing retailer.[129]

5.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

While electricity customers in regional Queensland are technically contestable,[130] in practice most small customers currently have no choice of retailer because the government-owned incumbent, Ergon Energy, is the only retailer accepting customers in their area.

Further, Ergon Energy is not permitted to offer market contracts so customers in regional Queensland are limited in their ability to shop around. For this reason, customer research was not conducted in regional Queensland.

The only choice available for most small regional electricity customers is between the type of regulated tariff that they are on. For residential customers these generally fall into three categories:[131]

- general supply tariffs, where usage is charged at a flat rate;
- time of use tariffs, where different prices apply depending on the time of day that electricity is used; and
- economy tariffs, which can be used to connect hot water systems, pool pumps and other controlled load appliances.

A fourth set of tariffs is available to farming customers. Similar tariffs are available for small business customers.

---

129 Queensland Competition Authority, *Review of Small Customer Gas Pricing and Competition in Queensland*, final report, November 2008, p25.

130 A small number of customers in regional Queensland are excluded through legislation from being able to choose their electricity retailer, including small customers in 33 isolated communities and in Mount Isa, Cloncurry (who are not connected to the main grid) and Weipa (who are supplied by a private network). Customers who buy their electricity through an on-supplier are also unable to choose their retailer.

131 See www.ergon.com.au.

Less than one per cent of all electricity customers in regional Queensland are on market contracts.[132] The majority of these are large customers so, in effect, almost no small customers in regional Queensland are on market contracts. We understand that one other retailer had been operating in some areas of regional Queensland, but following a change in the QCA's approach to setting regulated prices, found that it was no longer profitable to supply these areas and ceased retailing in these areas.[133]

Gas customers in the Wide Bay-Burnett region, Gladstone and Rockhampton are also currently limited in their choice of retailers, with just one retailer, Origin Energy, currently operating. As elaborated on below, the challenges for retailers entering the gas market are different to those for electricity.

Retail natural gas prices are not regulated, so all customers are on contracts where the retailer determines the price. Origin Energy offers three different contracts to customers in these areas that differ based on the level and conditions of the discounts.[134] These contracts have the same terms and conditions as the contracts offered in South East Queensland, although the underlying tariffs are structured differently and have different rates

5.4 Retailer barriers to entry, exit and expansion

Barriers to entry, exit and expansion are another important indicator of the state of competition. Low barriers to entry and expansion place competitive pressure on retailers due to the threat of new entrants or other incumbents attracting away customers. These competitive pressures should lead to retailers charging prices that are commensurate with their costs and providing customers with the products and quality of service that they demand.

Retailers were asked what the main impediments to entry and expansion were in the electricity and gas retail markets in regional Queensland.[135] Their responses to this question revealed the following:

- **Electricity retail market** – The UTP is perceived to be the primary barrier to entry in the electricity retail market. This was the only barrier to entry retailers focussed on. However, their views on entry conditions in regional areas in other jurisdictions suggest that there may be some other non-regulatory impediments that could affect entry and/or expansion in these areas, even if changes are made to the design of the UTP to facilitate competition.

132 Queensland Competition Authority, Draft Determination, QCA, December 2013, p10.

133 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer interviews*, a report for the AEMC, June 2014, p21.

134 As at 29 May 2014 these are: Flexichoice, eSaver and DailySaver Plus. They offer conditional discounts for paying by direct debit, paying the bill in full and on time and receiving bills by email.

135 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer interviews*, a report for the AEMC, June 2014, pp19-22.

- **Gas retail market** – The small size of the customer base in the Gladstone, Rockhampton and Wide Bay-Burnett regions is perceived to be the main barrier to entry into this market. Retailers also noted that the tightening demand and supply conditions in the wholesale gas market, which have been triggered by the development of liquefied natural gas (LNG) facilities, may discourage entry in these areas.

5.4.1 Factors affecting entry and expansion in the electricity retail market

The UTP was identified by retailers as the most significant barrier to entry into the regional Queensland electricity retail market. Under this policy, all customers of the same class in Queensland must have access to the same 'notified' (regulated) price.

The notified price is currently based on the cost of serving a customer in South East Queensland. The notified price is therefore based on Energex's network costs and an estimation of energy losses for Energex's network, rather than the equivalent measures for Ergon Distribution's network, which are much higher than for Energex. To account for the difference between Ergon Energy's costs and the revenues from selling electricity at the notified price, the Queensland Government pays Ergon Energy a subsidy. In 2013-14, the subsidy is expected to cost $615 million.[136]

A subsidy is also paid by the Queensland Government to Origin Energy so that small customers in the Goondiwindi, Texas and Inglewood areas, who are supplied by Origin Energy via the NSW distribution network, also pay the same price as other Queenslanders. In 2013-14, the Queensland Government is expected to pay Origin Energy a subsidy of $5 million.[137]

In the retailer interviews, a number of retailers noted that the UTP as it is currently applied is deterring entry in regional Queensland because:

- retailers are unable to supply electricity at the same price as in South East Queensland (ie because transmission and distribution costs and losses are higher in regional Queensland than they are in South East Queensland); and
- the subsidy the Queensland Government pays to maintain the UTP is not available to any other retailers, so the higher costs of supplying electricity to regional areas must be borne by the retailer.

In mid-2013, the Queensland Government announced that it will examine options to improve competition in regional areas, including the development of a more effective subsidy arrangement to maintain the UTP.

136 Queensland Government, State Budget 2013-14, Concessions Statement, June 2013, p19.

137 Ibid.

As part of the Government's review, the QCA was directed to investigate and report on:[138]

- the efficiency and effectiveness of the current UTP arrangements;
- the options for maintaining a UTP, or more targeted subsidy payments and related options for retail price regulation in regional Queensland; and
- the extent to which options for determining notified prices will support a competitive retail electricity market in regional Queensland.

The QCA reported to the Queensland Minister for Energy and Water Supply on these matters at the end of April 2014.

The Commission of Audit Taskforce has also been directed to examine recommendations to better target community service obligation payments to those in need and improve the transparency of subsidies.[139]

It is unclear at this point in time when the Queensland Government will make a decision on how to proceed with the UTP. The Commission understands from the 30-year electricity strategy discussion paper that, if the Queensland Government decides to restructure the UTP, this change is likely to occur within three years in parallel with the reform of Ergon Energy's retail business.[140]

While restructuring the UTP to facilitate competition may remove one of the more significant barriers to entry in regional Queensland, there are a range of other regulatory and non-regulatory factors that could still be perceived by retailers to impede entry and/or expansion in this market. This includes:

- **The continued application of retail price regulation in regional Queensland.** According to retailers, the 'mere presence' of retail price regulation deters entry due to the risk that the regulated price is set below the retailer's cost of supply.
- **The small size and geographic dispersion of the customer base.** From a retailer's perspective, these features of the market are likely to make regional Queensland a less attractive proposition because the costs of acquiring new customers in this area are likely to be higher than they are in more populated or geographically central areas.
- **Customers are likely to exhibit a high degree of brand loyalty towards Ergon Energy,** because of the familiarity they have with Ergon Energy as both a retailer and distributor, its government ownership and involvement in the community.

---

138 Queensland Competition Authority, *Retail Electricity Price Regulation in Regional Queensland*, Issues Paper, December 2013, pp2-3.

139 See Queensland Government response to the Interdepartmental Committee on Electricity Sector Reform, p7 and p11.

140 Department of Energy and Water Supply, *The 30-year electricity strategy - Discussion paper*, September 2013, p10.

To overcome this, a new entrant retailer may have to spend more on marketing its products and developing a local presence (eg sponsorship of local sporting teams or community events).

- **Low levels of awareness amongst customers** about their ability to choose their own retailer given that choice has not really existed to date.

Further detail on how the latter two of these impediments could be addressed is set out in section 5.8.

5.4.2 Factors impeding entry into the gas retail market in regional Queensland

Unlike electricity, the retail gas market in Queensland is not subject to the UTP or to retail price regulation. The only impediments to entry in the Gladstone, Rockhampton and Wide Bay-Burnett region that retailers cited were therefore non-regulatory in nature.

One of the more significant non-regulatory factors that retailers claimed is deterring entry into these areas is the small size of the customer base. As noted in section 4.4.4, the size of a market will not, in and of itself, usually constitute a barrier to entry. However, if the costs of supplying that market are largely fixed or sunk (ie there are regional specific economies of scale associated with supplying that market), as the Commission understands there are in gas,[141] then the size of the market may place a cap on the number of retailers that can enter and effectively compete in the market. This is coupled with the fact that retailers are unable to attain any economies of scope by retailing both gas and electricity in these areas.

The other factor the Commission is aware may be affecting entry in these areas is the tightening demand and supply conditions in the wholesale gas market, which have been triggered by LNG developments and are reportedly making it 'extremely difficult' for retailers to secure competitively priced gas in Queensland. As outlined in section 4.4.4, these conditions are not expected to ease in the short to medium term. The Commission would therefore expect constraints on the availability of competitively priced gas in Queensland and continued uncertainty about how changes in the wholesale market will play out to continue to act as a barrier to entry in regional areas of Queensland in the short to medium term.

5.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

As explained above, the way in which the UTP is given effect impedes other retailers from entering the electricity retail market and earning a reasonable return.

141 K Lowe Consulting, *Gas Market Scoping Study*, a report for the AEMC, July 2013, pp42-45.

Consequently there is currently no rivalry in the electricity retail market for small customers.

Similarly, impediments to entry in the gas retail market have resulted in a single gas retailer supplying small customers in regional Queensland with reticulated natural gas (outside of Toowoomba and Oakey). Hence there is no rivalry in this market.

5.6 Customer outcomes

As an indicator of customer outcomes in the regional Queensland electricity market, we looked at trends in complaints made to Ergon Energy. We did not commission Newgate Research to analyse customer outcomes in regional Queensland as this research focussed on jurisdictions where multiple retailers are competing for small customers.

5.6.1 Complaints

The level of retail electricity complaints in regional Queensland (ie to or about Ergon Energy) is currently low compared to other jurisdictions and has remained relatively steady over the last few years. This is despite customers in regional Queensland experiencing considerable price rises over recent years.

A low number of complaints could be indicative of higher satisfaction than in other NEM jurisdictions. However, other reasons for fewer complaints could also include:

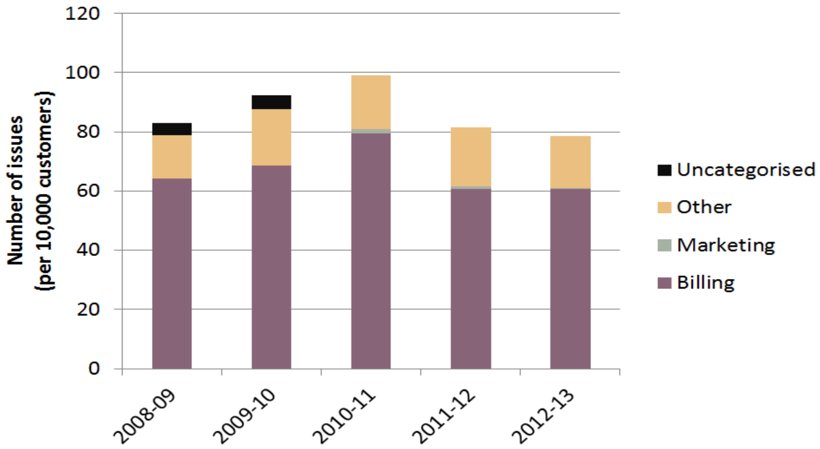
- there is limited or no marketing and no switching between retailers since there are no other retailers currently in the market and Ergon Energy cannot offer market contracts. Consequently there are no complaints relating to these issues; and
- customers in regional Queensland may have a higher level of disengagement than in other jurisdictions since electricity customers have no alternative retailer.

For gas, it is not possible to distinguish between complaints received by customers in regional Queensland versus those received in South East Queensland. This issue was therefore addressed in section 4.6.

Complaints to retailers

Figure 5.1 shows retail electricity issues raised with Ergon Energy. When a customer makes a complaint, multiple issues may be raised. Billing is consistently the largest retail issue category raised with Ergon Energy, making up 78 per cent of the retail issues raised with Ergon Energy in 2012-13.

Figure 5.1 Electricity issues raised with Ergon Energy (retail)

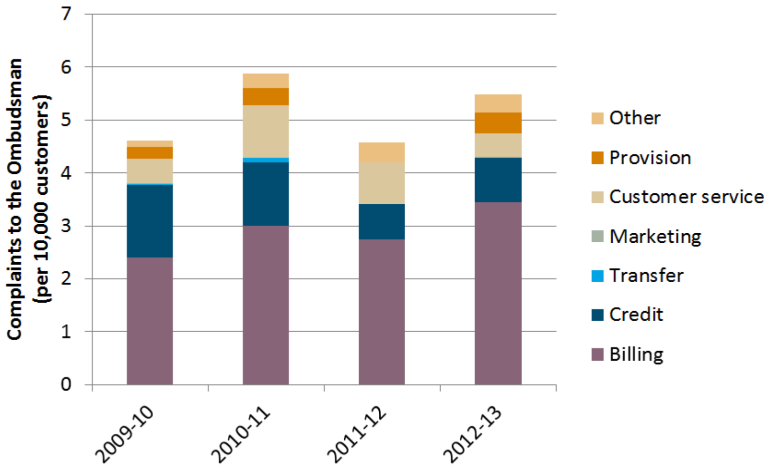


Source: Complaints data from Queensland Competition Authority, customer numbers estimated from QCA and AEMO data, AEMC analysis.

Complaints to the Ombudsman

In 2012-13, 391 retail electricity issues regarding Ergon Energy were raised with the Electricity and Water Ombudsman Queensland (EWOQ),[142] which equates to 5.5 issues per 10,000 customers (see Figure 5.2).[143] Sixty-three per cent of retail electricity complaints regarding Ergon Energy were related to billing. Note that issues raised with EWOQ include referrals back to retailers, which are also captured in complaints to retailers described above.

Figure 5.2 Electricity complaints to the Ombudsman – number of complaints – Regional Queensland



Source: Complaints data from EWOQ, *Annual Report 2012-13*, customer numbers estimated from QCA and AEMO data.

142 Energy and Water Ombudsman Queensland, *2012-2013 Annual Report*, 2013, p21.

143 Data on complaints to EWOQ excludes cases which were out of jurisdiction or not complaints.

5.7 Retailer outcomes

As discussed above, Ergon Energy is currently paid a subsidy, estimated to be $615 million in 2013-14. This is to compensate it for financial losses incurred in serving electricity customers in regional Queensland. Other retailers are not able to access this subsidy and so retailers cannot enter this market and offer a price at which they can compete with Ergon Energy. Consequently, margins do not appear to be sufficiently high in regional Queensland to support a competitive market.

There is limited information available on the profitability of retailing natural gas in regional Queensland. As discussed in section 4.7, there were a range of views put forward by retailers on the competitiveness and profitability of the gas market in South East Queensland. The median rating provided by retailers for profitability in South East Queensland was two, which was the same as for New South Wales and South Australia. Given the costs and risks of retailing gas in Wide Bay-Burnett, Gladstone and Rockhampton, it is likely that profitability for a new entrant in these areas would be rated lower than in South East Queensland.

5.8 Future developments

The main issue impacting competition in the regional Queensland electricity retail market is the way in which the UTP is given effect, which impedes entry by new retailers. In interviews, retailers have indicated that they do not expect any changes in the level of competition in regional Queensland for electricity until the UTP is removed or the way in which it is given effect is changed. For example, retailers considered that entry may occur if the subsidy is paid to the distribution network rather than the retailer, such that all retailers can compete on an even playing field.

The Queensland Government is currently considering ways in which competition in regional Queensland could be improved. In developing options, the following considerations will be relevant:

- the objective of the UTP and how that objective can best be achieved;
- the level and target of any continued subsidies;
- the mechanism that is used to deliver those subsidies to ensure they are reaching those customers that are identified as being in need;
- the consequences of any increase in prices as a result of moving customers off subsidies towards cost reflective tariffs;
- how to prevent price shocks for any customers that are transitioned to cost reflective pricing. Additional support may need to be considered for vulnerable and low-income customers; and

- how to continue to regulate electricity prices in the Ergon distribution network if the Queensland Government removes electricity retail price regulation in South East Queensland.

The way in which prices are regulated will also influence the development of competition. Price regulation can impede the development of effective competition if prices are set too low such that retailers cannot make a reasonable return on their investment. The AEMC has previously set out recommendations on an appropriate methodology for regulating retail prices in advice to the COAG Energy Council on Best Practice Retail Price Regulation.[144]

In other markets, including South East Queensland, part of the reform process has been to separate vertically integrated distribution/retail businesses and privatise the retail arm.[145] The Queensland Government has signalled an intention to sell Ergon Energy's retail arm in its 2014-15 Budget, subject to seeking a mandate at the next election.[146]

If this occurs, the government may wish to consider how this sale can best be conducted to promote competitive outcomes. This includes whether, and if so how, Ergon Energy's retail arm is divided and sold and whether Ergon Energy’s name should be changed to minimise the potential for brand loyalty to act as an impediment to entry or expansion.

If the UTP arrangements are changed such that new retailers are more likely to enter the market, an information campaign could help raise awareness amongst customers that they can choose their electricity retailer and so help them capture the benefits of greater competition.

While retailers have an incentive to raise awareness of retail competition, there is a role for the Queensland Government to ensure customers are aware of the options available, tools to help compare options and their rights and responsibilities. As discussed in Chapter 3, the AEMC developed a blueprint to assist the NSW Government in developing a campaign to improve customer engagement.

The recommendations set out in the blueprint are likely to be equally applicable to Queensland. However, two issues that are likely to be particularly important in regional Queensland are:

- **Informing customers that the reliability of supply will not change if they switch retailer.** In NSW we found that customers were concerned that supply

144 AEMC, *Advice on Best Practice Retail Price Regulation Methodology*, Final Report, AEMC, 27 September 2013, Sydney.

145 In Victoria the distribution businesses were also privatised. The Queensland Government has not proposed to sell its electricity transmission or distribution assets. However, it has proposed to allow private sector investment while retaining ownership of 100 per cent of the ordinary shares. See the Queensland Government's *The Strongest & Smartest Choice: Queensland's Plan for Secure Finances and a Strong Economy*, June 2014, pp26.

146 Queensland Government, *The Strongest & Smartest Choice: Queensland's Plan for Secure Finances and a Strong Economy*, June 2014, p27 and p33.

issues would not be resolved as promptly if they switched to another retailer.[147] This is likely to be an issue in regional Queensland, where customers may be familiar with "Ergon" as both their distributor and retailer. Consequently, customers need to know that their supply will not change if they change retailer.

- **Reaching a geographically dispersed population.** We recommended a number of ways in which to reach customers, particularly those that may not be captured by mass media or that may require additional support. For example, customers in regional or rural areas may be better targeted through local newspapers and Member of Parliament offices. Given the geographic dispersion of regional Queensland, some of these alternative means of reaching customers may be appropriate.

147 Newgate Research, *NSW Consumer and Stakeholder Research Report*, a report for the AEMC, September 2013, p26.

6 New South Wales

Box 6.1: Key findings

- Competition is effective in New South Wales electricity and gas retail markets, although less so in certain regional areas for gas. The New South Wales Government removed electricity retail price regulation on 1 July 2014. This should further increase competition through entry, expansion and innovation.
  - Customers can choose from a range of retailers and products, and many are shopping around. Three in ten customers looked for a better deal in 2013 and almost one in five changed their retailer. Others found a better deal with their existing retailer.
  - Fourteen retailers are competing to acquire and retain electricity customers. Two retailers have indicated they may enter the New South Wales electricity retail market and four second tier retailers may expand their existing activities.
  - The majority of customers surveyed are generally satisfied with their retailer and the quality of service they receive. Many customers want greater choice in the market, with some perceiving little difference between the offers available and many unaware of the extent of choice in the market.
- Competition is less intense but still effective for the majority of customers in the gas retail market, where four retailers compete. There are some customers in certain regional areas that continue to be served by a single retailer.
- Our findings for the New South Wales markets are consistent with our findings in the review the Commission completed in October 2013.

6.1 Overview

This is the second time the AEMC has performed a competition review for New South Wales (NSW) and our findings are broadly consistent with our previous review.

Our first review was completed in October 2013 (2013 NSW review) and found that competition is delivering benefits to small customers. The Commission recommended a package of measures to further enhance competitive outcomes, including the removal of retail price regulation and measures to increase customer participation through a ‘consumer engagement blueprint’.

In April 2014, the NSW government announced the removal of electricity price regulation from 1 July 2014. The majority of qualitative and quantitative information for this review was collected prior to the Government's announcement as our assessment of competition primarily focuses on the 2013 calendar year for all jurisdictions.

The findings for this 2014 review of NSW can be summarised as follows:

- **Customer activity:** Many customers are actively investigating options and there are high switching rates for electricity and gas. NSW has a relatively high proportion of customers on electricity standing offers.[148] Implementation of the consumer engagement blueprint developed in the AEMC's 2013 review could provide customers with the information and tools they need to switch to a market offer that suits their needs.

- **Barriers to entry, exit and expansion:** Retailers consider entry and exit relatively easy for the retail electricity and gas markets. Expansion was considered more difficult, primarily due to the retail price regulation in both markets, as well as upstream issues in the gas market.

- **Independent rivalry:** There is rivalry in the retail electricity market despite the high market concentration, with increasing activity of second tiers. Rivalry appears weaker for retail gas, particularly in regional areas.

- **Customer satisfaction:** Many customers are satisfied with the level of choice in the market and with their current retailer, though some perceive little difference between the choices available.

- **Retailer outcomes:** No new evidence has emerged for this review that would suggest outcomes for retailers have changed since the last review. Margins in the electricity and gas market appear to be consistent with a competitive market.

We have noted throughout the chapter where any changes in the competitive market indicators are evident since our previous review. These differences are marginal in most instances and primarily relate to customer research survey results.

Further improvement to the above competitive market indicators can be expected now that price regulation has been removed, but the full impact of this policy decision is unlikely to be evident over the short term as it will take time for retailers and consumers to respond to new opportunities.

148 Up until 1 July 2014, standing offers were generally the same as the regulated offer.

6.2 History and market characteristics

Full retail competition was introduced for retail electricity and gas markets in NSW in 2002. At this time, price regulation was retained for the retail electricity and gas markets.

The NSW Government removed retail price regulation for electricity on 1 July 2014. Customers on regulated prices that have not chosen a market contract have been transferred to a 'transitional tariff' for two years. The transitional tariff is 1.5 per cent lower in the first year than the previous regulated price and increases in line with the consumer price index the following year.[149]

Gas prices continue to be subject to voluntary price agreements between incumbent gas retailers and the Independent Pricing and Regulatory Tribunal (IPART).

In July 2013, NSW adopted the National Energy Customer Framework (NECF) subject to a number of derogations. Under the NECF, all electricity and gas retailers are required to offer a standing contract with regulated terms and conditions. Retailers can also offer market contracts that include minimum terms and conditions prescribed by law. The prices of standing and market contracts are determined by retailers and monitored by IPART.

6.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

Our analysis of this criterion considers analysis of data provided to the AEMC on customer switching, as well as findings from the following customer research conducted for this review and the 2013 NSW review:

- 2014 Newgate Research survey: a quantitative survey of small customers in NSW conducted by Newgate Research in early 2014 for this review;[150]
- 2013 Newgate Research: a survey and qualitative forums to inform the development of a consumer engagement blueprint in 2013;[151] and

---

149 NSW Department of Trade and Investment, http://www.resourcesandenergy.nsw.gov.au/energy-consumers/energy-sources/electricity/removal-of-electricity-price-regulation.

150 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014. See Chapter 2 for further discussion on our methodology. Newgate Research did not conduct qualitative forums in 2014 since these had recently been completed for the 2013 NSW review.

151 Newgate Research, *NSW Consumer and Stakeholder Research Report*, a report for the AEMC, 20 September 2013.

- Roy Morgan Research: surveys and qualitative research to inform analysis of the state of competition in NSW in 2013.[152]

Where customer survey statistics are discussed in this section, we are referring to the 2014 Newgate Research survey unless noted otherwise.

The Commission's analysis of the customer research findings suggests the following:

- **Most customers have chosen market offers, but many remain on standing offers.** Approximately 60 per cent of electricity customers and 70 per cent of gas customers are on market offers.[153] For electricity this is the lowest proportion of all jurisdictions that the Commission has found to have effective competition.

- **Many customers are investigating their options and choosing between different market offers**. Switching rates appear high for gas and electricity, with price the main trigger for switching retailer or plan. More can be done to improve awareness among customers in regional NSW that they have a choice of retailer and plan.

- **Some customers are less engaged** and are not interested in shopping around for a better deal, primarily because they are satisfied with their existing arrangements or they perceive little difference between the options available. Previous qualitative research suggests there is confusion among many customers about the options on offer and low awareness of comparison tools available.

- **The most confident customers surveyed are those who have recently investigated their options**. These customers were significantly more confident that they understood the energy options available in the market than those who had not done any research.

The Commission considers that customer activity in the market could further improve over the coming years following the removal of price regulation. Customers need to be appropriately informed and empowered to make it easier to compare offers and choose an energy plan that suits their needs. The AEMC developed a consumer engagement blueprint as part of the 2013 NSW competition review, which includes a series of actions to promote these outcomes.

6.3.1 Customer awareness and understanding

For customers to actively participate in the market, they first need to be aware of their choices. There was a high level of awareness among survey respondents that they have

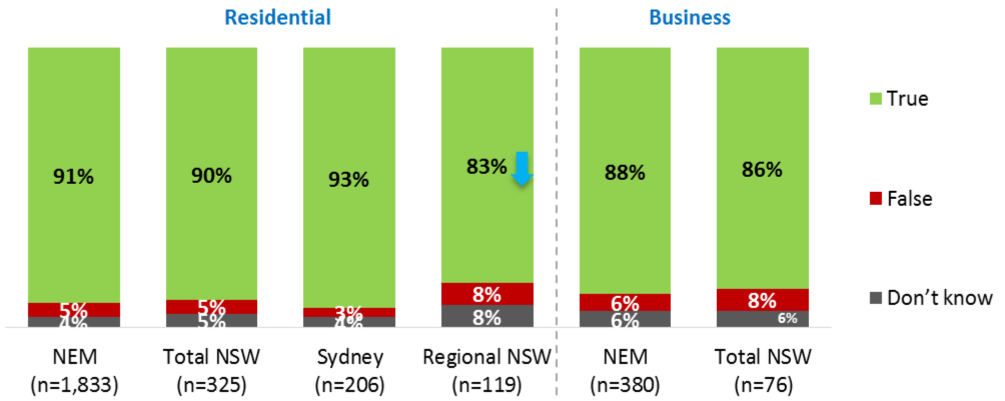
152 Roy Morgan Research, *Survey of Residential Customers of Electricity and Natural Gas in New South Wales: Effectiveness of Retail Competition*, report for the AEMC, February 28 2013; Roy Morgan Research, *Survey of Business Customers of Electricity and Natural Gas in New South Wales: Effectiveness of Competition*, report for the AEMC, February 28, 2013; and Roy Morgan Research, *Retail competition in the NSW Electricity and Natural Gas markets: Focus Groups with Residential and Small Business Customers*, a report for the AEMC, February 28, 2013.

153 Data provided by the Australian Energy Regulator (AER).

a choice between multiple retailers and plans in the market. Of those surveyed in NSW in 2014, around 90 per cent of electricity customers and 85 per cent of gas customers were aware they could choose their retailer. This was similar to Roy Morgan's survey results in 2013.

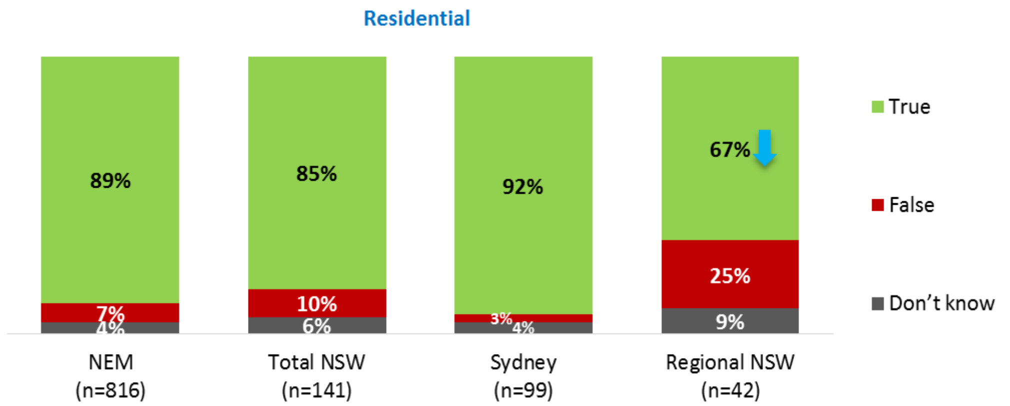
As can be seen in Figure 6.1 and Figure 6.2 below, there was lower awareness among energy customers in regional NSW relative to Sydney and the regional areas in the other NEM jurisdictions surveyed. The arrow indicates a result that is statistically different from the NEM average at the 95 per cent confidence level.

Figure 6.1 Awareness of being able to choose electricity retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, June 2014, p124. Survey question: Do you think it is true or false that consumers in your state [territory] can choose their electricity company. Customers surveyed: All.

Figure 6.2 Awareness of being able to choose gas retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, June 2014, p125. Survey question: Do you think it is true or false that consumers in your state [territory] can choose their gas company. Customers surveyed: Customers who have mains connected gas.

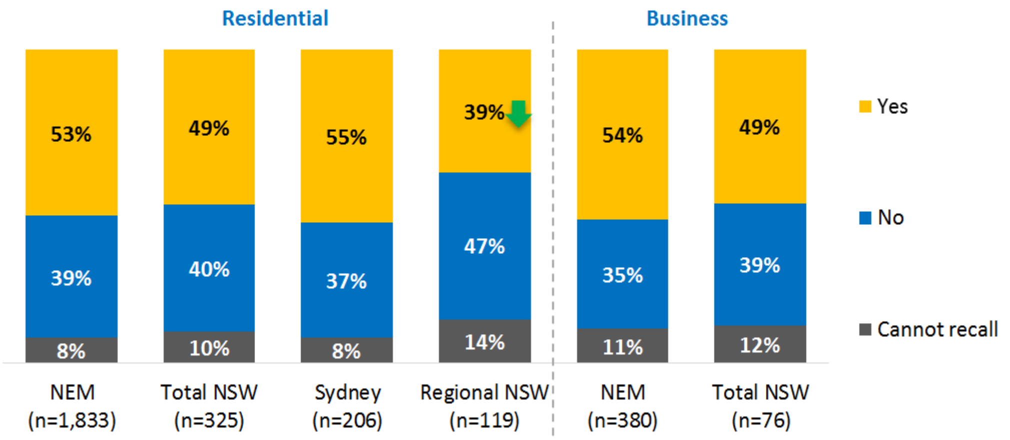
Eighty-three per cent of regional customers were aware they have a choice of electricity retailer, which is significantly lower than in any other regional area surveyed in the NEM but close to the 2013 survey result of 86 per cent.

Of the regional gas customers surveyed, 67 per cent were aware that they could choose their retailer in the 2014 survey compared to 78 per cent in the 2013 Roy Morgan survey. This suggests that regional areas should be a particular target for information campaigns.

Most customers were aware that they could choose from a range of different energy plans, though numbers were again slightly lower for the regional customers surveyed. In Sydney, 86 per cent of customers were aware they could choose from a range of different plans compared to 72 per cent in regional NSW. These results are broadly comparable to the 2013 Roy Morgan survey.

Retailer marketing activity can be responsible for generating awareness among customers that they have a choice between retailers and plans. It is possible the lower awareness among customers in regional NSW reflects a lower level of retailer activity in these areas. As shown in Figure 6.3, fewer regional customers reported being approached by retailers relative to customers in Sydney, and relative to in regional areas in other NEM jurisdictions.

Figure 6.3 Customers approached by an energy retailer in past 12 months



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, 2014, p128. Survey question: In the past 12 months have you been approached by an energy company offering to see you electricity or gas? Customers surveyed: All.

In order for customers to shop around, it is important they have confidence in their ability to investigate and understand the options available to them. Confidence levels were comparable with other jurisdictions, with 80 per cent of customers surveyed in NSW stating they were at least 'fairly' confident that they understood the different offers and options available. Of these customers, just over half were 'quite' or 'very' confident they understood their options. Confidence levels were similar for Sydney and regional customers.

Confidence was highest among customers with solar panels and customers who had investigated their options in the past 12 months. These survey results suggest that, for some customers, the information available on their energy options is not too complex to present a barrier to switching. Customers may feel more confident about switching plan or retailer if they are encouraged to take the first step of investigating the options available to them. .

Qualitative research in other jurisdictions and in the Newgate Research forums in 2013 suggest that confidence levels can overstate actual knowledge of the different features of energy plans and bill components.

> "It's a nightmare trying to read an electricity bill. All of them are different, and different retailers use different terms. It's very confusing…The bills are designed for accountants running a database, not for people to understand their consumption and how they are being charged. They are not accessible and they are not readable. On the bill it says 'residential control load 2' but who would know that is actually their off-peak hot water cost?"
>
> "When I called up (my electricity retailer) they started talking about kilowatts and I had no idea what they were talking about. They should explain that to customers and what it all means so that we can compare prices. I had no idea.[154]"

The 2014 Newgate survey and 2013 Newgate survey also suggest low awareness of the extent of choice in the market. Survey respondents considerably underestimated the number of retailers in the market and most forum participants were surprised when they saw the list of energy companies offering plans in their area.[155]

6.3.2 Customers investigating offers and switching

For a market to be effectively competitive, it is not sufficient for customers simply to be aware of their ability to choose their retailer. They also need to have the right information and tools to investigate their options and switch plan or retailer where they may receive a lower price or better service.

Evidence suggests that a considerable proportion of the market are investigating their options and switching plans or retailers in NSW.

Close to one quarter of residential customers had actively investigated energy options to switch to in the past 12 months. Results were higher for small business customers at 41 per cent, which is consistent with the NEM average for small businesses.

More than half of all customers surveyed in NSW reported they had switched electricity retailer or plan in the last five years, with an average of between one and two switches during that time. This is higher than the reported switching rates for service providers of car insurance, phone, internet, banking, home insurance or health insurance. Switching was marginally higher in Sydney, with 63 per cent of Sydney

---

154 Newgate Research, *NSW Consumer and Stakeholder Research Report*, a report for the AEMC, 20 September 2013, p22.

155 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, pp124-125. Newgate Research, *NSW Consumer and Stakeholder Research Report*, a report for the AEMC, 20 September 2013, p26.

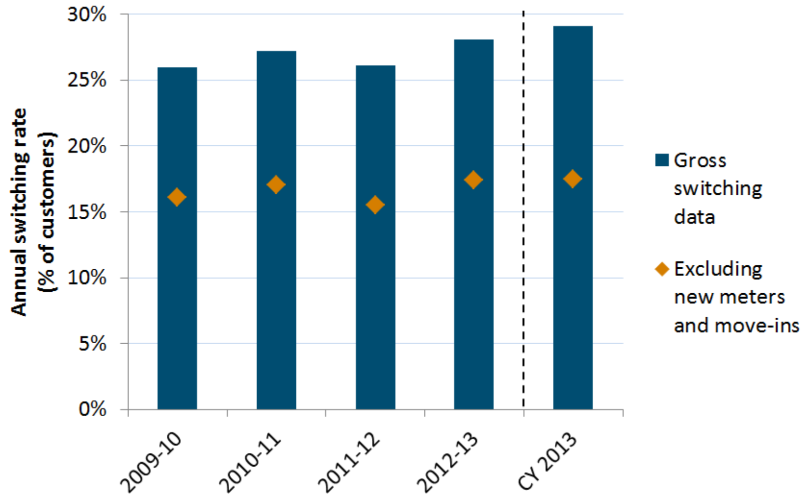
customers switching electricity retailer or plan in the last five years compared to 56 per cent in regional areas.

Switching was similarly high for gas customers. Forty-eight per cent of gas customers reported changing their gas retailer or plan in the last five years. This is considerably higher than in other NEM jurisdictions surveyed, with the exception of Victoria where 56 per cent reported switched gas plan or retailer over the same period.

Data on customer transfers between retailers for electricity in Figure 6.4 and for gas in Figure 6.6 also illustrates high customer switching rates.[156] This data should be interpreted with caution, as discussed in Chapter 2, but can provide an indication of the level of customer activity in a market.

For electricity, the average gross switching rate during 2013 was 18 per cent. Much of the switching activity in 2013 occurred in the first half of the year, when retailers were competing strongly on price. Aggressive discounting appears to have reduced and there were lower switching rates in the latter part of 2013. Switching rates may increase again following the removal of retail price regulation, with some retailers reportedly planning to increase marketing activity in NSW. This is further discussed in section 6.4.1.

Figure 6.4 History of electricity customer switching rates - NSW

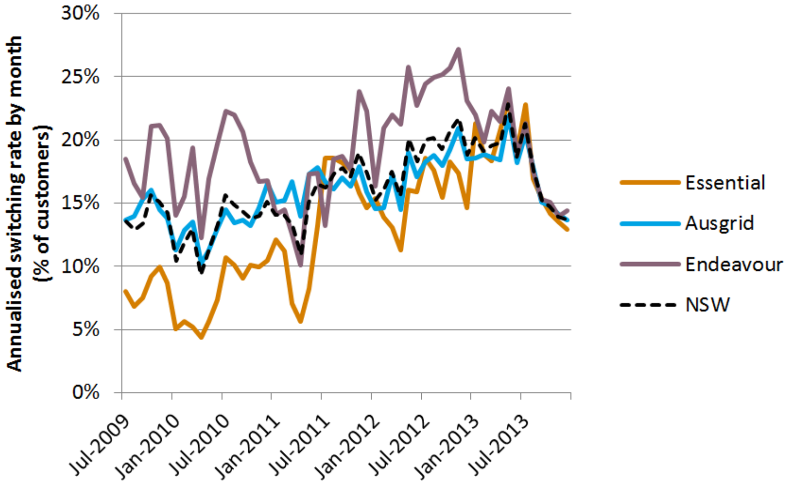


Source: AEMO data, AEMC analysis.

Switching rates for electricity were historically lower in regional areas, represented by Essential Energy's distribution network area (formerly Country Energy). However, switching rates in regional areas have broadly matched those in urban areas since the three formerly integrated distribution and retail businesses were separated and the retail businesses sold in March 2011. This is demonstrated in Figure 6.5 below.

156 See Chapter 2 for a discussion of the limitations of this data.

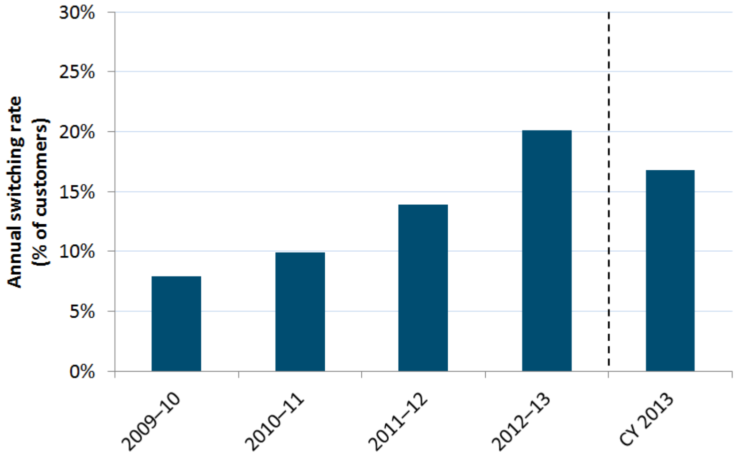
Figure 6.5 Electricity switching rates by distribution network area



Source: AEMO data, AEMC analysis.

Gas switching broadly mirrors electricity switching with the switching rate increasing over the past 5 years. The average gas switching rate for 2013 was close to 17 per cent, which is just below the switching rate for electricity. The majority of gas switching occurs on the Jemena distribution network, which covers Sydney and its surrounds, as well as some regional towns.

Figure 6.6 Gas switching rate - NSW



Source: AER, *State of the Energy Market 2013*, 2013 and AER Retail Statistics[157].

Switching data for electricity and gas does not capture customers who have actively investigated their options and either chosen to remain on their existing plan or have chosen to switch plans with their existing retailer. Data provided by retailers suggests that up to 30 per cent of a retailer's customers changed their electricity plan with that retailer in 2013. For gas, up to 24 per cent of a retailer's customers changed plans with their retailer.[158]

157 http://www.aer.gov.au/Industry-information/industry-statistics/retail

158 Some retailers cautioned that these estimates are indicative only.

Price appears to be the key driver for switching behaviour

Customer surveys suggest the key reason for switching energy retailer or plan in all NEM jurisdictions was to obtain a better price. In NSW, close to 60 per cent of residential and business customers stated that price was the main reason they switched electricity retailer or plan. Similarly for gas, half of the NSW residents surveyed who had switched gas retailer or plan did so for price reasons.[159]

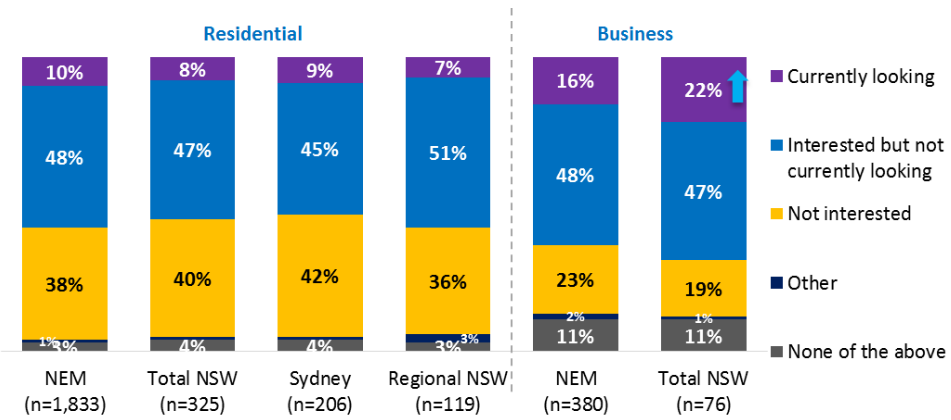
A distant second to obtaining a better electricity price was moving house, with 12 per cent of respondents citing this as their key reason for switching electricity retailer or plan. For gas, the second most common reason for switching retailer or plan was to have gas and electricity with the same retailer with 13 per cent of residents citing this reason.

Poor customer service was cited by four per cent of residents and seven per cent of businesses who changed electricity retailer or plan. This was also the key reason cited by three per cent of gas customers who changed retailer or plan.

Some customers are less engaged

Most customers surveyed expressed an interest in energy issues, energy prices and investigating their energy options. While there is a high level of participation in the market, there is a considerable proportion of customers who are less engaged. Forty per cent of residents and 19 per cent of businesses surveyed in NSW stated they had no interest in looking for a better deal. This is just slightly above the NEM average for residents and slightly below the average for small business.

Figure 6.7 Interest in looking for a better deal



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, 2014, p141. Survey question: When it comes to your household's energy company, which of the following statements is most applicable to your household? Customers surveyed: All.

For many, this may reflect satisfaction with their existing arrangements which appears to be a common reason across all NEM states for not investigating options or

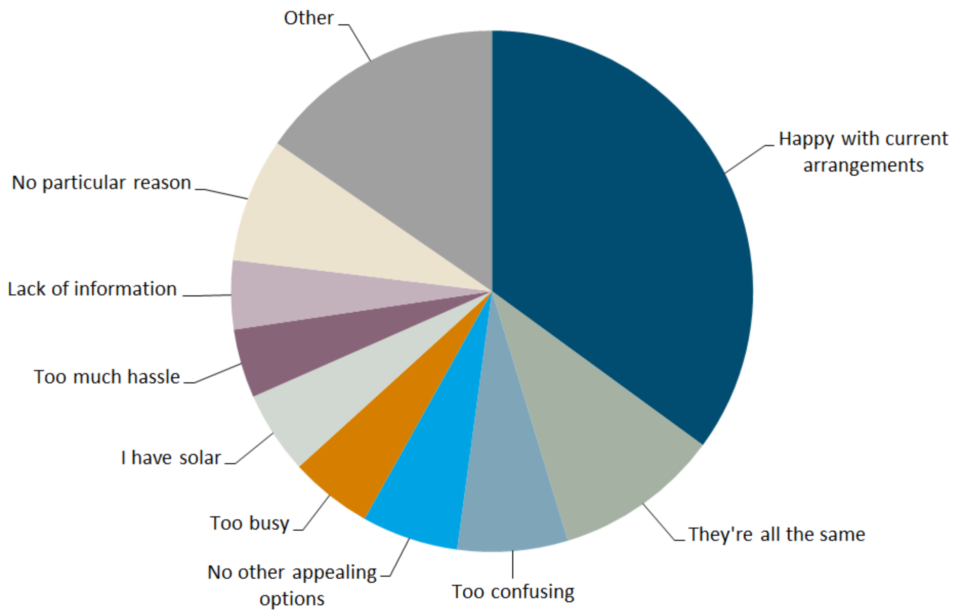
159 Unlike the results for electricity, results for gas only include responses from residents as the sample size was too small for business customers.

switching. For others, it could reflect perceptions about the lack of appealing alternatives in the market.

It is possible that some customers do not want to investigate deals or switch in the next twelve months if they have already recently done so. Close to one quarter of residential customers surveyed had already investigated options in the last twelve months.

Of NSW customers who had not investigated options in the last 12 months or switched retailer or plan in the last five years, 41 per cent stated it was because they were happy with their current arrangements, followed by 12 per cent who considered that all retailers were the same and switching would make no difference to the price they paid. Figure 6.8 shows the most common reasons cited.

Figure 6.8 Most common reasons for not investigating or switching



Source: Data from Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p134. Survey question: Are there any reasons why you haven't investigated different options or why you haven't changed your energy company or plan in the last few years? Customers could select multiple responses. Customers surveyed: Customers who hadn't investigated options or changed their energy company.

Perceptions that all offers are the same could be misconceived for certain customers. In particular, there may be differences for the 40 per cent of NSW customers on standing offers if they switch to a market offer, as suggested by AEMC analysis summarised in Box 6.2 below.

Box 6.2: Potential savings from moving off a standing offer to a market offer

The AEMC's 2013 Residential Electricity Price Trends report found that the average residential customer in NSW may have saved around $190 or nine per cent off their total annual bills by switching from a standing offer to a market offer in 2012-13.[160] This does not capture the full savings which could be made by switching to the lowest advertised market offer or by negotiating with retailers to obtain lower prices than those advertised.

The AEMC's survey of offers available as at 31 March 2014 also shows a reasonable degree of difference between the various offers available. This product differentiation is discussed further in section 6.5.2 below.

NSW had the highest proportion of respondents of all the NEM jurisdictions surveyed who cited having solar arrangements as their main reason for not investigating options or switching, though this was still a relatively small proportion at five per cent of respondents. Considerably fewer customers in NSW relative to the other jurisdictions cited being "too busy" or it being "too much hassle" as their main reason for not investigating or switching. These were the second most common reasons cited in most other jurisdictions surveyed.

Some of the customer issues highlighted above could be addressed through promoting greater awareness of the Energy Made Easy price comparator website. This is an independent, government website that can help reduce the time and complexity of finding and comparing energy plans.[161] The comparator website can also highlight that all plans are not the same and there may be some appealing alternatives available for customers.

Customers that are more engaged may also benefit from using this website to help them compare offers. All customers should be encouraged to reassess their energy needs and shop around regularly to take advantage of new offers or move to more suitable plans as their energy needs change.

There was very low awareness of the Energy Made Easy website among survey respondents. Just one per cent of businesses and none of the residential respondents mentioned the website without prompting. When prompted, ten per cent of residents and 13 per cent of small business customers said they had heard of the site. The possible benefits of promoting greater awareness of the independent price comparator websites are discussed further in Chapter 3. Improving awareness of the availability of

160 Nine per cent would be saved by switching from a representative standing offer to a representative market offer. The representative standing offer is based on a population weighted average of the regulated offer for each distribution region. The representative market offer is a population weighted average across the distribution regions using retailers' lowest generally available offers for each region, as nominated by retailers.

161 www.energymadeeasy.gov.au

this website is just one part of a broader customer engagement blueprint developed by the AEMC in 2013 for the NSW Government.

6.4 Retailer barriers to entry, exit and expansion

Barriers to entry, exit and expansion are another important indicator of the state of competition. Low barriers to entry and expansion place competitive pressure on retailers due to the threat of new entrants or other incumbents attracting away customers. These competitive pressures should lead to retailers charging prices that are commensurate with their costs and providing customers with the products and services that they demand.

Our analysis of this criterion considers key findings from retailer interviews and surveys conducted by consultants engaged for this review, K Lowe Consulting and Farrier Swier Consulting.[162]

Eleven of the 14 energy retailers that are currently active in NSW agreed to participate in the retailer interview and/or survey process.[163]

One of the key issues that these retailers were asked to provide their opinion on is the ease with which entry and expansion can occur in gas and electricity retail markets in NSW. Retailers were also asked whether they plan to enter, expand or exit either market in the next five years.

The interview and survey process was conducted prior to the NSW Government's announcement that electricity retail price regulation would be removed on 1 July 2014. It is possible therefore that the views expressed by retailers on entry and expansion conditions in the NSW retail electricity market may have changed since the interviews and surveys were carried out. This should be considered when interpreting the following responses:

- **Electricity retail market** – Entry into the electricity retail market was considered reasonably easy by retailers, while expansion was considered more difficult.[164] The main impediment to entry and expansion that retailers identified in this market was retail price regulation, although a number of other non-regulatory impediments were also cited.

- **Gas retail market** – Entry into the gas retail market was considered reasonably easy by retailers, while expansion was considered more difficult. The main impediments to entry and expansion that retailers identified in this market were retail price regulation, access to some pipelines and conditions in the wholesale

162 For full details refer to K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014.

163 As at December 2013, AGL owned Australian Power and Gas and Powerdirect and these are treated as one retailer for our analysis of competition in the market.

164 Smaller retailers attributed the difference between entry and expansion conditions to prudential and credit support requirements, which can become more significant as retailers expand. Larger retailers, on the other hand, claimed that 'vigorous competition' can act as a barrier to expansion.

gas market. Retailers also noted that entry can be more difficult in some regional areas because of the small size of the customer base in these areas and constraints on the availability of capacity on some regional pipelines.

The views expressed by retailers on entry and expansion conditions in these two markets are broadly consistent with our observations on the level of entry that has occurred in the last two years and the success that second tier retailers have had in expanding their activities in NSW over this period, as outlined below:

- **Electricity retail market** – In the last two years three second tier retailers[165] have entered the electricity retail market, which is indicative of relatively low barriers to entry. Second tier retailers also appear to have had some success expanding in this market over the last two years, which suggests that the barriers to expansion are relatively low.

- **Gas retail market** – In the last two years just one second tier retailer[166] has started supplying gas to customers in the Sydney area, which suggests that the barriers to entry in this market are higher than they are in the NSW electricity retail market and the Victorian gas retail market. In regional areas, like Wagga Wagga, Tamworth and Albury, it would appear that there has been no new entry in the last two years and that the host retailer remains the dominant retailer in these areas.[167]

The views expressed by retailers and the observations set out above are also broadly consistent with the findings of the Commission's 2013 review of the effectiveness of retail competition in NSW. This review found there are no significant barriers to entry or expansion in the retail electricity market but there were some barriers to entry in the retail gas market.[168]

6.4.1 Factors potentially affecting entry and expansion in the electricity retail market

In general, retailers view the NSW electricity retail market as a relatively attractive market in terms of its size and the degree of regulatory and political stability. Concerns were raised though during the retailer interviews about the effect that the following factors have had on entry and expansion:

- **Retail price regulation** – The ongoing application of retail price regulation was considered the most significant impediment to entry and expansion by retailers, with a number of retailers noting that further entry was likely to occur once it was removed. As noted previously, the retailer interviews were conducted before

165 The second tier retailers that have entered in this period are Click Energy, Momentum Energy and QEnergy.

166 Lumo Energy is the only retailer that has entered in this period.

167 Envestra, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p3.

168 AEMC, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, Draft Report, 23 May 2013, p29 and p67.

the NSW Government's announcement that electricity retail price regulation would be removed on 1 July 2014.

- **Brand loyalty to EnergyAustralia and Origin Energy** – Although not considered a significant impediment, a number of smaller retailers noted that customers exhibited some degree of loyalty to EnergyAustralia and Origin Energy and claimed that this was reinforced by the confusion some customers have about the relationship between retailers and distributors. While it is possible that some small customers may be confused about the choices available to them, brand loyalty was not raised as a significant issue in the customer survey. The fact that EnergyAustralia's and Origin Energy's market shares have been declining over the last two years also suggests that this is not a significant barrier to entry or expansion.

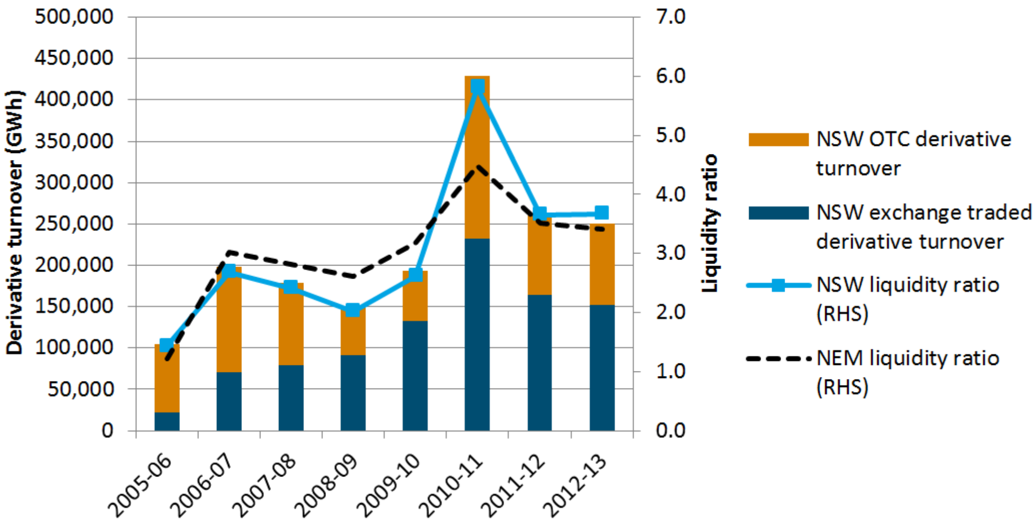
- **Credit support requirements** – This perceived impediment is not unique to NSW and has been raised by retailers as a potential impediment to entry and expansion in all jurisdictions. The Commission's views on this perceived impediment are set out in Chapter 3.

During the interviews, retailers were asked whether access to hedging instruments in NSW had affected entry and/or expansion conditions in the NSW retail market or was likely to do so in the future. The responses to this question suggest that this has not been a significant issue to date. While, some retailers have reportedly had difficulties obtaining over the counter (OTC) products from NSW Government owned generators, they have been able to overcome this impediment by using interregional hedges, or having recourse to financial intermediaries and/or the futures market.

The response provided by retailers to this question is consistent with the conclusion the Commission reached in the 2013 review, which was that access to competitively priced hedging instruments was not impeding entry or expansion in the NSW retail electricity market. The observation that retailers made about being able to have recourse to the futures market is also consistent with our own analysis of the degree of liquidity in this market, which in 2012-13 was higher than the NEM average (see Figure 6.9).[169]

169 Section 2.3 sets out why this data should be interpreted with caution.

Figure 6.9 Annual electricity derivatives turnover and liquidity ratios



Source: AEMO *National Electricity Forecasting Report*, the Australian Financial Markets Association (AFMA), *Australian Financial Markets Report* and ASX Energy.

While access to hedging instruments has not been an issue to date, concerns were raised by a small number of retailers about the potential for this to change in the future if AGL acquires Macquarie Generation.[170] This view was not universally held, as the following comments from two small retailers interviewed highlight:

> "If AGL doesn't acquire Macquarie Generation, AGL would eventually reach a maximum number of customers that it could service without having generation and this could adversely affect competition. That is, because Origin Energy and EnergyAustralia would be the only retailers able to compete at the larger scale, which, in effect, would result in a duopoly in the state. Such an outcome could be worse for customers. "

> "If AGL acquires Macquarie Generation there will be scraps and crumbs for smaller players, but not enough access to hedging instruments to underpin a fourth big player."

The Commission also notes the Australian Competition Tribunal's (the Tribunal) comments on the ability of retailers to compete in its decision to permit AGL's acquisition of the key assets of Macquarie Generation. The Tribunal stated:[171]

> "Whilst [the Tribunal] accepts that the number of small retailers in NSW is significantly less than that in Victoria...the probable cause of that relatively lower participation of smaller retailers is, in part, the consequence of retail price regulation. The Tribunal also accepts that the consequence of retail price regulation may have been to limit the "head room" between the retail

170 Interviews took place before the Australian Competition Tribunal decision allowing the acquisition to proceed.

171 Application for Authorisation of Acquisition of Macquarie Generation by AGL Energy Limited [2014] ACompT 1 [26].

price (the regulated price) and all the costs incurred by second tier retailers in servicing their customers. While the Tribunal appreciates that the price of acquiring hedges is a significant component of retail cost, it is of the view that the lower market penetration achieved to date by second tier retailers in NSW compared with Victoria is not caused by a tight market for hedges in NSW."

The Tribunal went on to state that "retailers of electricity in NSW, including small retailers, will still have available a significant competitive "market" in NSW for the acquisition of hedge contracts".[172]

6.4.2 Factors potentially affecting entry and expansion in the gas retail market

To retail gas in NSW, a retailer must enter into gas supply and transportation contracts and participate in the short term trading market (STTM). Entry into all of these contractual and market arrangements can involve relatively high transaction costs. When coupled with the fact that the prices payable under gas supply and transportation contracts tend to be predominantly fixed, it is not surprising that entry into the NSW gas retail market is considered more difficult than in Victoria, which operates under a different transportation and balancing market model.

The other reason that Victoria may be easier to enter than NSW is that the penetration of gas and overall consumption by small customers is far higher in Victoria than it is in NSW.[173]

Some of the other factors that retailers claimed may impede entry and/or expansion in the NSW retail gas market are:

- retail price regulation, which the NSW Government has decided to retain for gas (albeit a relatively light-handed form of regulation);
- access to the Eastern Gas Pipeline;
- tightening demand and supply conditions in the wholesale gas market, which has been triggered by the development of LNG facilities in Queensland; and
- the small size of the customer base in some regional areas and constraints on the availability of capacity on some regional pipelines.

---

172 Application for Authorisation of Acquisition of Macquarie Generation by AGL Energy Limited [2014] ACompT 1 [27].

173 The penetration of gas in Sydney has been estimated by the Australian Bureau of Statistics (ABS) to be 48 per cent whereas the penetration rate in Melbourne is estimated to be 91 per cent. The overall consumption of gas by residential customers in Victoria is also far higher than it is in NSW, with the Bureau of Resources and Energy Economics (BREE) estimating that in 2011-12 residential customers in Victoria consumed over 100 PJ of gas while their counterparts in NSW consumed 25 PJ. BREE, *2013 Energy Consumption by Industry and Fuel Type*, Table F (2011-12) and ABS, 4602.0.55.001 *Environmental Issues: Energy Use and Conservation*, March 2011, Table 6.

The concerns raised by retailers in this context about retail price regulation are identical to those raised in other jurisdictions where retail price regulation continues to be applied. The remainder of this section focuses on the last three impediments cited by retailers.

Access to transmission pipelines

During the retailer interviews, one retailer noted that it can be difficult for small retailers to secure a firm transportation service on the Eastern Gas Pipeline (EGP) for small and/or variable volumes of gas. While this may appear to be an impediment for smaller retailers, the Commission understands that there are other options that retailers can use to transport gas from Victoria to NSW.

Gas can currently be supplied to NSW from the Cooper/Eromanga and the Bowen/Surat basins via the Moomba to Sydney Pipeline (MSP) or the Gippsland, Otway and/or Bass basins in Victoria via the EGP or the Victorian Transmission System (VTS) and the MSP. Retailers can also enter into an arrangement with another user on the EGP to transport the gas on its behalf. This therefore does not appear to constitute an insurmountable barrier to entry.[174]

Conditions in the wholesale gas market

In the interview and survey process, a number of retailers noted the potential for conditions in the wholesale gas market to deter new entry in some retail gas markets until conditions in the wholesale market 'settle down.' NSW is one of the markets that retailers claimed was likely to be affected by the changes. This is because of its historic reliance on gas supplied from the Cooper and Bowen/Surat basins, both of which are now largely committed to the LNG developments.

The Commission is aware that there is currently a high degree of uncertainty about how conditions in the wholesale gas market are likely to play out in the short to medium term. This creates uncertainty about wholesale gas prices in some jurisdictions and, in turn, the demand for gas by small customers. Faced with this level of uncertainty, it is quite possible that prospective entrants into the NSW retail gas market could decide to defer their entry until conditions in the wholesale gas market ease. Consequently conditions in the wholesale gas market may impede entry into this market until conditions become more certain.

Constraints in regional and rural areas

During the interviews, a number of retailers noted that entry into regional areas of NSW can be more difficult because:

---

174 Expansions have recently occurred in the VTS to enable the transport of a greater quantity of gas out of Victoria into NSW via the MSP, so there doesn't appear to be binding capacity constraints on this alternative, and there will be some capacity on the MSP flowing south from the Cooper/Eromanga and Bowen/Surat basins.

- the size of the customer base in these areas is too small to make entry by a large number of retailers economically viable given the fixed cost nature of retailing gas; and/or

- the capacity of the regional pipelines has been fully contracted by a single retailer or a small number of retailers.

Information provided by Envestra[175] also indicates that the host retailer is still the dominant retailer in the regional areas of NSW that Envestra services (ie Wagga Wagga and Albury).

Economies of scale appear more important in gas retailing than they are in electricity retailing and they tend to be region specific because of the fixed costs associated with transporting gas to particular locations. Analysis undertaken for the 2013 NSW review suggested that there may be other structural barriers limiting entry in some regional areas.[176] Consequently the small size of the customer base in some regional areas, and other structural factors, may act as barriers to entry and/or expansion in these areas.

6.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

Our analysis of this criterion considered findings from retailer interviews and advertised market offers, which suggest the following:

- **Market concentration is high** in NSW and product differentiation is not as varied as some other states, but other indicators suggest that there is a sufficient level of independent rivalry indicative of effective competition.

- **Second tier retailers are gaining market share.** There are now 14 active electricity retailers and an increasing proportion of switches involve customer transfers from the largest three incumbent retailers to smaller, second tier retailers.

- **Retailers are differentiating their market offers** based on discounts and non-price incentives. The level of differentiation is expected to further increase with the removal of retail price regulation.

- **Rivalry appears weaker in the gas market, particularly in regional NSW** with only one retailer operating in some areas.

175 Envestra, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p2.

176 AEMC, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, Final Report, 3 October 2013, p51.

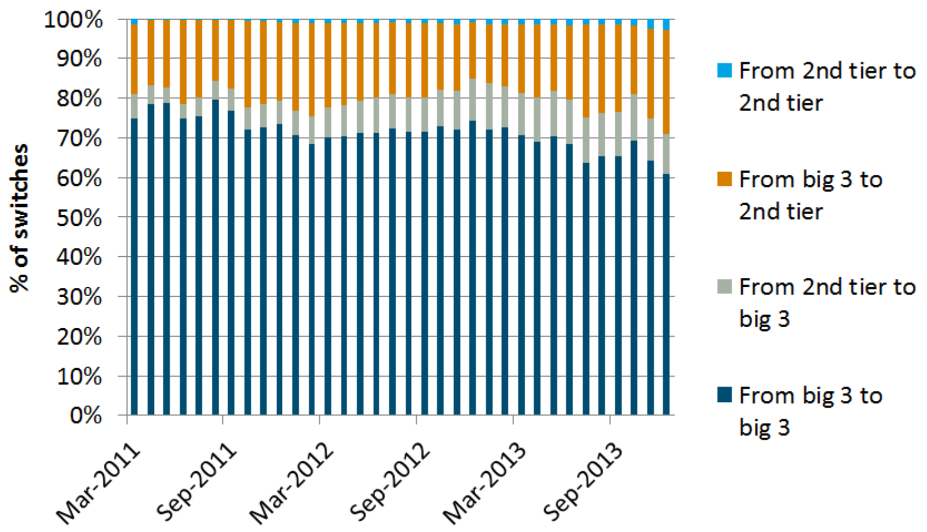
6.5.1 Market share and concentration

There are 14 active retailers in the small customer market, four of which also offer gas. However, AGL and ActewAGL do not compete within each other's supply areas. All electricity retailers report operating in both urban and regional areas of NSW with the exception of one retailer that operates only in the Ausgrid network area and one that operates in the Essential and Endeavour network areas.

Market concentration as measured by the Herfindahl-Hirschman Index (HHI) is reasonably high for electricity at 3,096.[177] Of the "big three" retailers,[178] Origin Energy has the largest market share at close to 40 per cent, followed by EnergyAustralia and AGL. Their collective market share is around 97 per cent of the electricity market.[179]

Despite the market concentration, data suggests there is considerable rivalry between electricity retailers. The Australian Competition Tribunal has also highlighted the significant competition in NSW between all retailers, big and small.[180] Data on customers switching between the big three and other retailers shows the increasing activity of second tier retailers in the retail electricity market, as illustrated in Figure 6.10. Second tier electricity retailers appear to be progressively attracting customers away from the big three. Switching between the big three retailers has been declining overall since October 2011 and there are some signs that rivalry between second tier retailers is emerging.

Figure 6.10 Electricity switching rates by tier in NSW



Source: AEMO data, AEMC analysis.

177 The HHI maximum is 10,000, which represents a pure monopoly market. The ACCC uses a score of 2000 as a threshold when considering the level of competition for merger assessments.

178 Throughout this report, the "big three" retailers refers to Origin Energy, EnergyAustralia, and AGL.

179 AER, *State of the Energy Market 2013*, 2013, p122.

180 Application for Authorisation of Acquisition of Macquarie Generation by AGL Energy Limited [2014] ACompT 1 [361].

The gas retail market has a slightly higher level of market concentration with an HHI of 4,192. The big three retailers offer gas in NSW as well as two second tier gas retailers, Lumo and ActewAGL (noting that ActewAGL does not compete in AGL's supply areas). AGL has the largest market share, at approximately 65 per cent, and the big three retailers have a collective market share of close to 100 per cent.

Of the NSW gas customers who switched retailer in 2013, most switched between the big three retailers.

6.5.2 Product differentiation

Retailers interviewed stated that NSW has a limited degree of product differentiation and innovation. They attributed this to retail price regulation (which has since been lifted) and the small number of smart meters in the state.[181] Our analysis of offers available as at 31 March 2014 supports this view. There is a high number of offers advertised in NSW but there is limited differentiation and innovation between these offers, with retailers mainly differentiating in terms of the level of discount offered and cash rebates.

In addition to the features discussed below, retailers also differentiate their brand through service quality such as call centre operation hours, information provision, policies on hardship and complaints, policies on door knocking and cold calling, online account access and, in some cases, shopfronts for customers to visit and discuss their options.

Standing offers

Retailers are required to offer a contract with regulated terms and conditions known as a 'standing offer'. As at 31 March 2014, there were 12 standing offers[182] and one regulated offer advertised on the Energy Made Easy website for residential Sydney customers. The tariffs for these offers were very close to the tariffs for market offers without discounts.

Electricity market offers

As at 31 March 2014, the Energy Made Easy website showed 31 market offers. Many of these were very similar in terms of their tariff structures, discounts, contract types and other features. Key differences between the offers available are summarised in Table 6.1.

181 K Lowe Consulting and Farrier Swier Consulting, *AEMC Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p17.

182 Diamond Energy offers a standing offer that was not listed on the Energy Made Easy website. One NSW retailer only offers electricity to small business customers and an additional two retailers offer electricity in the Endeavour and/or Essential distribution network areas but not in the Ausgrid distribution network area.

Table 6.1 Differences in electricity offers in Sydney as at 31 March 2014

Difference between offers *(high number of offers: >30; moderate: 15-30; low: 0-15)*	
Time of use tariffs	High number of time of use offers available, but very low level of differentiation between offers. All analysed appeared to have the same structure, and many had identical prices. Some offers had slight variations with regards to the pricing structure they used.
Other tariffs	High number of offers with a low level of difference. Most tariff structures were inclining block tariffs with identical or very similar structures. A small number of flat tariffs were also available.
Discounts	High number of offers with high level of difference. Unconditional discounts ranged from 3-10 per cent off usage charges. Conditional discounts ranged from 1-20 per cent off usage and include discounts for paying on time, signing up to direct debit or receiving bills by direct debit.
Contract duration	High number of offers with low level of difference. Fixed term contracts were for 1 or 2 years. A high number of offers had no fixed term.
Non-price incentives	Moderate number of offers with non-price incentives with a moderate level of differentiation. Options include: • bonus sign-up rebates from $20 - $50; • bonus $20 rebate for signing up to direct debit; • store vouchers; • frequent flyer points; • no risk offer - no termination fee if the retailer cannot beat a better offer; • ability to purchase renewable energy certificates equivalent to proportion of energy consumption; • advantage online rewards program; and • rate freeze for 24 months with no exit fees.
Solar feed-in tariff	High number of offers with low level of difference. Retailers offered feed in tariffs for solar panels from 5c to 10 c per kWh.[183]

183 The 2013-14 benchmark range recommended by IPART was 6.6c to 11.2 c per kWh. IPART, Final report - Solar feed-in tariffs - The subsidy-free value of electricity from small-scale solar PV units from 1 July 2013, June 2013, p4. More information on solar arrangements is provided in Appendix D.

The range of offers available and the level of product differentiation appear similar for residential and small business customers in terms of the range of discounts available and the types of tariffs on offer.

While there were fewer offers available for customers in regional areas, differentiation in terms of the discounts, non-price incentives, contract duration, and availability of solar feed-in tariffs was similar. However, the types of tariffs available were different. Unlike urban customers, there were no inclining block tariffs available, and a much higher number of tariffs with a flat consumption charge. The time of use tariffs available had different peak, shoulder and off peak periods to those available for urban customers.

Gas market offers

Consistent with other NEM jurisdictions there is less differentiation in gas offers in NSW with just four retailers offering gas products. As at 31 March 2014, there were 15 gas market offers provided on the Energy Made Easy website for the Sydney area surveyed. There was little or no variation between the prices of these offers and the tariff structures. All offers had an almost identical inclining block structure, with the exception of one retailer.

For gas customers in regional areas, there appears to be little or no choice. In the Wagga Wagga area surveyed, there was only one offer available for residential customers, and one for small businesses, both of which consisted of a flat rate and daily supply charge. See the 2013 NSW review for further discussion on this issue.

6.6 Customer outcomes

Effective competition is characterised by how well markets promote the long term interest of customers, including satisfaction with the level of choice available as well as with the quality of service and value for money provided by retailers. Our analysis of this criterion considered the findings of customer surveys and data on customer complaints, which suggest the following:

- **Some customers want greater choice.** Approximately 16 per cent of residential customers were somewhat or very dissatisfied with the level of choice in the market.

- **Most customers are satisfied with their current retailer,** with slightly higher ratings for quality of service than value for money.

- **The level of complaints to retailers increased** in 2012-13, consistent with trends in other jurisdictions, and appear to be largely due to billing system issues or high bills.

6.6.1 Satisfaction with the level of choice

Slightly fewer customers surveyed were satisfied with the level of choice in NSW relative to the NEM average. Approximately 47 per cent of residential customers were satisfied, 16 per cent dissatisfied and the remainder were neutral or undecided. Satisfaction with the level of choice in Sydney was broadly consistent with the NEM average, but it was much lower in regional NSW with respondents twice as likely to say they were somewhat or very dissatisfied.

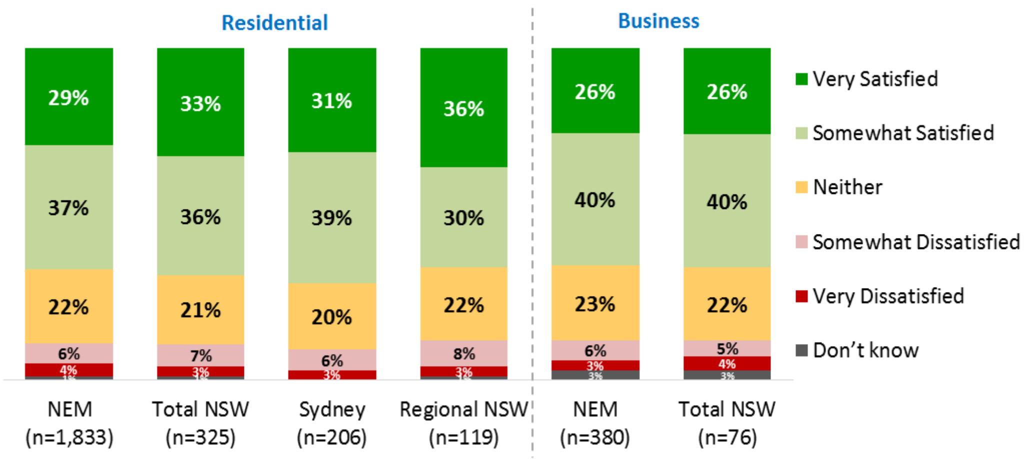
Dissatisfaction levels could reflect less product differentiation in NSW relative to some other states. However, qualitative research conducted by Newgate Research in 2013 suggests it is most likely due to lower awareness of the extent of choice or perceptions that there is little difference between the choices available.

6.6.2 Satisfaction with retailers

The majority of customers were satisfied with their retailer in all NEM jurisdictions surveyed. In NSW, 69 per cent were somewhat or very satisfied with their electricity retailer, which is similar to the NEM average. Those with solar panels were significantly more likely to be satisfied than those without.

Ten per cent of residential customers and nine per cent of business customers surveyed were either somewhat or very dissatisfied with their retailer. Findings in other NEM jurisdictions suggest low levels of dissatisfaction do not necessarily imply high levels of satisfaction. Rather, many customers provided 'somewhat satisfied' or 'neutral' ratings due to the absence of supply issues or customer service issues. High satisfaction ratings in forums in other jurisdictions often related to an absence of negative issues with their retailer rather than a particularly positive experience.

Figure 6.11 Satisfaction with current electricity retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p143. Survey question: How satisfied are you with your current electricity company? Customers surveyed: All.

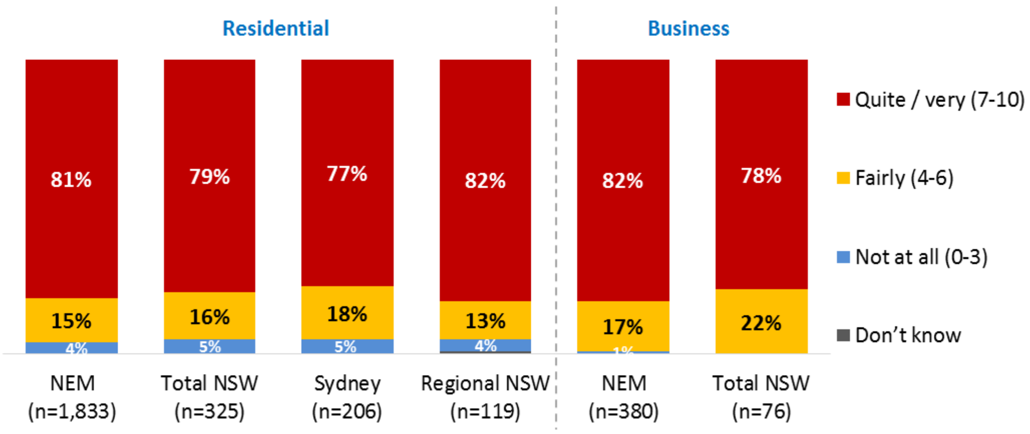
The overall quality of service for electricity and gas was largely perceived as good or excellent by survey respondents. Residential electricity customers in regional NSW rated the quality of service lower than customers in Sydney.

Value for money was rated at least fair overall and around half of residential and business customers considered electricity value for money good or excellent. However, 11 per cent of residential customers and seven per cent of business customers rated electricity value for money as poor. This was consistent with the NEM average and the 2013 Roy Morgan survey results.

It is likely that value for money ratings primarily relate to higher electricity bills in recent years. Price increases have been experienced by customers on market and standing contracts, largely driven by increases in network costs. A full discussion of the drivers of price movements and trends in electricity prices is available in the AEMC's annual residential pricing trends report.

Around 80 per cent of customers surveyed in NSW stated that they were 'quite' or 'very' concerned about future electricity prices. This is broadly consistent with the NEM average and the results of the 2013 Newgate survey.[184]

Figure 6.12 Level of concern about future energy prices



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p123. Survey question: How concerned are you about future energy prices? Customers surveyed: All.

For NSW customers on high and middle incomes, annual electricity bills are estimated to represent approximately 0.6-1.5 per cent of the average disposable income. For low income customers, annual electricity bills are estimated to represent approximately 4.3-5.0 per cent of annual income, depending on whether the customer receives a concession.[185]

184 Newgate Research, *NSW Consumer and Stakeholder Research Report*, a report for the AEMC, 20 September 2013, p20.

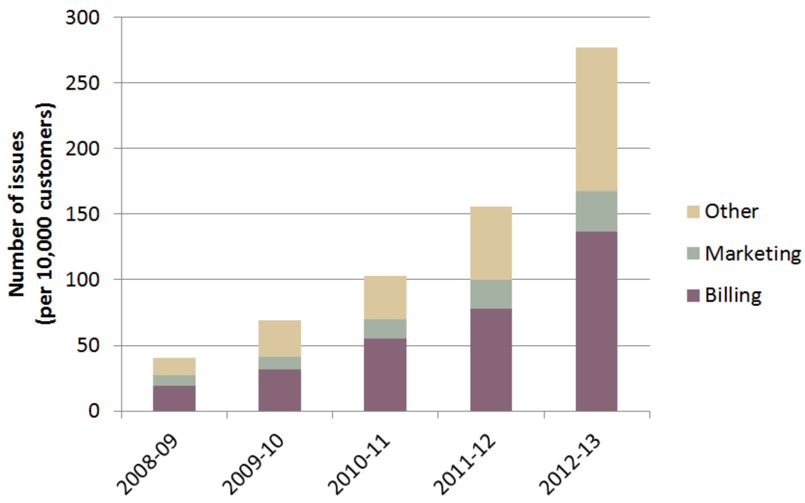
185 This AER analysis is based on average annual electricity consumption of 5,300 kWh for low income customers and 6,700 kWh for high income customers. AER, *Annual report on the performance of the retail energy market 2012-13*, 2013, p66.

Pensioners, Health Care Card holders and Veterans can be eligible for concessions through Low Income Household Rebates. Concessions are also available to customers with medical issues through the Medical Energy Rebate. There are also a Family Energy Rebate, a Life Support Rebate and an Energy Accounts Payment Assistance Scheme. Concessions are discussed further in B.

Complaints to retailers

When a customer makes a complaint, multiple issues may be raised. The number of issues raised with electricity retailers in 2012-13 in NSW was higher than in any of the previous four years, with a 177 per cent increase between 2011-12 and 2012-13 (see Figure 6.13). Billing was the most common issue category since 2008-09, making up 49 per cent of the issues raised with electricity retailers in NSW in 2012-13.

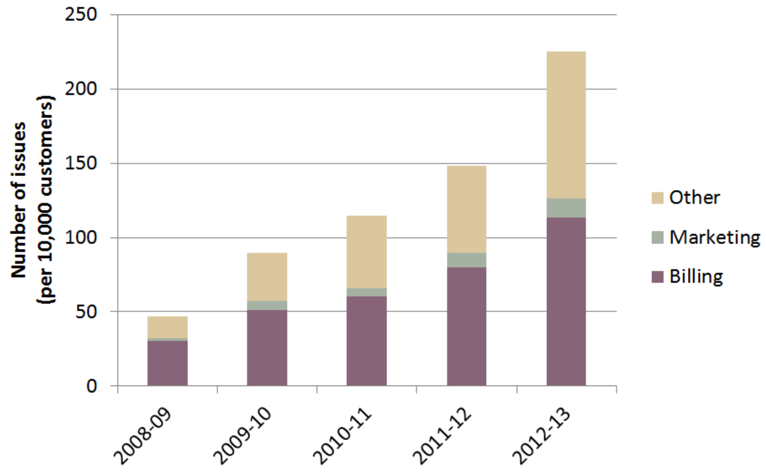
Figure 6.13 Electricity complaints to retailers - number of issues raised



Source: Complaints data from IPART, *Customer service performance of electricity retail suppliers*, December 2013, p16. Customer numbers from AEMO, AEMC analysis.

The number of issues customers raised with gas retailers in NSW has been comparable to electricity, when adjusted for market size. Similar to electricity, the number of issues raised in 2012-13 was higher than in the previous four years (see Figure 6.14). Fifty per cent of issues raised related to billing.

Figure 6.14 Gas complaints to retailers - number of issues raised

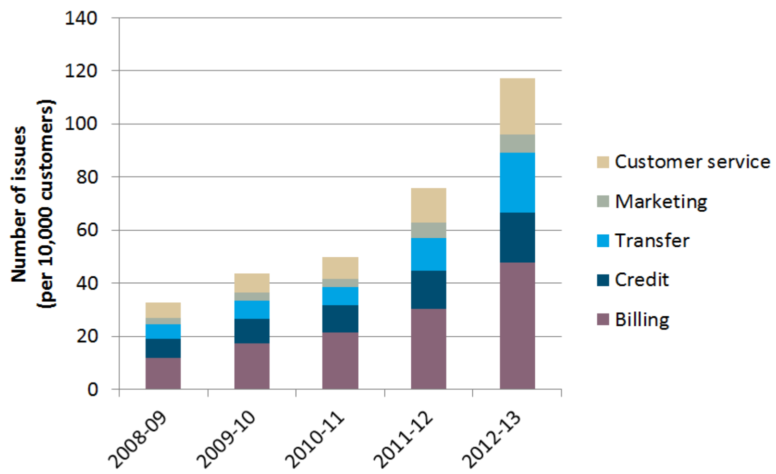


Source: Complaints data from IPART, *Customer service performance of electricity retail suppliers*, December 2013, p16. Customer numbers from AEMO and Energy Supply Association of Australia (ESAA) *Electricity Gas Australia* reports. AEMC analysis.

Complaints to the Ombudsman

In 2012-13, the number of retail electricity issues raised with the Energy & Water Ombudsman NSW (EWON) was 55 per cent higher than in 2011-12 (see Figure 6.15).[186] EWON noted that customer service issues underlie many complaints received by EWON which should have been resolved directly between the retailer and the customer.[187] Note that issues raised with EWON include referrals back to retailers, which are also captured in complaints to retailers described above.

Figure 6.15 Electricity complaints to the Ombudsman - number of issues raised



Source: Complaints data from EWON, customer numbers from AEMO, AEMC analysis.

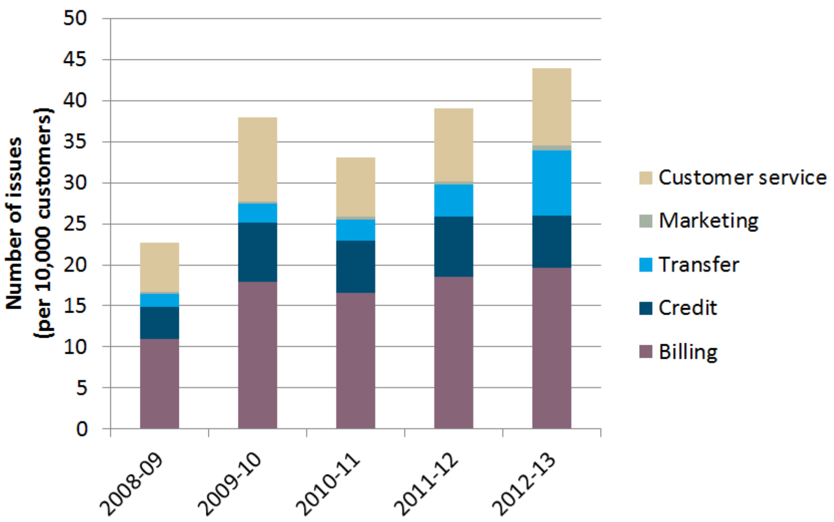
186 Data on complaints to EWON excludes cases which were out of jurisdiction or not complaints.

187 EWON, *Annual Report 2012-2013*, p4.

In the past two years, the number of retail gas issues customers raised with EWON was much lower than for electricity, even when adjusted for market size. While the sharp increase in the number of issues raised with gas retailers was not reflected in the trend of gas issues raised with EWON, the number of issues raised has been increasing.

In addition to issues reported to EWON about electricity and gas, 2,241 issues were also raised regarding dual fuel in 2012-13.

Figure 6.16 Gas complaints to the Ombudsman - number of issues raised



Source: Complaints data from EWON, customer numbers from AEMO and ESAA *Electricity Gas Australia* reports, AEMC analysis.

Billing issues were the most commonly raised complaints to EWON for both retail electricity and retail gas, making up 41 per cent for electricity and 45 per cent for gas. According to EWON's 2013 Annual Report, the most common billing issue was "high or disputed account."[188] Credit, transfer and customer service issues were also common. The number of retail electricity complaints relating to each of these issues has increased in the past two years. EWON noted that there have been energy price rises and increasing numbers of households switching energy retailer in "a more competitive energy market."[189]

6.7 Retailer outcomes

Profit margins can provide an indication of the level of competition in a market. However, they can also be expected to fluctuate over time. Consequently it is important to carry out analysis of retailer margins over a sufficiently long time period. It is also important to consider the results of such analysis in the context of other competitive indicators. While retail margins in NSW have not been estimated for the purpose of this review, we make a number of observations on retailer outcomes drawing from retailer interviews and work conducted for the 2013 NSW review.

188 Energy and Water Ombudsman New South Wales, *Annual Report 2012-2013*, 2013, p22.

As part of the 2013 NSW review, NERA Economic Consulting (NERA) was engaged to undertake an analysis of retailer margins in NSW from 2002 to 2012 and comment on the implications for competition. NERA found that margins in electricity under the regulated tariff "were adequate to support effective competition in NSW between 2002 and 2012".[190] The Commission concluded that there appeared to have been sufficient margins to support competition by allowing new entrants to offer prices lower than the regulated rate while maintaining a margin for profit.[191]

Retailers surveyed for the current review rated electricity retailing in NSW as somewhat profitable, but lower than in Victoria. They attributed lower profitability to the presence of price regulation and the deep discounting that has occurred over the last two years. Profitability was rated similar to South Australia and South East Queensland.

Some comments made by individual retailers interviewed for this current review included:[192]

- there was a 'vicious fight' for customers in NSW with deep discounting, but that it had not been profitable;
- the margins in the Ausgrid area are reasonable, but lower in the Essential Energy and Endeavour distribution areas; and
- the allowances provided for by IPART for costs such as customer acquisition did not reflect the actual costs that retailers would incur, so the margins available in NSW are not as cost reflective as they are in Victoria.

The Commission notes that, despite claims that margins are not as good in the Essential Energy and Endeavour network areas, all but one retailer operates in all these network areas. Further, there is one retailer that operates in the Essential Energy and Endeavour network areas but not the Ausgrid area. This suggests that, to the extent that margins are lower outside of the Ausgrid area, they are not too low to deter entry.

Similarly, to the extent that margins in NSW overall are lower than in Victoria, again this has not prevented entry by new retailers.

NERA also found retail margins in gas to be adequate to support effective competition between 2002 and 2012. The analysis suggested that margins for gas were slightly higher than those for electricity. This was inconsistent with retailer views expressed

189 Ibid, p2.

190 NERA, *Prices and Profit Margin Analysis for the NSW Retail Competition Review*, a report for the AEMC, 25 February 2013, p26.

191 AEMC 2013, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, Final Report, 3 October 2013, p28.

192 K Lowe Consulting and Farrier Swier Consulting, *AEMC Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p82.

during the 2013 NSW review that gas is less profitable than electricity.[193] In a survey of retailers for this 2014 review, retailers rated profitability slightly higher for gas than for electricity, however a different set of retailers responded to the electricity and gas surveys and so comparisons between these markets must be interpreted with caution. We also note the particular difficulty in assessing margins in gas due to the confidential nature of wholesale gas contracts and the lack of publicly available reference data. Consequently there is considerable room for error in estimating gas retail margins.

In the 2013 NSW review the Commission concluded that margins in gas were consistent with a competitive market.[194] We found that the regulated tariff had sufficient headroom to support competitive activity, and that new retailers were offering discounts and incumbents are responding by offering discounts. No new evidence has emerged for this review that would suggest outcomes for retailers have changed since that time.

6.8 Future developments

Competition in the NSW retail electricity market continues to deliver discounts and other benefits to small customers. With the removal of price regulation on 1 July 2014, the Commission expects competition to further increase in the NSW electricity market. This is consistent with the Australian Competition Tribunal's decision where it stated:

> "As has been observed in other states, it could be expected that competition will intensify in NSW when retail prices are deregulated on 1 July 2014."[195]

The market will continue to mature as retailers' activity increases and with developments in technology, allowing innovative new products and services to emerge.

Some of the retailers interviewed for this review noted there is potential for activity in NSW to overtake Victoria as customers become more engaged and further new entry occurs. One retailer indicated that it was in the process of entering the NSW electricity market, another small retailer is considering entry, and four existing second tier retailers are intending to expand over the next five years. This is consistent with retailer views that NSW is an attractive market in terms of size and regulatory and political stability, particularly now that price regulation has been removed.

In the retail gas market, competition is providing choices for the majority of small customers in NSW. Prices in this market continue to be regulated, which could deter further entry and expansion. However, the overriding issues affecting retailer entry are

---

193 Sapere, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales - Report of Interviews with Energy Retailers*, a report for the AEMC, February 2013, p67.

194 AEMC, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, 2013, Final Report, p39.

195 Application for Authorisation of Acquisition of Macquarie Generation by AGL Energy Limited [2014] ACompT 1 [361].

likely to be the ability of retailers to access transmission pipelines and the ability of retailers to obtain competitively priced gas in the wholesale market.

Some gas customers in rural and regional areas have limited choices and this is not expected to change in the short term due to the size of the customer base and other structural factors acting as a barrier to entry and/or expansion in these areas.

One retailer indicated that it is considering entering the gas market and another existing retailer is considering expanding over the next five years.

Despite this, retailers that were interviewed did not expect any real improvements in competition to occur in the small customer segment of the NSW retail gas market, given the tightening demand and supply conditions in the wholesale gas market. Some retailers considered that the tightening wholesale market conditions would be felt most acutely in NSW, with retail gas prices expected to rise and possible supply shortfalls in peak periods from 2016.

7 Australian Capital Territory

Box 7.1: Key findings

- Competition is not effective in Australian Capital Territory's electricity or gas retail markets with limited activity from either retailers or customers.
  - Two retailers currently service the residential electricity and gas markets. Rivalry between the two retailers is limited and the incumbent retailer, ActewAGL, has approximately 95 per cent of the electricity and gas customers. Small market size and ActewAGL's dominance are cited by retailers as the key deterrents for entry or expansion in energy retail markets. Price regulation is also seen as an impediment in electricity.
  - Customer awareness of the ability to choose a retailer is low. The Australian Capital Territory has the highest proportion of customers on regulated offers, the lowest proportion of customers investigating options, and the lowest switching rates in the national electricity market.
  - There is a small number of market offers available to customers and they are very similar. The key point of difference is the discount offered by the incumbent retailer for 'bundling' multiple services such as mobile phone, landline and internet.
  - More customers in the Australian Capital Territory are 'very satisfied' with their retailer and have fewer complaints than other jurisdictions surveyed, however fewer customers were satisfied with the level of choice of retailer or plan.
- The Commission has previously provided advice on how the Australian Capital Territory could become more competitive and those recommendations continue to apply.

7.1 Overview

This is the first AEMC review of competition in the retail gas market and the second review of the retail electricity market in the Australian Capital Territory (ACT). The AEMC's first review was completed in March 2011 and found that competition in the ACT retail electricity market was not effective. This was due to several factors such as the lack of customer awareness, the relatively small size of the market, and the way retail price regulation was applied.[196]

196 AEMC, *Review of the Effectiveness of Competition in the Electricity Retail Market in the ACT*, Final Report, March 2011, p i.

The final report recommended ways to promote competition in the ACT through a package of reforms to empower customers and make it easier for second tier retailers to enter and expand within the market.

The findings of the AEMC's 2014 review of competition in the electricity and gas markets in the ACT are summarised below. For electricity, these findings are broadly consistent with the AEMC's first review and the Commission's previous recommendations still apply.

- **Customer activity:** There is little evidence of customer activity in the market. Most customers remain on regulated offers, there is low awareness of the ability to choose a retailer or plan, and very few customers are investigating their options or switching between retailers or plans.

- **Barriers to entry, exit and expansion:** Entry into the electricity and gas retail markets appears to be difficult and expansion is reportedly even more difficult. The two commonly cited issues for both markets are ActewAGL's dominance and the small size of the markets. An additional issue for the electricity market, which appears to be the key deterrent for entry and expansion, is the way in which retail prices are regulated.

- **Independent rivalry:** There is little evidence of retailer rivalry. ActewAGL has a market share of approximately 95 per cent for electricity and gas and the level of product differentiation appears limited. Among the offers available in the market, there is little differentiation in terms of tariff structure, non-conditional discounts or non-price incentives. The key difference is 'bundling discounts' where the greatest discount available is 25 per cent off usage if customers bundle seven services with the incumbent retailer.

- **Customer outcomes:** More customers are very satisfied with their energy retailer in the ACT than other jurisdictions surveyed and the ACT has some of the lowest reported complaint numbers of the four jurisdictions that have adopted the National Energy Customer Framework (NECF). For many customers, high satisfaction appears to reflect an absence of reasons to contact their retailer. Fewer customers are satisfied with the level of choice relative to other jurisdictions surveyed and would like greater choice in the market.

- **Retailer outcomes:** Retailers rated the profitability of the ACT electricity and gas markets as relatively low. This is consistent with previous AEMC analysis that suggested the absence of headroom costs in regulated retail prices results in very low margins for competing retailers. This is also evidenced by the continuing lack of entry by second tier retailers.

7.2 History and market characteristics

Full retail competition was introduced for small customers[197] in the ACT in 2002 for gas and 2003 for electricity. At this time, regulation of retail gas prices was removed. Price regulation has been retained for electricity and these prices are determined by the Independent Competition and Regulatory Commission (ICRC).

The ACT adopted the NECF on 1 July 2012, with retailers offering standing contracts with regulated terms and conditions and a regulated price. Retailers can also offer market contracts with the price determined by retailers.

The market for electricity is the smallest in the national electricity market (NEM), with approximately 170,000 small electricity customers.[198] The gas market is the second smallest in the NEM with 112,000 customers, but it has a high average household gas consumption of close to double the average of New South Wales and 80 per cent of Victoria's average.

7.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

Our analysis of this criterion considers the findings of a customer survey and qualitative forums performed by Newgate Research, as well as data from the Australia Energy Market Operator (AEMO) and the Australian Energy Regulator (AER). The analysis suggests the following:

- **The ACT had the lowest proportion of customers on market offers of all jurisdictions where market offers were available** for all small customers in 2013. Approximately 19 per cent are on market offers for electricity and 20 per cent for gas.[199]
- **Customer awareness of their ability to choose a retailer or plan is very low.** Close to half of the customers surveyed did not know they had a choice of electricity retailer and even fewer were aware they could choose their gas retailer. Awareness of choice of different energy plans was similarly low. These results are considerably below the average for the NEM jurisdictions surveyed.
- **There is minimal customer activity** relative to other jurisdictions and industries. Just ten per cent of customers investigated their energy options last year, which is one third of the NEM average, and the electricity switching rate was close to 2 per cent in 2013.

197 Small customers are defined in the ACT as consuming less than 100 megawatt hours per annum.

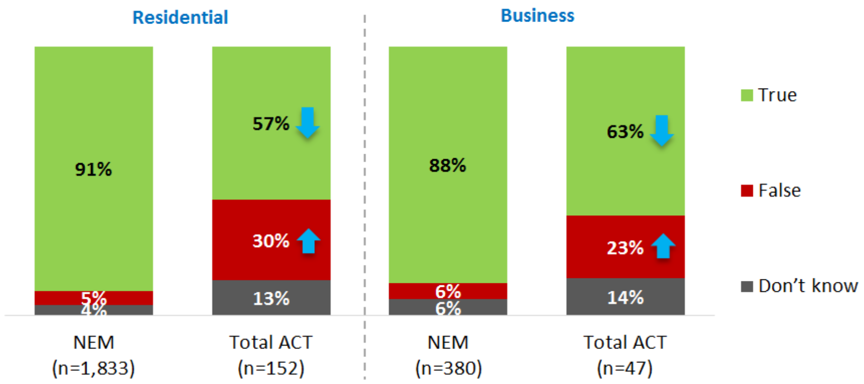
198 For the second quarter of 2013-14. Data sourced from AER.

199 Statistics provided by the AER.

7.3.1 Customer awareness and understanding

For customers to actively participate in the market, they first need to be aware of their choices. A significant proportion of customers in the ACT are unaware they have a choice of retailer or plan as shown in Figure 7.1. The arrows indicate results that are statistically different from the NEM average at the 95 per cent confidence level. Of those surveyed in the ACT, 57 per cent of residential customers and 63 per cent of small businesses were aware they could choose their electricity retailer compared to the NEM average of 91 per cent and 88 per cent, respectively. Almost one half of residential customers surveyed in the ACT believed they did not a have a choice of retailer or were not sure.

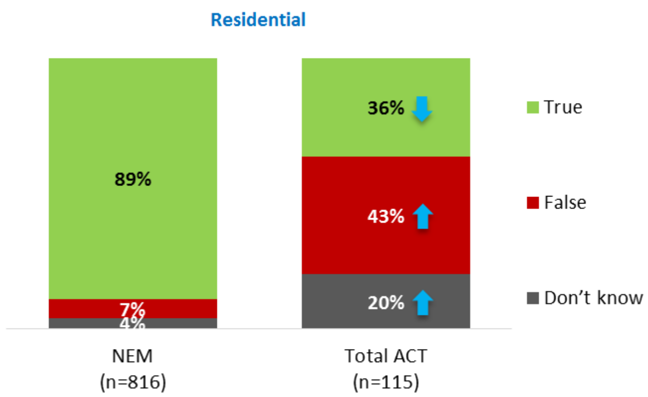
Figure 7.1 Awareness of being able to choose electricity retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p203. Survey question: Do you think it is true or false that consumers in your state [territory] can choose their electricity company. Customers surveyed: All.

Even fewer were aware of their choices in the gas market. As shown in Figure 7.2, almost half of customers surveyed believed they did not have a choice of retailer.

Figure 7.2 Awareness of being able to choose gas retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p204. Survey question: Do you think it is true or false that consumers in your state [territory] can choose their gas company. Customers surveyed: Customers who have mains connected gas.

Awareness was similarly low among forum participants in Canberra, where most believed ActewAGL was the only energy retailer in the ACT.

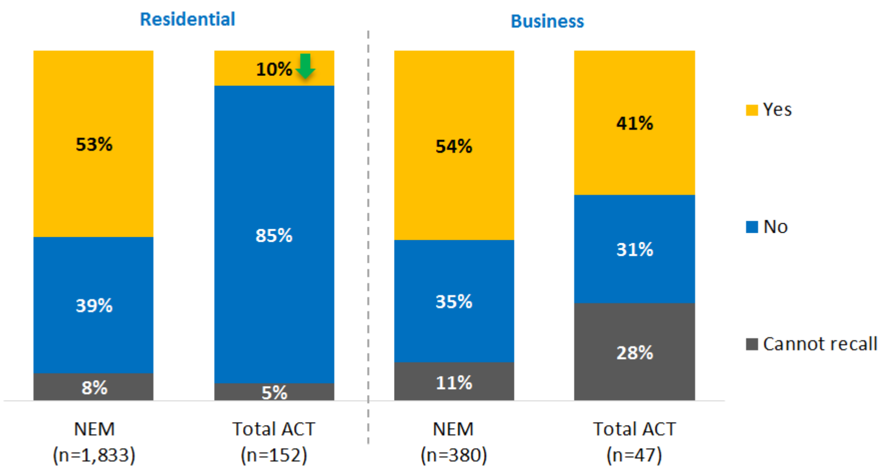
> "I didn't know there was more than one energy company. I was told all we could get was ActewAGL. (Canberra, income unidentified)"

> "I've lived here forever and thought ActewAGL was all we could get. I saw a 'Welcome to Canberra' ad sponsored by ActewAGL. (Canberra, income unidentified)"

Customer awareness in other jurisdictions appears to be largely driven by retailer marketing activity. In the ACT, ten per cent of residential customers reported being approached by an energy retailer in the last twelve months, compared to 53 per cent of customers across all NEM jurisdictions surveyed. As discussed in section 7.5, there are fewer market offers available in the ACT than in other jurisdictions. Consequently, it is not surprising that there is lower customer awareness in the ACT.

Retailers appear to be focussing on the small business segment of the market in the ACT with 41 per cent of small businesses being approached by an energy retailer over the same period of time.

Figure 7.3 Customers approached by an energy retailer in past 12 months



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p210. Survey question: In the past 12 months have you been approached by an energy company offering to see you electricity and gas? Customers surveyed: All.

One quarter of customers surveyed were 'not at all' confident they understood the various options and product offers available in the ACT. Confidence appeared even lower in the forums, particularly after participants discovered during discussions that they had a choice of retailer and plans.

7.3.2 Customers investigating offers and switching

ACT residents reported high levels of interest in looking for a better deal, but very few are actually shopping around. Ten per cent of residential customers reported investigating their options in the past twelve months. This is considerably below the NEM average of 31 per cent.

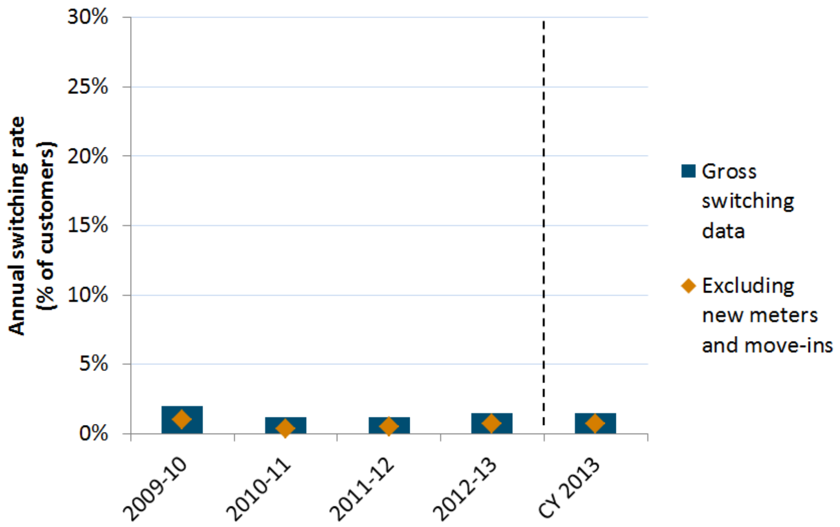
Even fewer small business customers appeared to be shopping around. Six per cent of small business customers investigated their options in the past twelve months compared to the NEM average of 43 per cent.

Unlike customers surveyed in other NEM jurisdictions, ACT customers switched their providers of car insurance, internet and mobile phones more frequently than they switched electricity or gas retailer or plan.

Low awareness of options in the electricity and gas market is reflected in low reported switching rates. Across all NEM jurisdictions surveyed, an average of around 60 per cent of residential customers and 56 per cent of small business customers switched their electricity plan or retailer in the last five years. These figures were close to half that in the ACT, with 27 per cent of residential customers and 36 per cent of business customers switching plan or retailer. Ten per cent of gas customers reported switching their gas retailer or plan in the last five years, compared to 49 per cent of gas customers surveyed across the NEM.

Data on customer transfers between retailers for electricity in Figure 7.4 also shows low customer switching between electricity retailers.[200]

Figure 7.4 History of electricity customer switching rates[201]



Source: AEMO data, AEMC analysis.

The ACT had the lowest electricity switching rate in 2013 of all the NEM jurisdictions that had full retail competition for all small customers. Over the past four years, rates for switching retailer have not exceeded 3.5 per cent and were close to two per cent for

200 See Chapter 2 for a discussion of the limitations of this data. Data was unavailable for gas switching in the ACT.

201 Data has been presented with the same scale for the switching charts for all jurisdictions.

the 2013 calendar year. If adjusted to focus on active switches by excluding new meter additions or move-ins, the rate is even lower.

Switching rates can underestimate the level of customer activity as they do not include customers who switched plans with the same retailer.[202] Newgate Research found that slightly more ACT residents reported switching their electricity plan than their retailer in the last five years, but this level of switching was still close to half the NEM average.

Price and moving house are key drivers of switching behaviour

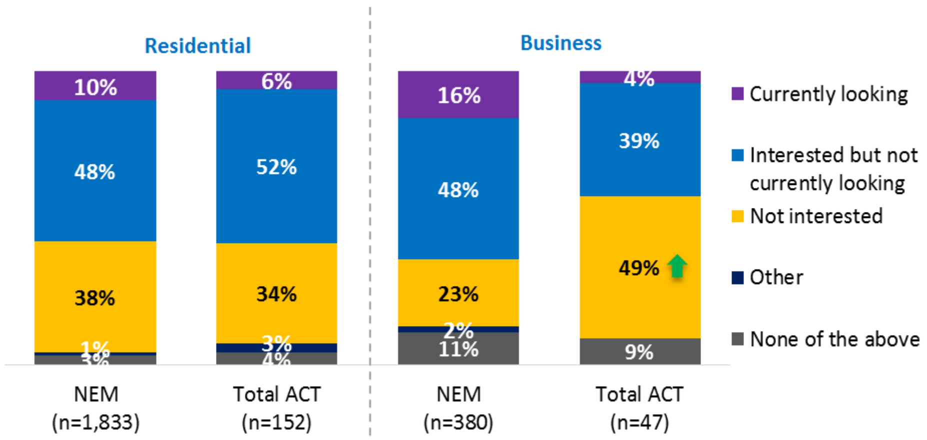
Of the few customers who did report switching, 41 per cent cited price as their main reason for switching retailer or plan, closely followed by 32 per cent who cited moving house. In other jurisdictions, moving house was a very distant second to price.

Lower prices coupled with higher average disposable income in the ACT may partially contribute to the low switching rates. Customers in the ACT also have fewer options to switch to. However, Newgate Research found that the key issue in the ACT for switching appears to be a lack of awareness that customers are able to switch.

Many customers are less engaged

Most customers surveyed expressed an interest in energy issues, energy prices and investigating their options. However, 90 per cent did not investigate options in the last 12 months and approximately one third of residential customers surveyed in the ACT were not at all interested in looking for a better deal. Businesses in were even less inclined to shop around, as shown in Figure 7.5.

Figure 7.5 Interest in looking for a better deal



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p220. Survey question: When it comes to your household's energy company, which of the following is most applicable to your household? Customers surveyed: All.

202 ActewAGL considers that an over emphasis on switching between retailers (and not incorporating switching offers with the same retailer) can lead to an under assessment of the effectiveness of competition. ActewAGL, submission to the *2014 Retail Competition Review*, Approach Paper, p2.

ActewAGL attributes the low switching rates to the consistently high level of customer satisfaction that it achieves. In its submission to the Approach Paper, ActewAGL noted that it won gas provider of the year for 2011, 2012 and 2013, and electricity retailer of the year for 2012 in the Roy Morgan Research annual customer satisfaction awards.[203]

The AEMC's 2011 review of competition in the ACT found that there was a low level of customer engagement in the ACT energy markets due to two reasons:

- a low level of customer awareness of the ability to switch retailers and who those alternative retailers may be; and
- little customer understanding of the implications of switching retailers (for example, that this does not have an impact on the physical supply of electricity).[204]

Results from the 2014 customer research suggest these remain key issues for the ACT. Low awareness of choice is evident in the survey results and forum discussions. Limited understanding of the impact of switching on physical supply was raised in forum discussions in the ACT and in other jurisdictions.

> "EnergyAustralia might have a better deal but will anyone ever respond if I have a power outage? Service is very important. (Canberra, higher income)"

> "I'd like to hear they have a response if something goes wrong with the power. I know ActewAGL has it and I'm very happy with that response. Before I sign up for roadside assistance I need to know they have cars on the road. Can they respond? Do they own the lines, can they touch the lines? I need to know they can be serviced by another company. Do I get a service charge? (Canberra, income unidentified)"

During discussions in the customer forum, most participants did not know they had a choice and hearing this information made them want to explore their options.

Increasing awareness of choice is not the only step required to drive greater customer engagement. Customers also need to find value in shopping around. Our analysis of the offers available suggests there could be savings in energy bills for customers who switch from a standing offer to a market offer, provided they pay on time or are willing to bundle multiple services (see Box 7.2 below).

Of the few forum participants who had investigated their options, most noted they had limited success as they could not find an alternative retailer or the plans of the other retailer were more expensive than their current plan. Many did not perceive a 'real choice' in terms of the options available.

---

203 ActewAGL, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p2.

204 AEMC, *Review of the Effectiveness of Competition in the Electricity Retail Market in the ACT*, Final Report, March 2011.

As the ACT has adopted the NECF, energy customers have access to the AER's Energy Made Easy price comparator website. This website can simplify the search process for an alternative plan or retailer. None of the customers surveyed mentioned this website unprompted when asked if they were aware of comparison sites. Once prompted, six per cent of residents and ten per cent of small business customers said they had heard of the site. Awareness was similarly low in other jurisdictions surveyed.

Box 7.2: Potential savings from moving off a standing offer to a market offer

As at 31 March 2014, an average residential customer in the ACT may have saved around $230 (or 12 per cent) off their total annual bill by switching from their standing offer to either another standing offer or a market offer, without bundling. Customers may have saved even more by bundling services. Customers who bundled five or more services may have saved up to $650 (or 33 per cent) by switching from their standing offer. The savings depend on which standing offer is used as a base.

7.4 Retailer barriers to entry, exit and expansion

This section discusses key findings from retailer interviews and surveys conducted by consultants engaged for this review, K Lowe Consulting and Farrier Swier Consulting.[205]

Two energy retailers that are currently active in the ACT agreed to participate in the retailer interview and survey process. A number of other retailers that are not currently active in the ACT also offered their views on gas and electricity retailing in the ACT.

One of the key issues that these retailers were asked to provide their opinion on is the ease with which entry and expansion can occur in both the gas and electricity retail markets in the ACT. This group of retailers were also asked whether they plan to enter, expand or exit either market in the next five years. The responses to these questions revealed the following:

- **Electricity retail market** – Entry into the electricity retail market is considered by retailers to be difficult and expansion even more difficult. The more significant factors that retailers claimed are impeding entry and expansion in this market include retail price regulation, ActewAGL's dominance in the market, the relatively small size of the market and credit support requirements.

- **Gas retail market** – Like electricity, entry into the gas retail market is perceived by retailers to be difficult and expansion even more difficult despite not having price regulation. Two of the more significant factors that retailers claim are impeding entry and expansion in this market are the small size of the market and ActewAGL's dominance.

205 For full details refer to K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014.

The views expressed by retailers about the difficulties associated with entry and expansion in the electricity retail market are broadly consistent with the Commission's finding in the 2011 review of the effectiveness of competition in the electricity retail market, which is that there are a number of barriers to entry and expansion in this market that may limit effective competition. They are also consistent with the observation that no new retailers have entered either market in the last two years.

In its submission, ActewAGL noted that there are low barriers to entry and expansion in the ACT residential market, and that the introduction of the NECF has further lowered barriers to entry as retailers are only required to have one licence authorisation to sell gas or electricity in all NECF jurisdictions.

Further detail on the perceived impediments to entry and expansion in both the gas and electricity retail markets is provided below.

7.4.1 Regulatory impediments in the electricity retail market

One of the more significant barriers to entry and expansion in the electricity retail market that retailers identified is retail price regulation, consistent with other jurisdictions that have maintained price regulation. Gas prices were deregulated in 2002 and a number of other factors appear to be impeding entry into this market, which are discussed in the next section.

The concerns raised by retailers about electricity retail price regulation in the ACT were two-fold:

- First, retailers claim that the mere presence of retail price regulation constitutes a risk to retailers, because there is always the chance that the regulated price will be set below the retailer's cost of supply.[206] Consequently a new entrant may not be able to offer a competitive price while making a commercial return.
- Second, retailers claim that the manner in which retail price regulation is currently applied by the ICRC provides retailers with little or no incentive to enter or actively compete in the market because:
  - the ICRC makes no provision for customer acquisition and retention costs in the regulated price; and
  - the retail operating cost allowance used in the derivation of the regulated price is based on ActewAGL's costs, rather than a new entrant's costs.[207]

206 ActewAGL, submission to the *2014 Retail Competition Review*, Approach Paper, p2.

207 As noted in the Commission's review of the effectiveness of competition in the ACT retail electricity market, the Commission understands that the ICRC's terms of reference require it to set prices to allow for the recovery of the efficient costs incurred by the incumbent retailer and that it is also required to consider the social impacts of its decision. It is on these grounds that the ICRC has decided not to make an allowance for customer acquisition and retention costs and to base the retail operating cost allowance on ActewAGL's costs. AEMC, *Review of the effectiveness of competition in the electricity retail market in the ACT*, First Draft Report, 30 July 2010, p28.

A number of retailers also raised concerns about statements contained in the ICRC's 2014-2017 standing offer draft decision, which they claim indicate the ICRC has 'given up on competition' in the ACT.

The concerns raised by retailers about the manner in which retail price regulation is currently applied in the ACT mirror those that were raised in the Commission's 2010 review. As the Commission noted in that review, excluding customer acquisition and retention costs from the regulated price and basing the retail operating cost allowance on ActewAGL's costs,[208] can result in the regulated price being set too low to promote entry and expansion.[209]

The Commission considers that if jurisdictional governments decide to facilitate competition, then some form of headroom should be included in the regulated retail price. Such headroom should be set and included in the retail electricity price in a transparent manner.[210]

The fact that there has been no recent entry in the electricity retail market suggests that the approach employed by the ICRC may be one factor that is continuing to act as a barrier to entry and expansion in this market.

7.4.2 Other impediments affecting both the gas and electricity retail markets

Two other factors that retailers claimed are impeding entry and expansion in both the electricity and gas retail markets in the ACT are:[211]

- ActewAGL's dominance in the market, which retailers claimed is being reinforced by its multi-utility bundling capabilities, the degree of brand loyalty exhibited by customers in the ACT and the absence of any allowance for customer acquisition and retention costs in the regulated price; and
- the small size of both the gas and electricity retail markets in the ACT.

On the first of these claimed impediments, the Commission agrees that the manner in which retail price regulation is currently being applied in the ACT could be contributing to ActewAGL's dominance in the market, because other retailers are unable to effectively market their products in the ACT. It is this factor, rather than

208 The concern that the Commission had with basing the retail operating cost allowance on ActewAGL's costs rather than a new entrant's costs is that ActewAGL's costs are likely to incorporate an element of economies of scale and scope that may not be available to a new entrant or stand-alone retailer. AEMC, First Draft Report: Review of the effectiveness of retail competition in the ACT, 30 July 2010, p57.

209 AEMC, *Review of the effectiveness of retail competition in the ACT,* First Draft Report, 30 July 2010, pp35 and 57.

210 AEMC, *Advice on Best Practice Retail Price Regulation Methodology*, Final Report, September 2013, p71.

211 Retailers also noted that prudential and credit support requirements can impede entry and expansion in the electricity retail market. The Commission's views on this perceived impediment are set out in section 4.4.2.

ActewAGL's dominance in the market, that in the Commission's view is impeding entry and expansion.

As to the claim that the size of the electricity retail market in the ACT is impeding entry, the Commission notes that a similar claim was made in the 2010 review. The Commission concluded at the time that the small size of this market by itself was unlikely to constitute a barrier to entry or expansion.[212]

Because the 2011 review only focused on the electricity retail market, no consideration was given to whether the size of the gas retail market in the ACT may act as an impediment to entry and/or expansion in this market. The size of a market will not, in and of itself, usually constitute a barrier to entry. However, if the costs of supplying that market are largely fixed or sunk (ie there are economies of scale associated with supply in this market), then the size of the market may place a cap on the number of retailers that can enter and effectively compete in the market.

The Commission is aware from the work that was done as part the gas market scoping study and from information provided by retailers through the interviews and survey, that the costs faced by retailers can exhibit these types of characteristics. It is quite possible therefore that the small size of the retail gas market in the ACT may limit the level of entry.

Finally, the reluctance of retailers to enter the electricity retail market is likely to act as a further impediment to entry in the retail gas market. This is due to the high risks and costs associated with securing and transporting gas without an existing electricity customer base to directly market to. Further, given that gas tends to be a secondary consideration for customers, gas-only retailers may find it more difficult to win customers.

7.4.3 Economies of scale and scope are considered important

Through the retailer interview and survey process, retailers were asked to rate the importance of economies of scale[213] and economies of scope[214] in each jurisdiction. The responses to this question suggest that these two sources of efficiencies may be more important in the ACT for the following reasons:

- **Economies of scale** – Retailers noted that there are a range of jurisdictional specific arrangements applying in the ACT (eg billing requirements and energy efficiency schemes) which, when coupled with the fact that the ACT market is relatively small, can mean that achieving a minimum scale in the ACT is more important than it is in most other jurisdictions. The need to achieve a minimum

---

212 AEMC, *Review of the effectiveness of retail competition in the ACT*, First Draft Report, 30 July 2010, p31.

213 Economies of scale exist when a retailer's average costs decrease as they acquire customers and sell larger volumes of energy.

214 Economies of scope exist when a retailer's average costs decrease when they supply two or more products together (eg a dual fuel or multi-utility product).

scale is considered even more important in gas, because of the fixed cost nature of retailing gas.

- **Economies of scope** – Retailers noted that economies of scope can be more important in the ACT given the relatively high penetration of gas and the prevalence of bundling.

Neither of these factors was viewed by retailers as an insurmountable barrier to entry or expansion, which is consistent with the Commission's findings from earlier reviews in the ACT and other jurisdictions.

7.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

Our analysis of this criterion considered findings from retailer interviews and advertised market offers, which suggest the following:

- **Rivalry appears very limited in the residential electricity and gas markets.** Rivalry may be slightly higher in the small business electricity segment with three retailers competing and signs of marketing activity.
- **The energy market remains highly concentrated.** EnergyAustralia is the only alternative retailer to ActewAGL offering contracts to residential customers, but its marketing activity in the ACT appears low relative to other jurisdictions.
- **There is limited product differentiation,** with few offers available and the main point of difference being conditional discounts for bundling services.

7.5.1 Market share and concentration

ActewAGL and EnergyAustralia are the two active retailers in the ACT small customer electricity and gas market. ERM Power also offers electricity in the small business market.

The ACT has very high energy market concentrations with the Herfindahl-Hirschman Index (HHI) close to monopoly levels for the small customer electricity and gas markets.[215]

215 The HHI for the small customer electricity market is 9,178 and 9,183 for the small customer gas market. The HHI maximum is 10,000, which represents a pure monopoly market. The ACC uses a score of 2000 as a threshold when considering the level of competition for merger assessments. The HHI calculation for the ACT electricity market may understate the level of concentration in the residential market as data could not be disaggregated for the small business and residential market (the residential market has two retailers but the HHI includes data for the three retailers in small business market).

The electricity market share of the incumbent retailer, ActewAGL, has not dropped below 90 per cent since the introduction of full retail competition in the ACT. Its market share in the electricity market reached the lowest levels in 2007 at close to 92 per cent due to EnergyAustralia's increased presence in the market.[216] ActewAGL's share has gradually increased since then to return to the current level of approximately 95 per cent. It has a similar share of the retail gas market.[217]

ActewAGL considers that it has such a substantial share of the market in the Australian Capital Territory due to its significant investment in the community and continuously delivering high levels of satisfaction.[218]

As discussed in section 7.3, residential customers surveyed in the ACT reported considerably less direct contact from energy companies than the NEM average. More business customers reported being contacted by an energy retailer, suggesting rivalry may be somewhat higher in this segment of the market.

7.5.2 Product differentiation

Retailers interviewed stated that product differentiation in the ACT is relatively high, which they attributed to ActewAGL's approach to bundling.[219] This involves customers receiving up to seven different services through the one retailer.

The Commission's assessment of the offers available on the Energy Made Easy price comparator website suggests a low level of differentiation for electricity and an even lower level of differentiation for gas. This appears consistent with the findings of the customer research performed for this review were many customers were dissatisfied with the level of choice or were unable to find an alternative retailer or plan.

Most offers in the ACT appear very similar, with little or no difference between market and standing offers. The market offers are all based on a single tariff, differing only in termination fees and discounts.

Standing offers

Under the NECF, all electricity retailers in the ACT are required to offer a contract with regulated terms and conditions known as a 'standing offer'. ActewAGL has an additional requirement to offer the regulated rates as the designated local area retailer. ActewAGL offers this rate as a standing offer (ie the terms and conditions and the price in this contract are all regulated).

---

216 AEMC, *Review of the Effectiveness of Competition in the Electricity Retail Market in the ACT*, March 2011.

217 AER, *State of the Energy Market 2013*, 2013, p122.

218 ActewAGL, submission to the *2014 Retail Competition Review*, Approach Paper, p2.

219 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer interviews*, a report for the AEMC, June 2014, p14.

As at 31 March 2014, there were four standing offers available, with two for the small business market and two for the residential market. The standing offers differed in that they either had an inclining block or flat tariff structure. The bands within the inclining block offers also differed.

Gas retailers in the ACT are also required to offer a standing contract. As at 31 March 2014, there were two standing gas offers available. One retailer offered an inclining block tariff and the other offered a flat tariff.

Electricity market offers

As at 31 March 2014, the Energy Made Easy website showed a total of seven market offers from ActewAGL and EnergyAustralia for residential electricity customers in Canberra. These offers were very similar in terms of their tariff structures, discounts, contract types and other features. The table below summarises their key differences to provide examples of how retailers are differentiating electricity offers to residential customers in the region.

Table 7.1 Differences in electricity offers in Canberra as at 31 March 2014

Areas of difference between offers ***(high number of offers: >30; moderate: 15-30; low: 0-15)***	
Time of use tariffs	Low number of offers available with a low level of differentiation. There were three time of use tariffs available which had the same tariff structure but varied slightly by price.
Other tariffs	Low number of offers with a low level of differentiation. There are non-inclining block tariffs and one type of inclining block tariff.
Discounts	Low number of offers with a moderate level of difference. Conditional discounts from one retailer for bundling range from 3 to 25 per cent off usage.[220] One retailer offers a 3-8 per cent discount off usage charges for paying on time, while another offers a $0.055 per day discount for direct debit.
Contract duration	Low number of offers with a low level of difference. Choice of a two year fixed term, evergreen contract, or no fixed term.
Non-price incentives	No offers. In other jurisdictions, non-price incentives typically include cash bonuses for sign-up, loyalty programs, frequent flyer miles, etc.
Solar feed-in tariff	Low number of offers. Retailers offered feed in tariffs for solar panels of either 6 or 7.5 c per kWh.[221]

220 Customers who combine or bundle seven services from ActewAGL and TransACT such as electricity, landline, mobile phone, and internet will receive a 25 per cent discount on their electricity usage charges.

221 More information on solar arrangements is provided in Appendix D.

In addition to the features highlighted above, retailers also differentiate their brand through their marketing activities and customer service. This includes sponsorships and events in the community, energy efficiency services, shopfronts and offering solar systems with payment plans.

Seven offers were available to small business customers, with only marginal differences to the residential offers. The discounts available to small businesses were also similar.

Gas market offers

As at 31 March 2014, ActewAGL did not provide a market offer for gas in the ACT. EnergyAustralia offered four products which had the same inclining block structure but varied by the conditional discounts on offer which ranged from three to eight per cent.

7.6 Customer outcomes

Effective competition is characterised by how well the process of markets promote the long term interest of customers, including satisfaction with the level of choice available, the quality of service and the value for money provided by retailers. Our analysis of this criterion considered the findings of customer surveys and data on customer complaints, which suggest the following:

- **Many customers want greater choice of retailers and plans.** In the ACT, 35 per cent of customers surveyed were dissatisfied with the level of choice, which is more than double the NEM average.
- **Significantly more residential customers in the ACT are 'very' satisfied with their retailer** compared to other jurisdictions. Most business customers surveyed were 'somewhat' satisfied. Qualitative research suggests satisfaction relates to an absence of negative issues, rather than a particularly positive experience.
- **Complaints are relatively low in the ACT.** Complaints to the tribunal increased in 2012-13, but the number of complaints still remains relatively low.

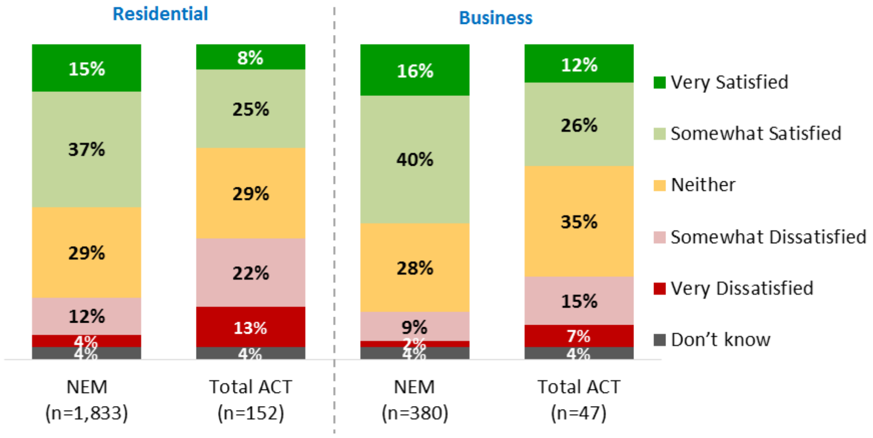
7.6.1 Satisfaction with the level of choice

Customer satisfaction with the level of choice in the ACT was lower than in any other jurisdiction surveyed. In the ACT, 35 per cent of residential customers surveyed were dissatisfied with the level of choice, 33 per cent were satisfied and the remainder were neutral or undecided. This is shown in Figure 7.6 below.

Forum participants who were dissatisfied with the level of choice mostly fell into two categories:

- those who were aware that customers had choice in other markets (many were not aware that the ACT differed to most other jurisdictions where there are many retailers to choose from); and/or
- those who were dissatisfied with their retailer's customer service and wanted to transfer to another retailer.

Figure 7.6 Satisfaction with the level of market choice



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p230. Survey question: When it comes to energy companies and energy plans, how satisfied are you with the level of choice available to consumers in your state /territory? Customers surveyed: All.

Statistics on satisfaction with the level of choice may not accurately represent customer sentiments as many customers falsely believed there was no choice in the market. In forums, some participants were more satisfied when they heard there was more than one retailer. Others noted that there still was not a 'real choice' in the ACT.

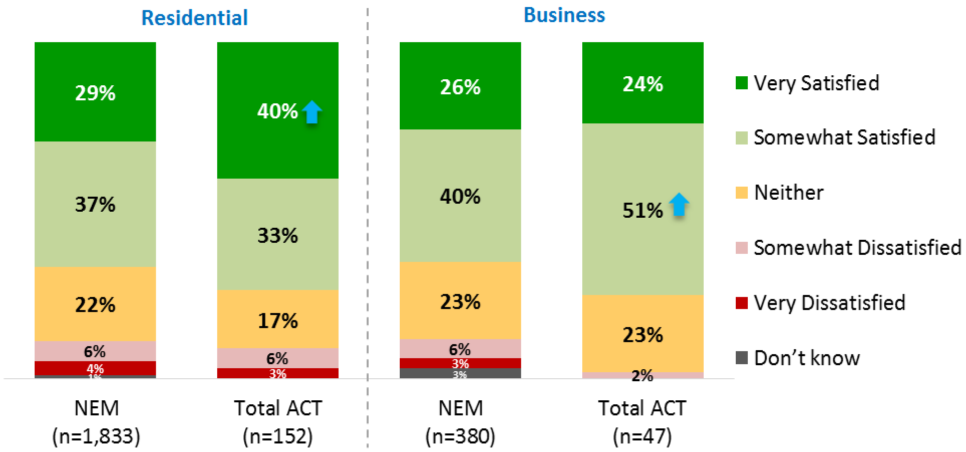
> "Coming from Sydney you could negotiate and ring other providers. Not here. I was told 'That's the price mate'. (Canberra, higher income)"

> "I had a bad monopoly experience and started to search but I found no other options, so just sucked it up (Canberra, income unidentified)"

7.6.2 Satisfaction with retailers

The majority of customers were satisfied with their retailer in all NEM jurisdictions surveyed. In the ACT, a similar proportion of residential customers were at least somewhat satisfied relative to the NEM average, but a considerably higher proportion was 'very satisfied' as shown in Figure 7.7 below. Small business customers in the ACT were less likely to be dissatisfied and more likely to say they were 'somewhat satisfied'. The majority of customers were satisfied with their retailer in all NEM jurisdictions surveyed, with 66 per cent somewhat or very satisfied with their electricity retailer.

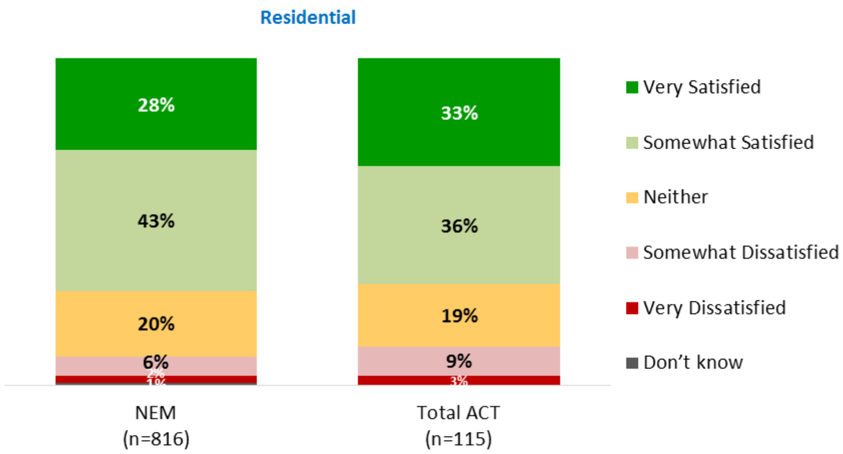
Figure 7.7 Satisfaction with current electricity retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p223. Survey question: How satisfied are you with your current electricity company? Customers surveyed: All.

Overall satisfaction with the customer's current gas retailer was slightly lower than the NEM average, but customers in the ACT were more likely to be 'very satisfied' than 'somewhat satisfied'. This is shown in Figure 7.8 below.

Figure 7.8 Satisfaction with current gas retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p224. Survey question: How satisfied are you with your current gas company? Customers surveyed: Customers who have mains connected gas.

Consistent with findings in other NEM jurisdictions, customer satisfaction may reflect an absence of supply issues or customer service issues. High satisfaction ratings in forums often related to an absence of negative issues with their retailer rather than a particularly positive experience.

> "I have no reason not to be satisfied. (Canberra, lower income)"

> "Unless you've got a problem you usually don't speak with your energy company. (Canberra, lower income)"

In forums, many were satisfied with their retailer due to the reliability of supply and were unaware this was an electricity network issue.

> "I'm very happy with the reliability. We don't have rolling blackouts like they do in Saudi Arabia. (Canberra, higher income)"

> "We don't get many outages. It just works. (Canberra, income unidentified)"

The overall quality of service for electricity and gas was largely perceived as good or excellent by survey respondents.

Satisfaction with customer service was mixed among forum participants. Some were satisfied with being able to speak to a 'real person' over the phone and speak to someone who is friendly and knowledgeable. Dissatisfaction often stemmed from having a particular issue and contacting the retailer. It was during this contact with the retailer they became unhappy with the customer service.

> "…I was very very angry. I thought about putting gas bottles in so I wouldn't have to deal with them. I had no other supplier to go to. No-one senior there would address it and good luck with the ombudsman. (Canberra, higher income)"

Value for money was rated at least fair overall. Over half of residential and business customers considered electricity value for money good or excellent. Eight per cent of residential customers and two per cent of business customers rated electricity value for money as poor. These results are broadly consistent with the NEM average, with the exception of small business customers where fewer in the ACT rated value for money as 'good' or 'excellent'.

Dissatisfaction may reflect concerns about price increases in the ACT in recent years. The largest driver of the price increase in 2013-14 was high network charges, accounting for two-thirds of the increase. The ACT's energy efficiency scheme accounted for the remaining third.[222] A full discussion of the drivers of price movements and trends in electricity prices is available in the AEMC's annual residential pricing trends report.

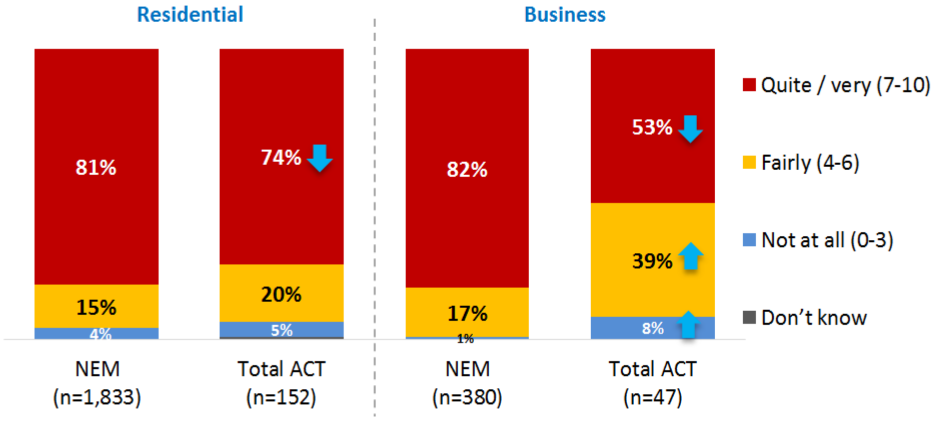
Seventy-four per cent of residential customers and 53 per cent of small business customers surveyed in the ACT stated that they were 'quite' or 'very' concerned about future electricity prices. These are lower than the NEM average, particularly for small business.[223]

---

222 AER, *State of the Energy Market 2013*, 2013, p131.

223 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p201.

Figure 7.9 Level of concern about future energy prices



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p201. Survey question: How concerned are you about future energy prices? Customers surveyed: All.

Slightly lower concern about electricity prices may reflect the fact that energy represents a smaller proportion of disposable income on average in the ACT relative to other jurisdictions. For ACT customers with high and middle incomes, annual electricity bills are estimated to represent approximately 0.4-1.0 per cent of the average disposable income. For low income customers on market contracts, annual electricity bills represent approximately 3 per cent of annual disposable, or slightly lower if the customer receives a concession.[224]

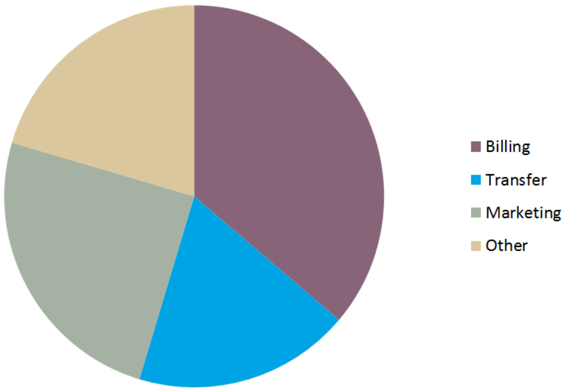
Pensioners, Health Care Card holders and veterans can be eligible for concessions through the Energy Concession and the added Utility Concession. Concessions are further discussed in Appendix B.

Complaints to retailers

When a customer makes a complaint, multiple issues may be raised. An accurate data time series on the number and type of issues raised with retailers was not available for the ACT. For 2012-13, approximately 3,200 issues were raised with electricity and gas retailers in the ACT. As shown in Figure 7.10, billing complaints made up 36 per cent of issues raised.

224 This AER analysis is based on average annual electricity consumption of 7,000 kWh for low income customers and 8,000 kWh for middle and high income customers. AER, *Annual report on the performance of the retail energy market 2012-13*, 2013, p84.

Figure 7.10 Electricity and gas complaints to retailers in 2012-13 - number of issues raised



Source: Data provided by the AER.

Since issues for electricity and gas are combined, the level of complaints regarding each service cannot be directly compared to the data presented for other NEM jurisdictions in this report. It is understood, however, that the ACT has considerably fewer electricity and gas complaints per 100 customers relative to New South Wales and South Australia.[225] Low complaint numbers in the ACT may be partly due to low marketing activity and fewer customers who are switching retailer or plan, when issues with retailers often arise.

Complaints to the Tribunal

In 2012-13, the number of issues raised with the ACT Civil and Administrative Tribunal (ACAT) regarding electricity retailers was slightly higher than in 2011-12 (see Figure 7.11).[226] Billing and credit issues have been the most common retail electricity issues raised with ACAT in the past two years. Close to 40 per cent of issues raised in 2012-13 related to billing and 24 per cent related to credit. Note that issues raised with ACAT include referrals back to retailers, which are also captured in complaints to retailers described above.

For the retail gas market in 2012-13, the number of issues raised with ACAT was lower than in 2011-12 (see Figure 7.12). Billing issues were the most commonly raised, closely followed by credit, making up approximately 42 per cent and 36 of gas issues raised in 2012-13, respectively.

ACAT primarily attributed the increase in total energy and water complaints between 2011-12 and 2012-13 'to increased complaints about EnergyAustralia and marketing during the 'One Big Switch' campaign which began in June 2012.'[227] ACAT also noted

---

225 The AER publishes quarterly complaints data on its website for NECF states (the ACT, New South Wales, South Australia and Tasmania).

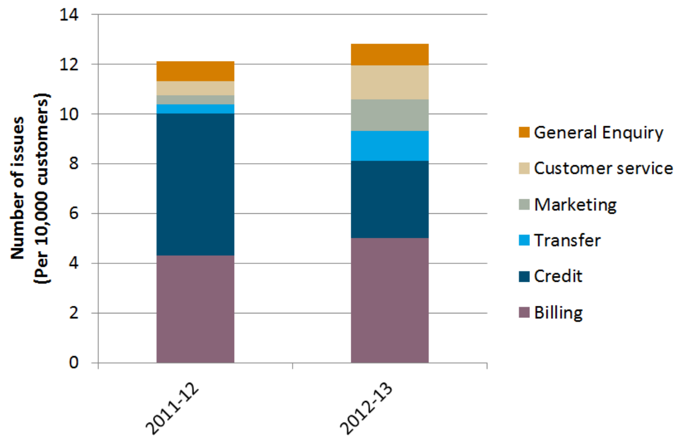
226 Data on complaints to ACAT excludes cases which were out of jurisdiction or not complaints.

227 ACT Civil and Administrative Tribunal, *ACT Civil and Administrative Tribunal 2012-13 Annual Report*, 2013, p375.

the number of electricity complaints against ActewAGL increased. 'The majority of ActewAGL Retail complaints concern unexpectedly high bills, responsibility for accounts and credit/debt collection issues.'[228]

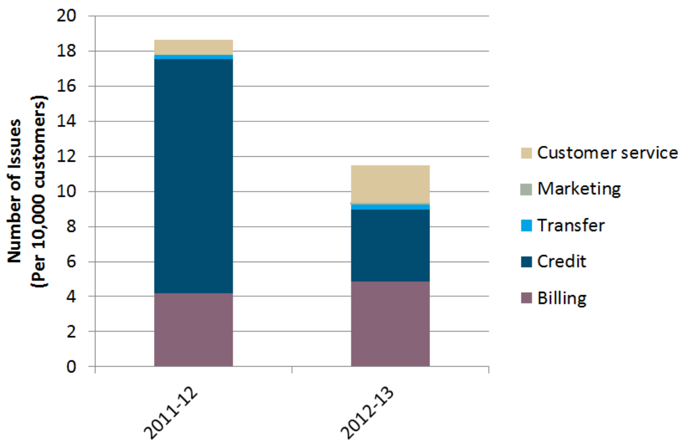
The data presented in Figure 7.11 and Figure 7.12 underestimates the number of credit issues relative to other jurisdictions because ACAT handles many credit issues through its hardship program. Applications to ACAT's hardship program are not included in Figure 7.11 and Figure 7.12. ACAT received 573 electricity hardship applications and 196 gas hardship applications in 2012-13, equating to 35 and 15 applications per 10,000 customers, respectively.

Figure 7.11 Electricity complaints to the ACT Civil and Administrative Tribunal - number of issues[229]



Source: Complaints data from ACAT, customer numbers from AEMO, AEMC analysis.

Figure 7.12 Gas complaints to the ACT Civil and Administrative Tribunal – number of issues



Source: Complaints data from ACAT, customer numbers from AEMO and Energy Supply Association of Australia (ESAA) *Electricity Gas Australia* reports, AEMC analysis.

228 ACT Civil and Administrative Tribunal, *ACT Civil and Administrative Tribunal 2012-13 Annual Report*, 2013, p376.

229 Complaints regarding solar feed-in tariffs are recorded as "general enquiry" complaints by ACAT.

7.7 Retailer outcomes

Profit margins can provide an indication of the level of competition in a market. However, they can also be expected to fluctuate over time. Consequently it is important to carry out analysis of retailer margins over a sufficiently long time period. It is also important to consider the results of such analysis in the context of other competitive indicators. This section makes a number of observations on retailer outcomes drawing from retailer interviews, submissions, ICRC price determinations and the findings of our previous review of competition in the ACT.

Several retailers noted in their submissions to the Approach Paper that new entrant retailers would be unable to recover their efficient costs of operating in the ACT as the regulated price does not accurately reflect the costs and risks of operating in the market.[230] This is consistent with the retailer survey, where the profitability of the ACT electricity and gas markets were rated as relatively low.

Retailer interview responses focussed on the electricity market.

The ICRC's approach to price regulation was the key issue cited in retailer interviews for the low profitability of the electricity retail market for new entrants. A series of issues were raised regarding the ICRC's methodology for determining regulated retail tariffs, discussed in section 7.4, and included a lack of competition allowance.

The ICRC's pricing determination for 2014-15, released in June 2014, explains the lack of competition allowance on the basis that it would not currently have benefits for ACT customers. The ICRC considers that introducing a competition allowance is:[231]

> "a high-risk strategy because there is a reasonable probability that any benefits it may produce will be long delayed, and therefore of little present value, and a distinct possibility that it will not produce benefits even in the long term."

Work undertaken by the Allen Consulting Group on behalf of the AEMC in the review of effectiveness of competition in the electricity retail market of the ACT found that the absence of headroom costs in ACT regulated retail prices results in very low retail margins for competing retailers. The Commission concluded in that review:[232]

> "...regardless of whether or not certain elements of CAC/CARC are included in the retail allowance in the ACT, the margins available to second tier retailers based on the relatively low allowance, are not perceived to be sufficient to encourage entry and expansion, given the risks associated with the provision of retail services and the unique characteristics of the market."

---

230 Alinta Energy, submission to the *2014 Retail Competition Review*, Approach Paper, p6 and Origin Energy, submission to the *2014 Retail Competition Review*, Approach Paper, p4.

231 ICRC, *Standing offer electricity prices from 1 July 2014*, Final Report, June 2014, p xi.

While we have not undertaken similar analysis for this current review, it would appear that margins continue to be insufficient to promote entry and so competition in the ACT electricity market. This is evidenced by the continuing lack of entry by second tier retailers and views put forward by retailers, both in response to the ICRC's pricing determination and in interviews for this review.

The AEMC provided advice to the COAG Energy Council on Best Practice Retail Price Regulation Methodology at the end of 2013. Some of these recommendations, if adopted, may address this potential barrier to entry and so competition.

Retailers did not specifically comment on the profitability of retailing gas in the ACT, but those that participated in the survey rated it the same profitability as retailing electricity and lower than other gas markets.

There is limited available information on the profitability of gas, particularly due to the confidential nature of wholesale gas contracts and the lack of publicly available reference data. However we note that, as discussed above, the need to achieve a minimum customer base is particularly important for gas because of the fixed cost nature of retailing gas. While economies of scope may not be an insurmountable barrier to entry, the risks associated with entering a small market could be high. Consequently, a higher return may be required to justify entry.

7.8 Future developments affecting competition in the market

Retailers do not expect any material change in the level of competition in the ACT electricity or gas retail markets over the next five years. Retailers have indicated little appetite to enter or actively compete in the ACT for the reasons outlined in this chapter. While survey responses suggest that one small retailer may consider entry into the small business segment and another may consider entry into the residential segment, neither have firm plans to do so. No retailers are intending to enter the gas market over the next five years.

In the event that new retailers enter the market or existing retailers expanded their range of offers, a customer engagement campaign could help to promote greater awareness that customers can shop around and choose between plans and retailers. The campaign could also generate greater awareness of the AER’s comparator website and provide additional tools and information to support customers to investigate their options.

---

232 AEMC, *Review of the effectiveness of competition in the electricity retail market of the ACT, Stage 1 Final Report*, 24 November 2010, Sydney, p65.

8 Victoria

Box 8.1: Key message

- Competition is effective in the Victorian electricity and natural gas retail markets and is delivering customers a choice of retailers and plans.
  - Customers can choose from a range of retailers and products and many are shopping around. Four in ten energy customers looked for a better deal in 2013 and around a quarter of customers switched retailer. Others found a better deal with their existing retailer.
  - Sixteen retailers are competing to acquire and retain electricity customers by offering a range of discounts and other incentives. Six electricity retailers are intending to expand in the next five years.
  - Eight gas retailers are already competing and two second tier retailers are intending to enter the gas market. Three gas retailers are planning to expand in the next five years.
- Estimates of gross retailer margins appear higher in Victoria than in other jurisdictions, however margin estimates should be interpreted with caution as margins are expected to fluctuate over time and estimates are prone to error. Further, other competitive indicators suggest that the Victorian electricity market exhibits the right conditions to promote competition between retailers as it continues to evolve and mature.
- There is an opportunity to further increase competition by encouraging all energy customers to become ‘energy shoppers’, particularly the 25 per cent of Victorian customers who remain on high priced standing offers.
- Raising awareness of the Victorian Government's price comparator websites could encourage customers to shop around by providing them with a trusted tool that makes it easier to compare offers and find possible savings.
- The requirement for retailers to provide a standing offer may create an artificial benchmark for retailers' pricing strategies and can make it difficult for some customers to compare offers. This issue may warrant further investigation.

8.1 Overview

The AEMC first reviewed competition in Victoria's energy market in 2007 and found that competition was effective in the small customer electricity and gas retail markets.[233]

The Commission's assessment of competition against the five criteria set out in Chapter 2 has found that competition continues to be effective in the electricity and gas markets. The findings for the Victorian retail market can be summarised as follows:

- **Customer activity**: Most customers have chosen market offers, many are actively investigating their options and Victoria has the highest level of switching between plans and retailers.
- **Barriers to entry, exit and expansion**: Retailers consider there are fewer barriers to entry or expansion in the gas or electricity market than in other jurisdictions. Retailers identified Victoria as the preferred jurisdiction to enter the retail energy markets in Australia.
- **Independent rivalry**: There is evidence of strong rivalry between the 16 electricity and eight gas retailers through a high level of retailer product differentiation and marketing activity. Second tier retailers are very active and winning electricity customers from the three incumbent retailers.
- **Customer satisfaction**: Most customers surveyed were satisfied with the level of choice in the market, the quality of service and the value for money provided by retailers.
- **Retailer outcomes**: Based on analysis undertaken as part of the AEMC's 2013 Residential Electricity Price Trends review, estimated gross retailer margins for February and September 2013 appeared higher in Victoria then in other jurisdictions. However, these results should be interpreted with caution due to the inherent challenges of estimating retailer margins and the propensity of margins to fluctuate over time. For instance, these results could be driven by:
  - market modelling that under-estimates wholesale energy costs in the current environment of falling demand; and/or
  - operational/regulatory costs faced by retailers in Victoria being higher than in other jurisdictions.

233 AEMC, *Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in Victoria*, First Final Report, 19 December 2007, Sydney.

8.2 History and market characteristics

Full retail competition was introduced for Victorian small customers in the electricity market in January 2002 and in the gas market in October of that year.[234] In January 2009, the Victorian Government removed price regulation for both markets.

All retailers are now required to offer a standing contract for electricity and gas with regulated terms and conditions.[235] Retailers in Victoria are also able to offer market contracts where the terms and conditions are determined by the retailer. The prices for standing contracts and market contracts are determined by the retailer and monitored by the Essential Services Commission of Victoria.

The Victorian Government has deferred the implementation of the National Energy Customer Framework (NECF). In the interim, the Victorian Minister for Energy and Resources has asked the Essential Services Commission to harmonise the Victorian retail regulations to the extent possible with the NECF.[236]

8.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

Our analysis of this criterion considers the findings of a customer survey and qualitative forums performed by Newgate Research and data provided to the AEMC on customer switching. This analysis suggests the following:

- **Customers in Victoria are the most active** of all national electricity market (NEM) jurisdictions.
- **Most customers have chosen market offers**. Approximately 75 per cent of electricity and gas customers are on market offers, however more could be done to encourage those remaining on standing offers to switch to cheaper plans.
- **There is high awareness of the ability to choose from a range of plans** with different price structures, contract lengths, discounts and other incentives.
- **More Victorian customers are investigating their options and switching** between different market offers than in any other NEM jurisdiction.

---

234 The consumption threshold for defining small electricity customers in Victoria is below 40 megawatt hours per annum, which is lower than the 100 megawatt hour threshold of most other NEM jurisdictions and less than 1 TJ per annum for gas.

235 Essential Services Commission, *Progress of electricity retail competition in Victoria*, Research Paper, May 2013, p3.

236 http://www.esc.vic.gov.au/Energy/Harmonisation-of-Energy-Retail-Codes-and-Guideline

8.3.1 Customer awareness and understanding

Ninety five per cent of residents and 89 per cent of businesses were aware they have a choice of electricity retailer. The numbers were similar for natural gas retailers, with more customers in Victoria aware of this choice than in other NEM jurisdictions.

> "There's a wealth of information out there – on the internet, over the phone. There's so many companies that fight to have you and they will release more information to make themselves look better. (Ballarat, income unidentified)"

Knowledge of the different options for energy customers was higher among forum participants in Victoria than in other jurisdictions. Most forum participants could name between four and eight electricity companies and between three and five gas companies. In other jurisdictions, most participants could name one or two of the large retailers and few could name any smaller (second tier) retailers.

Residential customers had a higher than average awareness that they can choose between different plans in Victoria, but small businesses were slightly below the NEM average. Eighty-six per cent of residents and 78 per cent of businesses in Victoria were aware of this choice. Victorian forum participants also had a high awareness of the different types of contracts and the range of discount options. There was also a broad range of incentives or 'bonus gifts' listed, more so than in any other jurisdiction.

While there was high awareness of the options available, survey respondents report mixed levels of confidence in understanding these options, with customers in regional Victoria considerably less confident than those in Melbourne. Almost 20 per cent of residential customers surveyed in Melbourne were 'not at all' confident they understood the offers available, compared to 28 per cent of customers in regional Victoria. This pattern of lower confidence in regional areas was not seen in other NEM jurisdictions surveyed.

In the Victorian forums, a key message was that energy offers were too numerous and hard to compare because they were all presented differently and in ways that were hard to understand. Smart meters were the second most frequently mentioned energy issue in Victoria (behind price), with most of the discussion centred on questions around the value and use of smart meters, and the added cost.

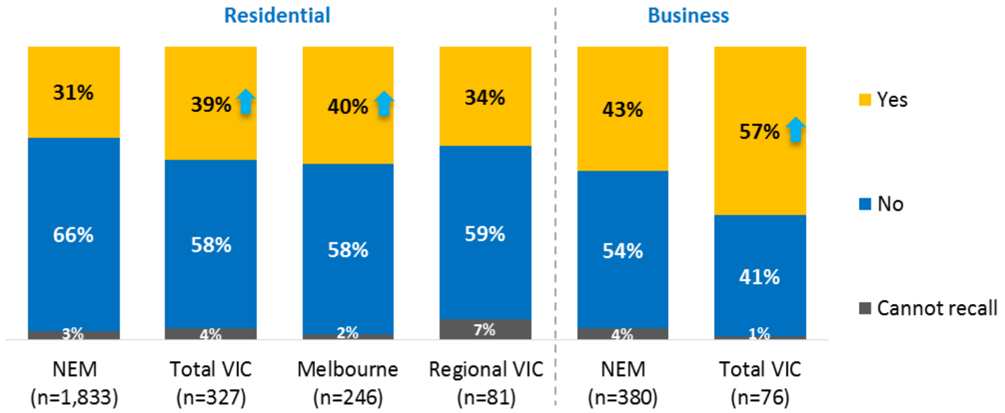
8.3.2 Customers investigating options and switching

For a market to be effectively competitive, it is not sufficient for customers to simply be aware of their ability to choose their retailer. They also need to have information and tools to investigate their options and switch plan or retailer to receive a lower price or better service.

Evidence suggests Victorian customers are the most active of all NEM jurisdictions based on the number of customers who investigated their options, as well as data and survey responses on customers who switched retailer or plan.

Thirty-nine per cent of residential customers investigated options in the last twelve months, compared to the NEM average of 31 per cent (as shown in Figure 8.1). For small business the numbers were even higher, with 57 per cent of customers investigating options, compared to the NEM average of 43 per cent. The arrow indicates a result that is statistically different from the NEM average at the 95 per cent confidence level.

Figure 8.1 Customers who actively investigated offers or options in past 12 months



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p32. Survey question: In the past 12 months, have you actively investigated different offers or options that you could potentially switch to? Customers surveyed: All.

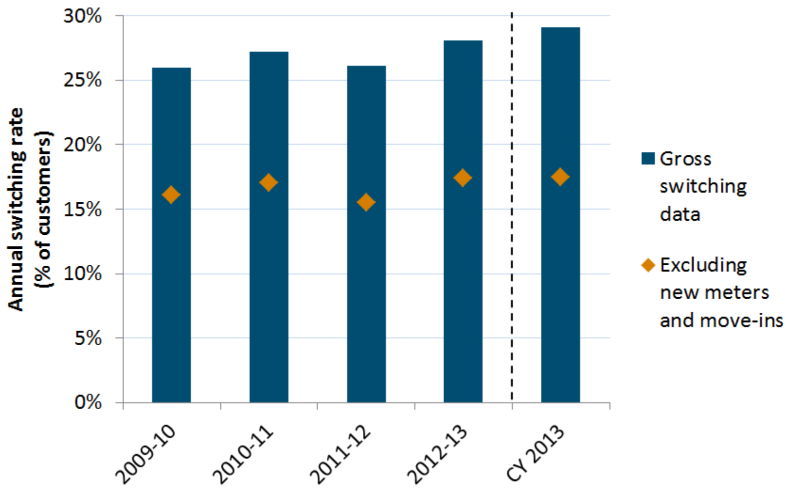
Victorian customers were also the most active of those surveyed in terms of switching retailer or plan, with around two thirds having switched provider or plan twice in the last five years. The number of switches was notably above the NEM average for gas, but this represents the higher sample of gas customers surveyed in Victoria due to high gas penetration in the state.

There was a strong relationship between the number of times people had changed their retailer or plan and the number of retailers that had approached them. Around two thirds of customers had been approached by a retailer in the last twelve months, which is above the NEM average of 53 per cent. Customers in Victoria also reported being approached by more retailers than in other jurisdictions.

Figure 8.2 shows actual customer transfer data from one retailer to another per year.[237] Consistent with the survey results, this data illustrates the high level of customer switching between retailers. Electricity switching rates exhibit monthly volatility but have been gradually increasing since 2009-10 and reached an average of approximately 28 per cent for 2013.

237 See Chapter 2 for a discussion on interpreting this data.

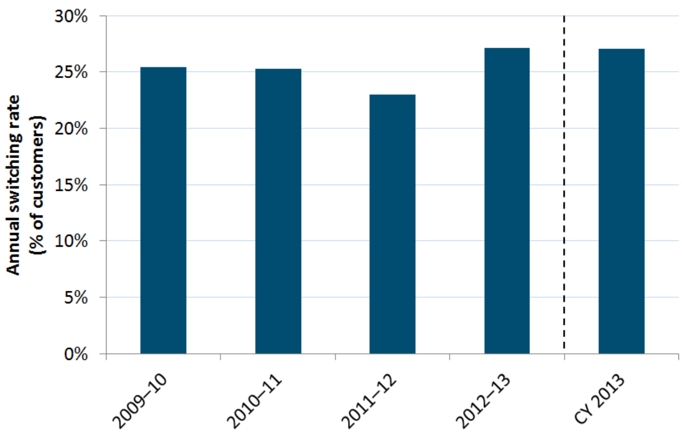
Figure 8.2 Victorian electricity switching



Source: AEMO data, AEMC analysis.

For gas, Figure 8.3 shows that actual gross switching rates are almost identical to electricity with an average of approximately 27 per cent in 2013. Trends in annual switching rates for gas have closely followed those for electricity. Findings from retailer interviews and customer research suggest that gas is a secondary consideration for most customers and that gas switching decisions appear to be linked to electricity switching decisions, with many choosing to bundle their gas and electricity with the same retailer.

Figure 8.3 Victorian gas switching



Source: AER State of the Energy Market, 2013 and AER Retail Statistics[238].

Switching data for electricity and gas may under-represent how active customers are in the market. Many customers have actively investigated their options and either chosen to remain on their existing plan or have chosen to switch plans with their existing retailer. Data provided by retailers suggests that up to 25 per cent of customers

238 http://www.aer.gov.au/Industry-information/industry-statistics/retail

changed their electricity plan with their existing retailer in 2013. For gas, up to 24 per cent of customers did so.

Electricity price appears to be the key driver for switching

In its submission to the Approach Paper, the Victorian Government asked the AEMC to determine the key reasons why customers switch between retail offers. We were also asked to identify potential barriers to switching.[239]

The findings of a customer survey and qualitative forums performed by Newgate Research for this review suggest the key reason for switching energy retailer or plan in all NEM jurisdictions was to obtain a better price.

Of Victorian customers that switched electricity retailer or plan, 66 per cent of residents and 68 per cent of businesses stated that price was the main reason to do so. Similarly for gas, 66 per cent of residents and 56 per cent of businesses stated that price was the main reason they switched retailer or plan.

In forums, the main trigger for investigating options and switching was customers discovering that they could save money, either through word of mouth, direct marketing or advertising.

> "I got a marketing phone call and was offered a Royal Auto membership with Simply Energy. It was 30 per cent off the usage for electricity and 10 per cent for gas, but no discount off the service charge. They had a cooling off period so I signed up and looked into it by going to different energy company websites. The offer was good so I stayed with it. (Melbourne, income unidentified)"

Others were driven to investigate and switch of their own volition when they received unexpectedly high bills or noticed costs increasing over time.

A distant second to price, nine per cent of respondents cited moving house and nine per cent cited being unhappy with customer service as being their main reason for changing retailer or plan. Customer service was a lower order issue for respondents who switched gas retailer or plan, with more citing moving house or wanting to bundle electricity and gas with the same retailer.

In regional Victoria, nine per cent of customers stated the main reason they switched electricity retailer was because they have solar panels, which is considerably higher than the one per cent of respondents in Melbourne who cited this reason. Customers in all NEM jurisdictions are able to switch retailer without losing their government feed-in tariff rate, except for Victorian customers who are on the 'Standard Scheme'. This is discussed in further detail in Appendix D.

---

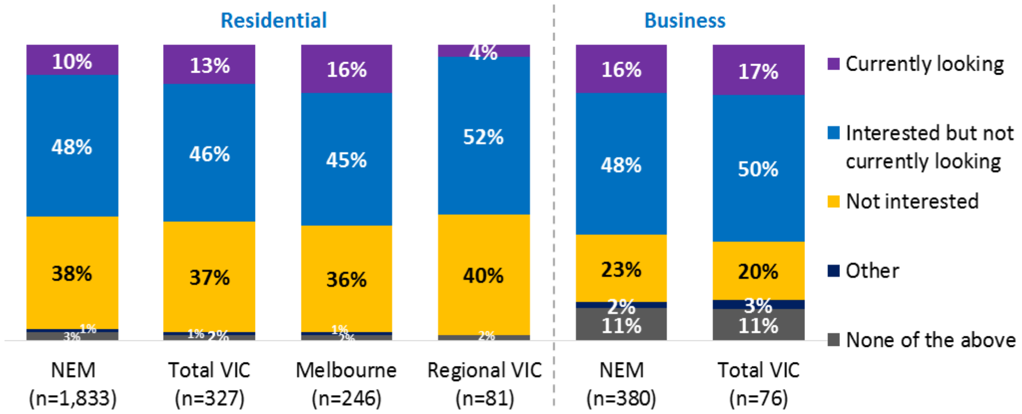
239 Victorian Department of State Development, Business and Innovation, submission to the *2014 Retail Competition Review*, Approach Paper, p4.

Some customers are less engaged

After five years of deregulation, around 25 per cent of customers are on standard contracts for electricity and gas in Victoria.[240] This roughly correlates to the survey findings that around one third of electricity customers had not switched retailer or plan in the last five years.

While the majority of customers stated they are interested in looking for a better deal, 37 per cent of residents surveyed were not interested (see Figure 8.4), which is consistent with the NEM average. We note that 39 per cent of residential customers surveyed had already investigated options in the last twelve months, which may explain why there is some disinterest in investigating deals or switching in the next twelve months.

Figure 8.4 Interest in looking for a better deal

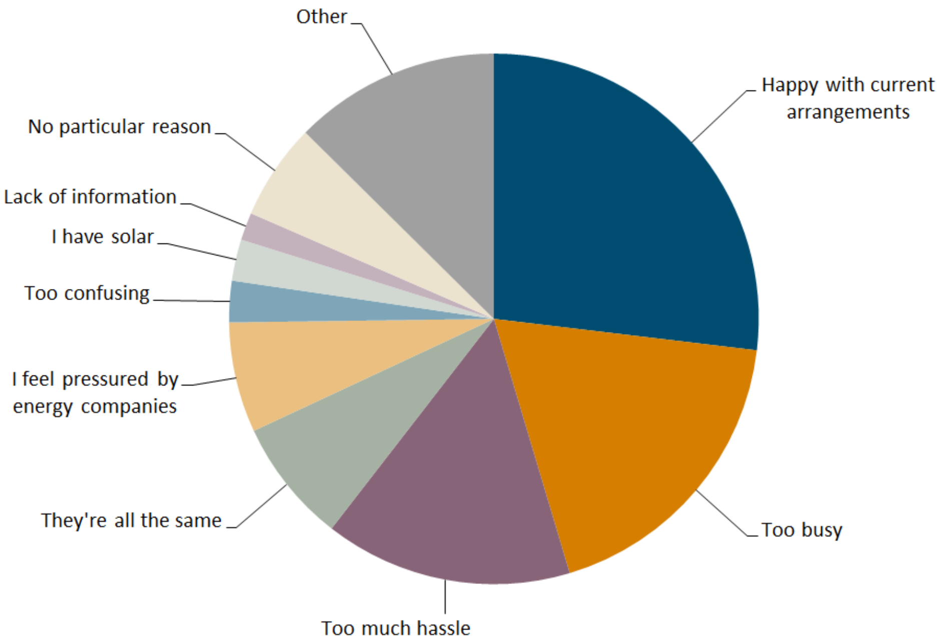


Source: Newgate Research, *Customer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p50. Survey question: When it comes to your household's energy company, which of the following statements is most applicable to your household? Customers surveyed: All.

Figure 8.5 shows the most common reasons cited by customers surveyed in Victoria who had not investigated options in the last 12 months or switched retailer or plan in the last five years.

240 AER, *State of the Energy Market 2013*, 2013, p126.

Figure 8.5 Most common reasons for not investigating options or switching



Source: Data from Newgate Research, Consumer Research for Nationwide Review of Competition in Retail Energy Markets, a report for the AEMC, June 2014, p39. Survey question: Are there any reasons why you haven't investigated different options or why you haven't changed your energy company or plan in the last few years? Customers could select multiple responses. Customers surveyed: Residential customers who hadn't investigated options and hadn't changed their energy company.

The most common barrier to investigating options or switching raised in the survey and in forums was a strong sense it was not worth the time involved. This was because they had no issues with their current arrangements or, in some cases, because they thought they would not get a better deal elsewhere.

> "You end up paying the same no matter which provider you're with. It doesn't make any difference in the long run. The difference is $10. I've done all the research, but I'm not confident once it's done. (Melbourne, did not switch)"

AEMC analysis shows that the higher level of product differentiation in Victoria means many customers could actually benefit from changing plans, particularly if they are currently on standing offers.

Box 8.2: Potential savings from moving off a standard offer to a market offer

The AEMC's 2013 Residential Electricity Price Trends report found that customers in Victoria may have saved around $240 or 16 per cent off their total annual bill by switching from a standing offer to a market offer in 2012-13. This does not capture the full savings which could be made by switching to the best advertised market offer or by negotiating with retailers to obtain lower prices than those advertised.

In many cases, forum participants had decided not to switch simply because their retailer did not annoy them.

> "They don't annoy me and I don't annoy them. I had a couple of years where different energy companies were calling me up. My time is worth more not talking to them than it is being interrupted. (Melbourne, looked but did not switch)"

Customers surveyed were mostly satisfied with the switching process, but some forum participants who had started looking at switching found the process too time consuming, confusing and difficult, and dropped out.

Many forum participants also cited mistrust of retailers as a reason for not engaging in the market. These customers felt they could not trust the information provided by retailers or their behaviour, with some believing the retailer would increase prices shortly after signing a new contract. Negative perceptions were largely based on personal experiences with their retailer, with door knockers and, to a lesser extent, word of mouth. Many of these negative experiences occurred some years ago and there was a general sense that telemarketing calls and door knocking had receded over the last two years.

Qualitative research suggests that in the early days of deregulation, the impetus to look into switching came from approaches over the phone or door knocking. More recently this has moved towards word of mouth and mainstream advertising. While door knocking was seen as a barrier to switching in the survey, it did form an effective trigger for some customers to look into switching.

Evidence suggests that most customers prefer to make choices using online information. However, in the quantitative survey, only one per cent were able to name a government price comparator website and over two thirds of residents and 60 per cent of small businesses could not name any comparison websites.

8.4 Retailer barriers to entry, exit and expansion

Barriers to entry, exit and expansion are another important indicator of the state of competition. Low barriers to entry and expansion place competitive pressure on retailers due to the threat of new entrants or other incumbents attracting away customers. These competitive pressures should lead to retailers charging prices that are commensurate with their costs and providing customers with the products and service that they demand.

Our analysis of this criterion considers key findings from retailer interviews and surveys conducted by K Lowe Consulting and Farrier Swier Consulting for this review.[241]

---

241 For full details refer to K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014.

Eleven of the 16 energy retailers that are currently active in Victoria agreed to participate in the retailer interview and survey process.[242] One of the key issues that retailers were asked to provide their opinion on is the ease with which entry and expansion can occur in gas and electricity retail markets in Victoria. The responses to this question revealed the following:

- entry into the Victorian gas and electricity retail markets and expansion within these markets is perceived to be relatively easy by retailers; and
- Victoria is the preferred entry point for new electricity and gas retailers because:
  - retail price regulation has been removed, alleviating the risk of retail prices being set below the efficient cost of supply by a regulator;
  - the level of customer awareness is relatively high;
  - conditions in the wholesale electricity market in Victoria have been relatively conducive to entry to date; and
  - the penetration and volume of gas consumed by small customers in Victoria is higher than in any other jurisdiction and the design of the Declared Wholesale Gas Market (DWGM) and the market carriage model has been conducive to entry by small gas retailers.

The views expressed by retailers on entry and expansion conditions in these two markets are consistent with the Commission's finding in the 2007 review of the effectiveness of retail competition in Victoria that there are no significant barriers to entry or expansion in either market.[243] They are also consistent with the following observations on the level of entry that has occurred in the last two years and the success second tier retailers have had in expanding their customer bases over this period:

- **Electricity retail market** – In the last two years, five second tier retailers[244] have entered the electricity retail market, which is indicative of relatively low barriers to entry. The success that a number of second tier retailers have had in expanding in this market also suggests that the barriers to expansion are relatively low.[245]
- **Gas retail market** – In the last two years, two second tier retailers have entered the gas retail market and another two retailers are reportedly planning to enter in 2014, which suggests that the barriers to entry are relatively low. Like their

242 As at December 2013, AGL owned Australian Power and Gas and Powerdirect and these are treated as one retailer for our analysis of competition in the market. Alinta and Neighbourhood Energy are also treated as one retailer for the purpose of our analysis.

243 AEMC, First Final Report: Review of the Effectiveness of Retail Competition in Victoria, December 2007, p134.

244 The five second tier retailers are Alinta Energy, Blue NRG, People Energy, Powershop and QEnergy.

245 ESC, Progress of Electricity Retail Competition in Victoria – Research Paper, May 2013, p. 20, AER, State of the Energy Market 2012, p. 121 and AER, State of the Energy Market 2013, p122.

electricity counterparts, second tier gas retailers appear to have had some success in expanding their customer base over the last two years, which suggests that barriers to expansion are relatively low.

While there is no evidence to suggest that there has been a material increase in the height of the barriers to entry or expansion in this market since the last review, retailers have identified a range of regulatory and non-regulatory factors that may affect the ease with which entry and/or expansion can occur in these two markets. Further detail on the factors cited by retailers is provided below.

We also note that as part of the survey process, retailers were asked whether they plan to enter, expand or exit either the gas or electricity retail market over the next five years. The responses to this question indicate that:

- six existing retailers are planning to expand in the electricity retail market over the next five years; and
- two second tier retailers are planning to enter the retail gas market in 2014 and three existing gas retailers are planning to expand in the next five years.

8.4.1 Regulatory impediments are perceived to be increasing

During the retailer interviews, a number of gas and electricity retailers noted the potential for the following factors to affect the ease with which entry and/or expansion can occur in the market:

- The level of regulatory risk, such as the recent announcements of back billing regulations, which retailers claim is increasing and giving rise to higher levels of uncertainty for retailers.[246]
- The absence of any firm commitment by the Victorian Government to implement the NECF, which retailers claim is giving rise to higher system and compliance costs and is acting as an impediment to retailers seeking to expand across multiple jurisdictions. Retailers also noted that the current customer protection framework in Victoria is:[247]
  - more onerous and costly than the NECF; and
  - resulting in retailers holding higher levels of debt and for longer periods of time in Victoria than in other jurisdictions.[248]

246 Some of the factors that retailers pointed to in support of this view are the absence of a commitment to implement the NECF and the recent announcement of new back billing regulations.

247 Amongst other things, the term 'customer protection framework' is used in this context to refer to hardship schemes and regulations pertaining to wrongful disconnections, back billing, late payment fees and disconnection/re-connection timeframes.

248 The specific aspects of the customer protection framework that retailers noted are resulting in retailers having to hold higher levels of debt are the wrongful disconnection and back billing regulations.

- The concession schemes in Victoria, which retailers claim are more complex and therefore costly to administer than in other jurisdictions.

The following quote from the retailer interviews illustrates the experience of one retailer when entering the Victorian retail energy market:[249]

> "Setting up our systems for Victoria was by a distance the most difficult. Firstly, they have an onerous and complex concession system. Secondly, they have an onerous and complex set of derogations around customer service. So they have things like the collection cycle has to be 14 days as opposed to 10 days everywhere else. They have the wrongful disconnection structures. There is a significant raft of consumer benefits that are given in Victoria but not elsewhere."

While it is clear that entry is still occurring in Victoria in the presence of these factors, they may be giving rise to higher compliance and system costs, and exposing retailers to higher levels of risk than in other jurisdictions. To the extent that retailers pass these costs on to small customers in the form of higher retail prices, then Victorian customers could benefit from a more consistent regulatory environment through further moves to harmonise the consumer protection and concession schemes with other jurisdictions.

A comparison table that outlines the differences between retail customer protections/requirements in Victoria and the NECF is in Appendix F.

8.4.2 Non-regulatory factors potentially affecting entry and expansion in electricity

Some other factors that retailers claimed may affect the ease with which entry and/or expansion occurs in the Victorian retail electricity market include:

- the increased degree of vertical integration in the Victorian wholesale electricity market;
- the wholesale market settlement process in Victoria, which following the roll out of smart meters is based on actual consumption rather than the net system load profile (NSLP);
- the importance of offering both gas and electricity; and
- prudential and credit support requirements.

Prudential and credit support requirements are not unique to Victoria and these are discussed further in section 3.2.3. The remainder of this section provides further detail on the remaining non-regulatory factors.

249 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p87.

Wholesale market conditions

The Commission understands from feedback provided by small and large retailers that conditions in the wholesale electricity market have been relatively conducive to entry and expansion in the Victorian retail electricity market to date. Concerns were raised though by a number of non-vertically integrated retailers about the effect that increasing vertical integration may have on the ability of new entrants and smaller players to access competitively priced hedging instruments going forward.

The degree of vertical integration in Victoria increased in mid-2012 when AGL acquired the remaining share of Loy Yang A. As a result of this acquisition, the proportion of generation capacity in Victoria that is controlled by vertically integrated retailers rose from 70 per cent to 94 per cent.[250]

While there has been an increase in the degree of vertical integration in the last two years, the ability to access competitively priced hedging products does not appear to constitute a significant barrier to entry or expansion in Victoria at present for the following reasons:

- there are still a small number of independent generators operating in Victoria that are able to offer over the counter (OTC) hedging products;[251]
- the generation capacity controlled by both Snowy Hydro and International Power is much larger than they require to supply their respective electricity customer bases and therefore should be in a position to offer OTC hedging products to non-integrated retailers;[252]
- there have been some recent losses of large industrial loads in Victoria, including the Alcoa aluminium smelter at Point Henry, which should free up some contracted capacity; and
- the turnover of electricity derivatives in Victoria has been relatively high in recent years at three to four times underlying energy sold, supporting the ability of new entrants to purchase hedge cover; the liquidity ratio in 2012-13 was slightly below the NEM average (see Figure 8.6).[253]

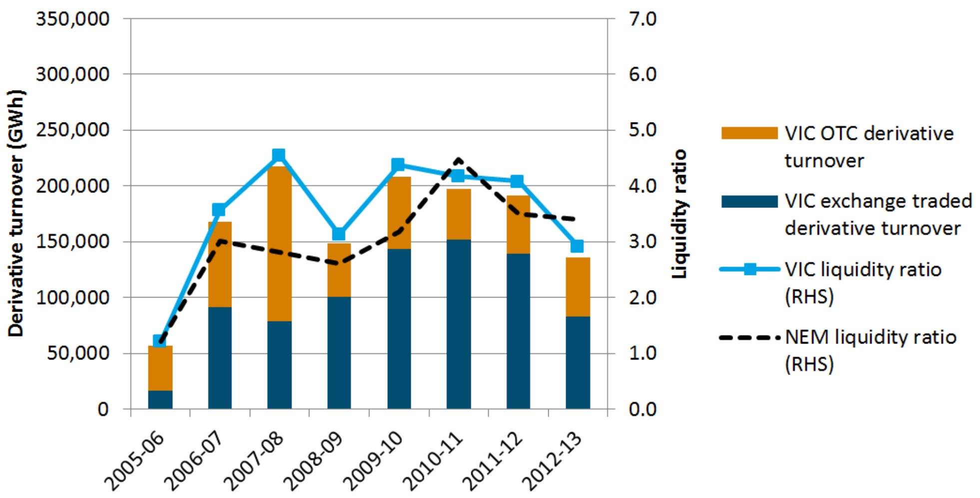
250 AGL 29 per cent, International Power/Simply Energy 22 per cent, Snowy Hydro/Red Energy 20 per cent, EnergyAustralia 19 per cent and Origin Energy 4 per cent (AER, *State of the Energy Market 2013*, 2013 p32)

251 ibid, p31.

252 ibid, p124.

253 See chapter 2 for discussion on interpreting this data.

Figure 8.6 Annual electricity futures turnover and liquidity ratios



Source: ASX Energy and AEMO data; AEMC analysis.

While current conditions in the Victorian wholesale market do not appear to be impeding entry or expansion in the retail electricity market, it is possible that this could change in the future. The Commission will monitor this issue as part of the annual competition reviews.

Wholesale market settlement process

According to some smaller retailers, the movement from settling the Victorian wholesale market on the basis of the net system load profile to actual metered consumption has exposed new entrants and smaller retailers to a greater degree of demand volatility and higher hedging costs. This is because the customer base of smaller retailers is not as diverse as larger retailers and peakier loads are more expensive to hedge against.

There is no evidence to suggest moving to settlement based on actual metered consumption has prevented the entry of efficient new retailers into Victoria or led to any retailers exiting the market. The Commission considers that the new settlement process is therefore unlikely to constitute an insurmountable barrier to entry and over the medium to long term may provide for more accurate and efficient hedging strategies.

Importance of offering a dual fuel product

The penetration of gas and the volume of gas consumed by small customers in Victoria is far higher than they are in other jurisdictions.[254] Retailers made it clear that offering

254 According to estimates published by the Australian Bureau of Statistics (ABS) and Bureau of Resources and Energy Economics (BREE): in 2011 the gas penetration rate in Melbourne is 91 per cent while in regional areas of Victoria it is 57.5 per cent; and in 2011-12 residential customers in Victoria consumed just over 100 PJ of gas. ABS, 4602.0.55.001 Environmental Issues: Energy Use and Conservation, March 2011, Table 6 and BREE, 2013 Energy Consumption by Industry and Fuel Type, Table F.

a dual fuel product was not a condition of entry into the Victorian electricity retail market, but due to the high level of gas penetration, if a retailer wants to expand beyond a certain threshold they need to offer both.

The retailers' proposition that a dual fuel product offering is more important in terms of expansion than entry is consistent with the fact that there are a number of electricity only retailers currently operating in Victoria and that all of the larger second tier retailers are offering both gas and electricity. However, in the Commission's view the need to offer both gas and electricity is unlikely to constitute a significant barrier to expansion in the Victorian retail electricity market. Given the ease with which entry can reportedly occur in the retail gas market, electricity retailers can presumably offer a dual fuel product if they need to, in line with their business strategy.

Dual fuel product offerings are also a point of differentiation, allowing retailers to bundle two products used by households at a lower average cost than if a customer purchased each from separate retailers. This is known as economies of scope and retailers compete by passing the savings on to customers through lower prices.[255]

8.4.3 Other factors potentially affecting entry and expansion in gas

As noted previously, the Victoria retail gas market is considered the preferred entry point for new entrant gas retailers because the penetration of gas in Victoria is far higher than it is in other states and the design of both the DWGM and market carriage model are conducive to entry.[256] Retailers did note the potential for the following factors to affect the ease with which entry and/or expansion can occur:

- the Gas Safety Case, which all new retailers in Victoria are required to develop and have approved by Energy Safety Victoria (ESV) before they start retailing; and
- tightening demand and supply conditions in the wholesale gas market brought about by the development of liquefied natural gas (LNG) facilities in Queensland.

Retailers also noted that entry and expansion in regional areas outside the DWGM can be more difficult due to the small size of the customer base in these areas and constraints on the availability of capacity on some regional pipelines. Further detail on each of these factors is provided below.

---

255 Economies of scope occur when it is cheaper to produce two products together instead of both separately. In this case, the savings arise through common back office systems, people and infrastructure.

256 The market carriage model and DWGM are seen as being conducive to entry because retailers do not need to enter into long term gas transportation agreement and they have equivalent access as incumbent shippers to trade imbalances and purchase gas at the spot price. New entrants have also been known to rely on purchases of gas from the DWGM in the initial stages of entry, rather than entering into a gas supply agreement.

Gas Safety Case

Before a gas retail licence can be granted in Victoria, a retailer must develop a Gas Safety Case and have it approved by the ESV. According to two recent entrants and two retailers that are in the process of entering the Victorian gas retail market, the Gas Safety Case process is 'unduly difficult, time consuming and costly'. Retailers also questioned the value of retailers having to comply with this requirement given that many of the risks are beyond the control of retailers.

The Commission is not in a position to express an opinion on the merits of retailers having to comply with this requirement. However, it would appear from the retailers' recent experiences that the process is costly (estimated to have cost one retailer over $100,000) and has slowed the entry process down (two retailers reportedly delayed their entry by over four months). While there is no indication that these costs or delays are deterring entry, there may be value in the relevant body considering whether improvements can be made to the current process to try and reduce compliance costs and/or the time retailers spend developing a Gas Safety Case.

Conditions in the wholesale gas market

As noted in section 3.3.3, conditions in the wholesale gas market are starting to tighten as a result of the development of LNG facilities in Queensland and wholesale gas prices are rising. While the Victorian retail gas market is some distance from these developments and is located in close proximity to significant gas reserves, retailers still expect the effect of higher wholesale gas prices to be felt in Victoria, albeit to a lesser extent than in other jurisdictions.

Whether or not higher wholesale gas prices in Victoria will deter entry or expansion in this market over the next five years is yet to be determined. However, given that two retailers are planning to enter this market in 2014 and a number of existing retailers are planning to expand, it would appear that retailers in Victoria are still able to access competitively priced gas and that this is unlikely to be as significant an issue as it may be in the northern jurisdictions.

Constraints in rural and regional areas

In a similar manner to South Australia, Victorian retailers noted that entry and expansion in regional areas (located outside the DWGM) can be more difficult because:

- the capacity of the regional pipelines has been fully contracted by either a single retailer or a very small number of retailers; and/or
- the size of the customer base in these areas is too small to make entry by a large number of retailers economically viable given the fixed cost nature of retailing gas.

The pipelines that retailers identified in this context include the Carisbrook to Horsham pipeline, the South Gippsland Gas Pipeline and the Berri to Mildura Pipeline.

For the reasons set out in section 9.4.2, the Commission agrees that these structural features may constitute a barrier to entry and/or expansion in some regional areas of Victoria.

8.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

Our analysis of this criterion considered findings from retailer interviews and advertised market offers, which suggest the following:

- There is a high degree of rivalry in Victorian energy markets between 16 retailers competing for electricity customers and eight competing for gas customers.
- Second tier retailers are very active and winning electricity customers from the "big three."[257] There is considerable switching between the three incumbents, but most switching is now occurring from the three incumbent retailers to second tier retailers.
- A high degree of product differentiation is occurring and innovation is emerging. Retailers are offering different tariff structures, discounts and a broad range of non-price incentives. These innovative developments enable services to be more closely tailored to the particular requirements of individual customers or groups of customers and they reflect a move away from the 'one size fits all' characteristic of monopolistic supply. With greater choice and complexity, it is increasingly important to provide the information and tools customers need to compare offers. This is further discussed in section 8.7.6 and Chapter 3.

8.5.1 Market share and concentration

There are 16 active electricity retailers competing in the small customer market in Victoria, eight of which also offer gas.[258]

Victoria has a relatively low level of market concentration compared to other jurisdictions, with the Herfindahl-Hirschman Index (HHI) for the retail electricity and retail gas markets at 1718 and 2014, respectively.[259] The electricity market share of the three incumbents, AGL, Origin and EnergyAustralia, has been reducing over time.

---

257 The "big three" refers to the three largest retailers in the NEM: AGL, EnergyAustralia and Origin Energy.

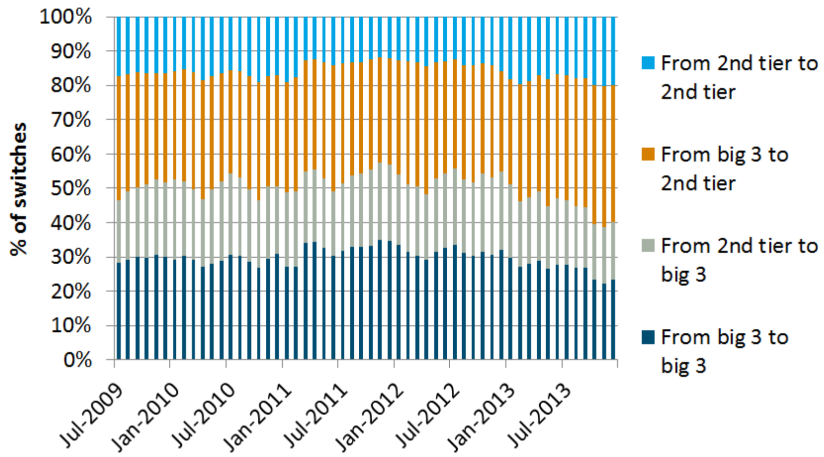
258 AGL acquired Australian Power and Gas in 2013 and also owns Powerdirect. These retailers are treated as one for the purpose of this review.

259 The HHI maximum is 10,000, which represents a perfect monopoly market. The ACCC uses a score of 2000 as a threshold when considering the level of competition for merger assessments. HHI is an indicative measure of concentration and is therefore just one of several competitive market indicators that we have considered in our assessment.

Collectively, they have approximately 70 per cent of the electricity market and smaller retailers have approximately 30 per cent. For the gas market, the same three retailers collectively have a market share of approximately 80 per cent.

In the electricity market, there appears to be strong rivalry between the "big three" incumbents as well as between these retailers and smaller, second tier retailers. Data on customers switching between the big three and other retailers shows the increasing activity of second tier retailers in the retail electricity market, as illustrated in Figure 8.7. There is considerable switching between the three incumbents, but more occurs from the three incumbent retailers to second tier retailers. This suggests that second tier retailers are effectively attracting customers away from the incumbents to gain market share and is a healthy sign of competition.

Figure 8.7 Switching between the "big three" and other retailers in Victoria



Source: AEMO data, AEMC analysis.

8.5.2 Product differentiation

Retailers interviewed stated that Victoria has a relatively high level of product differentiation and innovation. Our analysis of offers advertised in March 2014 supports this view.

Retailers noted that the removal of retail price regulation, in conjunction with the widespread availability of smart meters, has paved the way for the development of more innovative products (see Box 8.3). However, retailers cautioned that regulatory constraints on flexible pricing and the poor quality of some smart meter data may constrain further innovation.[260]

In addition to the features of the offers discussed below, retailers also differentiate their brand through service quality such as call centre operation hours, information

260 Farrier Swier Consulting and K Lowe Consulting, *AEMC Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p29.

provision, policies on hardship and complaints, policies on door knocking and cold calling, online account access and, in some cases, shopfronts for customers to visit.

Box 8.3: Examples of product differentiation in Victoria

Retailers interviewed by our consultants considered the Victorian market the most conducive to innovation due to the removal of retail price regulation and the high penetration of advanced meters. Two examples were provided that are specific to Victoria.

Dodo Power & Gas is offering a free hour of power between six and seven am every day to customers on its residential time of use tariff. Customers are credited on their bills for any usage charges incurred during this off-peak hour.

Powershop is offering customers the option to purchase electricity from Powershop's online shop in 'packs' of varying sizes and costs. The four types of packs that Powershop is currently offering include:

- Special Packs, which are discounted packs that are offered at various times;
- Future Packs, which enable customers to buy electricity for coming months and, in doing so, spread the costs over the year;
- Green Packs, which support renewable energy; and
- Top-up Packs, which can be used at any time.

Flexible pricing has only recently begun in Victoria and greater innovation is expected over time, but the above provide examples of emerging forms of electricity product differentiation unique to the Victorian market.

Electricity standing offers

Retailers in Victoria are required to offer a contract with regulated terms and conditions (other than price) known as a 'standing offer'. As at 31 March 2014, there were 13 standing offers available on the My Power Planner price comparator website.

Electricity market offers

As at 31 March 2014, the My Power Planner price comparator website showed 78 market offers for Melbourne.[261] As set out in Table 8.1, there is a relatively diverse range of discounts available and a range of contracts varying in duration or with no fixed term. There is a high degree of differentiation between tariff structures in Victoria with time of use, flexible, non-inclining and inclining block structures on offer.

261 My Power Planner is an interactive electricity price comparison tool that allows customers to view most of the available offers to them based on consumption and location. It is available through the Victorian Government's Switch On website (https://mpp.switchon.vic.gov.au).

Table 8.1 Differences in electricity offers in Melbourne as at 31 March 2014

Difference between offers *(high number of offers: >30; moderate: 15-30; low: 0-15)*	
Time of use tariffs	High number of offers available with a moderate range of tariff structures. There were slight variations between the supply, off peak and peak charges on offer. In addition to time of use offers, there are also flexible pricing options which appear to be quite similar, the key difference being that they also contain shoulder periods.
Other tariffs	High number of offers with a moderate level of difference. Options include: • flat rates with a supply tariff and a consumption charge; and • inclining block tariffs with two bands and a non-inclining block.
Discounts	High level of difference. Unconditional discount options range from 4 to 16 per cent off usage. Conditional discount options range from 1 to 25 per cent of usage. Options include discounts for: • pay on time; • direct debit; and • signing up online.
Contract duration	High number of offers with moderate level of difference. Choice of fixed terms ranging from 1 to 3 years or contracts with no fixed term.
Non-price incentives	High number of offers available with high level of difference. Options include: • bonus sign-up account credits from $20-50; • bonus $20 rebate for signing up to direct debit; • 'safe try' periods where a customer can try out an offer and has the option to revert to their original offer after the first bill; • frequent flyer and other rewards programs; • daily free hour of electricity during a specified time; • pre-purchase of electricity; • 'Golden Bill' giveaway where select customers do not have to pay their bill for the last quarter'; • 'One free move' where customers receive one free standard connection and disconnection per year; and • ability to purchase renewable energy certificates equivalent to a proportion of electricity consumption.
Solar feed-in tariff	Low level of difference. Typically, retailers offer the minimum 8 c per kWh feed-in tariff however as at 1 July 2014, there were offers of up to 10 c per kWh available.[262]

262 More information on solar arrangements is provided in Appendix D.

The range of offers available and the level of product differentiation appear similar for residential and small business customers and for customers in urban and regional areas. For example, as at 31 March 2014, the number of offers available for regional customers, and the terms and discounts available with those offers, were almost identical to those for customers in urban areas.

There were considerably fewer options available for small business customers in urban and regional areas compared to residential customers. However, these offers were similarly differentiated in terms of their tariff structures and the range of conditional discounts available.

Gas offers

Consistent with other NEM jurisdictions, there were fewer options available to gas customers in terms of the numbers of offers available.[263] Standing offers were available from eight retailers.

The differentiation between these offers was consistent with the differentiation of electricity offers – they varied mainly on the structure of the tariff, term of the contract, level and types of fees charged, the level of discounts available and other non-price variations. Conditional discounts were available ranging from 3 to 20 per cent of usage.

The gas offers available to customers in regional areas were similar to those available in regional areas.

8.6 Customer outcomes

Effective competition is characterised by how well the process of markets promote the long term interest of customers, including satisfaction with the level of choice available, the quality of service and the value for money provided by retailers. Our analysis of this criterion considered the findings of customer surveys and data on customer complaints, which suggest the following:

- **Some customers want greater choice**, but more than half were satisfied with the current level of choice in the market.
- **Most customers were at least somewhat satisfied with their current retailer**, citing good customer service, incentives, discounts, payment options, reliability of supply or the provision of useful information.
- **Most customers were very satisfied with the quality of service and value for money** provided by retailers. Value for money ratings were slightly lower than

---

263 Data sourced from www.yourchoice.vic.gov.au. Your Choice is a Victorian Government initiative designed to help residential and small business customers make informed choices with regards to their electricity and gas contracts. It includes information on how to choose a retailer, billing rights, flexible pricing and solar power. It contains a comparator tool for gas customers and redirects those looking to compare electricity offers to the My Power Planner website.

quality of service, which may relate to higher electricity bills for many customers in recent years.

- **The level of complaints to retailers in Victoria is relatively high and has been increasing** for billing issues in particular, which is consistent with trends in other jurisdictions. Complaints to the Ombudsman have not increased at the same rate.

8.6.1 Satisfaction with the level of choice

The degree of customer satisfaction with the level of choice in Victoria is slightly higher than the NEM average, with 57 per cent satisfied, 13 per cent dissatisfied and the remainder being neutral or undecided. Satisfaction with the level of choice in regional Victoria is lower than for Melbourne but is consistent with the NEM average.

Forum participants had mixed views on the benefits that competition was delivering, with many stating they saw little evidence of lower prices, better service or greater difference between offers. Many customers found it difficult to compare between options and some considered market choice as a negative due to added confusion.

There was, however, general agreement that competition would be enhanced if there was better communication and it was easier to compare plans.

> "We're comparing apples with pears. (Melbourne, lower income)"
>
> "I didn't know there was an independent website. An independent body to provide information is a good thing. (Melbourne, higher income)"
>
> "It depends what position you're in. If you can't be bothered shopping around then not so competitive but if you can shop around it is very competitive. I wouldn't have any idea how competitive it was if I hadn't done the research. (Ballarat, higher income)"

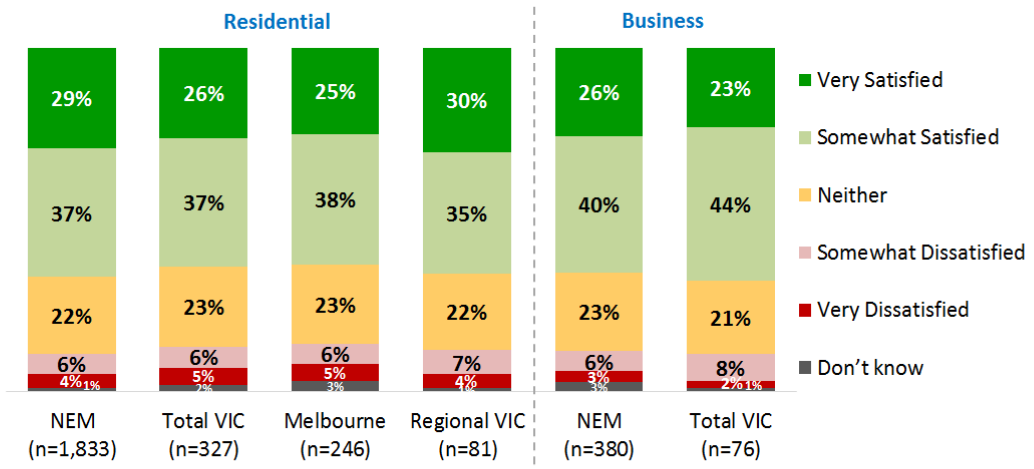
The perceptions of forum participants suggest there is value in generating greater awareness of the Victorian Government's price comparator websites.

8.6.2 Satisfaction with retailers

The majority of customers were satisfied with their retailer in all NEM jurisdictions surveyed. In forums in all jurisdictions, most customers linked satisfaction with the retailer to a reliable supply of power or simply not having any particular issues with their retailer. Participants in Victoria also cited a series of other reasons for being satisfied. This included good customer service, incentives and discounts, having a range of payment options and the provision of useful information (eg weekly usage enabled by smart meters).

Figure 8.8 presents survey results on customer satisfaction with their electricity retailer. Approximately 11 per cent of residential customers and ten per cent of business customers surveyed were either somewhat or very dissatisfied with their retailer, which is broadly consistent with the NEM average. Reasons cited in forums for dissatisfaction included retailer billing and account errors, not understanding the reasons for particularly high bills, disputes over charges and communication issues.

Figure 8.8 Satisfaction with current electricity company



Source: Newgate Research, *Customer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p54. Survey question: How satisfied are you with your current electricity company? Customers surveyed: All.

Overall quality of service and value for money were largely perceived as good or excellent by survey respondents. More customers rated the quality of service good or excellent than they did value for money, at 64 per cent and 52 per cent respectively. Regional Victorian customers rated value for money higher, with 59 per cent rating it good or excellent compared to 49 per cent in Melbourne.

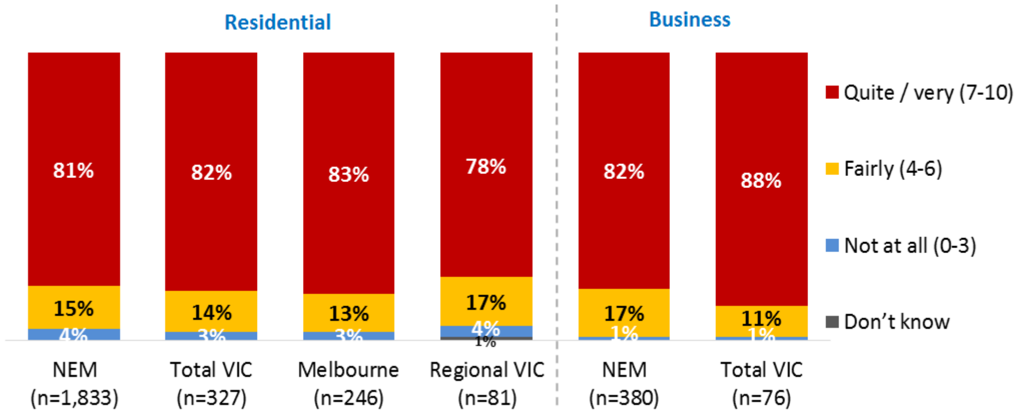
It is likely that value for money ratings primarily relate to higher electricity bills in recent years, driven mainly by increases in regulated distribution network costs.[264] A full discussion of the drivers of price movements and trends in electricity prices is available in the AEMC's annual residential pricing trends report.

In Victoria, around 80 per cent of customers surveyed stated that they were 'quite' or 'very' concerned about future electricity prices, as shown in Figure 8.9. This is broadly consistent with the NEM average.[265]

264 AEMC, *Electricity Price Trends Final Report – Possible future retail electricity price movements: 1 July 2012 to 30 June 2015*, 22 March 2013, pp 66 and 69, and AEMC, *2013 Residential Electricity Price Trends*, 13 December 2013, p96.

265 Newgate Research, *Customer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p22.

Figure 8.9 Level of concern about future energy prices



Source: Newgate Research, *Customer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p22. Survey question: How concerned are you about future energy prices? Customers surveyed: All.

For Victorian customers on high and middle incomes, annual electricity bills are estimated to represent approximately 0.5-1.3 per cent of the average disposable income. For low income customers, annual electricity bills are estimated to represent approximately 3.9-4.6 per cent of disposable income, depending on whether they receive concessions.[266] Victoria is the only NEM jurisdiction where concessions are calculated as a percentage of costs rather than as a flat rate.

Victorians holding a Pensioner Concession Card, a Health Care Card or a Department of Veterans' Affairs Gold Card can receive a variety of concessions on the cost of their electricity. Concessions include, for example, a 17.5 per cent discount on all electricity costs after the first $171.60 and concessions for electricity related to medical cooling and life support machines. Further information on concessions is provided in Appendix B.

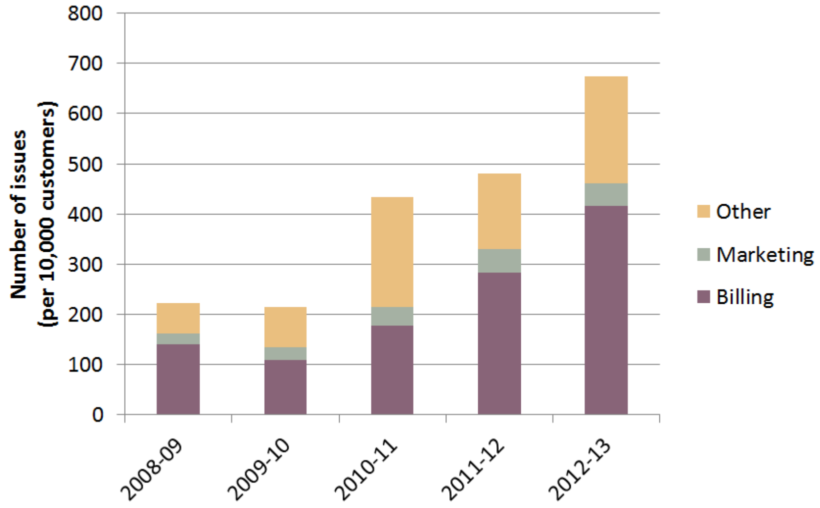
Complaints to retailers

Figure 8.10 illustrates the increasing trend in the number of complaints to electricity retailers in Victoria over the last four years. Consistent with other NEM jurisdictions, billing was the most common issue raised, making up 62 per cent of all issues raised.[267]

266 This AER analysis is based on average annual electricity consumption of 4,700 kWh for low income customers and 5,400 kWh for high income customers. AER, *Annual report on the performance of the retail energy market 2012-13*, 2013, p 71.

267 Note that when a customer makes a complaint, multiple issues may be raised.

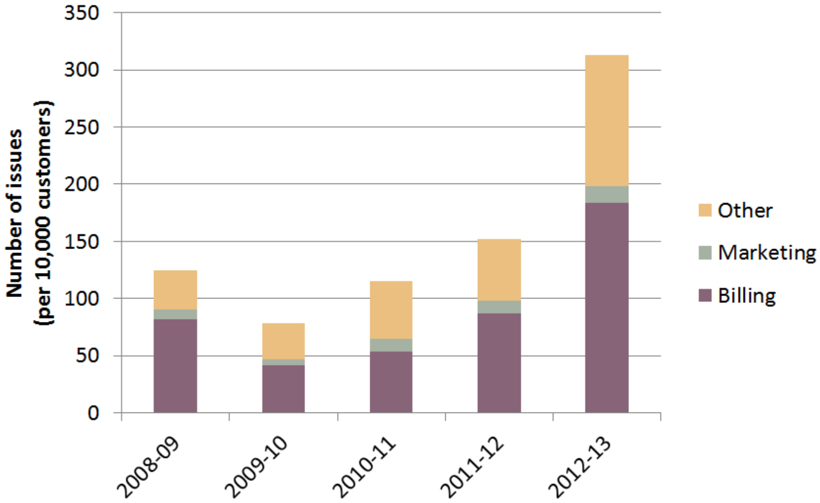
Figure 8.10 Electricity complaints to retailers – number of issues raised



Source: Complaints data from the Essential Services Commission, customer numbers from AEMO, AEMC analysis.

The number of issues raised with gas retailers in Victoria has been much lower than for electricity, even when adjusted for market size. Similar to electricity, the number of issues raised in 2012-13 was higher than in the previous four years. Close to 60 per cent of issues raised related to billing, as can be seen in Figure 8.11.

Figure 8.11 Gas complaints to retailers – number of issues raised

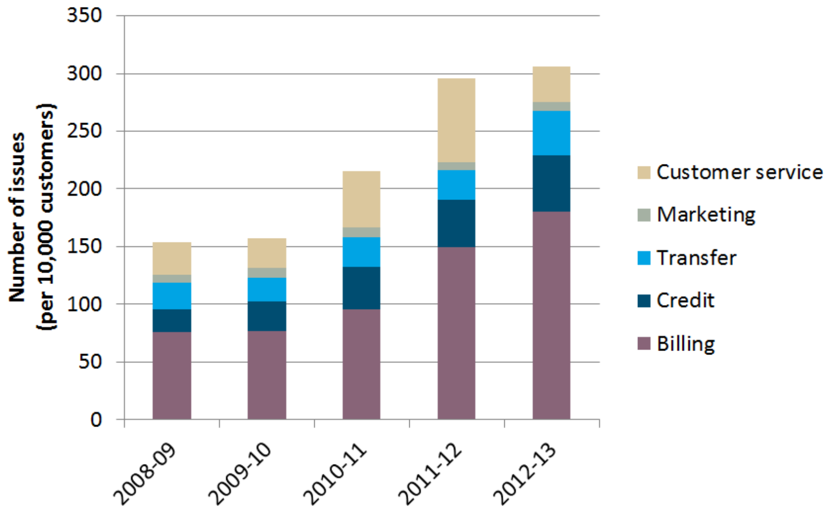


Source: Complaints data from the Essential Services Commission, customer numbers from AEMO and Energy Supply Association of Australia (ESAA) *Electricity Gas Australia* reports, AEMC analysis.

Complaints to the Ombudsman

The number of issues raised with the Energy and Water Ombudsman (Victoria) (EWOV) about electricity retailers was higher in 2011-12 and 2012-13 than in previous years (see Figure 8.12).[268] Note that issues raised with EWOV include referrals back to retailers, which are also captured in complaints to retailers described above.

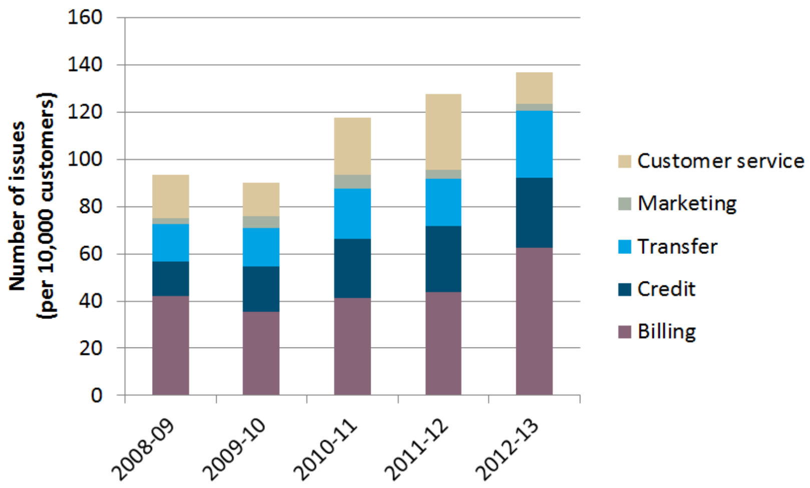
Figure 8.12 Electricity complaints to the Ombudsman – issues raised



Source: Complaints data from EWOV, customer numbers from AEMO, AEMC analysis.

The number of retail gas issues customers raised with EWOV was much lower than for electricity, even when adjusted for market size. The number of issues raised with gas retailers has been increasing over the past three years (see Figure 8.13).

Figure 8.13 Gas complaints to the Ombudsman – issues raised



Source: Complaints data from EWOV, customer numbers from AEMO and Energy Supply Association of Australia (ESAA) *Electricity Gas Australia* reports, AEMC analysis.

Billing issues were the most common complaints to EWOV for both retail electricity and retail gas. Billing made up 59 per cent of retail electricity issues raised with EWOV in 2012-13, with high bills, billing delay and tariffs the most common within this

268 EWOV data excludes cases which were not complaints.

category.[269] Billing made up 46 per cent of retail gas issues raised, with the most common issues in this category being high bills, billing error and billing delay.[270]

EWOV largely attributes billing issues to price increases and energy companies not dealing with customer concerns.[271] Billing delay issues are largely attributed to the billing system problems of one large retailer that changed its system in September 2012.[272]

Credit issues were also common, making up 16 per cent of retail electricity issues and 22 per cent of retail gas issues raised in 2012-13, with supply disconnection, debt collection and payment difficulties being the most common credit issues for both.[273]

8.7 Retailer outcomes

Victorian retail electricity and gas prices have been deregulated for over five years, the longest period of any Australian jurisdiction. As such, there is a particular focus in this review on retailer outcomes in Victoria. Furthermore, reports by the Essential Services Commission of Victoria and the AEMC in 2013 indicated that estimated retailer margins appeared to be higher in Victoria than in the other states.

In its submission to our Approach Paper, the Victorian Government requested that the AEMC develop a robust methodology to test the accuracy of current findings on retailer margins and determine whether there is any correlation between margins and the broader state of retail competition. The submission requested that this serve as a tool to observe future retail market trends and inform future policy approaches, as appropriate.[274]

The Victorian Government also suggests that the results of any additional analysis of profit margins undertaken by the AEMC could inform "additional policy initiatives…to further drive competition in Victoria for the benefit of all customers".[275]

The AEMC's annual Residential Electricity Price Trends Report considers possible drivers of price trends and includes estimates of gross margins at single points in time. Similar work has been performed by other bodies, including the Essential Services Commission. While such estimates can be informative, particularly when compared over a long time series, they cannot be considered as 'evidence' alone of a systemic issue in a market.

---

269 Energy and Water Ombudsman (Victoria), *2013 Annual Report,* p38.

270 Ibid, p43.

271 Ibid, p18.

272 Ibid p22.

273 Ibid p38, and p43.

274 Victorian Department of State Development, Business and Innovation, submission to the *2014 Retail Competition Review,* Approach Paper, p2.

275 Ibid.

This review has looked at a range of competitive market indicators to determine whether there are any systemic issues affecting competition in the Victorian retail market that may warrant further investigation. It was not within the scope of this NEM-wide competition review to extensively analyse net retailer margins in Victoria or consider specific policy interventions. Estimating net margins is a complex and resource-intensive task that is prone to error due to the assumptions that are required to be made.

We have concluded that competition is effective in Victoria's electricity market. The market has the right conditions to promote competition between retailers and we have not identified issues that warrant policy interventions to alter retailer behaviour.

For instance, there are low barriers to entry which place competitive pressure through the threat of new entrants. Five retailers have entered the market in the last two years, there is a high degree of rivalry through product differentiation, and second tier retailers are increasingly attracting customers away from the large incumbents.

There is, however, an opportunity to further increase competition by encouraging all energy customers to become 'energy shoppers', particularly the 25 per cent of Victorian customers who remain on higher priced standing offers.

Initiatives to provide clearer information to customers and promote awareness of the tools available to compare offers could help customers who are on high priced offers to select from a range of cheaper offers currently available, while placing greater competitive pressure on all retailers, particularly the incumbents. Such initiatives are discussed in sections 3.2 and 8.7.6.

8.7.1 Defining retail margins

Before discussing these outcomes we define key terms for the analysis.

Retailer outcomes are generally measured in terms of 'gross' and 'net' margins. Gross retailer margin is defined as the difference between an energy retailer's revenue and total wholesale costs of supply. It is commonly calculated by subtracting estimates of wholesale energy costs, environmental policy costs and network costs from a nominated tariff. This could be a standing offer, average market offer or lowest available offer at a point in time. Gross margin does not account for the costs incurred by a retailer in running its business (operational costs).

Net retailer margin is related to gross retailer margin, but retailers' operational costs are also subtracted from the nominated tariff. Operational costs include:

- customer acquisition and retention costs (i.e. marketing campaigns, discounts and other promotions);
- customer service (i.e. call centres, billing and collecting revenue);
- information technology (IT) systems;

- finance, including working capital requirements; and
- regulations (i.e. paying licence fees and complying with other government obligations, such as customer protection schemes).

Estimating gross and net retailer margins requires wholesale energy costs to be calculated. This is usually done by estimating the long run marginal cost of new generation or using exchange traded futures as a proxy for market prices.

However, both methods assume the same wholesale costs for different types of retailers, when in practice these will vary depending on the business's size, types of customers and business strategy, including level of vertical integration. Changing market conditions, such as falling demand and uncertainty over the carbon price repeal, can also make it difficult to accurately estimate a retailer's energy costs.

Estimating net retailer margins is a particularly complex task due to the requirement to estimate operational costs. These will vary depending on the size and business strategy of different retailers, such as whether a retailer outsources or retains key functions in-house.

Estimating compliance, regulation, customer-related and finance costs is also imprecise and will be different depending on the type of retailer, the credit worthiness of its customer base and the number and type of jurisdictions it operates in.

For a given retail tariff at a point in time, over-estimating or under-estimating wholesale energy costs and/or retailers' operational costs will lead to errors when estimating retailer margins. It is therefore important to carefully test the results to the extent that this is feasible.

Both gross and net retailer margins are presented as a percentage of a retailer's costs. For instance, a ten per cent gross retailer margin implies that a retailer is earning revenue that is ten per cent greater than its total wholesale costs of supply.

8.7.2 Recent reviews

In May 2013, the Victorian Essential Services Commission undertook reviews into the progress of retail competition and retailer profit margins in Victoria. With respect to profit margins, the Essential Services Commission found that since electricity standing offer prices had been deregulated, retailer margins appear to have increased.

Consultants SKM MMA published a report commissioned by the Essential Services Commission that estimated gross and net retailer margins between 2006 and 2012.[276] This analysis showed that gross margins on market offers, including discounts, have fluctuated between 10 per cent and 30 per cent on average across all Victorian retailers

276 SKM MMA 2013, Analysis of Electricity Retail Prices and Retail Margins 2006 - 2012, Report for the Essential Services Commission, 10 May.

and distribution networks.[277] Gross margins on standing offers were estimated to be higher at 30 per cent to 45 per cent.[278]

SKM MMA estimated net margins by applying the retailer operating cost allowance developed by the Independent Pricing and Regulatory Tribunal (IPART) for New South Wales retailers to Victorian retailers. This analysis showed that net retail margins between 2006 and 2012 for market offers ranged from around -2.5 per cent to 10 per cent on average across all Victorian retailers and networks.[279] Net margins on standing offers were estimated to be higher at 15 per cent to 25 per cent.[280]

This approach assumes that operating costs are the same for retailers in Victoria and New South Wales, which we note is inconsistent with statements by some retailers, as discussed in section 8.7.4.

8.7.3 2013 Retail Price Trends Review - Victoria

Each year the AEMC publishes the Residential Electricity Price Trends review. The report estimates the cost components of retail electricity prices, including wholesale energy, network and environmental policies. Subtracting these components from a representative electricity retail tariff provided by retailers leaves a residual. To the extent that these components accurately reflect a retailer's costs, this residual represents the gross retailer margin.[281] Net retailer margins are not estimated as part of the Residential Electricity Price Trends review.

The 2013 Residential Electricity Price Trends review found that the average gross retailer margin for Victoria appeared higher than in other states. This analysis was based on February and September 2013 best market offers provided by Victorian retailers. The gross margin was between 34 per cent and 37 per cent of total wholesale costs for Victorian retailers, while for other jurisdictions the gross margin was between 11 per cent and 18 per cent.[282]

We that note this analysis was conducted at two points across a short period of time and does not take account of retailers' operating costs.

As discussed earlier, estimates of gross and net margins are sensitive to a number of assumptions, including the time period of analysis, the retail tariffs used to calculate the margins, how wholesale energy costs are estimated and the operational costs assumed for retailers. Changes in these assumptions can have material effects on the results and therefore care needs to be taken when interpreting the numbers and

277 Ibid., pix.

278 Ibid.

279 Ibid., pxii.

280 Ibid.

281 For an explanation of the methodology of calculating the representative market offer see: AEMC, *2013 Residential Electricity Price Trends report*, 13 December 2013, Sydney, Appendix A.

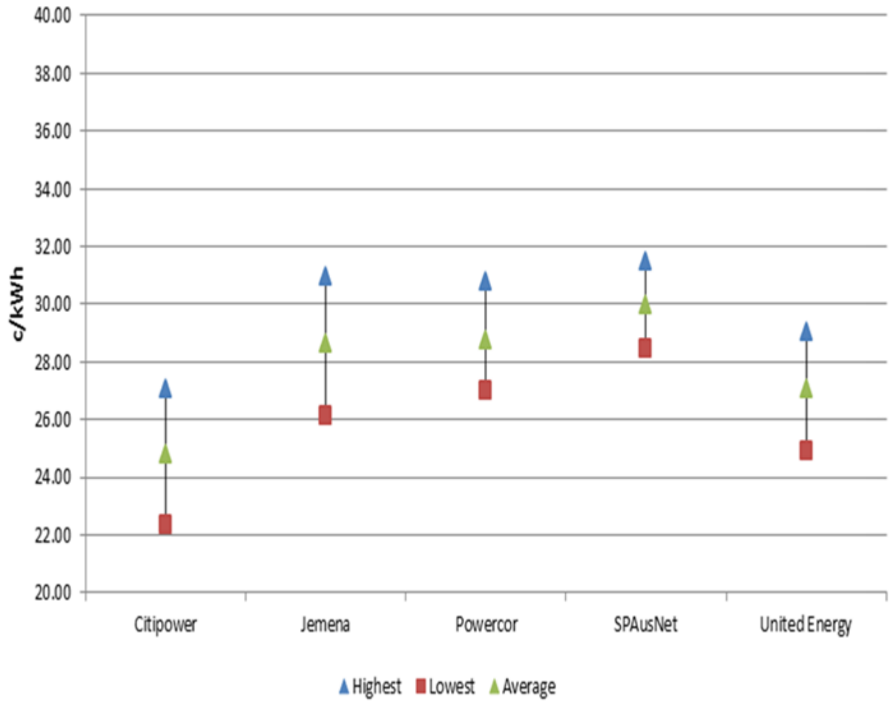
282 AEMC, *2013 Residential Electricity Price Trends report*, 13 December 2013, Sydney, p94.

forming conclusions. Gross and net retailer margins will also vary over time, as was demonstrated in the SKM MMA work.

Figure 8.14 shows the difference between the lowest and highest market offer prices offered to customers within a given distribution area in Victoria, based on 1 February 2013 tariffs supplied by retailers.[283] Over the same period standing offer prices were around 33 c per kWh. This is around 50 per cent higher than the lowest market offer price of around 22 c per kWh and, combined with the range of market offers, demonstrates the sensitivity around choice of tariff when doing margin analysis.

This also highlights the substantial savings that customers who continue to remain on standing offers in Victoria can make if they switched to a market offer.

Figure 8.14 Highest, average and lowest post-discount residential electricity charge by distribution network area, Victoria, February 2013



Source: AEMC, *2013 Residential Electricity Price Trends report*, 13 December 2013, Sydney, p. 94.

8.7.4 Retailer views on Victorian margins

Electricity retailing in Victoria was rated as moderately profitable by retailers that participated in our survey and more profitable than other jurisdictions.[284] Retailers claim that Victorian prices are more cost reflective in Victoria than New South Wales, South East Queensland or South Australia.

283 Ibid, p39.

284 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p29.

> "When you compare Victoria with New South Wales or South East Queensland, Victorian prices are more cost reflective than New South Wales or South East Queensland, because the prices in these other jurisdictions have been kept artificially low by [retail price regulation] and are not, in our view, cost reflective. That is why you would see a disparity. In South Australia you currently have price monitoring and AGL's voluntary price agreement (which involved reducing the standing offer by 9.1%), both of which are constraining retail prices. So again prices in South Australia are unlikely to be truly cost reflective."[285]

Some retailers who operate across multiple jurisdictions consider that retailer margins in Victoria reflect higher wholesale energy and operational costs compared to other jurisdictions due to:[286]

- differences in administrative costs in complying with "more onerous" customer protection obligations[287] and energy efficiency schemes;
- billing and IT infrastructure costs associated with the roll-out and integration of smart meters;
- higher wholesale market hedging costs, particularly over summer, due to price volatility imported from South Australia over the Heywood Interconnector;
- wholesale market settlement based on actual consumption, rather than net system load profile, which may expose retailers in Victoria to greater demand volatility, especially smaller retailers; and
- higher switching rates that result in greater marketing spend to acquire and retain customers.

With respect to operational costs, it is possible that Victorian-specific requirements could add costs for retailers operating across jurisdictions, as discussed in Box 8.4 and Appendix F. Retailers did not provide evidence of the magnitude of Victorian-specific costs and the AEMC is not in a position to estimate or verify these costs.

---

285 K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014, p85.

286 Ibid, p87.

287 For example, the Commission understands that new arrangements introduced to reduce fraud and misuse of the Annual Electricity Concessions are cumbersome for retailers to implement. The arrangements require retailers to: identify customers with electricity bills above a certain threshold; cease concessions to those customers and send them an application form for the Excess Energy Concession; forward the completed form to the Department of Human Services; and, if approved, reinstate the concession, including any back payments.

Box 8.4: Comparison of customer protections – standard NECF and Victorian requirements

The NECF is a suite of legal instruments that regulate the sale and supply of electricity and gas to retail customers. The purpose of the NECF is to create a unified framework across Australia's states and territories.

As discussed above, the Victorian Government has deferred the implementation of the NECF. As such, retailers who operate across jurisdictions may incur additional regulatory and IT systems costs in complying with Victorian-specific requirements and may need to operate with multiple systems to deal with jurisdictional differences. Appendix F provides further detail on some of the Victorian customer protection requirements that vary from the NECF, including:

- a ban on late payment fees;
- compensation for wrongful disconnection;
- community service agreements;
- advanced metering infrastructure (smart meters); and
- bulk hot water billing.

8.7.5 Competition as a process

The Victorian retail energy market has been developing free of price regulation for around five years, which is a relatively short period given the commercial and regulatory requirements that need to be met to enter the market and grow.

Over time, as firms enter and exit, the market will evolve and mature, and retailer margins can be expected to vary with the business cycle. Periods of temporarily elevated margins stimulate new entry and give customers incentives to seek out lower-price suppliers and/or to reduce consumption. Periods of depressed margins put pressure on suppliers to exit the market and/or to seek cost efficiencies.

As the market matures, customer engagement can be expected to change with a growing awareness of smaller new entrant retailers, comparator websites and available products and savings from shopping around. In this sense, competition is best described as an adaptive discovery process where firms and customers continually interact: retailers compete to attract customers and maximise profit, while customers seek out the best deals that meet their needs.

In a market that exhibits effective competition, retailer margins will fluctuate over time. An analysis of retailer margins therefore needs to be carried out over a sufficiently long period to understand the profitability of the industry through multiple business cycles and changes in market conditions.

When examining the competitiveness of a market, one of the most important indicators is whether firms are entering and competing and/or whether there is a legitimate threat of new entry. If this is the case, as it is in Victoria, then competitive pressure can be expected to lead to efficient outcomes for customers.

Intervening in a competitive market based on inconclusive evidence can lead to unintended outcomes and reduce the effectiveness of competition. In a recent example, the regulator in the United Kingdom restricted the ability of retailers to offer discounted tariffs in areas where they were not the incumbent. As this limited the ability of retailers to attract customers in the regions where their competitors had an incumbency advantage, retailers responded by withdrawing to their profitable markets, resulting in higher profit margins and reduced switching rates.[288]

8.7.6 Increasing the effectiveness of competition

An important means of increasing the effectiveness of retail market competition is to encourage customers to become 'energy shoppers' and seek out better deals. This is a change in mindset for some customers away from treating energy like the government supplied, regulated monopoly it used to be and more like other goods that involve exercising choice regularly.

We have identified the following factors that may contribute to more effective retail competition in Victoria:

- informing customers, particularly those who remain on standing offers, of the savings they could make; and
- promoting awareness of the Victorian Government comparator websites.

In addition, the requirement to provide a standing offer may create an artificial benchmark for retailers' pricing strategies and can make it difficult for some customers to compare offers. This issue may warrant further investigation.

Potential savings for customers on standing offers

Over five years after retail price regulation was removed, around 25 per cent of Victorian customers continue to remain on high standing offer tariffs.[289] Most of these customers likely sit with the three incumbent retailers, who acquired their customer base through the privatisation process or subsequent sale.

As these customers are on standing offers, and may have never shopped around for a better deal and switched, they are likely to be some of the most profitable customers for retailers. This means there is little incentive for the incumbent retailers to launch an aggressive marketing campaign to attract these customers, due to the risk of losing

---

288 Gammons, S., et. al 2014, *Tantalus and Other Myths of the British Energy Market*, NERA Energy Market Insights, 10 March 2014.

289 AER, State of the Energy Market 2013, p. 32.

profitable standing offer customers in a price war. A further disincentive is that any customers won would be on less profitable market offers, not standing offers.

For smaller, lesser known retailers without the resources of the incumbents, convincing customers who have not engaged in the market to switch is likely to require expensive marketing campaigns and discounts to attract their attention. As such, this is probably not a commercially sustainable strategy and may limit the ability of smaller retailers to compete for this customer segment.

We note that in most markets there can be expected to be a proportion of customers for whom switching is simply not worth it. This could be because energy makes up a relatively small proportion of household expenditure, or that the total cost is split between different parties, such as in a share house. However, given the size of discount on offer when moving from a standing offer to a market offer in Victoria, there may be further useful work in understanding the reasons why 25 per cent of customers choose to remain on standing offers.

Government campaigns to encourage all energy customers to shop around for a better deal, with a focus on customers who remain on standing offers, are likely to have positive impacts for competition that flow through to the broader market.

With fewer customers on standing offers, the incentive for incumbent retailers to protect this profitable customer base may decrease. It may also enhance the ability of smaller retailers to compete as, once customers begin to shop around for better deals and use comparator websites, it will be less expensive for smaller retailers to attract their attention.

Promoting awareness of the Victorian Government comparator websites

A number of respondents to the customer survey considered they were unlikely to get a better deal if they switched retailer and 71 per cent of Victorian customers, when prompted, had not heard of the Victorian Government comparator websites "YourChoice" or "My Power Planner". However, when unprompted only one per cent of customers across all jurisdictions were able to name any government comparator website.

As has been demonstrated throughout this analysis, there can be large savings for customers who choose to shop around and switch, particularly if they are on standing offers.

Raising awareness of the Victorian Government's price comparator websites will encourage customers to become ‘energy shoppers’ by providing them with a trusted tool that makes it easier to compare offers. Customers who may have never switched supplier need to be confident in their ability to compare deals and change retailers. In this respect, our survey findings indicate that most customers are sceptical of commercial comparator websites and prefer to use a government one.

Providing customers with the right information and tools to compare offers is also important with the introduction of flexible pricing, which can add complexity in comparing offers. This is further discussed in Chapter 3.

In the absence of Victoria joining the NECF and adopting the Australian Energy Regulator's comparator website, "Energy Made Easy", it will be important to ensure that the Victorian Government's price comparator websites are as user friendly as possible for customers who have never investigated switching and are not familiar with the retail energy market.

Standing offers and retailer's pricing strategies

In Victoria, retailers are required to publish a standing offer with terms and conditions that are regulated by the Victorian Government. The standing offer is generally the most expensive tariff offered by a retailer and generally varies between retailers.

When promoting market offers, which are not subject to regulated terms and conditions, a common strategy used by retailers is to advertise the deal as a discount off the relatively high standing offer to attract the attention of customers. This way of 'framing' the price, while appearing attractive to customers, may result in an actual price that is higher than a competitor's. It may also make comparing products more difficult for some customers. As noted by Professor George Yarrow of the Regulatory Policy Institute, Oxford in 2007:[290]

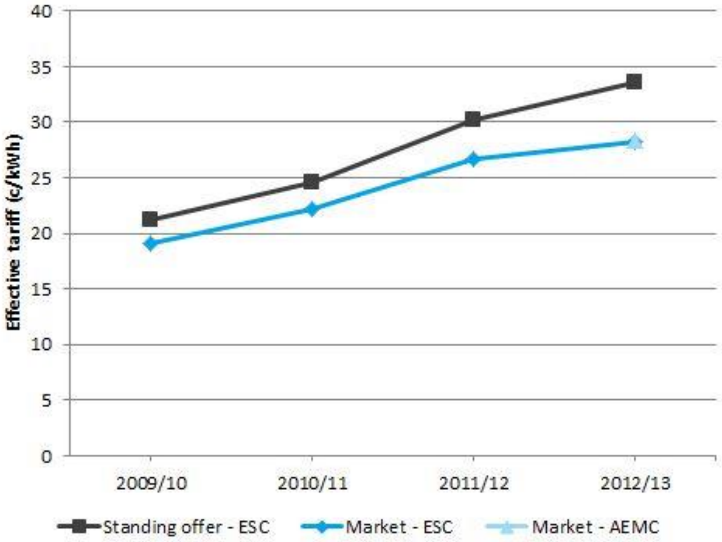
> "...in framing the evaluation of alternative tariffs relative to a standard offer, consumers may falsely believe that they are getting a very good deal if the alternative offers a significant discount, when in fact the discounted tariff may still be above a market clearing level. In these ways the policy could harm the very people it is intended to assist."

As can be seen in Figure 8.15, average standing offers across all Victorian retailers have been increasing since 2009-10, while market offers have plateaued and the gap between standing and market offers has increased.

This demonstrates that the potential savings for customers who remain on standing offers is growing. It also shows that, if retailers are pricing market offers as discounts from standing offers, the discounts may be increasing while the market offer prices paid by consumers are growing slightly or remaining unchanged.

290 Yarrow, G., et. al 2007, Report on the impact of maintaining price regulation, Regulatory Policy Institute Oxford, January, p28.

Figure 8.15 Victorian standing and market offer prices 2009-10 to 2012-13



Source: Victorian Essential Services Commission, *Energy Retail Performance Reports, 2010 to 2013*; and AEMC, *Future Possible Retail Electricity Price Movements: 1 July 2010 to 30 June 2014*, December 2010.

As discounting occurs from a relatively high standing offer, new retailers who enter the market can also adopt this pricing strategy and earn profitable margins on what appear to be substantial discounts. Indeed, if customers have become accustomed to comparing deals based on the level of discount, not the actual price, this may be an essential way for new entrant retailers to attract the attention of customers.

With around 25 per cent of customers remaining on standing offers, there is little incentive for retailers to reduce them, even if comparing deals on the basis of discounts, rather than price levels, can be more difficult for customers looking to switch.

In a competitive market, retailers are attempting to attract customers by differentiating themselves through discounts and non-monetary offerings. However, the requirement to provide a standing offer may create an artificial benchmark for retailers' pricing strategies and can make it difficult for some customers to compare offers.

If the requirement for retailers to provide a standing offer is removed, this may encourage retailers to consider alternative, clearer ways of pricing their products and engaging with customers. This issue may warrant further investigation.

8.8 Future developments

Victoria continues to stand out as having indications of a highly competitive retail market for both electricity and gas. In terms of electricity, retailers attribute this to the time that has elapsed since privatisation, the introduction of full retail competition and the removal of retail price regulation. For gas, retailers attribute high levels of competition to the high penetration of gas and the advantages of the DWGM over other gas wholesale market designs.

It is likely that Victoria will remain the preferred market for developing and testing new products and services for some time, given the higher levels of customer engagement and the additional options for innovation that the widespread availability of smart meters provides. As discussed in Chapter 3, while these innovations could lead to benefits to customers including lower bills, they could also lead to greater complexity. Customers must have access to effective tools and trusted information to support their decisions, with the right protections and access to assistance if required.

Retailers also expect the Victorian electricity market to remain highly competitive. However, concerns were raised by some retailers about the possibility of customer fatigue and have speculated that South Australia or New South Wales could overtake Victoria in terms of the level of competition. Some retailers also raised concerns about increasing concentration in the wholesale market. Despite this, six electricity retailers indicated that they are planning to expand in Victoria over the next five years.

Based on analysis undertaken as part of the AEMC's 2013 Residential Electricity Price Trends review, gross retailer margins in February and September 2013 appear higher in Victoria then in other jurisdictions, although it is unclear whether this is due to issues around accurately measuring wholesale energy and operational costs. Retailer margins will vary over time and it is important to analyse margins in the context of changing market conditions and the business cycle.

Government initiatives to encourage customers who remain on higher standing offers to move to market offers are likely to increase the effectiveness of competition. Raising awareness of the Victorian Government's comparator websites will be an important part of promoting the benefits of customers becoming energy shoppers and engaging in the market. The requirement to provide a standing offer may create an artificial benchmark for retailers' pricing strategies and can make it difficult for some customers to compare offers. This issue may warrant further investigation.

Retailers did not provide much commentary on the outlook for the Victorian retail gas market. Some retailers noted that while Victoria is relatively well-placed in terms of its close proximity to large gas reserves, retail customers may still feel the effect of the tightening demand and supply conditions in the wholesale gas market through higher retail gas prices.

Two retailers indicated they are in the process of entering the Victorian gas retail market and three existing retailers intend to expand their customer base within the next five years. This could lead to increased rivalry in the gas market going forward.

9 South Australia

Box 9.1: Key Findings

- Competition is effective in the South Australian electricity and natural gas retail markets, although less so for gas customers in regional areas.
  - Electricity customers are active in the market with 80 per cent of customers on market contracts, one in three investigating their options last year and over half switching plan or retailer in the last five years.
  - 13 electricity retailers and five gas retailers are competing to acquire and retain customers by offering discounts and other incentives. While AGL still has a strong market share in electricity, rivalry from and between second tier retailers is increasing.
  - New entry has occurred in both electricity and gas in the last few years. Entry into the retail electricity market is expected to continue to occur, despite some concerns about wholesale market conditions and the ability of non-vertically integrated second tier retailers to hedge volatile wholesale costs.
  - The majority of customers surveyed are satisfied with their retailer and the choices available.
- Raising awareness of the independent price comparator website Energy Made Easy could encourage customers to become 'energy shoppers' by providing them with a trusted tool that makes it easier to compare offers.
- Gas market structure issues continue to impede entry into regional areas. Only two retailers compete outside of Adelaide and the incumbent retailer has close to a 100 per cent market share in some regional locations. Competition in the gas market is not expected to change considerably in the near future as a result of tight wholesale conditions and lack of uncontracted capacity on the South East Australian Gas Pipeline.

9.1 Overview

The AEMC first reviewed competition in South Australia's energy market in 2007/08 and found that competition was effective for small electricity and gas customers, although there were some structural limitations affecting the ability of small gas customers in regional areas to access the full benefits of competition.[291]

291 AEMC, *Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia*, 2008, pix.

The Commission's assessment of competition against the five criteria set out in Chapter 2 has found that competition continues to be effective in the electricity and gas markets. The findings for the South Australian retail market can be summarised as follows:

- **Customer activity:** South Australia has the highest proportion of customers on energy market offers of all the national electricity market (NEM) jurisdictions, many customers are active in investigating options and there are high switching rates for electricity and gas.
- **Barriers to entry, exit and expansion:** Retailers consider entry, exit and expansion relatively easy for the retail electricity and gas markets. Some noted challenges in expanding in the electricity market without having interests in generation assets.
- **Independent rivalry:** There is strong rivalry in retail electricity and gas markets despite the high market concentration, with increasing activity of second tiers. Rivalry appears weaker for retail gas in regional areas.
- **Customer satisfaction:** Many customers are satisfied with the level of choice in the market and with their current retailer, though some perceive little difference between the choices available.
- **Retailer outcomes:** Retailers rated the electricity market as somewhat profitable, consistent with their rating for New South Wales. Less information is available on the profitability of the gas market, but retailers suggest it is similarly profitable as the electricity market.

9.2 History and market characteristics

Full retail competition was introduced in South Australia for small electricity customers in January 2003.[292] The gas market was opened up to competition on 1 July 2001 but systems were not in place to handle mass transfers until 28 July 2004.

In February 2013, South Australia adopted the National Energy Customer Framework (NECF) subject to a number of derogations. At the same time, it removed retail price regulation for electricity and gas markets. The Essential Services Commission of South Australia (ESCOSA) is now required to undertake price monitoring and market oversight.

Retailers in South Australia are required under the NECF to provide customers with a standing offer, however the prices of these standing offers are determined by the retailers. AGL is the incumbent electricity retailer and, as part of the deregulation process in 2013, it entered into a voluntary price arrangement with the South Australian Government. Under this arrangement, AGL agreed to reduce the electricity

292 Small electricity customers in South Australia are defined as customers with annual consumption below 160 MWh. This threshold is higher than in any other jurisdiction, where most other jurisdictions use a threshold of 100 MWh/annum.

standing offer by 9.1 per cent for residents and 4.5 per cent for small business. It agreed to maintain prices at that level for two years, subject to changes in network charges and environmental scheme costs.[293]

Origin Energy is the incumbent gas retailer and, as part of the deregulation process, it agreed to reduce its standing offer for gas by one per cent.[294]

There are currently over 800,000 small electricity customers in South Australia. This is less than Victoria, New South Wales and Queensland. There are approximately 400,000 gas customers. Again, this is smaller than the Victorian and New South Wales markets but larger than the Queensland gas market. Most gas customers are in Adelaide, which has a penetration rate of 75 per cent.

9.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

Our analysis of this criterion considers the findings of a customer survey and qualitative forums performed by Newgate Research and data provided to the AEMC on customer switching. The analysis suggests the following:

- **South Australia has the highest proportion of customers on market offers**. Approximately 83 per cent of electricity customers and 81 per cent of gas customers have chosen market offers.[295]
- **The majority of customers are aware that they can choose their plan and retailer**, which appears to be largely due to high retailer activity and word of mouth.
- **Many customers are investigating their options and choosing between different market offers**. Switching rates appear high for gas and electricity, with price the main trigger for switching retailer or plan. However, some customers are not interested in looking for a better deal, particularly among the small businesses surveyed.

---

293 Government of South Australia, News Release, Premier Jay Weatherill and Minister Tom Koutsantonis, 18 December 2012.

294 Ibid.

295 AER retail statistics for Q3 2013-14, available at http://www.aer.gov.au/Industry-information/industry-statistics/retail.

9.3.1 Customer awareness and understanding

There was a very high level of awareness among survey respondents and forum participants that there are multiple retailers and plans in the market to choose from.

Ninety-two per cent of electricity customers and 89 per cent of gas customers surveyed were aware they could choose their energy retailer. This is an increase from the 2007/08 review where 82 per cent of electricity and 84 per cent of gas customers were aware of this choice. Most forum participants had become aware of their ability to choose an energy retailer or plan through telemarketing, advertising or word of mouth.

Customers were less aware of how much choice they had, with most underestimating the number of retailers in the market to choose from. This is consistent with results in other NEM jurisdictions.

The majority of customers were aware that they could choose from a range of different energy plans and reported being confident they understood the different offers and options available. Customers in regional areas were somewhat more confident than those in Adelaide and small businesses were more confident than residential customers.

Qualitative research found that actual understanding of the different features of energy plans and bill components is varied. Many participants were aware of different contract durations, various conditional and non-conditional discounts on usage, and other incentives. Most were unsure of the details of various tariff types, the difference between the terms 'market offer' and 'standing offer', and whether the government had a role in determining prices. Lower understanding of these latter details does not, however, appear to be a major barrier for customers to investigate their options and switch plans.

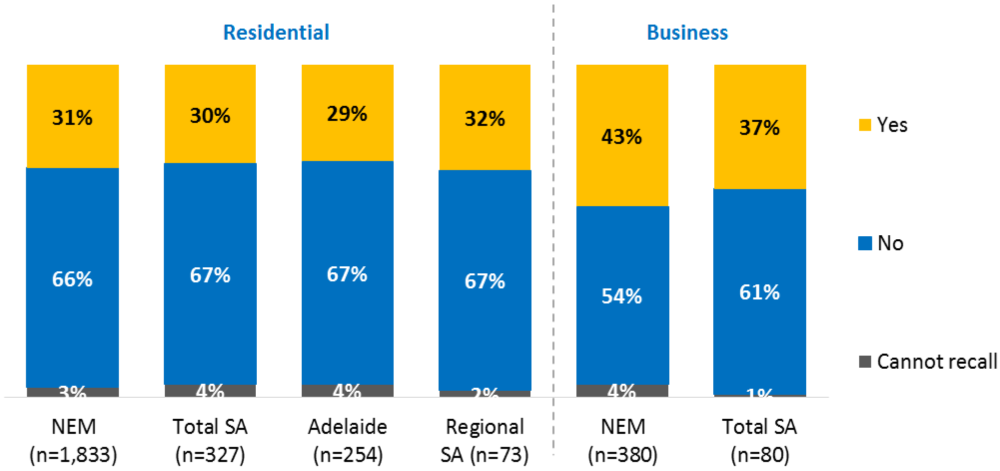
A small number in both forums were quite savvy about their energy usage, often among small business participants and participants with solar panels. Many participants with solar panels would actively monitor their electricity meters and their bills.

> "I take my last reading, put in my rate cost and account for the solar, and work out the cost. (Murray Bridge, higher income)."

9.3.2 Customers investigating options and switching

South Australian customers are actively investigating their energy options and switching to alternative retailers or energy plans. Close to one third of residential customers surveyed in South Australia had actively investigated energy options or offers to switch to in the past twelve months. Of these customers who investigated their options, almost all reported switching to a different plan or retailer and most reported being satisfied with the switching process.

Figure 9.1 Customers who actively investigated offers or options in past 12 months



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014, p88. Survey question: In the past 12 months, have you actively investigated different offers or options that you could potentially switch to? Customers surveyed: All.

High customer activity in South Australia may be partly attributable to the level of retailer marketing activity, with around 58 per cent of customers reporting that they were approached by an energy retailer in the last twelve months. Qualitative research supports this link and also suggests customer awareness and activity has been generated through media articles and the One Big Switch campaign.[296]

Survey responses and market data both suggest a strong level of electricity customer switching in South Australia. Over half of customers surveyed stated they had switched electricity retailer or plan in the last five years. Consistent with trends in other jurisdictions, switching was lower for gas than electricity with 39 per cent of gas customers switching retailer or plan over the same period.

While many customers in South Australia have switched electricity plans, fewer reported switching their retailer than the NEM average. Nonetheless, reported switching rates are relatively high, with over one third of respondents switching their electricity retailer in the last five years. This is slightly higher than the number of customers who reported switching their mobile, internet, landline and insurance providers over the same period.

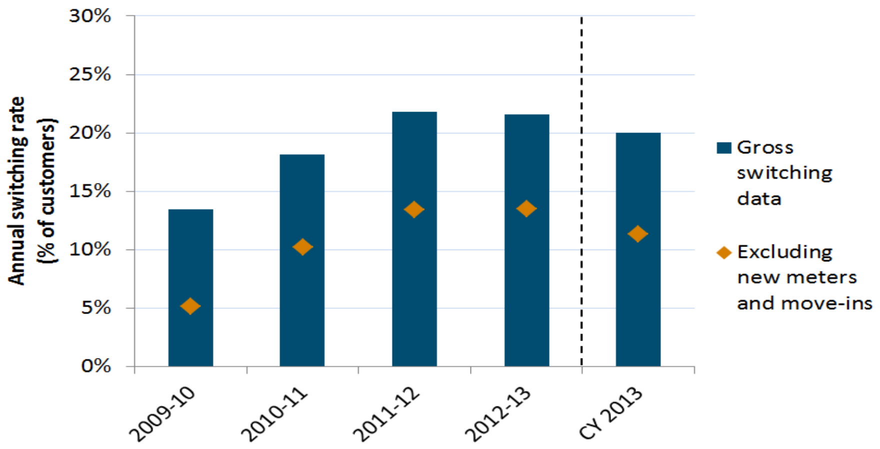
Figure 9.2 below shows data for actual customer transfers from one retailer to another per year. Consistent with the survey results, this data also shows high customer switching rates between retailers.

Gross switching rates remained above 15 per cent per annum since late 2010 and reached a peak of around 26 per cent in the first half of 2012. Switching rates grew rapidly from 2009 to 2012 and appear to have stabilised or dropped slightly over the

296 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p87.

2013 calendar year to reach an average of 20 per cent.[297] A report by Deloitte submitted to this review from the Energy Retailers Association of Australia attributes this decline to a change in marketing strategy where AGL, EnergyAustralia and Origin Energy ceased door knocking in October 2012, March 2013 and September 2013, respectively.[298]

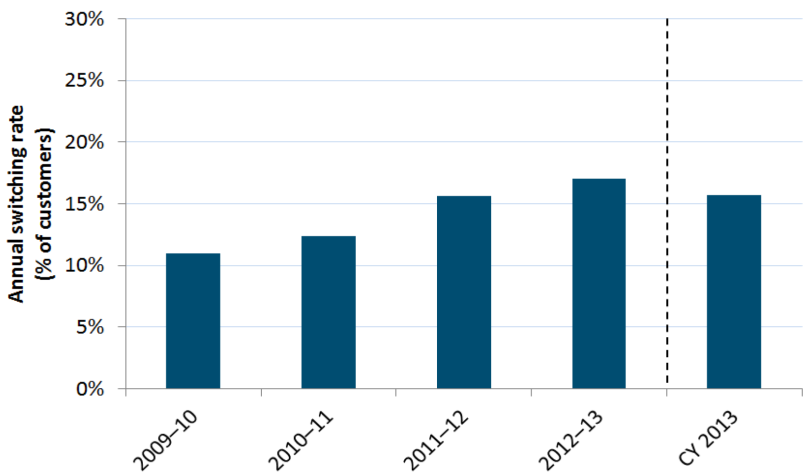
Figure 9.2 Electricity switching rates - South Australia



Source: AEMO data, AEMC analysis.

For the gas market, data in Figure 9.3 shows gross switching rates are slightly lower than electricity with 15 per cent of customers switching their gas provider in 2013.

Figure 9.3 Gas switching rates - South Australia



Source: AER state of the energy market 2013 and AER Retail Statistics.[299]

297 See Chapter 2 for a discussion of the limitations of this data.

298 Deloitte, *South Australian Energy Market Reform - one year on*, a report for the ERAA, February 2014, p14.

299 http://www.aer.gov.au/Industry-information/industry-statistics/retail

Switching data for electricity and gas may under-represent how active customers are in the market. Many customers have actively investigated their options and either chosen to remain on their existing plan or have chosen to switch plans with their existing retailer. Data provided by retailers suggests that, depending on the retailer, up to 28 per cent of customers changed their plan with their existing retailer in 2013. For gas, up to 17 per cent of customers changed plan with their retailer.[300]

Price appears to be the key driver for switching behaviour

Customer surveys suggest the key reason for switching energy retailer or plan in all NEM jurisdictions was to obtain a better price.

Of customers surveyed in South Australia that switched electricity retailer or plan, 64 per cent of residents and 71 per cent of businesses stated that price was the main reason to do so. Similarly for gas, 60 per cent of South Australian residents stated that price was the main reason they switched electricity retailer or plan.

Moving house was a distant second to price in motivating residential customers to switch electricity or gas retailers or plans. Around 10 per cent of respondents cited this as their key reason for switching energy retailer or plan.

For small businesses, customer service was the second most common reason cited for switching and this was a more important driver in South Australia than other NEM jurisdictions.

Nineteen per cent of those small businesses who switched stated they did so because they were unhappy with the customer service they had received. In our 2008 review of retail competition in South Australia, only three per cent of small businesses surveyed who had switched did so because they were unhappy with their former retailer. While this difference may be partly due to different question and response formats for the two surveys, the results suggest there has been, at the very least, a marginal increase in small businesses shopping around due to dissatisfaction with their retailer.

Unlike small businesses, poor customer service does not appear to be a key driver of switching for most residential customers, with 8 per cent of residents citing this as their main reason for switching.

Some customers are less engaged

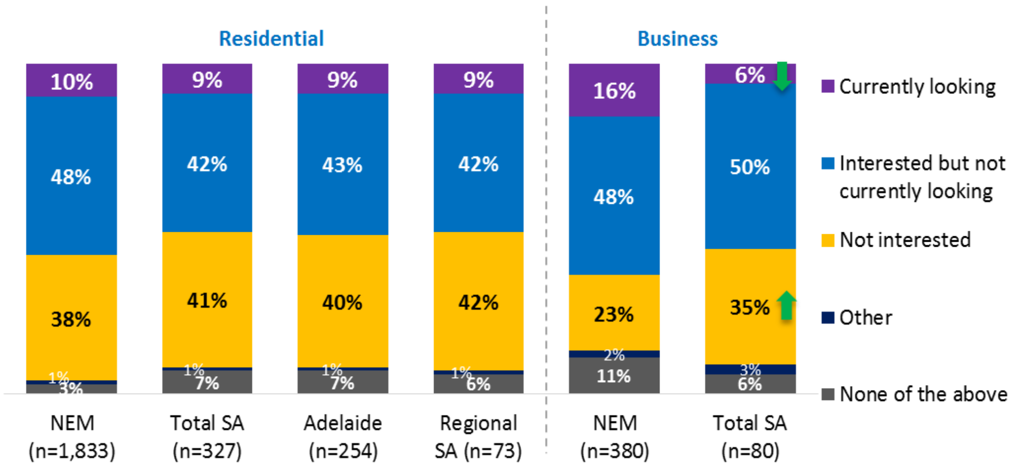
While the majority of customers stated they are interested in looking for a better deal, 41 per cent of residents surveyed were not interested. This is consistent with the NEM average.

In all jurisdictions surveyed except for the Australian Capital Territory, small businesses reported higher levels of interest in finding a better deal than residential customers. However, this interest was significantly lower among the small businesses

300 Some retailers cautioned that their estimates were indicative only.

surveyed in South Australia, with 35 per cent not interested compared to the NEM average of 23 per cent. This is shown in Figure 9.4. The arrow indicates a result that is statistically different from the NEM average at the 95 per cent confidence level.

Figure 9.4 Interest in looking for a better deal



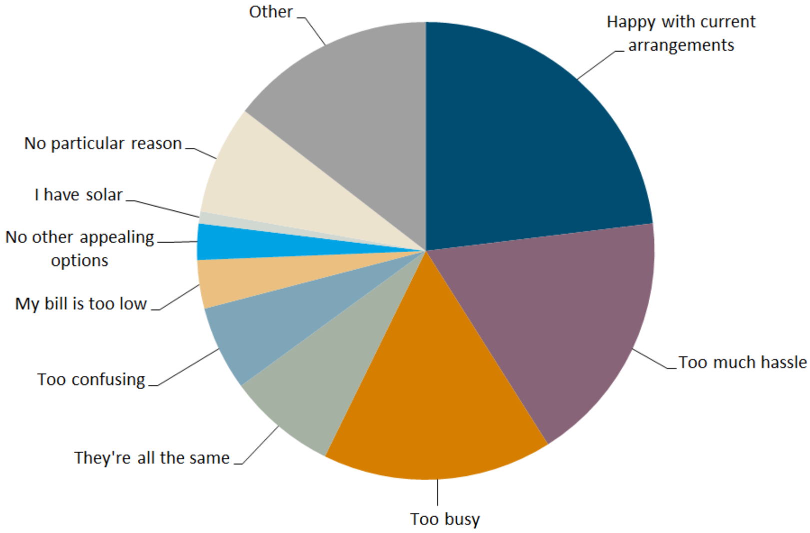
Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p104. Survey question: When it comes to your household's energy company, which of the following statements is most applicable to your household? Customers surveyed: All.

Most small customers said they were unlikely to switch in the next 12 months. Again, the South Australian small businesses surveyed were less likely to switch in the next 12 months compared to the NEM average.

It is possible there is some disinterest in investigating deals or switching in the next twelve months if customers have already recently done so. Close to a third of residential customers surveyed had already investigated options in the last twelve months. Similarly, close to a third of residential customers were not interested in going through this process in the next twelve months.

Figure 9.5 shows the most common reasons cited by customers in South Australia who had not investigated options in the last 12 months or switched retailer or plan in the last five years.

Figure 9.5 Most common reasons for not investigating or switching - SA



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p94. Survey question: Are there any reasons why you haven't investigated different options or why you haven't changed your energy company or plan in the last few years? Customers could select multiple responses. Customers surveyed: Residential customers who hadn't investigated options or changed their energy company.

In the deliberative forums and survey responses, customers that had switched generally found the process quite straight-forward and simple. Survey responses suggest that the key reasons customers are not investigating their options or switching retailers relate to a lack of value proposition and more general disengagement. That is, most of these customers hadn't switched or investigated options because they are happy with their current arrangements or they didn't have sufficient energy or time to do so. This is consistent with survey and qualitative forum results for all other NEM jurisdictions and is discussed in more detail in Chapter 3.

> "The bill comes, it seems fine, I can afford it so I pay it. (Adelaide, lower income)"

> "[I have] other priorities in life, not having the time [to research]. (Murray Bridge, higher income)"

The AEMC found that customers can save by shopping around, as set out in Box 9.2.

Box 9.2: Potential savings from moving off a standing offer to a market offer

The AEMC's 2013 Residential Price Trends report found that the average residential customer in South Australia may have saved around nine per cent per annum (or approximately $160 a year) by switching from a standing offer to a market offer in 2012-13. This does not capture the full savings which could be made by switching to the lowest advertised market offer or by negotiating with retailers to obtain lower prices than those advertised.

Seven per cent of customers were dissuaded from investigating options or switching as they found the options confusing. The issue of complexity was more evident during the qualitative forums where barriers to switching were discussed in detail. This was a particularly strong barrier for those who had previously gone through the process of switching. The most common complaints from participants were that information is unclear, hard to read, full of fine print and jargon, inconsistent, incorrect or misrepresented.[301]

> "I'm not sure about the options, what they all mean. (Adelaide, small business)"

> "The discount doesn't tell you if you're saving money over something else without knowing what the rate is. (Murray Bridge, lower income)"

Another common complaint in all forums was the difficulty with comparing options. Very few were aware of the government's comparator website, Energy Made Easy.[302] This was supported by the survey results where only one per cent were able to name the website. When prompted, 14 per cent of residential customers and 11 per cent of small businesses said they had heard of the website.

Improving awareness of Energy Made Easy as a tool to reduce the time, effort and complexity of investigating options may help to improve the level of engagement among this group of customers. The South Australian Council of Social Services (SACOSS) notes that 17 per cent of households do not have access to the internet and that low income households and the elderly in particular are less likely to benefit from internet-based comparator websites.[303] As discussed in section 3.2.2, the AEMC's consumer engagement blueprint developed in 2013 recommends ways to engage such customers.

It may also encourage some customers that do not trust retailer information to investigate their options using an independent source of information. High levels of retailer mistrust were apparent in the forums, primarily due to marketing behaviour. There was also greater mistrust of smaller retailers they had not heard of before.

> "...underhanded tactics to sign up new customers. Door knocking - it's not necessary. (Adelaide, customer who had switched)"

> "I'd rather pay a bit more and have a company that I know has a good reputation. (Murray Bridge, higher income)"

Customers that are more engaged may also benefit from increased awareness of the tools that are available to help them compare offers. All customers should be encouraged to reassess their energy needs and shop around regularly to take advantage of new offers or move to more suitable plans as their energy needs change.

---

301 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p96-97.

302 www.energymadeeasy.gov.au

303 SACOSS, submission to the *2014 Retail Competition Review,* Approach Paper, p3 and p7.

9.4 Retailer barriers to entry, exit or expansion

Barriers to entry, exit and expansion are another important indicator of the state of competition. Low barriers to entry and expansion place competitive pressure on retailers due to the threat of new entrants or other incumbents attracting away customers. These competitive pressures should lead to retailers charging prices that are commensurate with their costs and providing customers with the products and quality of service that they demand.

Our analysis of this criterion considers key findings from retailer interviews and surveys conducted by consultants engaged for this review, K Lowe Consulting and Farrier Swier Consulting.[304]

Nine of the 13 energy retailers that are currently active in South Australia agreed to participate in the retailer interview and/or the survey process.[305]

One of the key issues that these retailers were asked to provide their opinion on in both the interview and survey, is the ease with which entry and expansion can occur in gas and electricity retail markets in South Australia. The responses to this question revealed the following about entry and expansion conditions in these two markets:

- **Electricity retail market** – Entry into the electricity retail market is considered relatively easy by retailers, but expansion is perceived to be more difficult, particularly by retailers that do not have generation interests in South Australia.
- **Gas retail market** – Entry and expansion conditions in the gas retail market are perceived to be reasonably easy by retailers, although entry into this market is considered to be harder than in it is in both the electricity retail market and the Victorian gas retail market. Retailers also noted that entry can be more difficult in regional areas because of the small size of the customer base in these areas and constraints on the availability of capacity on some regional pipelines.

The views expressed by retailers and the observations set out below are broadly consistent with the Commission's findings in the 2007/08 review of the effectiveness of retail competition in South Australia.[306]

While there is evidence of recent entry and expansion in both the gas and electricity retail markets, retailers have identified a range of regulatory and non-regulatory factors that may affect the ease with which entry and/or expansion can occur in these two markets. Further detail on the factors cited by retailers is provided below.

304 For full details refer to K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014.

305 As at December 2013, AGL owned Australian Power and Gas and Powerdirect and these are treated as one retailer for our analysis of competition in the market.

306 AEMC, *Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia*, First Final Report, 19 September 2008, pp32-36.

9.4.1 Factors potentially affecting entry and expansion in the electricity retail market

The factors that retailers cited as potential impediments to entry and/or expansion in the South Australian retail electricity market include:

- wholesale market conditions and the ability of retailers that don't have generation interests in the state to access competitively priced hedging instruments;
- the dominance of the host retailer, AGL, which some retailers claimed is reinforced by AGL's generation interests in South Australia and its 'aggressive' retention strategies;
- the Residential Energy Efficiency Scheme (REES),[307] which some retailers claimed is imposing higher costs on smaller retailers because the scheme is not tradable and the 5,000 customer threshold is too low to enable smaller retailers to achieve any economies of scale in the delivery of the required services; and
- prudential and credit support requirements.[308]

Of the factors listed above, the ability to access competitively priced hedging instruments in South Australia was considered to be the most significant impediment by retailers. Further detail on the views expressed by retailers about this perceived impediment is provided below.

Wholesale market conditions and access to competitively priced hedging instruments

In the 2007/08 review, concerns were raised by a number of electricity retailers about the effect that higher spot prices, increased spot price volatility and increased vertical integration in South Australia were having on entry and expansion conditions in the retail electricity market.[309] Similar concerns were also raised during this current review, with a number of smaller retailers claiming that constraints on the availability of competitively priced hedging products in South Australia remains a significant issue for retailers without generation interests in the state because:

- wholesale prices in this market can exhibit greater volatility than some other regions;
- retailers are unable to rely on interregional hedges given the potential for the interconnector to become constrained;

---

307 The REES is a South Australian Government initiated scheme, which requires energy retailers with more than 5,000 customers to provide energy audits to residential customers and carry out other energy efficiency activities.

308 The Commission's views on this perceived impediment are set out in section 4.4.2.

309 AEMC, *Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia*, First Final Report, 19 September 2008, p33.

- non-renewable generation in South Australia is predominantly owned by vertical integrated retailers and according to some retailers, renewable generation 'doesn't cut it as a hedging instrument in SA'; and
- the market for South Australia futures products is 'highly illiquid and only provides coverage for a couple of quarters'.

This group of retailers went on to note that:

- the inability to secure competitively priced hedging instruments in South Australia is acting as a barrier to entry and expansion in the market and has prompted one recent entrant to wind back its activities in the state; and
- vertical integration is becoming more important in South Australia given the conditions prevailing in the wholesale market and reduced liquidity in the hedging market.

The concerns raised by retailers in this context about the conditions prevailing in the wholesale market were also cited as an impediment to entry by a second tier retailer with generation interests in South Australia. When asked about entry conditions, this retailer noted that even with generation interests in South Australia, entry into New South Wales would be easier because:

> "…while retail price regulation is no longer in effect in South Australia, the costs of operating in this state can be quite high given the risks in this market. For example, if the interconnectors go down retailers are more exposed to South Australia regional prices, so retailers may need a larger risk buffer on the energy component of their costs."

The SACOSS also raised a number of concerns about wholesale market conditions in South Australia and the influence they have had on competition in the retail market and the ability of non-vertically integrated retailers to expand:[310]

> "SACOSS…is strongly of the view that the extent of vertical integration in the South Australian electricity market means that consideration of 'retail' in isolation from 'generation' is problematic."
>
> "There is no evidence of substantial market share being achieved in South Australia without vertical integration – only Lumo has been seen to grow its market share since the 2008 allegations of the exercise of market power and this has been enabled by the portfolio of generators by Lumo's owners Infratil."

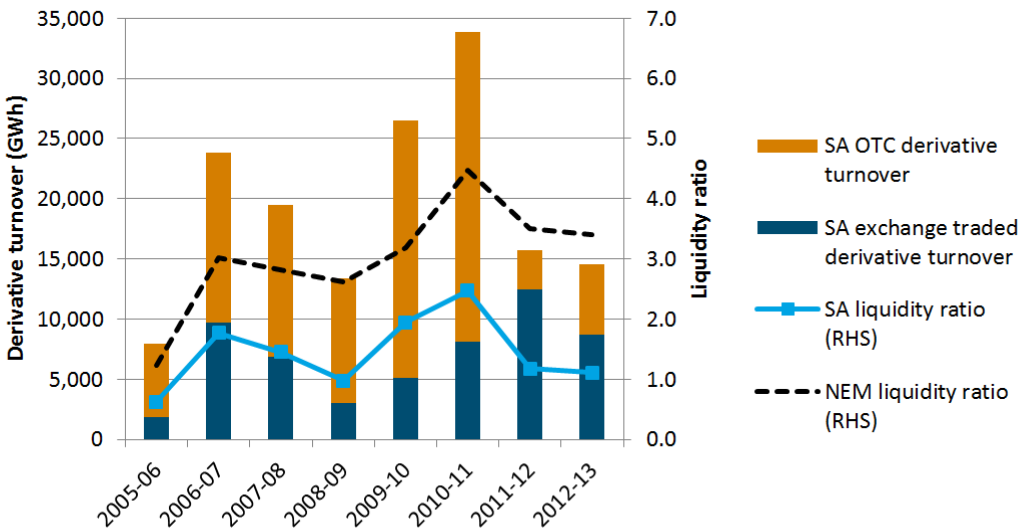
As noted in the introduction to this section, many of the issues that have been raised during this review about wholesale market conditions and constraints on the availability of competitively priced hedging instruments were also raised when the Commission undertook the 2007/08 review. While the Commission ultimately found

310 SACOSS, submission to 2014 Retail Competition Review Approach Paper, pp3 and 7.

that there were no insurmountable barriers to entry or expansion in the South Australian retail electricity market, it did note that entry and expansion conditions had become more difficult as a result of the conditions prevailing in the wholesale market and an increased level of vertical integration.[311]

Looking back over the last six years, it would appear that conditions in the wholesale market and constraints on the availability of futures and OTC products (see Figure 9.6)[312] have continued to influence entry and expansion conditions in the South Australian retail market. However, there has been entry over this period by retailers without generation interests[313] and non-vertically integrated retailers continue to operate in the market.[314] Therefore these market conditions do not appear to constitute an insurmountable barrier to entry. Further, planned upgrades to the Heywood interconnector may improve hedging options and lower risks for retailers.

Figure 9.6 Annual electricity futures turnover and liquidity ratios



Source: ASX Energy and AEMO data; AEMC analysis.

9.4.2 Factors potentially affecting entry and expansion in the gas retail market

To retail gas in South Australia, a retailer must enter into gas supply and transportation contracts and participate in the Adelaide Short Term Trading Market. Entry into all of these contractual and market arrangements can involve relatively high transaction costs. When coupled with the fact that the prices payable under gas supply and transportation contracts tend to be predominantly fixed, it is not surprising that entry into the South Australian gas retail market is considered more difficult than entry into either:

311 AEMC, *Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia*, First Final Report, 19 September 2008, p33.

312 Section 2.6 sets out why this data should be interpreted with caution.

313 For example, Dodo Power & Gas and Sanctuary Energy.

314 For example, Red Energy and Momentum Energy.

- the South Australian electricity retail market; or
- the Victorian gas retail market, which operates under a different transportation and balancing market model.

Some of the other factors that retailers claimed may impede entry and/or expansion in the South Australian retail gas market are:

- constraints on the availability of capacity on some of the transmission pipelines servicing South Australia;
- tightening demand and supply conditions in the wholesale gas market brought about by the development of liquefied natural gas (LNG) facilities in Queensland; and
- the small size of the customer base in some regional areas and constraints on the availability of capacity on some regional pipelines.

The views expressed by retailers about each of these factors are set out below.

Access to transmission pipelines

Gas can currently be supplied to South Australia from the Cooper/Eromanga and the Bowen/Surat basins via the Moomba to Adelaide Pipeline System (MAPS), the Otway Basin via the SEA Gas Pipeline and/or the Gippsland and Bass basins via the Victorian Transmission System (VTS) and the SEA Gas Pipeline. During the retailer interviews, a number of smaller retailers noted that the ability to transport gas from the Otway, Gippsland and Bass basins to South Australia is currently constrained because:

- all of the firm capacity on the SEA Gas Pipeline has been contracted by Origin Energy, GDF Suez, AGL and EnergyAustralia through to 2018; and
- there are difficulties associated with transporting gas in a westerly direction across the VTS.

While it was acknowledged by some retailers that there may be spare capacity on the MAPS, they claimed that it would be 'very difficult to purchase gas from producers in the Cooper and Bowen/Surat basins given demand from LNG is pulling gas north'. So this option was not considered a viable alternative.

On the basis of the information provided by retailers, it appears that:

- constraints on the availability of firm transportation capacity on the SEA Gas Pipeline may already be limiting entry into the South Australian retail gas market, although the fact that Alinta Energy has recently entered the market suggests that the impediment is surmountable; and
- constraints on the availability of capacity on the SEA Gas Pipeline and the difficulties associated with transporting gas across the VTS could act as more of a

constraint going forward if the LNG developments in Queensland result in South Australia becoming more reliant on gas supplied from Victoria.

Conditions in the wholesale gas market

In the interview and survey process, a number of retailers noted the potential for conditions in the wholesale gas market to deter new entry in some retail gas markets until conditions in the wholesale market 'settle down'.

One of the markets that retailers claimed was likely to be affected by the changes is South Australia, because of its historic reliance on gas supplied from the Cooper and Bowen/Surat basins, both of which are now largely committed to the LNG developments.

There is uncertainty in the gas industry about how conditions in the wholesale gas market are likely to affect wholesale gas prices in some jurisdictions and, in turn, the demand for gas by small customers. Faced with this level of uncertainty, it is possible that prospective entrants into the South Australian retail gas market could decide to defer entry until conditions in the wholesale gas market ease.

Constraints in rural and regional areas

During the interviews, a number of retailers noted that entry into regional areas of South Australia has been more difficult because:

- the capacity of the regional pipelines has been fully contracted by a single retailer; and/or
- the size of the customer base in these areas is too small to make entry by a large number of retailers economically viable given the fixed cost nature of retailing gas.

Information provided by Envestra[315] also indicates that Origin Energy is still the dominant retailer in regional areas of South Australia.

The information provided by both retailers and Envestra suggest there has been little change in the ability of retailers to supply regional areas since the Commission conducted the 2007/08 review and that structural factors are continuing to limit entry in these areas.[316]

315 Envestra, submission to the *2014 Retail Competition Review,* Approach Paper, 28 February 2014, p2.

316 AEMC, *Review of the Effectiveness of Competition in Electricity and Gas Retail Markets in South Australia*, First Final Report, 19 September 2008, p35.

9.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

Our analysis of this criterion considered findings from retailer interviews and advertised market offers, which suggest the following:

- **There is a high degree of rivalry** with 13 retailers competing for electricity customers and five competing for gas customers.
- **Market concentration is high, but rivalry appears strong** with increasing competition between the "big three" (ie AGL, EnergyAustralia and Origin Energy) and the second tier retailers over the last five years. The exception is the gas market in some regional and rural areas, where the market share of the host retailer is reportedly close to 100 per cent.
- **Retailers are differentiating their market offers** based on discounts, contract duration and non-price incentives. Time of use tariffs are not currently being offered.

9.5.1 Market share and concentration

There are thirteen energy retailers currently competing in the small customer market in South Australia, five of which offer gas as well as electricity.

Despite the reasonably high proportion of second tier electricity retailers, market concentration as measured by the Herfindahl-Hirschman Index (HHI) is reasonably high at 3,340.[317]

The market share of the incumbent retailer in South Australia, AGL, has reduced slightly since the 2007/08 competition review but it remains high at over fifty per cent. Retailers other than the big three collectively have a market share of approximately 20 per cent. Despite this high market concentration, rivalry between retailers appears relatively strong as discussed below.

The gas retail market has a similar level of market concentration with an HHI of 3,439. The incumbent gas retailer, Origin Energy, has a market share of slightly less than 50 per cent. The remainder of the market consists of four retailers. The most recent entrant obtained a gas retail license in July 2011 and has been gaining market share.

In regional and rural areas, the gas retail market is significantly more concentrated. Envestra has submitted that the host retailer market share in regional South Australia

317 The ACCC uses a score of 2000 as a threshold when considering the level of competition for merger assessments.

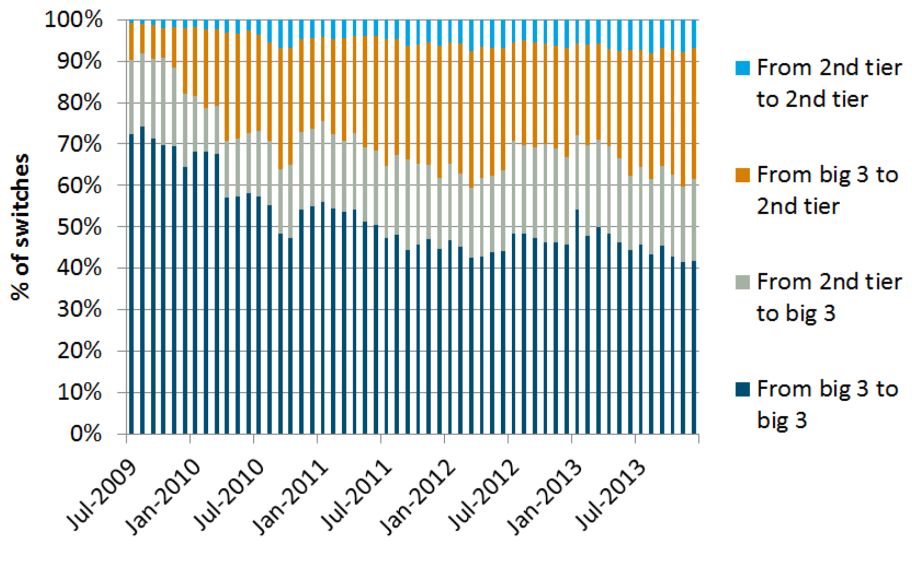
is close to 100 per cent.[318] As discussed in section 9.4, retailers have identified a number of impediments to offering gas in regional areas. Only Origin Energy and AGL appear to offer natural gas outside of Adelaide and there are some areas where Origin Energy is the only retailer.

Retailers rated South Australia as having a high degree of retailer rivalry in the electricity market. They noted that the removal of price regulation in February 2013 has not further increased rivalry. One retailer attributed this to the market already being fairly competitive. Another considers that "deregulation came out of the blue, so rivalry has taken time to ramp up."[319]

Switching between the big three and other retailers shows the increasing activity of second tier retailers in the market. Switching between the big three currently accounts for less than 50 per cent of switches, compared to 70 per cent in 2009. Switching between second tier retailers has been slowly increasing and second tier retailers continue to win customers from the big three.

Retailers also consider competition in the South Australian gas market to be relatively high. However, as discussed above, Envestra submitted that gas retail competition is less effective in regional areas.

Figure 9.7 Electricity switching rates by tier in South Australia



Source: AEMO data, AEMC analysis.

318 Envestra, submission to the *2014 Retail Competition Review*, Approach Paper, 28 February 2014, p1.

319 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, April 2014, p24.

9.5.2 Product differentiation

Retailers interviewed stated that there is a moderate level of product differentiation and innovation in South Australia. Our analysis of offers advertised in March 2014 in South Australia supports this view. While a static assessment of offers available at one point in time has some limitations, it can provide a useful snapshot of the type of differentiation occurring in a market.

In addition to the features discussed below, retailers also differentiate their brand through service quality such as call centre operation hours, information provision, policies on hardship and complaints, policies on door knocking and cold calling, online account access and, in some cases, shopfronts for customers to visit and discuss their options.

Standing offers

Retailers in South Australia are required to offer a contract with regulated terms and conditions known as a 'standing offer'. With the removal of retail electricity price regulation, AGL agreed to offer a transitional standing offer which would be fixed for two years from February 2013, subject to network and environmental scheme costs. As at 31 March 2014, there were 13 standing offers available. Standing offers varied between retailers in terms of tariff structure and levels. These were also identical or very similar to the tariffs for market offers before discounts.

Electricity market offers

As at 31 March 2014 the Energy Made Easy price comparator website showed 40 market offers for Adelaide from 13 different retailers. Many of these offers were very similar in terms of their features, but there are some key differences. The table below summarises these differences to provide an example of the way retailers are differentiating electricity offers to residential customers in South Australia.

As indicated in Table 9.1, there is a relatively diverse range of discounts available and a range of contracts varying in duration or with no fixed term. There is a high degree of differentiation of tariff structures in South Australia in terms of non-inclining and inclining block structures, however there are no time of use tariffs available.

The range of offers available and the level of product differentiation appear similar for residential and small business customers and for customers in rural and urban areas. For example, as at 31 March 2014, the same offers with the same tariffs were available in Murray Bridge and Adelaide for residential customers and small business.

Table 9.1 Differences in electricity offers in Adelaide as at 31 March 2014

Differences between offers *(high number of offers: >30; moderate: 15-30; low: 0-15)*	
Time of use tariffs	No offers available.
Other tariffs	High number of offers with moderate level of difference. Tariffs available were: • inclining block structures which differed by consumption threshold and the number of consumption bands (some also distinguished between consumption at different times of the year); and • flat consumption rate and supply charge tariffs.
Discounts	High number of offers with high level of difference. Unconditional discount options range from 3-7 per cent off usage charges. Conditional discounts range from 1-20 per cent off usage and include discounts for paying on time or by direct debit.
Contract duration	High number of offers with high level of difference. Choice of fixed terms ranging from 1 to 5 years or contracts with no fixed term.
Non-price incentives	Low number of offers with moderate level of difference. Options include: • Bonus signup rebates from $40-100; • Bonus $20 rebate for signing up to direct debit; • Store voucher; • Frequent flyer points; • No risk offer; • No termination fee if the retailer cannot beat a better offer; • Advantage online awards program; • 'Golden bill giveaway where select customers do not have to pay their bill for the last quarter; • 'One free move' where customers receive one free standard connection and disconnection per year; • Rate freeze offer for 24 months with no exit fees; • Ability to purchase renewable energy certificate equivalent to proportion of electricity consumption; and • One retailer offers an electric vehicle specific tariff.
Solar feed-in tariff	High number of offers with low level of difference. Retailers offered feed in tariffs for solar panels from 7.6-9.8 c per kWh exported to the grid.[320]

[320] More information on solar arrangements is provided in Appendix D.

Gas market offers

Consistent with other NEM jurisdictions there is less differentiation in gas offers. As at 31 March 2014, there were five retailers with a total of 16 gas offers. Similar to electricity, the offers available varied mainly on the term of the contract, level and types of fees charged, the level of discounts available and other non-price variations.

There appeared to be less choice for gas customers in regional areas than those in urban areas. For instance, there were only two retailers offering a total of 9 offers in Murray Bridge.

9.6 Customer outcomes

Effective competition is characterised by how well the process of markets promote the long term interest of customers, including satisfaction with the level of choice available as well as with the quality of service and value for money provided by retailers. Our analysis of this criterion considered the findings of customer surveys and data on customer complaints, which suggest the following:

- **Many customers are satisfied with the level of choice** in the market, though some perceive little difference between the choices available.
- **Most customers are satisfied with their current retailer**, due to an absence of supply interruptions or customer service issues.
- **Complaints to retailers increased considerably in 2012-13**, which may be due to issues with the new billing systems of two retailers.

9.6.1 Satisfaction with the level of choice

There was a slightly higher proportion of customers who were satisfied with the level of choice in South Australia relative to other jurisdictions surveyed. Fifty-six per cent were either very or somewhat satisfied. Twelve per cent were very or somewhat dissatisfied, with the remainder neither or not sure.

Customers in regional areas tended to be more satisfied than those in Adelaide. However, discussions in the forums suggested that the issue is complex and that real satisfaction with the level of competition and choice is lower. Many participants perceived little difference between the offers of different retailers.

> "There's lots of choice but prices are practically the same. (Adelaide, small business)"

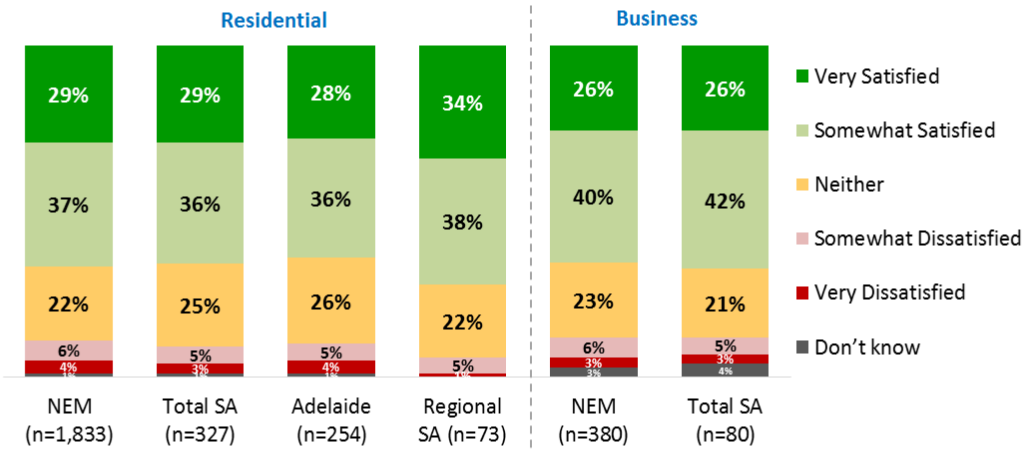
> "You can't see the honesty in the competition. (Murray Bridge, lower income)"

“One of my relatives used to read meters and they said that even though there’s 57 different offers, there’s a minimal amount of difference between them. (Murray Bridge, lower income)”

9.6.2 Satisfaction with retailers

The majority of customers were satisfied with their retailer in all NEM jurisdictions surveyed. In South Australia, most surveyed were at least somewhat satisfied with 65 per cent satisfied with their electricity retailer and 64 per cent satisfied with their gas retailer. In the qualitative research most customers linked satisfaction with the retailer to a reliable supply of power.

Figure 9.8 Satisfaction with current electricity retailer



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, 2014, p107. Survey question: How satisfied are you with your current electricity company? Customers surveyed: All.

Eight per cent of customers were somewhat or very dissatisfied, which is consistent with the NEM average. While the rate of dissatisfaction is low, this is not indicative of most customers having positive experiences with their retailers. Rather, satisfaction appears to relate to the absence of negative experiences, where customers in forums stated they were satisfied because they had no cause to contact their retailer. Those that were dissatisfied had complaints about billing issues, poor customer service experiences or marketing practices and general concerns about rising prices.

“I'm just ignorant to it all and happy, I have no problems. (Murray Bridge, lower income)”

“The power is there when you want it. (Adelaide, lower income)”

“I go in and the power comes on. I'm fortunate to have no problems with my bills. I'm fortunate that I can read and understand the bills. It's reasonable for what I get and what I know. (Adelaide, small business)”

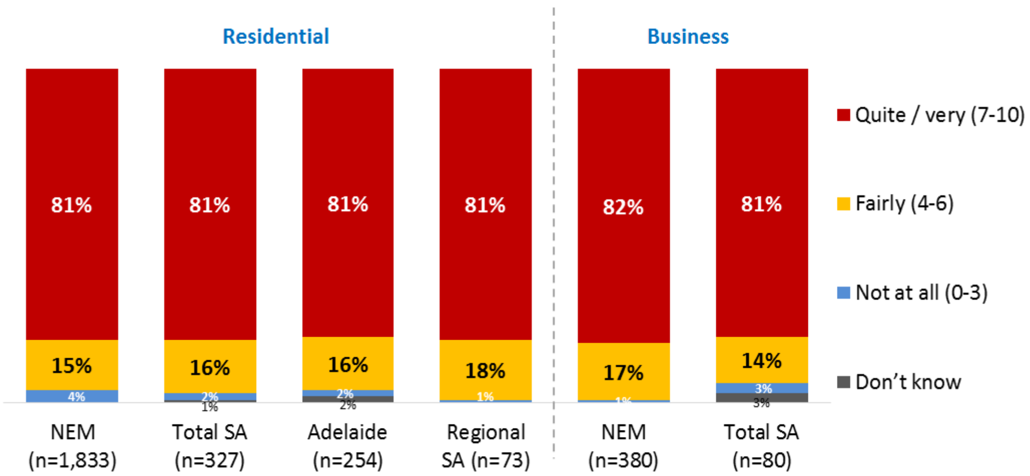
The overall quality of service was largely perceived as good or excellent by survey respondents. Customers in regional South Australia rated the quality of service even higher than customers in Adelaide. Business customers rated the quality of service higher than residential customers, however 19 per cent of the business customers who switched their electricity retailer or plan did so because they were unhappy with customer service. This result suggests that retailers are not meeting the expectations of some business customers with respect to quality of customer service.

Most customers were satisfied with value for money and 49 per cent rated it 'good' or 'excellent'. Customers in regional South Australia rated value for money slightly higher than those in Adelaide. More customers surveyed gave a poorer rating for value for money than for quality of service, with 14 per cent compared to three per cent respectively.

It is likely that value for money ratings primarily relate to higher electricity bills in recent years. Consistent with other NEM jurisdictions, customers in South Australia have experienced considerable price rises over recent years. The main driver of price rises have been regulated distribution network costs.[321] A full discussion of the drivers of price movements and trends in electricity prices is available in the AEMC's annual residential pricing trends report.

In South Australia, around 81 per cent of customers surveyed stated that they were ‘quite’ or ‘very’ concerned about future electricity prices, which is consistent with the NEM average.[322]

Figure 9.9 Level of concern about future energy prices



Source: Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, 2014, p75. Survey question: How concerned are you about future energy prices? Customers surveyed: All.

For South Australian customers on high and middle incomes, annual electricity bills are estimated to represent approximately 1-2 per cent of the average disposable

321 AEMC, 2013 *Electricity Price Trends* Final Report, 22 March 2013, p 77 and AEMC, *Possible Future Retail Electricity Price Movements: 1 July 2011 to 30 June 2014*, 2011, p53-54.

322 Newgate Research, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, a report for the AEMC, June 2014, p75.

income. For low income customers, annual electricity bills represent approximately 6 per cent of annual income.[323]

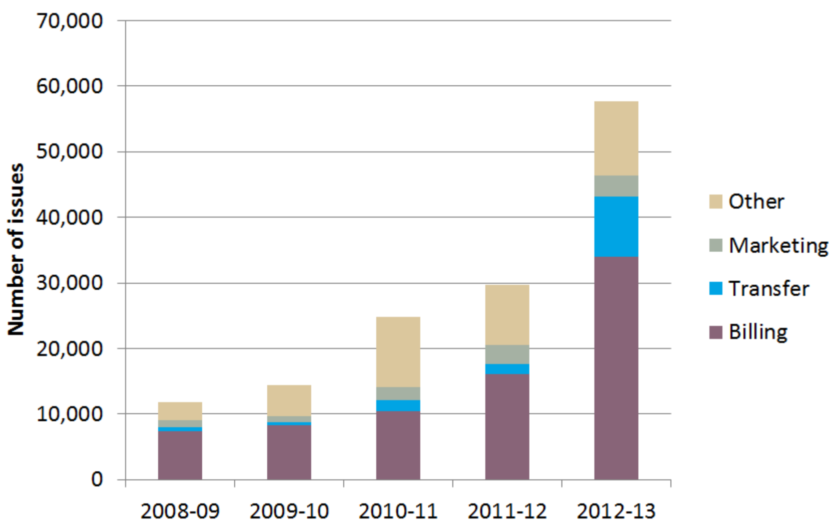
South Australians on low or fixed incomes[324] could access concessions to cover both electricity and gas payments of up to $165 per year in 2013-14, which has been increased by the South Australian Government to $215 from 1 July 2014. An energy concession is also available for low income customers that have a medical condition requiring the frequent use of heating or cooling. Concessions are further discussed in Appendix B.

Complaints to retailers

When a customer makes a complaint, multiple different issues may be raised. In South Australia in 2012-13, the number of issues raised with retailers was higher than in any of the previous four years. This number almost doubled between 2011-12 and 2012-13, driven by increased billing and transfer issues raised (see Figure 9.10). As discussed below, the increase in billing issues raised could be attributable to billing system problems. Consistent with other jurisdictions, billing issues were the most common, making up almost 60 per cent of issues raised in 2012-13.

Due to the way in which data is reported, separate data for electricity and gas complaints is not available for 2012-13 however, in every year from 2008-09 to 2011-12, over 75 per cent of issues raised regarded electricity retailers (see Figure 9.11).

Figure 9.10 Electricity and gas complaints to retailers – by issue type

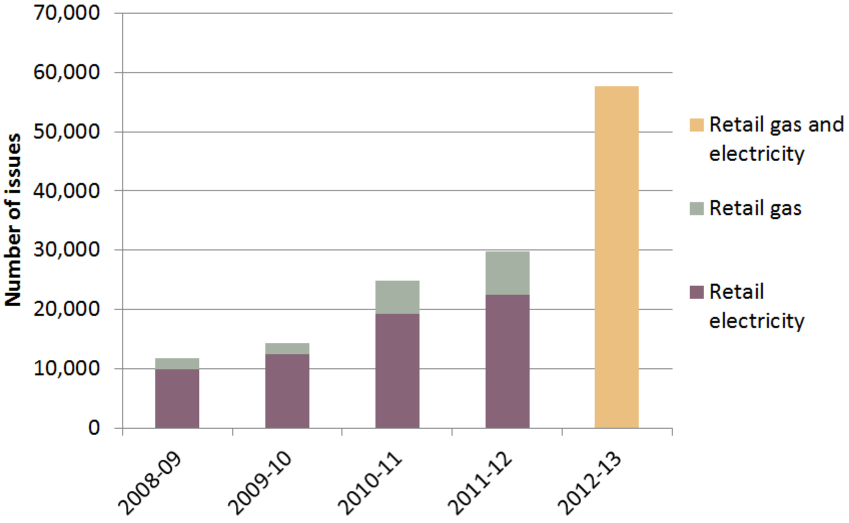


Source: Data provided by the AER and from ESCOSA Annual Performance Reports.

323 This AER analysis is based on average annual electricity consumption of 5,000 kWh for low income customers and 6,000 kWh for high income customers. AER, *Annual report on the performance of the retail energy market 2012-13*, 2013, p76.

324 Includes pensioners, veterans and people on certain Centrelink payments.

Figure 9.11 Electricity and gas complaints to retailers – by service



Source: Data provided by the AER and from ESCOSA Annual Performance Reports.

Complaints to the Ombudsman

Fewer issues about retail gas or retail electricity were raised with the Energy and Water Ombudsman South Australia (EWOSA) than with retailers. In 2012-13, around 14,200 electricity issues were raised with EWOSA, equating to 170 issues per 10,000 customers.[325] Around 2,100 gas issues were raised with EWOSA, equating to 50 issues per 10,000 customers. Additionally, there were around 1,700 dual fuel issues raised in 2012-13. Note that issues raised with EWOSA include referrals back to retailers, which are also captured in complaints to retailers described above. Consistent with complaints to retailers, the number of electricity, gas and dual fuel issues raised was higher in 2012-13 than in the previous year.[326] EWOSA noted that the conversion of the billing systems of two major energy retailers had led to billing delays and erroneous accounts in 2012-13, which may be driving the increase.[327]

Again, billing issues were the most commonly raised with EWOSA for retail electricity, retail gas and retail dual fuel. Billing issues made up 63 per cent of retail issues regarding electricity and 54 per cent of issues regarding gas (see Figure 9.12 and Figure 9.13). The most common sub-issue relating to billing was high billing, followed by "no bill or delay in billing". Complaints about high bills made up 34 per cent of the electricity billing issues and 26 per cent of gas billing issues.[328]

The remainder of issues raised with EWOSA regarding electricity and gas retail were sales and marketing, customer service, credit management and provision. Provision

---

325 Data on complaints to EWOSA excludes cases which were out of jurisdiction or not complaints.

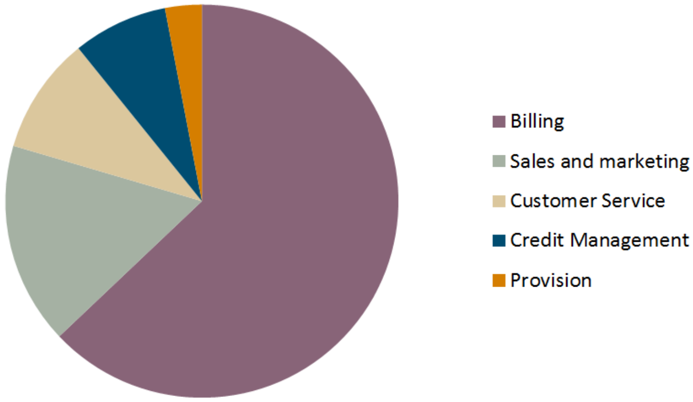
326 Including network complaints. Energy and Water Ombudsman South Australia, *Annual Report 2013*, 2013, p4.

327 Ibid, p8.

328 High billing issues are raised when a bill is higher than the customer expected.

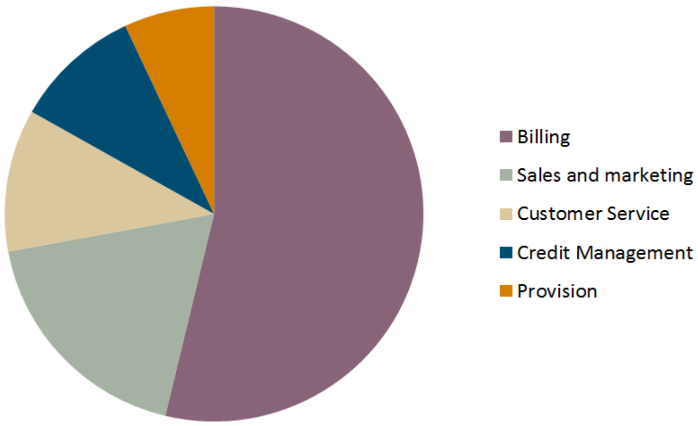
relates to the supply of electricity or gas to the property and may include, for example, issues relating to connections, disconnections or meter installations.

Figure 9.12 Electricity complaints to the Ombudsman – breakdown of issues raised in 2012-13 – South Australia



Source: Provided by the Energy and Water Ombudsman South Australia.

Figure 9.13 Gas complaints to the Ombudsman – breakdown of issues raised in 2012-13 – South Australia



Source: Provided by the Energy and Water Ombudsman South Australia.

9.7 Retailer outcomes

Profit margins can provide an indication of the level of competition in a market. However, they can also be expected to fluctuate over time. Consequently it is important to carry out analysis of retailer margins over a sufficiently long time period. It is also important to consider the results of such analysis in the context of other competitive indicators. While retail margins in South Australia have not been estimated for the purpose of this review, we make a number of observations on retailer outcomes drawing from retailer interviews.

The South Australian electricity market was rated as somewhat profitable by retailers that participated in the survey, consistent with New South Wales.

One retailer considered that despite prices no longer being regulated, the risks of operating in South Australia can be high. This is attributed to higher volatility in wholesale prices and the risks associated with using inter-regional hedges in the presence of congestion on the inter-connector. The retailer considered that, for this reason, a higher margin is required compared to other states. Another retailer made a similar observation about the impact of wholesale market volatility on margins, noting:[329]

> "Margins in South Australia are just all over the place. Some months it's good other months it's terrible. It just depends on your wholesale position."

There is limited information available on the profitability of gas, particularly due to the confidential nature of wholesale gas contracts and the lack of publicly available reference data. Retailers that responded to the survey considered gas retailing in South Australia as being on par with New South Wales and Victoria. Retailers that participated in both the electricity and gas surveys rated profitability in gas the same as for electricity.

9.8 Future developments affecting competition in the market

Competition in the South Australian electricity retail market in 2013 has been influenced by AGL's agreement with the South Australian Government to freeze standing offer prices for two years. This agreement is in place until the end of 2014, and consequently may continue to influence outcomes in that market in the short term.

Going forward, it is likely that competition will continue to evolve in South Australia. Customers may benefit from greater awareness of Energy Made Easy as an independent source of information to help them compare offers.

Some retailers consider that South Australia has the potential to overtake Victoria as the most competitive market in Australia, as customers become more engaged and further new entry by retailers occurs. Survey responses from retailers suggest that three smaller second tier retailers are considering entry into this market over the next five years, while four existing retailers are planning to expand over this period.

Retailers expect conditions in the wholesale and hedging markets in South Australia to continue to weigh on the market and, as a consequence, retailers with generation interests in South Australia are expected to continue to dominate. However, we note that there are currently five vertically integrated retailers competing in South Australia, two of which are second tier retailers. Further, as discussed above, planned upgrades to the Heywood Interconnector may improve hedging options and lower risks for non-vertically integrated retailers that wish to expand in, or enter, South Australia.

329 K Lowe Consulting and Farrier Swier Consulting, *AEMC 2014 Retail Competition Review: Retailer Interviews*, report for the AEMC p82.

Competition in the natural gas retail market is less likely to develop further over the next few years given technological limitations on innovation, less engaged customers compared to the electricity market and prevailing conditions in the wholesale gas market.[330] However, customers may become more active in this market if anticipated price rises materialise. This could lead to increased activity and higher churn rates as customers look for ways to lower their bills.

Survey responses indicate that no retailers are planning to enter the South Australian retail gas market in the next five years, but two existing retailers are planning to expand over this period. In addition to uncertain wholesale market conditions, more tempered retailer activity is influenced by capacity on the SEA Gas Pipeline being fully contracted to 2018. As a consequence, some retailers considered that competition may stagnate in the South Australian gas market.

330 See Chapter 3 for further discussion on these issues.

10 Tasmania

Box 10.1: Key findings

- Competition is not effective in the Tasmanian electricity retail market for small customers as the final tranche of full retail competition has only recently occurred.
  - Almost all small customers remain with the incumbent retailer. Fourteen per cent of residential customers are on pre-paid meters, with the remainder on a standing offer with the incumbent. A new retailer has very recently entered the market for small businesses consuming between 50 and 150 megawatt hours per annum.
  - None of the retailers interviewed had firm plans to enter the small customer market, although one small retailer stated it was considering entering the small business segment and another was considering entering the residential segment. Larger retailers stated that they did not have plans to enter the Tasmanian retail market.
  - Some retailers consider risks around the wholesale supply arrangements and the size of the customer base are impediments to entry.
- If new retailers enter the market, it will be important to raise customer awareness and understanding of their options. The AEMC's consumer engagement blueprint developed for the New South Wales retail competition review could be used as a basis to inform and engage customers in Tasmania as the level of choice in the market increases.
- While there is greater competition in gas, it is also somewhat limited.
  - There appears to be limited switching by small customers.
  - Two retailers operate in the market, but there is limited evidence of rivalry.
  - Very low penetration of gas distribution pipelines is a key impediment to entry and no retailers appear to be considering entry in the short term.

10.1 Overview

This is the first time the AEMC has reviewed competition for small customers in Tasmania's energy retail markets.

The Commission's assessment of competition against the five criteria set out in Chapter 2 has found that competition is not effective in the Tasmanian retail electricity market for small customers. There is some competition in the retail gas market in Tasmania, although this is limited.

The findings for the Tasmanian energy markets can be summarised as follows:

- **Customer activity:** Small customers currently have limited or no choice of their electricity retailer or plan. For gas, customer awareness and switching is reportedly low based on retailer feedback.

- **Barriers to entry, exit, and expansion:** The regulatory barrier preventing electricity retailers from competing in the residential and smaller business customer market was removed on 1 July 2014. The key remaining impediments to entry and expansion in the electricity market are the structure of the wholesale market and the nature of the customer base. The main impediment to entry in the gas market is the small size of the market and limited scope for growth.

- **Independent rivalry:** There is no retailer rivalry for residential or smaller business customers for electricity, and very limited rivalry for small businesses consuming more between 50 and 150 megawatt hours per annum. At the end of 2013, Aurora continued to have a 100 per cent market share of the electricity market. Rivalry also appears limited in gas, with two retailers operating in this market.

- **Customer outcomes:** Customer complaints appear low but this may be due to limited, or no, retailer marketing activity and a lack of customer engagement.

- **Retailer outcomes:** Retailers interviewed considered the Tasmanian retail electricity market not very profitable, primarily because of perceptions of higher risks associated with the wholesale arrangements and the smaller customer base across which fixed costs can be spread. Retail gas margins were rated somewhat higher by one retailer.

10.2 History and market characteristics

Full retail competition was introduced at different times for the gas and electricity markets and in different stages for different types of electricity customers.

The retail gas market has had full retail competition and no price regulation since the market's inception in 2007. Retail electricity prices are regulated by the Office of the Tasmanian Economic Regulator (OTTER). The Tasmanian Government has not announced any plans to remove electricity retail price regulation.

In the electricity market, full retail competition was introduced in July 2011 for small business customers with consumption of between 50 and 150 megawatt hours per annum. These customers are referred to as 'contestable small business customers' throughout this chapter, although we recognise that all customers are now contestable.

Small businesses consuming less than 50 megawatt hours are referred to as "smaller business" customers.[331]

Full retail competition was introduced on 1 July 2014 for residential customers and smaller businesses. From this date, retailers were permitted to offer electricity to all customers regardless of their consumption levels.

The Tasmanian Government has made a number of changes to the wholesale market arrangements, which it expects will encourage new retailers to enter the market.[332]

Tasmanian customers have been a part of the National Energy Customer Framework (NECF) since 1 July 2012. Under the NECF, all retailers are required to offer small customers a standing contract with regulated terms and conditions. Aurora is also required to offer a standing contract with a regulated price.

An expert panel was established under *The Electricity Supply Industry Expert Panel Act 2010* and made recommendations to the Tasmanian Parliament on the future development of Tasmania's electricity industry, including the retail electricity market. The Commission understands that the Tasmanian Government has also set up an Energy Working Group to assist it in developing a Tasmanian Energy Strategy, which is due to be finalised by the end of 2014.[333]

The market for electricity is the second smallest in the NEM with approximately 272,000 small electricity customers. Tasmania's gas market is the smallest of the national electricity market (NEM) jurisdictions, with approximately 7,400 small customers. The Commission understands that the roll-out of the gas network targeted large users and this, together with geographic barriers, has resulted in a low gas penetration rate of around 6 per cent in Hobart and 3 per cent in other parts of Tasmania.

10.3 Customer activity in the market

Customer activity in the market is an important measure of competition. By searching for better deals and switching to retailers that have lower prices or better service, customers play an important role in maintaining downward pressure on prices and driving retailers to provide the quality of service that customers want.

Until 1 July 2014, Aurora was the only retailer permitted to provide electricity to residential customers and smaller businesses. Contestable small businesses have been permitted to choose their electricity retailer since July 2011, and now have a choice of two retailers. However, the Commission understands that the vast majority of these

---

331 "Small customers" are defined under the National Energy Retail Law (Tasmania) Regulations 2012 as consuming less than 150 megawatt hours per annum.

332 The Tasmanian Government had also planned to sell Aurora's retail customer base to private retailers to coincide with completing the final tranche of full retail competition. In September 2013 it decided not to proceed with this process due to insufficient interest.

333 See www.stategrowth.tas.gov.au.

customers remain with the incumbent retailer. Consequently customer activity in the Tasmanian electricity market is very limited. For this reason consumer research was not conducted in Tasmania.

Small gas customers have slightly more choice than in electricity, as the gas market has been contestable since inception and customers have the choice between two retailers. However, retailers interviewed for this review suggested that customer awareness and switching in this market is low. Further, the market share of the two retailers does not appear to have changed in the last two years, which could suggest that any switching between retailers by customers has been limited.[334]

10.4 Retailer barriers to entry, exit and expansion

Barriers to entry, exit and expansion are another important indicator of the state of competition. Low barriers to entry and expansion place competitive pressure on retailers due to the threat of new entrants or other incumbents attracting away customers. These competitive pressures should lead to retailers charging prices that are commensurate with their costs and providing customers with the products and quality of service that they demand.

This section discusses key findings from retailer interviews and surveys conducted by consultants engaged for this review, K Lowe Consulting and Farrier Swier Consulting.[335]

All the retailers that participated in the interview process were asked to provide their opinion on whether entry into the Tasmanian retail electricity market is likely to occur post 1 July 2014, following the government's introduction of full retail competition for all small customers. They were also asked about any impediments to entry or expansion in this market.

In general, the retailers that participated in the interviews were broadly supportive of the decision by the Tasmanian Government to extend full retail competition to all small electricity customers, but they claimed that entry into this market was likely to be quite difficult for the following reasons:

- the wholesale market arrangements in Tasmania are considered to be less conducive to entry than in other jurisdictions;
- retail price regulation will continue to apply;
- the nature of the customer base is considered less attractive than in other jurisdictions;

334 See Australian Energy Regulator (AER), *State of the Energy Market 2012* and *State of the Energy Market* 2013.

335 For full details refer to K Lowe Consulting and Farrier Swier Consulting, *2014 Retail Competition Review: Retailer Interviews*, a report for the AEMC, June 2014.

- the level of customer awareness about the ability to switch is expected to be low and customers are expected to exhibit a high degree of loyalty toward Aurora; and

- economies of scale are expected to be of some importance given some of the jurisdictional specific regulatory requirements applying in Tasmania.

Unlike electricity, full retail competition has already been extended to all small gas customers in Tasmania. Gas retailers were therefore just asked to rate the ease with which entry and expansion can occur in the retail gas market. Retailers responded that entry and expansion in this market are difficult because:

- the volume of gas consumed by small customers in Tasmania is very low and the scope for further growth is considered limited;

- the costs of entering into wholesale gas supply and transportation contracts for small volumes of gas can be significant; and

- the viability of the retail market depends on the ongoing viability of industrial gas customers in Tasmania.

Higher wholesale gas prices brought about by tightening conditions in the east Australian wholesale gas market may also add to the difficulties associated with entry and expansion in this market.

Further detail on some of the more significant impediments to entry and expansion in the electricity and gas retail markets cited by retailers is provided below.

10.4.1 Factors potentially impeding entry into the electricity retail market

Two of the more significant factors that retailers claim are likely to deter entry into the Tasmanian retail electricity market are the wholesale market arrangements and the continued application of retail price regulation.

Wholesale market arrangements

In 2013 the Tasmanian Government announced that a number of changes would be made to the wholesale market arrangements in Tasmania to try and encourage retailers to enter the market as part of the broader implementation of full retail competition. The key elements of these new arrangements are summarised below:[336]

- Hydro Tasmania, which is currently the only large generator in Tasmania, will be required to:

336 Tasmanian Government, *Tasmanian Energy Reform – Market and Regulatory Framework – Position Paper*, March 2013.

- offer retailers that are authorised to operate in Tasmania a range of regulated hedging contract products (including a regulated load-following swap) at regulated prices and on standard terms and conditions;
- make available sufficient volume of the regulated products to enable retailers to adequately hedge their load in Tasmania; and
- determine the prices payable for regulated contract products using the mandated pricing methodology set out in the Wholesale Contract Regulatory Instrument.

- The first Wholesale Contract Regulatory Instrument is to be developed by the Tasmanian Government and, amongst other things, will set out the types of regulated contracts to be offered, the mandated pricing methodology and the standard contract terms.
- OTTER will be responsible for:
  - administering the Wholesale Contract Regulatory Instrument; and
  - monitoring the prices published by Hydro Tasmania.

  OTTER will also have the power to investigate Hydro Tasmania's regulated pricing.

With one or two exceptions, the retailers that participated in the interview process were critical of these arrangements and noted that they were unlikely to encourage entry because retailers would find it 'difficult to secure a competitive advantage in wholesale supply under the single provider model with all retailers facing the same price'. Some retailers went on to add that 'it would have been better if Hydro Tasmania had been split in two'. In contrast to the views expressed by this group of retailers, one smaller potential entrant noted that the arrangements would 'at least provide some hedge liquidity' to enable new entrants to compete effectively.

Retail price regulation

The continued application of retail price regulation was also seen as an impediment to entry in the electricity retail market. While a number of retailers viewed OTTER's most recent regulatory determination positively,[337] retailers have claimed that the 'mere presence' of retail price regulation deters entry due to the perceived risk that the regulated price is set below the retailer's cost of supply plus a reasonable margin.

337 The inclusion of an allowance for customer acquisition and retention costs in the regulated price was viewed positively by retailers. So too was the level of the retail margin that OTTER allowed.

Nature of the customer base

The nature of the small electricity customer base in Tasmania was also viewed by retailers as a potential deterrent to entry. The specific aspects of the customer base that retailers claim would make entry into Tasmania a less attractive proposition than other jurisdictions are:

- the relatively small size of the customer base (~272,000 customers);
- the geographic dispersion of the customer base, which retailers noted would make customer acquisition more difficult and costly; and
- the large number of Tasmanian customers that are reportedly on concessions.

A number of retailers also noted the potential for small customers to:

- exhibit a high degree of loyalty towards Aurora (the incumbent, government owned retailer); and
- have limited awareness of their ability to switch.

Retailers claimed that these factors would make it even more difficult for new entrants to compete effectively in the market and to attract sufficient customers to minimise the effect of the jurisdictional specific regulatory costs.

10.4.2 Factors potentially impeding entry and expansion in the gas retail market

Unlike electricity, the Tasmanian retail gas market is not subject to retail price regulation. The only impediments to entry and expansion that retailers cited were non-regulatory in nature.

Three of the more significant factors that retailers claim may impede entry and/or expansion in the gas retail market are:

- the small size of the market (~7,400 small customers) and the limited scope for growth;
- the costs associated with entering into wholesale gas supply and transportation arrangements, given the relatively small size of the customer base; and
- the ongoing viability of the retail market depends on whether industrial customers continue to use gas in Tasmania.

The size of a market will not, in and of itself, usually constitute a barrier to entry. However, if the costs of supplying that market are largely fixed or sunk (ie there are economies of scale associated with supplying this market), then the size of the market may place a cap on the number of retailers that can enter and effectively compete in the market. As noted in section 4.4.3, the Commission is aware from the work that was done as part the gas market scoping study[338] and from information provided by retailers through the interviews and survey, that the costs faced by retailers can exhibit these types of characteristics.

The other factor that retailers noted may discourage entry into this market is that the overall viability of the retail market is highly contingent on the demand for gas by industrial customers in Tasmania. One retailer noted that if any large industrial loads in Tasmania were to stop using gas, then the transportation tariffs payable by the remaining users of the Tasmanian Gas Pipeline would increase significantly (ie because they are having to be recovered fixed costs from a smaller customer base). The retailer went on to add that if this occurred, other industrial and retail customers may also decide to no longer use gas, which could result in further tariff increases and feedback effects. The retailer concluded that if any more large industrial loads were lost in Tasmania 'there may not be a retail gas market in Tasmania in the next five years.'

10.5 Independent rivalry

Rivalry between retailers is another key indicator of effective competition in a market. Independent rivalry can lead to improvements in service quality, pricing and innovation in order for retailers to attract customers from competitors and retain them.

As explained above, residential electricity customers and smaller business electricity customers only became contestable from 1 July 2014. Consequently there is only one retailer operating in this segment of the market. One new retailer has only very recently begun supplying contestable small businesses and so rivalry is also yet to emerge in this segment of the market. There are currently very few electricity offers available to contestable small business customers, and little or no differentiation between these offers.

There is limited information available to assess the degree of rivalry between the two gas retailers active in the gas market. The views of retailers that were interviewed for this review suggest rivalry is low.

10.5.1 Market share and concentration

There are currently two active retailers for contestable small businesses: Aurora and ERM Business Energy. While ERM Business Energy had previously been retailing to large contestable customers in Tasmania, the Commission understands that it only entered the small business market in March 2014 and so has had limited opportunity to gain market share. Consequently Aurora continues to dominate this segment of the market.[339]

---

338 K Lowe Consulting, *Gas Market Scoping Study* a report for the AEMC, July 2013, pp42-45.

339 While not directly relevant to this review, we note that Aurora Energy has retained a share of around 90 per cent of the contestable market, including large and some small customers.

There are also two active gas retailers: Aurora and Tas Gas. As at August 2013 these retailers had market shares of 40 per cent and 60 per cent, respectively. Market concentration is therefore fairly high, as measured by the Herfindahl-Hirschman Index, with a score of 5,200.[340] The AEMC does not have switching information for this market. However, as discussed in section 10.3, it appears that any switching between retailers by customers has been very limited.

10.5.2 Product differentiation

Electricity offers for residential and smaller business customers

Aurora has a standing offer for residential lighting and power (Tariff 31) and a choice of two lower tariffs for hard wired heating devices (Tariffs 41 or 42) that are used in conjunction with Tariff 31. There are also off-peak options.[341] All are non-inclining block tariffs and include a direct debit discount and GreenPower options.

Aurora has a single general standing offer (Tariff 22) for the majority of smaller businesses.[342] Off-peak tariffs are also available in association with the general standing offer (Tariffs 61 and 62).

As of 1 January 2014, Aurora has been permitted to offer market contracts as well as the standing offer to residential customers and smaller business customers. However, as of June 2014 Aurora appears to continue to only provide standing offers for these customers.

Aurora does provide an optional pre-paid metering offer for residential customers. Aurora's Pay As You Go (APAYG) offer has prices that vary according to time-of-use and time-of-year. These prices are not regulated by OTTER on the basis that it is a ‘choice’ product and all customers have the option of reverting to (or staying on) regulated tariffs. As at 30 June 2013, approximately 33,158 residential customers (14 per cent) were on this offer[343], down from 40,000 customers (19 per cent) in 2006[344]. However, the number of APAYG connections appears to be declining.[345]

OTTER publishes an annual comparison of APAYG rates and standard residential tariffs. Its 2012 report found APAYG may be less attractive for some non-concession customers than the standard regulated tariffs as they would appear to be paying more over the course of a year, though this depends on the customer and their usage patterns.

---

340 The HHI maximum is 10,000, which represents a perfect monopoly market. The ACCC uses a score of 2000 as a threshold when considering the level of competition for merger assessments.

341 Tariffs 61 and 62.

342 There are special nursing home and agribusiness rates.

343 AER, *Annual report on the performance of the retail energy market 2012-13*, p10.

344 OTTER, *Aurora Pay As You Go Price Comparison Report*, December 2006, p1.

345 AER, Annual Report on the Performance of the Retail Energy Market 2012-13, p10.

Electricity standing offers for contestable small business customers

As at 31 March 2014, Aurora offered contestable small business customers a standing contract with tariffs approved by OTTER. ERM Business Energy also offers a standing contract. Both have solar feed-in tariff options. Aurora also offers GreenPower options and a conditional discount if paying by direct debit.

Electricity market offers for contestable small business customers

As at 31 March 2014, Energy Made Easy showed 4 market offers for small business customers. These were:

- Aurora's "Simple Business Rate - Northern Tasmania" and "Simple Business Rate - Southern Tasmania" offers; and
- ERM Business Energy's "Adjustable" and "Fixed until 31st December" offers.

A comparison of these tariffs is set out in Table 10.1 below.

Table 10.1 Differences in electricity offers in Hobart as at 31 March 2014

Areas of difference between offers ***(high number of offers: >30; moderate: 15-30; low: 0-15)***	
Time of use	No time of use offers available.
Other tariffs	Low number of offers with a low level of difference. All market offers had a flat tariff with different rates.
Discounts	Low level of difference. The only discount was $5 off usage charges per bill each quarter for paying by direct debit through savings or cheque account.
Contract duration	Low number of offers with no difference. Choice of 1 year or no fixed term.
Non-price incentives	Low number of offers available with low level of difference. Options included: • GreenPower; and • Rates fixed until 31 December 2016.
Solar feed-in tariff	Low level of difference. All offers suitable for customers with solar panels.[346]

Small businesses can also access a number of other regulated tariffs, such as irrigation time of use tariffs and demand tariffs for different voltages.

346 Information on solar arrangements is provided in Appendix D.

Gas market offers

For gas, there are two retailers offering two residential gas plans and two small business gas plans.

There are only small differences in the tariff levels offered by each retailer and no difference in tariff structure, discounting or other incentives. Unlike most mainland gas companies, the two gas retailers operating in Tasmania currently do not have peak and off-peak pricing policies.[347]

10.6 Customer outcomes

Effective competition is characterised by how well the process of markets promote the long term interests of customers, including satisfaction with the level of choice available, the quality of service and the value for money provided by retailers.

As full retail competition was not in place for most small customers at the time of our research for this review, we did not commission Newgate Research to investigate customer outcomes in Tasmania. However, as an indicator, we looked at trends in complaints made to the Energy Ombudsman Tasmania.[348]

The level of electricity complaints to the Ombudsman appears to have decreased last year based on the number of issues raised (see Figure 10.1), noting that when a customer makes a complaint, multiple issues may be raised.[349] The number of issues raised increased between 2008-09 and 2011-12.

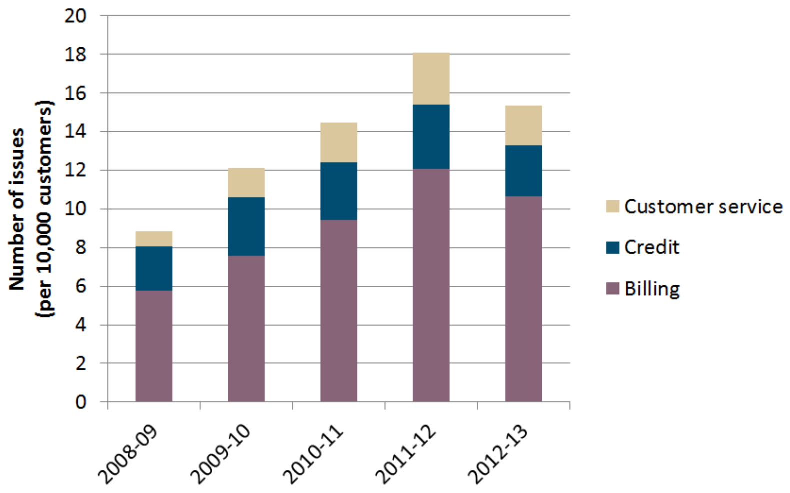
---

347 OTTER, Energy in Tasmania – Performance Report 2011-12, January 2013, p269.

348 Data is unavailable for the number of complaints made to retailers. The AER informed the AEMC that Aurora Energy did not provide complaint data on the same basis as other retailers and its inclusion would considerably understate the number of complaints. For this reason, it was excluded from AER publications and from this review. We therefore rely on data relating to complaints made to the Energy Ombudsman Tasmania.

349 Unlike complaints to the Ombudsman for other jurisdictions, this data excludes some cases where the customer has not first contacted their retailer and is referred to do so. It may also exclude some credit cases where customers are referred onto third parties such as a retailer's hardship program or a welfare agency. Some network issues may also be included. Similarly to in other jurisdictions, this data excludes cases which are out of jurisdiction or are not complaints.

Figure 10.1 Electricity complaints to the Ombudsman – number of issues raised



Source: Complaints data from the Energy Ombudsman Tasmania, customer numbers from AER Retail Statistics[350], AEMC analysis.

Billing was the most common issue raised since 2008-09, making up 69 per cent of electricity issues raised with the Ombudsman in 2012-13.

Despite electricity price increases in Tasmania in recent years, billing issues decreased between 2011-12 and 2012-13. The Energy Ombudsman Tasmania suggested this may be because of "a widespread acceptance within the community that utility costs are generally on the rise" which means fewer customers assume there has been an error when they receive a high bill.[351]

The Ombudsman also noted that there was a drop in complaints relating to disconnection (a credit issue), reflecting Aurora's hardship provisions under the newly introduced NECF.[352]

Unlike in other NEM jurisdictions, there are no complaints relating to marketing or transfer issues. This is consistent with there being a single electricity retailer for small customers and therefore limited or no marketing and no transfers between retailers.

There have been very few gas complaints to the Energy Ombudsman Tasmania. The Commission understands that gas complaints are very low due to the small size of the residential market and to retailers working to resolve complaints in house before they are escalated to the Ombudsman.

350 http://www.aer.gov.au/Industry-information/industry-statistics/retail

351 Energy Ombudsman Tasmania, Annual Report 2012-2013, p6.

352 Ibid.

10.7 Retailer outcomes

Profit margins can provide an indication of the level of competition in a market. However, they can also be expected to fluctuate over time. Consequently it is important to carry out analysis of retailer margins over a sufficiently long time period. It is also important to consider the results of such analysis in the context of other competitive indicators. While retail margins have not been estimated for the purpose of this review, we make a number of observations on retailer outcomes drawing from retailer interviews and pricing determinations by the jurisdictional regulator.

Retailers interviewed for this review considered that the Tasmanian retail electricity market is not very profitable. Reasons offered for this low rating included:

- higher risks associated with retailing in the Tasmanian electricity market because of the wholesale market arrangements; and
- the smaller customer base across which a retailer's costs can be spread.

This view is consistent with the broader view amongst some retailers that it would be difficult to compete effectively in the Tasmanian electricity market, as discussed in section 10.4.1 above.

Despite this, some retailers viewed OTTER's decision on standing offer prices as positive. Key elements of this decision include an allowance for customer acquisition and retention costs and a retail margin of 5.7 per cent following the commencement of full retail competition.[353] OTTER did not include an allowance for headroom as it considered that the regulated wholesale arrangements, combined with the allowance for customer acquisition and retention costs, were sufficient to encourage competition.[354]

Unlike electricity, the retail gas price in Tasmania is not regulated. Limited information is available on the profitability of the retail gas market. However, as discussed in section 10.4.2 above, we note that the ongoing viability of the gas market is linked to large industrial customers. Consequently the perceived risk of entering this market may be high.

10.8 Future developments affecting competition in the market

The Tasmanian electricity market is undergoing a period of change with the introduction of full retail competition for all customers from 1 July 2014. The completion of this final tranche of full retail competition is a good step towards promoting competition in the electricity market. However, based on the interview and

353 Between 1 January and 30 June 2014 the retail margin was set at 4.85 per cent to reflect the fact that there were lower volume risks associated with customer transfers, which were not permitted until 1 July 2014.

354 OTTER, *Report on the investigation of maximum prices for interim price-regulated electricity retail services for small customers on mainland Tasmania*, July 2013, pXVII.

survey responses by retailers to this review, the outlook for competition is unclear at this stage.

One small second tier retailer indicated it may consider entering the small business segment and another may consider entering the residential segment over the next five years. Neither retailer has firm plans to do so. Smaller retailers consider there to be risks associated with entry, primarily around the wholesale supply arrangements and the size of the customer base.

Larger retailers stated that they did not have plans to enter the Tasmanian retail market, with one claiming it would be 'more attractive to expand on the mainland than to enter the Tasmanian retail market'.

Retailers have mixed views on the Tasmanian Government's proposed approach to help retailers manage wholesale supply risk by regulating the price of four safety net contract products and ensuring there are adequate volumes of these products available. However, the majority of retailers viewed the wholesale arrangements as unfavourable.

If new retailers enter the electricity market, it will be important to increase customer awareness of their ability to choose between retailers and plans. At the same time, customers could be informed of the tools and information that is available to them to support their choice. The AEMC's consumer engagement blueprint developed for the New South Wales retail competition review could be used as a basis to inform and engage customers in Tasmania as the level of choice in the market increases.

The outlook for the retail gas market is also somewhat uncertain, particularly due to the very low penetration of gas distribution pipelines. One retailer suggested the market could shrink if any existing large industrial customers leave the market. No retailers appear to be considering entry into the gas market in the short term. It is possible that entry into the electricity market may drive entry into gas through dual fuel product offerings, but the likelihood is low due to low penetration rates and low total demand.

A Abbreviations

ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ACAT	ACT Civil and Administrative Tribunal
ACT	Australian Capital Territory
AEMA	Australian Energy Market Agreement
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
AFMA	Australian Financial Markets Association
ASX	Australian Securities Exchange
BREE	Bureau of Resources and Energy Economics
Commission	See AEMC
DWGM	Declared Wholesale Gas Market
ERAA	Energy Retailers Association of Australia
ESAA	Energy Supply Association of Australia
ESC	Essential Services Commission
ESCOSA	Essential Services Commission of South Australia
ESV	Energy Safety Victoria
EWON	Electricity and Water Ombudsman of NSW
EWOSA	Electricity and Water Ombudsman of South Australia
EWOQ	Electricity and Water Ombudsman of Queensland
EWOV	Electricity and Water Ombudsman of Victoria
FiT	Feed-in-Tariff
HHI	Herfindahl-Hirschman Index

ICRC	Independent Competition and regulatory Commission
IPART	Independent Pricing and Regulatory Tribunal
IT	Information Technology
kWh	kilowatt hours
LNG	liquefied natural gas
LPG	liquefied petroleum gas
MAPS	Moomba to Adelaide Pipeline System
MCE	Ministerial Council on Energy
MWh	Megawatt hours
NECF	National Electricity Customer Framework
NEM	national electricity market
NERA	NERA Consulting
NSLP	net system load profile
NSW	New South Wales
OTC	over-the-counter
OTTER	Office of the Tasmanian Economic Regulator
PAYG	Pay As You Go
PIAC	Public Interest Advocacy Centre
QCA	Queensland Competition Authority
QCOSS	Queensland Council of Social Services
Sapere	Sapere Research Group
SCER	Standing Council on Energy and Resources
STTM	Short Term Trading Market
TOU	Time of Use
UTP	Uniform Tariff Policy
VTS	Victorian Transmission System

B Concessions and hardship

Community Service Obligation payments (CSOs) are created by jurisdictional governments and the Commonwealth Government to assist customers to meet their energy needs and costs. Typically, a CSO might involve either subsidising the retailer to provide non-commercial services or concessions on energy bills for a customer that meets certain eligibility requirements. The range and level of CSOs is determined by each government and accounts for government spending as part of a broader range of concession programs.[355]

CSOs can be delivered to customers in a number of different ways. They can either be provided directly to customers as a rebate, through their retailer as a discount to their energy bill, or sometimes through community welfare organisations in the form of emergency payments. Table A.1 outlines NEM jurisdictional government and Commonwealth Government concession schemes and includes information regarding eligibility requirements and the level or amount of concession.

With the exception of Victoria, most energy-related concession schemes are paid as a lump sum, irrespective of consumption levels. In Victoria, energy concession schemes are provided as a percentage discount of the total energy bill.

Eligibility for most state, territory and Commonwealth energy CSOs is determined according to whether the customer is eligible for a variety of Commonwealth concession cards. Concession cards commonly used to determine CSO eligibility include the Department of Human Services (DHS) Pensioner Concession Card (PCC), the Department of Veterans' Affairs (DVA) PCC, the Health Care Card (HCC) and the DVA Gold Card.

Eligibility to hold concession cards is typically tested through a combination of income and asset tests (‘means tested’). DHS PCCs, for example, are available to a core group of government welfare recipients including job seekers, single parents and carers, age pensioners, and disability pensioners.

355 It should be noted that in Australia there is currently no operational definition employed by governments to define vulnerable consumers. The National Energy Customer Framework does not define vulnerable consumer, although it provides a regulatory process for retailers to implement hardship programs for customers experiencing either temporary or more permanent difficulties in meeting energy payments.

Table B.1 Commonwealth and NEM jurisdictional energy concession schemes

Jurisdiction	Concession	Eligibility	Calculation	Concession
Queensland	Electricity Rebate	Eligible customers hold a PCC, a DVA Gold Card (and receive the War Widow/er Pension or special rate TPI pension) or a Queensland Seniors Card. There are additional requirements on living arrangements.		**$282.54 per year**
Queensland	Reticulated Natural Gas Rebate	Eligible customers hold a PCC, a DVA Gold Card (and receive the War Widow/er Pension or special rate TPI pension) or a Queensland Seniors Card. There are additional requirements on living arrangements.		**$65.58 per year**
Queensland	Medical Cooling and Heating Electricity Concession Scheme	Eligible customers have a qualifying medical condition requiring cooling or heating and hold a PCC or a HCC.		**$282.54 per year**
Queensland	Home Energy Emergency Assistance Scheme	Eligible customers must have a concession card, be part of their energy retailer's hardship program or payment plan or have an income less than the Commonwealth Government's maximum income rate for part-age pensioners.	Scheme can provide up to $720 in any 12 month period for a maximum of two consecutive years.	**$720 per year**
Queensland	Electricity Life Support Concession Scheme	Eligible customers receive an oxygen concentrator or kidney dialysis machine free of charge from Queensland Health and hold a PCC, an HCC, a Health Care Interim Voucher, a Child Disability Allowance or a	Scheme offers a monthly concession (paid quarterly).	**Range: $32.11 - $47.95 per month**

Jurisdiction	Concession	Eligibility	Calculation	Concession
		Queensland Seniors Card.		
New South Wales	Low Income Household Rebate	Eligible customers hold a DHS PCC, a DVA PCC, an HCC or a DVA Gold Card marked with Totally and Permanently Incapacitated, Disability Pension or War Widow/er Pension.	$235 per year as of July 2014, rate was $225 per year for 2013-14. The rebate is 10 per cent higher for customers in retirement villages or caravan homes.	**$235 per year**
New South Wales	Family Energy Rebate	Eligible customers receive the Federal Government's Family Tax Benefit A or B.	$150 per year as of July 2014, rate was $125 per year for 2013-14. Those customers eligible for the Low Income Household Rebate as well as the Family Energy Rebate have their combined rebates capped at $250 per year. The rebate is 10 per cent higher for customers in retirement villages or caravan homes.	**$150 per year**
New South Wales	Medical Energy Rebate	Eligible customers cannot self-regulate body temperature and hold a DHS PCC, a DVA PCC, a DVA Gold Card or an HCC.	$235 per year as of July 2014, rate was $225 per year for 2013-14. The rebate is 10 per cent higher for customers in caravan homes.	**$235 per year**
New South Wales	Life Support Rebate	Eligible customers use certain approved medical equipment at home that is necessary to sustain life.	Amount payable depends on equipment type.	**Range: $0.05 - $1.66 per day**

Jurisdiction	Concession	Eligibility	Calculation	Concession
New South Wales	Energy Accounts Payment Assistance Scheme	Households struggling to pay their energy bills due to a crisis or emergency situation.	Scheme delivered through vouchers that provide part-payment of electricity and natural gas bills. Community Welfare Organisation assesses situation for eligibility for vouchers.	**$50 voucher**
Australian Capital Territory	Energy Concession	Eligible customers hold a DHS PCC, a DVA PCC or a Low Income HCC.	Calculated on a daily basis with separate summer and winter rates.	**$322.10 per year**
Australian Capital Territory	Utility Concession	Eligible customers hold a DHS PCC, a DVA PCC or a Low Income HCC.	Rebate added to existing energy concession.	**$84.05 per year**
Victoria	Annual Electricity Concession	Eligible customers hold a PCC, an HCC or a DVA Gold Card.	Discount of 17.5 per cent off household electricity costs over $171.60, all year round. If annual electricity cost is larger than $2,763 per year, an Excess Electricity Concession application must be made.	**17.5 per cent discount off electricity costs over $171.60**
Victoria	Winter Gas Concession	Eligible customers hold a PCC, an HCC or a DVA Gold Card.	Discount of 17.5 per cent off winter gas bills over $62.40, after any retailer discounts have been applied. If winter gas bills are more than $1,462, an Excess Gas Concession application must be made.	**17.5 per cent discount on winter gas bills over $62.40**

Jurisdiction	Concession	Eligibility	Calculation	Concession
Victoria	Service to Property Charge Concession	Eligible customers hold a PCC, an HCC or a DVA Gold Card. They have very low electricity usage - their electricity usage charge is less than the service charge.	If the electricity usage cost is less than the supply charge, the service charge is reduced to the same price as the electricity usage cost.	**The service charge is reduced to the same price as the electricity usage cost.**
Victoria	Non-mains Energy Concession	Eligible customers hold a PCC, an HCC or a DVA Gold Card. They rely on LPG, firewood or heating oil for domestic heating, cooking or hot water, access non-mains electricity via an embedded network or rely on a generator.	The amount of the rebate depends on the annual amount of non-mains energy purchased.	**Range: $44 - $484**
Victoria	Medical Cooling Concession	Eligible customers have a medical condition that affects the body's ability to regulate temperature and hold a PCC, an HCC or a DVA Gold Card.		**17.5 per cent of summer electricity costs**
Victoria	Controlled Load Electricity Concession	Eligible customers are charged a controlled load tariff for separately metered electric hot water or slab heating and hold a PCC, an HCC or a DVA Gold Card. Customers must have a dual element electricity meter or dual element smart meter.	Provides a 13 per cent reduction on the controlled load usage charges throughout the year.	**13 per cent off controlled load usage charges**
Victoria	Electricity Transfer Fee Waiver	Eligible customers hold a PCC, an HCC or a DVA Gold Card.	Full waiver of the fee that is normally payable to the electricity retailers when there is a change of occupancy at a property.	**Removal of transfer fee**
Victoria	Life Support Concession	Eligible customers use an eligible life support machine and hold a PCC, an HCC	Discount equals cost of 1,880 kWh of electricity used	**Full cost of 1,880 kWh per year.**

Jurisdiction	Concession	Eligibility	Calculation	Concession
		or a DVA Gold Card. Qualifying machines use at least 1,880 kWh per annum.	each year, based on the general domestic tariff of the customer's retailer.	
South Australia	Energy Bill Concession	Eligible customers receive an eligible Centrelink payment or hold a PCC, a DVA Gold Card marked with Totally and Permanently Incapacitated, Extreme Disablement Adjustment or War Widow, a Low Income HCC, a Commonwealth Seniors HCC or a State Concession Card.	Concession deducted from electricity account or in some cases reimbursed by cheque.	**Up to $215 per year**
South Australia	Medical Heating and Cooling Concession	In addition to the Energy Bill Concession requirements, eligible customers have a clinically verified medical condition which requires the frequent use of heating or cooling in the home.		**$215 per year**
Tasmania	Electricity Concession	Eligible customers hold a PCC, an HCC, an ImmiCard (Bridging Visa E) or a Tasmanian Concession Card.	125.71 c daily rate	**$458.84 per year**
Tasmania	Heating Allowance	Eligible customers hold a PCC and must not have more than $1,750 in cash assets or $2,750 for married/de facto partners.	Payments of $28 made in May and September	**$56 per year**
Tasmania	Life Support Machine Rebate	Eligible customers use an approved life support system.	Daily discount rate depends on the life support system, ranging from 5 to 176 c per day.	**Range: 5 – 176 c per day**
Tasmania	Medical Cooling Discount	Eligible customers have a medical condition that requires the cooling of their residence.	37.653 c daily rate	**$137.43 per year**

Jurisdiction	Concession	Eligibility	Calculation	Concession
Commonwealth	Utilities Allowance	Eligible customers receive the Disability Support Pension, the Partner Allowance or the Widow Allowance.	Paid quarterly, A couple where both members are eligible, receives the same allowance as a single customer ($588.40), combined.	**$588.40 per year**
Commonwealth	Essential Medical Equipment Payment	Eligible customers medically require specific equipment or heating/cooling and hold a Commonwealth concession card issued by the DHS or by the DVA.	$143 per year to help with increases in home energy costs from the carbon price.	**$143 per year**

C Summary of submissions to the AEMC's Approach Paper

Market definition

Stakeholder	Issue	AEMC response
AGL	AGL agrees with the Commission’s definition of separate product markets for gas and electricity retailing, however we consider that the geographic scope of the markets should be broader than State-wide. AGL considers that narrowing the definition of the market in the way that the Commission proposes would have any impact on the overall outcome of the Commission’s analysis, which AGL considers should be a finding that retail competition is effective in the NEM States in which AGL retails energy. (p1)	Noted. The AEMC has retained the definition of a market as outlined in the Approach Paper. This is addressed in section 2.2 of this report.
Alinta Energy	Believes that the market definitions proposed are appropriate and reflect accurately the markets to which the review relates. (p3)	As above.
COTA Queensland	Supports the proposal to treat South East Queensland as a separate geographic market to the rest of Queensland for this review and would like to see this distinction removed over time. (p1)	As above.
Envestra	The AEMC should, at a minimum, differentiate between metropolitan and regional areas in its review. Individual regional markets should be separately identified, particularly for the initial retail reviews, to determine whether any issues exist within a particular jurisdiction. (p3)	As above. However, we have specifically considered the extent to which there are differences between urban and regional areas within jurisdictions.
Origin	In the specific context of the Terms of Reference provided to the AEMC to assess competition in retail energy services, Origin supports the AEMC considering each NEM jurisdiction as a single geographic market with electricity and gas representing separate product markets, with the exception of Queensland where the Energex and Ergon regions should be considered separately. (p1)	As above.
Public Interest	Recommends that the AEMC examine competition in a variety of rural and	As above.

Stakeholder	Issue	AEMC response
Advocacy Centre (PIAC)	regional areas and analyse difference between these areas, as well as comparing competition to that in major cities. (p4)	
SACOSS	Supports the separate consideration of electricity and gas but is strongly of the view that the extent of vertical integration in the South Australian electricity market means that consideration of 'retail' in isolation from 'generation' is problematic. (p3)	As above. We have also considered the extent to which non-vertically integrated generators can access hedges to manage spot price risk.

Customer activity in the market

Stakeholder	Issue	AEMC response
ActewAGL	Awareness of market choice has increased since the AEMC's review of the ACT market. (p2)	A significant proportion of customers in the ACT are unaware they have a choice of retailer or plan. This is further discussed in section 7.3.1 of this report.
ActewAGL	Although switching behaviour in the ACT is not high, this is likely due to ActewAGL regularly delivering the highest levels of customer satisfaction of all electricity and gas retailers. (p2)	Noted. The level of customer switching in the ACT is discussed in section 7.3.2 of this report. Customer satisfaction in the ACT is discussed in section 7.6.
AGL	Being able to provide customers with useful, high quality information is a form of product innovation and product differentiation that is being increasingly embraced by energy retailers. (pp1-2)	The Commission considers that product differentiation is occurring within limits. Product differentiation is further discussed in section 3.2.3 of this report and in individual jurisdictional chapters.
AGL	Customers are generally influenced by a range of factors when choosing to switch from a regulated contract to a market offer contract, or to a product offered by a different energy retailer. These include factors such as price, convenience, and an ability to	Triggers for, and barriers to, customer switching are discussed in section 3.2.1 and in individual jurisdictional chapters.

Stakeholder	Issue	AEMC response
	reduce their overall energy consumption. (p2)	
AGL	Some customers make the choice to remain on a regulated contract because after assessing their personal circumstances, conclude that it is the most suitable option for them. Less price sensitive customers may choose to remain on a regulated offer if they consider the search and switching costs associated with moving to a market offer to exceed the financial benefits of switching. (p2)	As above.
AGL	There are no significant barriers that prevent customers from switching energy plans within their current retailer, or across different retailers. (p2)	Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
Alinta Energy	In terms of consumers ease of understanding, retailers have prescribed obligations on the way in which they communicate product information to consumers. It can be argued that some of these obligations placed on retailers inhibit a consumers ease of understanding thereby impacting their ability to make accurate comparisons. However an engaged consumer has access to all the required information with which to make an informed decision. (p3)	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is further discussed in section 3.2.1.
Alinta Energy	In addition to other triggers for consumers to move retailer, which will often result in a transfer from a standing offer to a market offer, are experiences of poor customer service, or the proposition of potential benefits directly marketed to the consumer. Often it is the presentation of available options direct to the consumer that creates the catalyst for considering the option to switch energy retailers. (p3)	Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
Alinta Energy	Apart from exit fees for some market contracts, barriers preventing consumers from switching energy plans within their current retailer or an energy plan offered by an alternative retailer would be considered to be low. (p4)	As above.
Consumer Action Law Centre (CALC)	The AEMC should also consider the accessibility and reliability of energy related information that is easy to understand. Such information is a necessary pre-requisite to any decision to change provider. Private as well as government run information sites/comparators can assist consumers with information as to deals available. Analysis	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is

Stakeholder	Issue	AEMC response
	needs to consider the extent that these sorts of tools are used by consumers, and whether it assists with their decision making and provides reliable information. (p3)	further discussed in section 3.2.1. As part of the customer research, customers were asked whether they were aware of comparator websites, about their confidence in understanding the information available and their satisfaction with the switching process. See individual jurisdictional chapters for results.
COTA Queensland	The majority of constituents do not understand the operation of the electricity and gas markets, or the roles of the various participants in the market. While some constituents do have the necessary skills and resources to seek out energy offers, they do not find the information easy to understand. The majority are not aware of the existence of any sources of reliable information about energy offers. There is no trusted ‘one-stop-shop’ where this information can be accessed in a face-to-face mode. (pp1-2)	As above.
COTA Queensland	There are a number of barriers to switching in Queensland: • lack of understanding that a competitive market exists; • difficulty in sourcing credible information about options for switching; • lack of trust in retailers, and a concern that they will finish up in a worse position due to misunderstanding/misrepresentation of the contract conditions; • for those with a solar PV installation, there is a concern that by switching retailer, they will lose access to the higher solar feed-in tariff. (p2)	Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
EnergyAustralia	Notes that in jurisdictions where the National Energy Customer Framework (NECF) is yet to be applied (Victoria and Queensland) that customers cannot access Energy Made Energy and that less sophisticated price comparators are run by local regulators. (p2)	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is further discussed in section 3.2.1.

Stakeholder	Issue	AEMC response
EnergyAustralia	Customers are motivated to take up market offers based on a range of factors including discounts, green power, solar feed in tariffs, acquisition incentives, dual fuel and payment channels. However, energy is a relatively low interest product or “grudge purchase” for most consumers and therefore a proportion of customers are reluctant to, and maybe will never, accept or seek a market offer. (p2)	Noted. Customer activity is discussed in section 3.2.1.
EnergyAustralia	Various marketing initiatives can influence consumers to switch retailer, such as: • online marketing initiatives; • third party comparator and sales channels; • independent website comparators; • above the line advertising; • direct marketing; and • door to door sales	Noted. This is consistent with the findings of the study carried out by Newgate Research for this report - *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014. See section 3.2.1 for more information.
EnergyAustralia	In our view there are no barriers preventing customers from switching retailers or switching plans with their existing retailer. (p3)	Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
Ethnic Communities' Council of NSW	Most small customers have great difficulty accessing information they can understand particularly those newly arrived migrants, refugees and older migrants. The small to medium sized business owners and managers are too busy to try to find the information. It is usually the marketers from the retailers who either call or visit these small customers that provide the information in the form of a verbal sales pitch followed by a detailed contract. (p2)	Noted. The AEMC's consumer engagement blueprint, developed for the NSW retail review in 2013, provided detailed recommendations on how many customer segments could be provided with support to choose an energy plan that suits their needs.
Ethnic	The greatest factor encouraging customers to switch energy retailers is reducing energy	Agreed. This is consistent with the findings of the

Stakeholder	Issue	AEMC response
Communities' Council of NSW	costs. (p2)	study carried out by Newgate Research for this report, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014.See section 3.2.1 for more information.
Ethnic Communities' Council of NSW	The greatest barrier to switching is the lack of information provided to customers. The government has provided websites where they enter data and find the best offer for their circumstances and translated material on how to use the site but many of the older migrants do not have access or do not use the internet. (p2)	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is further discussed in section 3.2.1.
Origin	Considers that customers are motivated to move to a market contract foremost by savings available from a cheaper offer. Other considerations include non-price benefits attached to market offers and the opportunity to secure green energy offers. (p3)	This is consistent with the findings of the study carried out by Newgate Research for this report, *Consumer Research for Nationwide Review of Competition in Retail Energy Markets*, report for the AEMC, June 2014. The majority of consumers surveyed changed retailer primarily to obtain a better price. See section 3.2.1 for more information.
Origin	Consider that customers may remain on a standing or regulated offer because they are satisfied with the price and level of service they currently receive, because their energy bill makes up only a small portion of their overall expenditure, because energy is a very low involvement product, or because they do not believe that the savings available are worth the time required to investigate other offers. (p3)	Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
SACOSS	The adoption of the National Energy Customer Framework (NECF) from February 2013 led to the launch of Energy Made Easy for SA. While generally welcomed, this was not a significant advance on the ESCOSA price comparison service available for many years before that date. (p4)	Noted.
SACOSS	SACOSS notes that access to comparison information relies heavily on access to the internet. This presents challenges for lower income households and the elderly. The	The AEMC's consumer engagement blueprint, developed for the NSW retail review in 2013,

Stakeholder	Issue	AEMC response
	Australian Bureau of Statistics (ABS) publishes data on household and personal Internet Access and Usage in 8146.0 – Household Use of Information Technology, 2012-13. According to the ABS, 17% of households do not have internet access. (p4)	recommends ways to support consumers that may not be captured by mass marketing or that may require additional support to choose a plan that suits their needs, including those that do not have access to, or do not feel confident using, the internet.
SACOSS	With regards to the reasons behind why some small customers remain on standing offers, internet access is almost a necessity to pursue an informed choice. Also, literacy, numeracy and confidence can be substantial barriers. For many though, the 'search costs' do not outweigh the perceptions of the savings on offer. (p7)	See above. Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
SACOSS	The accumulation of debt with a retailer can inhibit switching. (p7)	Noted. Section 3.2.1 refers to the barriers to customer switching and suggests that there are a broad range of factors which deter customers from switching.
Queensland Council of Social Service (QCOSS)	Regulation of energy market information should be improved to ensure that consumers have access to accurate, reliable and comparable information when making decisions about energy offers. (p4)	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is further discussed in section 3.2.1.
QCOSS	Initiatives to increase consumer engagement should include funding of targeted programs to improve knowledge about energy markets and provide independent advice to vulnerable consumers. (p4)	The AEMC's 2013 *Review of Competition in the Retail Electricity and Natural Gas Markets in NSW* recommended that, in order for consumers to engage in the market, consumers should be empowered so that they are confident that they have the right information and support to choose an energy plan that suits their needs. AEMC, *Empowering Consumers: A Blueprint for informing and empowering small consumers in NSW Energy Markets*, 2013, p3. See section

Stakeholder	Issue	AEMC response
		3.2.2 for more information.
QCOSS	A demonstrable improvement in customer engagement and the quality of information available about energy offers should be shown before the Queensland Government removes electricity price regulation in South East Queensland. (p4)	See above. We note that one of the Queensland Government's conditions for removing price regulation is improving customer engagement in the market.
QCOSS	Issues identified in Queensland include: • low levels of consumer knowledge and engagement in the market; • a lack of reliable, non-internet based sources of independent information and advice; • reliance on the information provided by marketers; • deficiencies in the Queensland Competition Authority's price comparator website; • issues with the quality and comparability of information provided by energy retailers; and • issues with impaired capacity faced by some vulnerable consumers. (p6)	Evidence suggests that a considerable proportion of the South East Queensland market are investigating their options and switching plans or retailers. Section 4.3.2 discusses customer activity in the energy market in South East Queensland. The AEMC's consumer engagement blueprint recommended a number of ways to reach different customer segments and provide them with support to choose an energy plan that suits their needs.
QCOSS	Poor understanding of the market, as discussed above, is a barrier to switching for some customers as well as leading others to make poor decisions. Issues that affect people’s access to and capacity to comprehend information, such as poor literacy, language barriers, mental health issues or psychological stress related to hardship, can also prevent customers from switching. (p12)	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is further discussed in section 3.2.1. The AEMC's consumer engagement blueprint recommended a number of ways to reach different customer segments and provide them with support to choose an energy plan that suits their needs.

Barriers to entry, exit or expansion

Stakeholder	Issue	AEMC response
AGL	Barriers to entry and expansion in electricity retailing are low. (p4)	Entry has occurred in most jurisdictions but some impediments remain to varying degrees across jurisdictions. See section 3.2.3 for more information.
AGL	The existence of retail price regulation stifles the incentive for retailers to roll out smart meters, which in turn limits the extent to which time of use tariffs can be offered. (p6)	Noted.
ActewAGL	There are low barriers to entry and expansion in the ACT and NSW residential market. (p1)	With regards to the ACT, retailers interviewed were of the view that entry into the electricity and gas retail market is difficult and expansion is reportedly even more difficult. The two commonly cited issues were ActewAGL's dominance and the relatively small size of the market. See Chapter 7 for more information. In NSW, retailers consider entry and exit relatively easy. Expansion was considered to be more difficult, primarily due to retail price regulation in both markets, as well as upstream issues in the gas market. See Chapter 6 for more discussion.
Alinta Energy	Regulatory burden and uncertainty, retail price regulation and credit support requirements are barriers to entry, exit and expansion. Credit support impacts expansion as when a retailer enters a market the levels of credit support required increases significantly, for an organisation without an acceptable credit rating generally the only form of acceptable support is a secured bank guarantee. Institutions that require credit support from retailers are generally reluctant to explore differing commercial arrangements for meeting credit support requirements. (p4)	Entry has occurred in most jurisdictions but some impediments remain to varying degrees across jurisdictions. See section 3.2.3 for more information.
CALC	We note the recent, apparent strategic exit of Australian Power and Gas (APG) from the Victorian market (it was subsequently acquired by AGL). Not only did this exit contribute	In a competitive market retailers can be expected to enter and exit over time as market

Stakeholder	Issue	AEMC response
	to further market concentration, it perhaps highlights a failure of competition producing durable consumer benefits. The customers of APG, who have, via a range of means, attempted to engage in the market, have likely ended up with an incumbent retailer, back at the price they originally paid, or more. (p5)	conditions change. Our research found that price is the main reason why customers switch. If customers find themselves on a higher price they may be motivated to shop around. As discussed in section 6.3, almost 40% of Victorian customers reported actively investigating offers or options in the past 12 months and 28% changed their retailer.
EnergyAustralia	The risk associated with regulated pricing poses potential a barrier to entry. In jurisdictions where prices are regulated, there is no guarantee that prices will be set at a level which enables market participants to recoup costs from one year to the next. (p4)	The Commission notes that retail price regulation poses a potential barrier to entry. See section 3.2.3 for more information.
Envestra	There are relatively low levels of retail competition in the smaller regional gas markets. Considers that this reflects a reluctance by retailers to supply these markets due to the high costs/risks relative to potential benefits. Is of the view that significant expenditure would need to be incurred by retailers on marketing in order to attract new customers, especially for a new retailer that is not active in the relevant gas sales market and needed to develop a brand presence to attract new retailers. (p5)	Noted. Section 3.2.4 discusses some of the barriers to entering gas retail markets.
Ergon Energy	Agrees that some barriers to competition may remain should the current UTP arrangements be removed or amended. With that being said, in advance of future uniform tariff policy arrangements being defined, it is difficult to speculate what barriers will remain. (p9)	Noted. Section 5.4.1 discusses what some of these barriers may be.
Origin	Origin supports the measures the AEMC has proposed to measure barriers to entry in the electricity and gas markets, highlighting also that uncertainty regarding future outcomes under price regulation can stifle the development of competition and has in the past been a barrier to entry in NEM markets. (p2)	Noted. The Commission notes that retail price regulation poses a potential barrier to entry. See section 3.2.3 for more information.
Origin	There are no barriers to entry, exit or expansion from the electricity or gas market, as the AEMC found in NSW. There are a large number of second tier retailers active in the four major NEM markets. The exceptions are the ACT, where regulated prices are not cost reflective, Tasmania where the Government's wholesale purchasing arrangements	Entry has occurred in most jurisdictions but some impediments remain to varying degrees across jurisdictions. See section 3.2.3 for more

Stakeholder	Issue	AEMC response
	constrain competition, and regional Queensland where subsidy arrangements preclude effective competition. (p4)	information.
PIAC	Recommends that the AEMC undertake analysis to determine the optimum number of suppliers in the retail energy market. (p6)	In a competitive market, retailers can be expected to enter and exit over time as market conditions change and innovations occur. Consequently the number of retailers in a market can be expected to change over time.
PIAC	PIAC believes low profit margins should not be considered as a barrier to entry but rather as an outcome of competition, bringing the price closer to the level of efficient costs. (p5)	Profit margins can be expected to fluctuate over time as market conditions change. Further, this indicator cannot be considered in isolation. Rather, it is one of a number of indicators that together determine the state of competition.
SACOSS	SACOSS is of the view that the dominant retail market barriers actually reside in the wholesale market. (p7)	Entry has occurred in most jurisdictions but some impediments remain to varying degrees across jurisdictions. See section 3.2.3 for more information and section 9.4 for a discussion of barriers to entry and expansion in the South Australian market.

Independent rivalry

Stakeholder	Issue	AEMC response
AGL	High levels of competition exist between gas and electricity retailers across all NEM States in which AGL retails, and retailers actively compete with each other to develop and market new products to existing and new customers and to grow their customer bases. (p5)	The state of competition varies across the NEM as retail markets have evolved at different rates. In electricity, competition has led to more choice of retailers and plans in Victoria, South Australia, New South Wales, and South East Queensland, but is yet to emerge in the ACT and Tasmania.

Stakeholder	Issue	AEMC response
		In gas competition has been more tempered as gas is a secondary consideration for most consumers and retailers. See Chapter 3 for further discussion on the overall state of competition in the NEM.
AGL	Retail price regulation of electricity and gas can impede the potential for tariff innovation, product differentiation and service competition where the prices being regulated are in a market in which effective competition exists, which is the case in South East Queensland and New South Wales. (p.5)	Noted.
ActewAGL	ActewAGL competes on price, bundling of energy and telecommunications services, and non-price terms through sponsorships, fundraising, events and philanthropy. (p2)	Noted.
ActewAGL	In the ACT and NSW there are 40 electricity and 16 gas retailers with AER authorisation. Retailers are competing in a variety of ways and delivering a range of competitive offers to customers. (p1)	Noted. However, while retailers may be authorised to retail energy, competition and so customer benefits will only arise where retailers enter the market. The Commission also notes that there is low availability of market offers in the ACT. See section 7.5 for discussion.
ActewAGL	Competition in the retail electricity and gas markets in the ACT and NSW is effective. (p1)	The Commission considers that competition in the ACT is not currently effective. See section 7.1 for further discussion. With regards to NSW, the Commission considers that competition is effective in the electricity and gas markets, although less so in certain regional areas for gas. See section 6.1 for more information.
Alinta Energy	A high level of competition exists, especially among second-tier and new entrant retailers. (p4)	The state of competition varies across the NEM as retail markets have evolved at different rates. In electricity, competition has led to more choice of retailers and plans in Victoria, South Australia, New South Wales, and South East Queensland,

Stakeholder	Issue	AEMC response
		but is yet to emerge in the ACT, Tasmania and regional Queensland. In gas competition has been more tempered as gas is a secondary consideration for most consumers and retailers. See Chapter 3 for more discussion on the overall state of competition in the NEM.
Alinta Energy	Retail price regulation impedes tariff innovation and the range of products and service offerings available to small customers. (p4)	Noted.
COTA Queensland	Until about 6 months ago, there were many complaints about the prevalence and aggressive behaviour of representatives of retailers using door-to-door sales techniques. These concerns appear to have abated in recent months, but have left behind a very poor impression and a lack of trust in retailers generally. There now appears to be a growth in telemarketing campaigns. (p2)	A common theme in the consumer research forums was "better the devil you know", signalling a high level of mistrust of energy retailers. Retailers appear to be starting to respond to customer mistrust - in 2013, AGL, EnergyAustralia and Origin Energy ceased using door-to-door sales techniques. See section 3.2.2 for more information.
Department of State Development, Business and Innovation Victoria (DSDBI)	Competition in the Victorian electricity retail sector is strong. There has been significant new entry and the market shares of incumbent retailers have declined. Further, switching rates are high. (pp2-3)	Agreed.
DSDBI Victoria	The removal of retail price regulation in Victoria has encouraged significant tariff and product innovation in Victorian retail markets. This has resulted in 'price dispersion' that is, the variation in prices of different tariffs. (pp3-4)	Agreed. The Commission considers that in Victoria, a high degree of product differentiation is occurring and innovation is emerging. Retailers are offering different tariff structures, discounts and a broad range of non-price incentives. See section 8.5.2 for further discussion on product differentiation in Victoria.

Stakeholder	Issue	AEMC response
DSDBI Victoria	DSDBI's preliminary analysis of customer-tariff matching on the Victorian Government's My Power Planner price comparator indicates: • the 'best tariff' shown to users who could save by switching is from a Tier 2 retailer in 99 per cent of cases; and • when the analysis broadened to consider the 'top 10' tariffs shown to website users, 96 per cent of offers are from Tier 2 retailers. (pp4-5)	Noted.
EnergyAustralia	There is a high degree of competitive rivalry in the Victorian, New South Wales, South Australian and (South East) Queensland markets, with strong price and non-price based competition between large and small energy retailers to win new customers and retain existing customers. (p4)	The state of competition varies across the NEM as retail markets have evolved at different rates. In electricity, competition has led to more choice of retailers and plans in Victoria, South Australia, New South Wales, and South East Queensland, but is yet to emerge in the ACT and Tasmania. In gas competition has been more tempered as gas is a secondary consideration for most consumers and retailers. See Chapter 3 for more discussion on the overall state of competition in the NEM.
EnergyAustralia	In general, a market with price regulation introduces a key regulatory risk to retailers. Even if regulated margins are reasonable in any one year, there is always the risk that a regulator may set the tariff too low in the next year. This risk alone will stifle innovation and investment even where margins are otherwise adequate. (p5)	Noted.
Envestra	Retailer participation/competition in gas retail markets is far stronger in metropolitan areas than in regional areas and is stronger in Victoria relative to other states. (p1)	Certain regional markets appear less competitive. See section 3.2.4 for discussion on the impediments to entry into gas retail markets.
Ergon Energy	In general, Ergon Energy regards competition in South East Queensland as reasonable, in spite of historical retail price regulation. (p9)	Agreed. Competition appears to be effective in the South East Queensland electricity market and is delivering benefits to customers through

Stakeholder	Issue	AEMC response
		choice of retailers and plans. While competition has been less intense in recent years, rivalry can be expected to increase once price regulation is removed. See Chapter 4 for more discussion on competition on South East Queensland.
Ethnic Communities' Council of NSW	Retailers are constantly using telemarketing to promote their product and compete for customers in the market. They are particularly active in areas of Sydney where there are large populations of newly arrived migrants. The retailers offer discounts to gain customers but do not explain the additional fees involved or what price the discount is related to. (p3)	Retailers appear to be starting to respond to customer mistrust - in 2013, AGL, EnergyAustralia and Origin Energy ceased using door-to-door sales techniques. Origin is no longer cold calling residential customers. See section 3.2.2 for more discussion on this point.
Ethnic Communities' Council of NSW	The majority of energy retailers have ceased marketing door-to-door. This practice was particularly confusing for some culturally and linguistically diverse community members, particularly the older and newly arrived migrants and refugees. Many of these customers believed that the marketers were from the government and that they did not have the freedom to reject the offer. (p3)	As above. The AEMC's consumer engagement blueprint recommended a number of ways to reach different customer segments and provide them with support to choose an energy plan that suits their needs.
Origin	Retailers actively compete for customers in all NEM jurisdictions except Tasmania, the ACT and regional Queensland. This is evident in high churn rates and the large numbers of customers on market contracts. Retailers have offered a range of price and non-price benefits to customers as well as flexible tariff packages where metering technology allows this. (p4)	Noted.
PIAC	Change over time (of offers of different products and services) will be an indicator of whether competition is effective. (p4)	Noted.
QCOSS	Considers that before removing price regulation in South East Queensland, the Queensland Government establishes a robust market monitoring framework including analysis of both price and non-price indicators, and empowering regulatory bodies with the authority and resources to proactively investigate and address issues to ensure the market is delivering in the best interests of consumers. (p4)	This is an issue for the Queensland Government to consider and is out of scope of this review.

Stakeholder	Issue	AEMC response
QCOSS	The date for removing price regulation in Queensland should not be earlier than 12 months after the implementation of NECF, in order to ensure that a more robust performance monitoring regime is in place that may provide customers with information and incentivise retailers to improve their performance. (pp4-5)	As above.

Customer satisfaction

Stakeholder	Issue	AEMC response
AGL	In a survey carried out on behalf of AGL, it was found that: • lower prices were the top factor for improving overall satisfaction, while better customer service was the second most important factor; • customers generally consider that they obtain a reasonable level of value for money from their energy retailers; and • the vast majority of customers across all States in which AGL retails are aware of their ability to switch retailers of gas and electricity. (p7)	This is broadly consistent with research conducted for this review. Section 3.2.1 discusses the drivers behind customer switching rates and the level of customer awareness. Section 3.2.2 discusses the level of customer satisfaction.
ActewAGL	ActewAGL has the lowest residential complaint rate of all retailers operating in NECF jurisdictions. (p2)	The Commission has found that more customers are very satisfied with their energy retailer in the ACT than other jurisdictions surveyed and the ACT has some of the lowest reported complaint numbers of the four jurisdictions that have adopted the National Energy Customer Framework. For many customers, high satisfaction appears to reflect an absence of reasons to contact their retailer. Fewer

Stakeholder	Issue	AEMC response
		customers are satisfied with the level of choice relative to other jurisdictions surveyed and would like greater competition in the market. See section 7.1 for further discussion.
CALC	Recent research found the average ability of customers to understand pricing offers had fallen steadily since 2004, as had the ease of comparing new offers to the customer's existing terms and conditions. This finding suggests that customer satisfaction and experience of the market has not improved with previous findings about the effectiveness of competition. (p7)	As part of the customer research that was conducted for this review, customers were asked about their confidence in understanding offers as well as other measures of satisfaction and experience of the market. Results are presented in individual jurisdictional chapters.
COTA Queensland	Some constituents face difficulties when a retailer insists that certain transactions can only be performed online. For example, one retailer would only pay out the solar bonus due to a customer if an application was submitted online. The transaction could not be completed over the phone. Call centre waiting times are a major concern for constituents who use pre-paid mobile phones as their primary mode of telecommunications. Customers are not satisfied with the speed with which they can switch retailers. (p3)	Noted. The AEMC as previously advised on ways to improve the switching process. See Box 3.2 for a summary of this advice.
EnergyAustralia	A number of the external factors which may have impacted complaint levels are: • increased media coverage and politicisation of energy industry issues; • increased customer awareness and accessibility of Ombudsman Schemes; • sustained price increases; and • significant industry upheaval in most jurisdictions (eg, price deregulation, NECF, smart meters, etc.). (p7)	Noted.
Ethnic Communities'	With regards to evidence of any long term jurisdictional or cross-jurisdictional trends in the number and nature of customer complaints to retailers or the ombudsman, unfortunately we do not ask the ethnicity of our callers and so the does not have	Noted.

Stakeholder	Issue	AEMC response
Council of NSW	statistics to report on culturally and linguistically diverse trends. It would be expected that these numbers are similar to the broader population, while remembering that more than 20 % of the population in Sydney and Melbourne speak a language other than English at home. (p3)	
IPART	Most customers in NSW who participate in the competitive market are experiencing positive outcomes. (p1)	See section 6.6 for discussion on customer satisfaction in NSW.
Origin	Origin supports the AEMC reviewing the incidence of complaints and carrying out customer surveys. However, we also concur with the AEMC's finding with respect to NSW that in markets where competition is effective customers will still encounter difficulties and need to raise complaints. The measure of an effectively competitive market is that these complaints are resolved. (p2)	Noted.
PIAC	Recommends that the AEMC compile and analyse customer complaint data across the NEM as part of its current review of the effectiveness of competition. Noted that there has been a sharp increase in retailer complaints in NSW between 2011/12 and 2012/13. If such figures continue, the capacity of the market to deliver benefits to consumers without stricter regulatory oversight may be called into question. Would suggest the competitive market is not exerting sufficient pressure on retailers to minimise customer complaints. (pp6-7)	Noted. We also note that complaints can be a sign that customers are starting to engage in the market, particularly as the market transitions from a monopoly provider to competition. Complaints can also prompt retailers to start competing on service quality.
Queensland Consumers Association	Major improvements are needed in the quality and quantity of information collected by public agencies, and publicised, on the quality of service provided by electricity and gas retailers. To facilitate increased consumer understanding of electricity prices and easier comparison of offers available, more use of consumer-friendly and meaningful units of measure to describe prices and less use of percentage discounts off base prices should be encouraged or required. (p2)	The Commission considers that knowledge of, and access to, a credible and easy to understand source of information can contribute to the likelihood of customer switching. This is further discussed in section 3.2.1. Careful thought needs to be given to when it may be appropriate to intervene in competitive markets to mandate marketing or pricing techniques. See section 8.7.5 for an example where intervention has led to unintended consequences.

Stakeholder	Issue	AEMC response
QCOSS	Recommends that current and future AEMC competition reviews include in-depth consultation with a diverse spread of customers across South East Queensland, and regional Queensland as competition develops in this area, to determine customers' experiences of retail competition. (p5)	Noted. Qualitative and quantitative research for this review included a representative sample of customers across South East Queensland. Research was not conducted in regional Queensland since there is only one retailer in the market and the research was to gain an understanding of how customers participate in the market.
QCOSS	Recommends that the Queensland Government incorporates into its price monitoring framework research into customer satisfaction with the range and type of offers available in the market. (p5)	This is an issue for the Queensland Government to consider and is out of scope of this review.

Retailer outcomes

Stakeholder	Issue	AEMC response
AGL	The operation of the regulated price as a 'price-cap' in the market means that if the regulated price does not adequately account for wholesale market fluctuations, then the ability of retailers to offer products and services will be compromised. The uncertainties associated with regulatory intervention, and in particular, the risk that future price resets will not be based on LRMC as floor methodology, significantly disincentivises tariff innovation by retailers, by increasing the risk that retailers will not be able to adequately cover their costs in the future. (p8)	Noted. The Commission considers that the benefits of price regulation need to be weighed against the costs. See AEMC 2013, *Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales*, Final Report, 3 October 2013, Sydney, section 7.2.1 for a discussion of this issue.
ActewAGL	The regulated price in the ACT is not fully cost reflective, but ActewAGL is able to offer discounts to customers that sign up online or pay bills on time. (p2)	Noted.
Alinta Energy	Energy retailers are unable to recover their efficient costs of operating in Queensland, NSW and the ACT where the regulated price does not accurately reflect retailer costs and risks of operating in these markets. (p5)	Noted. The Commission notes that retail price regulation poses a potential barrier to entry. However, we also note that there has been entry

Stakeholder	Issue	AEMC response
		in both NSW and Queensland while price regulation has been present.
Alinta Energy	In jurisdictions where price regulation exists it is our experience that competitive market costs have been depressed through the review of regulated retail prices. (p.5)	As above.
Alinta Energy	Operational market costs which are predominantly driven by the network businesses vary significantly, such as the cost of special meter reads, and contribute to inter-market divergence in retailer costs. (p5)	Noted.
CALC	We encourage the AEMC to undertake detailed analysis of profit margins of energy retailers and assess whether retail margins are covering efficient costs only. (p7)	See section 3.2.3 for discussion on retailer outcomes. In jurisdictions where prices are regulated, it is the role of the jurisdictional regulator to determine these factors for the purpose of calculating the regulated price. See section 8.7 for discussion on retailer outcomes in Victoria, which is the only jurisdiction to have deregulated prices for a period of time.
Energy Retailers Association of Australia (ERAA)	If retail prices are to be regulated, they should be cost-reflective and derived from a consistent and predictable price setting methodology. The different elements that contribute to the regulated retail price should be calculated in a transparent manner. The ERAA supports the use of a Long Run Marginal Cost floor for calculating wholesale energy costs. (p2)	Noted. The Commission has previously articulated its views on how regulated retail prices should be set. See AEMC 2013, *Advice on best practice retail price methodology*, Final Report, 27 September 2013, Sydney.
ERAA	In deregulated energy markets, margins are complex to assess and shift frequently due to factors unrelated to retail competition. Margins in particular are susceptible to inputs such as changes in wholesale costs, regulatory intervention, and fluctuation in consumer demand. Estimating retail margins and determining an acceptable range is akin to the work currently required to set regulated prices. Given the subjectivity involved, estimating retail margins using theoretical assumptions adds limited value to ascertaining the effectiveness of competition. (p1)	Agree that margins fluctuate over time so any assessment must be conducted over an appropriate period of time. See sections 3.2.3 and 8.7 for further discussion.

Stakeholder	Issue	AEMC response
Ergon Energy	Suggests that in redefining the uniform tariff policy, consideration needs to be given to the social impacts on communities, households and businesses from an increase in electricity prices. (p6)	This is an issue for the Queensland Government to consider and is out of scope of this review.
Ergon Energy	Given the recent interpretation of the uniform tariff policy has been to use the lowest cost network tariff applicable to customers eligible for notified prices, the introduction of price monitoring in South East Queensland (targeted for July 2015) would necessitate a re-consideration of the basis for notified prices for Queensland. (p10)	As above.
DSDBI Victoria	The presence of a number of active competitors in the Victorian retail market would be expected to limit the ability of any one retailer to sustain price or profit margin increases above underlying costs. (p3)	See section 8.7 for discussion on retailer outcomes in Victoria.
Envestra	Where it continues to be appropriate for retail prices to be regulated, that prices are set at levels that are supportive of retailer entry/participation. (p7)	The Commission has previously articulated its views on how regulated retail prices should be set. See AEMC 2013, *Advice on best practice retail price methodology*, Final Report, 27 September 2013, Sydney.
Origin	Price regulation increases regulatory risk and thereby overall costs. When prices are set below cost reflective levels retailers must either reduce their exposure to the relevant market or seek to recoup these losses in later years if prices return to cost-reflective levels. (p5)	Noted.
PIAC	Recommends that the AEMC examine retailer costs and profit margins, to determine whether the market is working to minimise retail costs and deliver competitive prices for residential consumers. (p5)	See section 3.2.3 for discussion on retailer outcomes. In jurisdictions where prices are regulated, it is the role of the jurisdictional regulator to determine these factors for the purpose of calculating the regulated price. See section 8.7 for discussion on retailer outcomes in Victoria, which is the only jurisdiction to have deregulated prices for a period of time.

Stakeholder	Issue	AEMC response
PIAC	A time series of price movements and cost components should allow the AEMC to determine whether increases in retail costs are working to cancel out lower costs in other areas. It is important that reductions in generation and network costs be passed through. (p5)	As above.
PIAC	Consumers should not be asked to pay higher than efficient costs for essential services in order to fund increased retailer activity and operations." (e.g. marketing costs). PIAC considers that effective competition cannot be said to exist if this is occurring. (p5)	Costs can be expected to change over time. Competition provides incentives for retailers to strive to lower their costs.
PIAC	Retailer profit margins are a useful indicator of the effectiveness of competition. Retailer costs in Victoria must be the subject of particular attention. (pp4-5)	See section 8.7 for discussion on retailer outcomes in Victoria. Also note that competitive indicators cannot be considered in isolation and that an adverse finding for a single indicator is not necessarily indicative of a systemic problem.

Other issues

Stakeholder	Issue	AEMC response
ActewAGL	ActewAGL considers the AEMC should provide opportunities for all stakeholders to lodge submissions on the draft report. (p2)	The Commission notes that stakeholders were provided the opportunity to make submissions on the Approach Paper for the review.
ActewAGL	ActewAGL considers competition to be effective in both the ACT and NSW and supports the removal of retail price regulation in both markets. (p2)	Noted.
ActewAGL	More weight should be given to evidence of market outcomes rather than evidence of competitive market characteristics. (p2)	The Commission has assessed five competitive indicators which together determine the state of competition in a market. See Chapter 2 for further discussion.

Stakeholder	Issue	AEMC response
Alinta Energy	Once it has been established that markets are competitive, further reviews should only occur when there has been a material market failure or market operational variance identified that has the potential to impact the level of competition. (p1)	The Terms of Reference for the review require the Commission to report annually on the state of retail energy competition across the NEM.
AER	The indicators that the AEMC has chosen to assess the effectiveness of competition are broadly consistent with the approach adopted by competition authorities and regulators. However it is not without its challenges. It can be difficult to weigh up qualitative and quantitative measures to reach firm conclusions on the overall effectiveness of competition, particularly where there is conflicting data. (p2)	Noted. See Chapter 2 for how we have done this.
AER	It may assist stakeholders to further understand the AEMC's assessment approach if some further guidance was given on the range of market outcomes that are intended to be represented by effective competition, or alternatively a scenario was outlined where competition may be considered less than effective. (p2)	As above.
AER	Considers that in areas where the AER already has ongoing reporting responsibilities, significant care needs to be taken to minimise unnecessary duplication of work. (p3)	Noted. The AEMC is required to report annually on the state of retail energy competition across the NEM.
AER	Measuring profit margins involves significant challenges. The work of assessing retailer revenues and margins will require detailed understanding retailer costs. This in turn requires wholesale market data and data on network costs. (p2)	Agreed. Section 3.2.3 discusses some of the challenges in assessing retailer margins.
CALC	We acknowledge that competition is the framework chosen by policy makers to ensure consumers benefit in the energy market. But we believe that the AEMC needs to more clearly analyse the role of competition in driving market exclusion. (p2)	The AER reports annually on the performance of retail energy markets in NECF states. This includes energy affordability.
EnergyAustralia	We are of the view that we are generally able to recover costs. We consider however, that in many instances regulators have understated input costs and consequently the headroom/margin component of the regulated tariff is unrealistic as a considerable portion of this component is taken up covering the other cost components, typically wholesale energy costs and retailer operating costs. In jurisdictions where an explicit headroom allowance is included in retail price determinations, it provides a perception	The Commission has previously articulated its views on how regulated retail prices should be set. See AEMC 2013, *Advice on best practice retail price methodology*, Final Report, 27 September 2013, Sydney.

Stakeholder	Issue	AEMC response
	of retailer margin which is grossly overstated. (p7)	
ERAA	The ERAA expects the 2014 Retail Competition Review will confirm the competitive nature of the retail energy market in South East Queensland, providing evidence to support price deregulation. (p.3)	The AEMC has found that competition in the electricity retail market in South East Queensland is effective. See Chapter 4 for discussion.
ERAA	The ERAA believes that the downstream retail gas market in all NEM jurisdictions is sufficiently competitive to protect customers from future uncertainty. (p4)	Section 3.3.3 discusses possible future developments in the natural gas retail market.
IPART	Groups of customers that cannot readily access the competitive market or that require financial assistance should be specifically considered/targeted. They cannot be protected through price regulation. (p2)	Noted. See section 3.2.2 for discussion on consumer protections. The AEMC's consumer engagement blueprint, developed for the NSW retail review in 2013, provided detailed recommendations on how many customer segments could be provided with support to choose an energy plan that suits their needs.
IPART	Small retail customers in NSW have continued to move from regulated prices to market-based prices. (p1)	Noted.
IPART	Standard retailers in NSW have continued to lose market share within their supply areas. (pp1-2)	Noted. See section 6.5.1 for discussion on market share and concentration in NSW.
IPART	Supports AEMC's findings on the effectiveness of competition in retail electricity and gas markets in NSW and have found no evidence of impediments to further development of competition over 2013-16. IPART considers regulation in NSW no longer necessary and there are benefits to removing it. (p1)	Noted.
PIAC	Ongoing monitoring of the market will illustrate its development and evolution as opposed to a snapshot at a single time point. (pp7-8)	Agree. See Chapter 2 for further discussion on how markets can be expected to change over time.

Stakeholder	Issue	AEMC response
PIAC	Recommends that the AEMC undertake its current review of retail competition in the NEM in a manner that would support the use of its findings in any future framework for the reintroduction of price regulation in a NEM jurisdiction. (pp7-8)	Noted.
PIAC	With regards to NSW, the AEMC should follow the example of work currently being undertaken by consumer representatives from the St Vincent de Paul Society in collaboration with Alviss Consulting. (p2)	Noted.
PIAC	Considers that if price regulation is removed in NSW, a series of triggers for re-regulation should be introduced. It believes that the AEMC's annual reviews could provide indicators for the activation of these triggers. (p2)	This is an issue for the NSW Government to consider and is out of scope of this review.
Queensland Consumers Association	The review should examine the extent to which retail competition is delivering lower electricity prices to consumers in the Energex area by obtaining information on the prices actually paid by consumers on market contracts. There is anecdotal evidence to suggest that a significant proportion of customers on market contracts pay the same as or very close to the regulated prices paid by consumers on standard contracts. (p2)	The AEMC considers that customers should be encouraged to shop around regularly as their energy needs change.
Queensland Consumers Association	The QCA's 2008 report on the future of gas retail competition in Queensland concluded that competition was likely to improve. This conclusion needs to be re-examined given that there are now only two retailers in most of the state and consumer engagement is almost certainly still very low. (p2)	Competition in the retail gas market in South East Queensland remains limited primarily due to low penetration of gas and a low level of average gas demand for heating or cooking. See section 4.4.3 for further discussion. In regional Queensland, competition is unlikely to develop further due to the relatively small size of the customer base and the regional specific economies of scale associated with gas retailing. See section 5.4 for more information.

D Solar arrangements

This appendix sets out government guaranteed, regulated retailer and competitive retailer feed-in tariffs (FiTs) for each jurisdiction. Tariffs are net unless otherwise stated.

As set out below, jurisdictional governments have taken different approaches to FiTs and there have been policy changes to these schemes over time. Consequently there may be some confusion for solar customers about what they are entitled to.

During the customer research conducted for this review, some solar customers also expressed uncertainty about whether they were able to switch retailers and still be eligible for their government FiT. We note that under all government schemes except the “Standard Scheme” in Victoria, customers can switch retailers without losing their government guaranteed FiT.

D.1 Queensland

The Queensland Solar Bonus scheme commenced in July 2008 and applications closed on 30 June 2014. Customers on this scheme that receive a government guaranteed rate fall into two categories depending on when they applied:

- Customers that applied for the scheme before July 2012 were eligible for a 44 c per kWh government FiT and will continue to receive this rate until July 2028.
- Customers that applied for the scheme between July 2012 and June 2014 received an 8 c per kWh government FiT until 1 July 2014.

Queensland customers on the Solar Bonus scheme can switch retailers without losing their government FiTs (where these still apply).

Retailers in South East Queensland also offered ‘top ups’ of 6 to 12 c per kWh as at 1 July 2014. These rates may vary if a customer switches retailer.

From 1 July 2014, customers in South East Queensland who were previously on the 8 c per kWh rates, as well as new solar customers, will receive FiTs that are set by their retailer. As of 1 July 2014 these ranged from 6 to 12 c per kWh.

From 1 July 2014 regional Queensland customers will receive a regulated FiT from their retailer which is currently set at 9.07 c per kWh.[356]

356 See Queensland Competition Authority, Final Report – Solar feed-in tariff for regional Queensland for 2014-15, May 2014, p10.

D.2 New South Wales

Customers who applied for the New South Wales Government Solar Bonus Scheme between January 2010 and April 2011 will receive 20 c per kWh or 60 c per kWh, depending on the dates of purchase or lease and application, until December 2016. Customers can choose between receiving a net or gross FiT. As at March 2014, one retailer offered a10 c per kWh 'top up'. Customers on the Solar Bonus Scheme can switch retailers without losing their government FiT however the 'top up' could change.

There are no government FiTs currently open for application in NSW. New solar customers receive competitive retailer FiTs which ranged from 5 to 10 c per kWh as at March 2014. The Independent Pricing and Regulatory Tribunal publishes a recommended range, which was 6.6-11.2 c per kWh for 2013-14 and is 4.9-9.3 c per kWh for 2014-15.[357]

D.3 Australian Capital Territory

The Australian Capital Territory's Micro Generator Scheme was open for applications between March 2009 and July 2011. The Medium Generator Scheme was open between February 2011 and July 2011. Government guaranteed rates range from 30.1 to 50.05 c per kWh gross, depending on the date of connection and capacity. These rates will be paid for 20 years from connection. Customers on these schemes can switch retailers without losing their FiT. Following the closure of these schemes to new applications, customers receive a FiT set by their retailer. These currently range between 6 and 7.5 c per kWh.

D.4 Victoria

Victoria has three government FiT schemes which are closed to new applicants but existing customers still receive a guaranteed rate. New solar customers and those which lose eligibility for their FiT scheme receive competitive retailer FiTs subject to a minimum tariff.

The Standard Scheme was open to applications from January 2008 to December 2012 and offers a 'fair and reasonable tariff' which is the same rate as that paid by the customer for their electricity. Since this rate is contracted with and funded by each customer's electricity retailer, customers on this scheme cannot switch retailers without losing their 'fair and reasonable tariff'. The Standard Scheme FiTs will be paid until December 2016.

The Premium Scheme was open to applications from November 2009 to December 2011. The Premium Scheme FiT of 60 c per kWh will be paid until November 2024. As of 1 July 2014, some retailers offer a 'top-up' of up to 10 c per kWh.

---

357 Independent Pricing and Regulatory Tribunal, Solar feed-in tariffs – the subsidy-free value of electricity from small-scale solar PV units from 1 July 2014, p1.

The Transitional Scheme was open to applications from January to December 2012. The Transitional Scheme FiT of 25 c per kWh will be paid until December 2016. As of 1 July 2014, some retailers offer a 'top-up' of up to 10 c per kWh.

Customers on the Premium Scheme and Transitional Scheme can switch retailers without losing their FiT, however the retailer 'top-up' could change.

From January 2013, there has been a minimum retailer FiT for new solar customers. For 2014, the Essential Services Commission set this at 8 c per kWh.[358] This rate must be offered by retailers with more than 5,000 customers. Typically, retailers offer the minimum 8 c per kWh FiT, however as of 1 July 2014 some retailers offered up to 10 c per kWh.

D.5 South Australia

The South Australian Solar Feed-in Scheme commenced in July 2008 and closed to new applications in September 2013. Customers on this scheme that receive a government guaranteed rate fall into two categories depending on when they applied:

- Eligible customers that applied for the scheme between July 2007 and September 2011 will receive a 44 c per kWh FiT until June 2028.
- Eligible customers that applied for the scheme between October 2011 and September 2013 will receive a 16 c per kWh FiT until September 2016.

Retailers in South Australia also offer a 'top-up' in addition to the government-guaranteed rate. Customers on this scheme can switch retailers without losing their FiT, while it still applies, however the retailer 'top up' could change.

Since January 2012, there has been a regulated minimum retailer FiT in South Australia. The Essential Services Commission of South Australia set the regulated minimum retailer FiT at 9.8 c per kWh for 2013, 7.6 c per kWh for the first half of 2014 and 6 c per kWh from 1 July 2014 following the carbon price repeal.[359] Retailer offers are consistent with these minimum rates.

D.6 Tasmania

Customers in Tasmania could apply for the Transitional Legacy Tariff until August 2013. This scheme pays 28.283 c per kWh until December 2018. Customers on the Transitional Legacy Tariff can switch retailers without losing their FiT. For new solar

---

358 Essential Services Commission, Minimum electricity feed-in tariffs – for application from 1 January 2014 to 31 December 2014 – Final Decision, August 2013, p1.

359 Essential Services Commission of South Australia (ESCOSA), Repeal of Carbon Price: Impact on Minimum Feed-in Tariff, 24 July 2014, http://www.escosa.sa.gov.au/article/newsdetail.aspx?p=16&id=1276; ESCOSA, Retailer feed-in tariff – Price Determination, December 2013, p2; and ESCOSA, 2012 Determination of solar feed-in tariff premium - Final Price Determination, January 2012, pvi.

customers, the Office of the Tasmanian Economic Regulator sets a regulated FiT. For January 2014 to June 2014, this rate was 8.282 c per kWh.[360]

360 Office of the Tasmanian Economic Regulator, Regulated Feed-in tariff for Tasmanian small customers – Final Report, October 2013, p43.

D Active retailers in NEM jurisdictions

The table below identifies the energy retailers that were active in the small customer electricity and gas markets in each NEM jurisdiction in 2013. Some retailers may only be accepting customers from one segment of the small customer market (either residential or small business customers), as set out in Chapters 4-10. In assessing which retailers are active in each NEM jurisdiction, we considered data on small customer numbers as well as offers made on retailer and government comparator websites.

Figure D.1

Retailer	SE QLD	Regional QLD	Vic	NSW	ACT	SA	Tas
ActewAGL				Electricity, Gas	Electricity, Gas		
AGL (also trading as Powerdirect and AP&G)	Electricity, Gas	Gas	Electricity, Gas	Electricity, Gas		Electricity, Gas	
Alinta (also trading as Neighbourhood Energy)			Electricity, Gas			Electricity, Gas	
Aurora							Electricity, Gas
Blue NRG			Electricity				
Click Energy	Electricity		Electricity	Electricity			
Diamond Energy	Electricity		Electricity	Electricity		Electricity	
Dodo Power and Gas	Electricity		Electricity, Gas	Electricity		Electricity	
EnergyAustralia	Electricity		Electricity, Gas	Electricity, Gas	Electricity, Gas	Electricity, Gas	
Ergon		Electricity					
ERM (small business customers only)			Electricity	Electricity	Electricity	Electricity	
Lumo Energy	Electricity		Electricity, Gas	Electricity, Gas		Electricity	
Momentum			Electricity	Electricity		Electricity	
Origin Energy	Electricity, Gas	Gas	Electricity, Gas	Electricity, Gas		Electricity, Gas	
People Energy			Electricity				
Powershop			Electricity				
QEnergy	Electricity		Electricity	Electricity		Electricity	
Red Energy			Electricity, Gas	Electricity		Electricity	
Sanctuary Energy	Electricity			Electricity		Electricity	
Simply Energy	Electricity		Electricity, Gas	Electricity		Electricity, Gas	
Tas Gas Retail							Gas
Number of electricity retailers	**10**	**1**	**16**	**14**	**3**	**13**	**1**
Number of gas retailers	**2**	**2**	**8**	**5**	**2**	**5**	**2**

Electricity retailer Gas retailer

F Victorian retail consumer protections

Table F.1 provides an overview of the differences for retailers between Victorian-specific retail consumer protections/requirements and those contained in the National Energy Customer Framework (NECF). Differences in retailer consumer protections/requirements were discussed as part of the Victorian assessment of retail competition in Chapter 8.

Table F.1

Requirement	Current Victorian position	NECF
Late payment fees	A retailer is prohibited from including a term or condition in a customer retail contract that permits a retailer to charge fees for late payment of bills.[361]	No equivalent prohibition in NECF
Compensation for wrongful disconnection	A retailer (electricity or gas) who wrongfully disconnects one of its household customers is required to make a $250 per diem payment to that customer.[362]	No corresponding equivalent in NECF
Community service agreements	A retailer is required to enter into an agreement with the State for the provision of community services. These take the form of several grants and rebates that are available to customers with low incomes and are otherwise in need of assistance with the affordability of energy.	No corresponding equivalent in NECF
Energy audits and appliance assistance	Retailers, as part of their financial hardship policies, are required to offer customers free or subsidised home energy audits and flexible options for the purchase or supply of electrical appliances.[363]	Some corresponding equivalence in NECF. Under section 44(g) of the National Energy Retail Law (NERL) retailers are required to include in their policies any assistance that is required by jurisdictional regulation.

362 Section 40B *Electricity Industry Act 2000 (Vic)*

363 Section 43C *Electricity Industry Act 2000 (Vic)* as to what contents of a financial hardship policy

Requirement	Current Victorian position	NECF
Pre-payment meters	Pre-payment meter systems are currently prohibited in Victoria (and will continue to be).	The National Energy Retail Rules (NERR) provides for pre-payment meters. Under section 56(2) of the NERL, regulation around the use of prepayment meters (as set out in the NERR) only comes into effect where a local instrument allows for the use of prepayment meters.
Extreme weather events	No current provisions in force.	Regulation regarding extreme weather events (as set out in the NERR) only comes into effect where a local instrument defines an extreme weather event (rule 108).
Advanced metering infrastructure (AMI)	Victorian electricity licences (for retailers) include a condition requiring the licensee to comply with any relevant Orders in Council including those in relation to advanced metering infrastructure**.** *The Advanced Metering Infrastructure (AMI Tariffs)* Order in Council 2013 provides a whole suite of additional obligations that a retailer must comply with. Some of these include an overlay to obligations that exist in the Victorian Energy Retail Code. Some of the obligations in the Order in Council go to ensuring that sufficient information is provided so that customers can make informed decisions about their energy consumption and price signals, and that they are treated fairly. Examples include: • requires that specific information is provided on customer bills so that customers can reconcile and understand their accounts, including use of graphs and in-home displays;[364]	No corresponding equivalent in NECF, though similar consumer protections regarding sufficiency of information do exist.

364 That is, retailers to provide customers with information setting out how any consumption and cost information displayed on the In-home Display compares to the consumption and cost information on the customer's bills.

Requirement	Current Victorian position	NECF
	• requires the retailers to obtain a customer's informed consent to tariff structure changes, for example, to change from a peak/off-peak tariff to a time-of-use tariff, and to provide advice of price variations in a timely manner; • requires disconnection notices to indicate that the disconnection may occur remotely; • ensures that customers in financial difficulties are not remotely disconnected without adequate assistance from the retailer to avoid that outcome; • requires that, once the customer has met their obligations and request reconnection in accordance with the law, the retailers use their best endeavours to have customers remotely reconnected within two hours if it is safe to do so; and • retains the current approach to only requiring the customer to pay for meter testing if they dispute their bills and the meter is found to be accurate.	
Bulk hot water billing	The Victorian Retail Code[365] sets out detailed requirements for retailers when charging for the energy used in the delivery of bulk hot water (in accordance with specific formulas).	No corresponding equivalent in NECF
Timeframes for disconnecting and reconnecting customers	Retailers are prohibited from disconnecting a domestic customer after 2pm.[366] Detailed prescription surrounding timeframes for reconnecting.	Under the NERR, disconnection is allowed up to 3pm.[367]
Energy price and	Retailers are required to comply with Guideline 19 – Energy Price and Product Disclosure – obligations regarding publication of standing offers, terms and conditions	Some corresponding equivalence in NECF. There is overlap between the Guidelines

365 Clause 3.2 and Appendix 2.

366 Victorian Energy Retail Code, clause 14

367 See definition of 'protected period' in rule 108

Requirement	Current Victorian position	NECF
product disclosures	etc.	and the AER Pricing Information Guidelines made under section 61 of the *NERL*.
Greenhouse gas disclosure on customer's bills	Retailers are required to include greenhouse gas information on customers' bills or to provide bill benchmarking information to a customer.[368]	Some corresponding equivalence in NECF. Part 11 of the NERR establishes a regime under which the AER must determine electricity consumption benchmarks and requires retailers to include a comparison of consumption against those benchmarks on customer's bills.
Additional retail charges	A retailer may impose an additional retail charge[369] on a customer, if allowed for in the Victorian Energy Retail Code. The amount charged must be fair and reasonable having regard to the related costs of the retailer.	No corresponding equivalent in NECF
Agreed damages terms	The particulars that must be included in an agreed damages term in an energy contract between a retailer and customer are set out in the Victorian Energy Retail Code.[370]	No corresponding equivalent in NECF
Energy Marketing	There is Code of Conduct for Marketing Retail Energy	Some corresponding equivalence in NECF. Division 10 of the NERR relates to energy marketing and in large part covers the same issues as in the Code of Conduct.

368 Section 40R *Electricity Industry Act 2000 (Vic)*

369 An additional retail charge is currently defined as any charge relating to the sale of energy by a retailer to a customer other than a charge based on a tariff that is applicable to a customer. Is does not include network charges, pass throughs of a distribution tariff, agreed damages (if provided for in a contract): clause 30 &34, *Energy Retail Code*.

370 Clause 31