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Submission to the

Electricity Supply Industry Expert Panel
on
An Independent Assessment of the Tasmanian Electricity Supply Industry Draft Report

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The Tasmanian Council of Social Service (TasCOSS) welcomes the opportunity to provide comments on the Electricity Supply Industry Expert Panel's *Draft Report*, *An Independent Assessment of the Tasmanian Electricity Supply Industry*.

TasCOSS is the peak body for the community services industry in Tasmania and represents the interests of the industry and of the low income, vulnerable and disadvantaged Tasmanians who are supported by the industry. We have a long history of involvement in electricity supply issues given the essential nature of electricity and the ongoing challenge experienced by many low income Tasmanian households to maintain an uninterrupted household electricity supply. In recent years, affordability has become an even greater challenge as prices have persistently increased.

We welcome the work of the Panel and its intensive focus on the electricity supply industry in Tasmania. The production of comprehensive information papers in the course of the Review has been particularly appreciated, as has the provision of public access to these papers. The Panel's research makes an important contribution to the public information base on energy supply issues in Tasmania and provides a foundation for constructive discussions on the future of Tasmania's energy supply.

While the *Draft Report* addresses a range of issues, our submission will focus on those issues, findings and recommendations that we believe are most relevant to the interests of the low income, vulnerable and disadvantaged Tasmanians. These are associated with the cost – and the affordability – of electricity for Tasmanian households.

Electricity – an essential service

TasCOSS has argued in previous submissions that the Panel must acknowledge the essential nature of electricity in its energy supply industry objective and that the articulation of that would rightly differentiate electricity supply from most other goods and services and thereby underline the importance of ensuring that electricity prices are not only efficient, but are also affordable.

Indeed, the Government's Terms of Reference document for the Expert Panel Review begins with an acknowledgement of electricity as 'a utility service that is essential to the Tasmanian community' and articulates the Government's commitment to ensure 'that cost of living impact of electricity prices is kept to a minimum' (Final Terms of Reference, Review of the Tasmanian Electricity Supply Industry, October 2010).

We are disappointed to see no acknowledgement of the essential nature of electricity in a revised energy supply industry objective or anywhere in the Panel's *Draft Report* and we urge the Panel to rectify those omissions.

Price setting framework

TasCOSS welcomes the finding and recommendation relating to the future setting of wholesale energy allowances for non-contestable customers.

We agree with the Panel that the current regulations – which mandate the use of a system using the long run marginal cost (LRMC) of a notional new electricity generation plant located on mainland Tasmania and supplying non-contestable customers – have significantly inflated the energy component of the regulated price. This has resulted in Tasmanian energy consumers paying far more than is necessary for electricity.

It is clear from both the Panel's research and submissions to the Panel from Hydro Tasmania that the regulated energy price is significantly higher than both the average annual spot market price and the probable price contracted between Aurora Energy and Hydro Tasmania.

While TasCOSS is not expert in pricing issues, we support the recommendation made by the Panel that the method for determining the wholesale energy price, as a component of the regulated retail price, be modified for future price regulation. The Panel's argument that prevailing conditions and likely supply-demand balances should be reflected in the energy price seems logical and more appropriate than the current method of employing a LRMC method based on costs of energy from a hypothetical new generator.

TasCOSS strongly supports this change and sees it as fundamental to fairer regulated prices in the future.

Network cost components

The *Draft Report* clearly demonstrates significant increases in network prices in recent years – including 300 percent growth in transmission charges between the years 2000 and 2010 – and states that 'higher transmission and distribution network charges have accounted for around half of the increases in non-contestable customer prices since 2000' (*Draft Report* p 50).

The *Draft Report* also notes that there is little evidence of increased demand necessitating network expansion, with capital network expenditure focused instead on 'non-demand asset replacement.' In other words, it appears that the bulk of spending on Tasmania's electricity networks has focused on replacement and maintenance of ageing infrastructure.

In addition, the *Draft Report* reveals that, in spite of regulation of Tasmania's network monopolies, there has been considerable over-spending by both network businesses in recent years. In the 2003-04 to 2010-11 period for instance, according to the *Draft Report*, 'Aurora Energy exceeded its cumulative capital expenditure allowances in relation to non demand asset replacement by 20 percent ($28 million, 2010 dollars).' (*Draft Report* p 61)

The *Draft Report* also notes the 2003 revaluation of Transend's transmission assets by the Tasmanian Treasurer which the ACCC was required to accept under conditions relating to the transfer of transmission network regulation from the Tasmanian Energy Regulator to the ACCC. The revaluation was $72 million or nearly 16 percent higher than the previous valuations by the Tasmanian Regulator (*Draft Report* p 56).

Both over-spending on capital expenditure and this revaluation have contributed considerable value to the assets of both network business. Since regulated revenue allowances are based on the value the Regulated Asset Base (RAB) of a network business, the higher the value of the RAB, the higher the allowable revenue. In other words, Tasmanian network businesses continue to reap the benefits of over-spending and over-valuation for the life of the assets, 'typically 40 years' (*Draft Report* p 61). And consumers continue to pay.

There appears to be serious problems with the Australian network regulatory system, so much so that the Australian Energy Regulator (AER) has recently lodged a Rule Change proposal with the Australian Energy Market Commission in an attempt to rein in network prices.

While the Tasmanian Government, as the owner of the State's network businesses, benefits from increased revenue allowances, it is Tasmanian consumers who pay the price. It is in the interests of Tasmanian consumers that the regulatory system provides fairer outcomes, and TasCOSS welcomes both the AER's Rule Change proposal and the recently announced Productivity Commission inquiry into national electricity network regulation.

We understand that these issues are outside the scope of the Panel's review; however, the substantial contribution that network costs have made to electricity price increases in recent years, necessitates consideration of these issues by anyone concerned with rising prices, and in particular, by the Tasmanian Government.

TasCOSS is interested in the Panel's options for structural reform to network services, with possible closer collaboration or integration of Tasmania's two network businesses. Given the potential for savings, it may be in the interests of Tasmanian consumers that more detailed exploration of these options is undertaken in the future.

Tariff structures

The *Draft Report* notes that, for residential customers in Tasmania,

> *fixed supply charges are generally higher than in other states (and most Tasmanians incur multiple fixed charges because of their connection to more than one tariff) ...*
> *Draft Report* p 34

This is an issue of concern that TasCOSS has raised in previous submissions to the Panel and we reiterate our concern briefly here.

Currently Tasmanian electricity consumers on standard tariffs pay just over $1.06 per day in fixed charges for their light, power and hot water heating supply, while those with the Aurora Pay As You Go (APAYG) prepayment meter systems pay slightly over $1.35 per day. These fixed costs are paid regardless of whether any electricity is used at all, and are accrued daily by prepayment meter customers even when their meters are uncharged with pre-paid credit.

Our major concern is that the relatively high fixed charges make it difficult for households to realise savings on electricity costs by reducing their usage through energy efficiency and other efforts.

We know that Tasmanian households use more electricity than other Australian households and that many low income households in Tasmania seek to reduce their costs, particularly in winter months, by rationing their electricity use. In addition, the Commonwealth Government is embarking on substantial energy efficiency programs, in an effort to reduce energy use as adjuncts of its *Clean Energy Future* policies.

Reducing electricity use *should* save households money; unfortunately this is limited in Tasmania by a tariff structure with high fixed charges compared to usage charges. TasCOSS contends that this must be addressed as part of the development of a State energy strategy, and we urge the Panel to include such a recommendation in its final report.

Competition – generation and retail

The unequivocal support in the *Draft Report* for the introduction of full retail competition (FRC) in Tasmania is a concern for TasCOSS. While there are repeated references to the provision of choice 'and other benefits of competition' throughout the *Draft Report*, there is little evidence of these benefits provided. Indeed the Panel's commitment to competition is largely unsupported by argument in the *Draft Report* and appears to be an article of faith.

TasCOSS remains sceptical regarding the potential benefits of competition for the majority of residential electricity consumers in Tasmania, and especially for low income consumers. There is no guarantee that FRC will result in lower prices. In fact in those Australian jurisdictions where retail competition is established (and deemed effective, in the case of Victoria) prices are comparable with Tasmanian prices, and continue to rise.

The *Draft Report* maintains that the 'key cost' of FRC would be Aurora Energy's distribution IT costs (p 190). However, TasCOSS believes that there are other ongoing costs associated with retail competition that would be passed on to consumers, including sales and marketing costs, customer acquisition and retention costs and increased retail margins. In addition, Tasmanian residential consumers may also be subject to aggressive and unwelcome marketing practices as have been common in other jurisdictions, particularly in the early stages of retail competition.

TasCOSS completely rejects the Panel's proposal that FRC be declared and that the Tasmanian Government,

> *proactively introduces new retailers into Tasmania by splitting Aurora Energy's retail business into smaller parcels and selling those parcels through a competitive process ...*
> *Draft Report* p 254

Since the potential for success of retail competition is considered by the Panel (and the Tasmanian Economic Regulator) to be contingent on increased and more effective wholesale energy competition, the Panel also recommends that wholesale competition be artificially created.

Both of these proposals appear to be driven by an ideology that values competition at all costs, and for its own sake. For this reason, TasCOSS rejects the proposals and the other options to introduce FRC in Tasmania, until such time as it can be demonstrated and supported by evidence that retail competition will benefit all Tasmanian households, including those living on low incomes.

TasCOSS believes that a reliable, safe and affordable supply of electricity is a right rather than a privilege and that access must be guaranteed as far as reasonably possible. Furthermore, no household should be disconnected only for inability to pay.

Tamar Valley Power Station

TasCOSS shares the Panel's concern with the acquisition of the TVPS by Aurora Energy and the effect that that has had on the company. TasCOSS therefore supports the Panel's recommendation that the TVPS be funded transparently and independently of Aurora Energy. We are unsure whether the second part of the Panel's recommendation in relation to the TVPS is feasible or most appropriate; however, it seems logical to ensure a current and future role for the power station by some means.

Transparent identification, delivery and funding of non-commercial activities

TasCOSS fully supports the Panel's contention that non-commercial activities of the electricity supply companies, as required by the Government, should be transparent and clearly reported annually in the State Government's Budget Papers.

In particular we would like to comment on the issue, raised in the *Draft Report*, concerning the ongoing subsidy provided by Aurora Energy to eligible concession customers using APAYG, in return for a lower annual dividend from Aurora Energy.

This arrangement, introduced in a highly charged political environment in which rising electricity prices were a major issue (and which was eight months out from the 2010 State election), was highly questionable in the view of TasCOSS. And it remains so today. TasCOSS contends that it is neither transparent nor fair, and that it undermines the regulatory system.

This 'unofficial subsidy' currently provides an additional 28.169 cents per day concession, as well as further per kilowatt hour subsidies in winter months to those concession card holders who choose the APAYG prepayment meter system. This additional concession can be seen as an incentive for concession card holders to switch to APAYG from the standard tariff (which offers additional consumer protections as well as regulated prices). It can also be seen as Government inequitably and non-transparently subsidising APAYG, and indeed propping up that tariff product.

APAYG is a tariff favoured by many low income households and has been promoted as a way to avoid unwelcome quarterly electricity bills. TasCOSS has long sought improved regulation of APAYG and has seen some improvements in consumer protections associated with the service over the past several years.

TasCOSS has also argued consistently for price regulation of APAYG to protect its users from unregulated and unsubstantiated price rises (as occurred in July 2009 when APAYG prices were increased by 12%, compared to the regulated increase of 7.2% for standard tariffs, and when this ‘unofficial subsidy’ was first introduced).

TasCOSS has called for the Tasmanian Economic Regulator to ‘declare’ APAYG services and to regulate APAYG prices through regular price determinations, as it does with standard tariffs. We repeat that call here.

TasCOSS maintains that concessions to low income Tasmanians should rightly be provided by the State Government and that concessions for electricity use should be equitable and based on openly negotiated Community Service Obligations with the service providers involved. Furthermore Government expenditure on concessions must be publicly reported each year.

We fully agree with the Panel’s conclusion that the funding of non-commercial activities through transparent Community Service Obligations rather than through private agreements to forego dividend revenue ‘is fundamental to good governance, performance management and the ability of government to hold the businesses to account’ (*Draft Report* p 294).

Gas

The role of natural gas in the State’s energy mix receives very little attention in the *Draft Report* in spite of the Panel’s Terms of Reference requiring it to look at the efficiency and effectiveness of the Tasmanian energy industry (ToR #1) and to report on ‘actions that guide and inform the development of a Tasmanian Energy Strategy’ (ToR #7).

While the roll-out of natural gas has largely stalled since the Government withdrew its financial support for a proposed Stage 2B, as the *Draft Report* notes, it is currently connected to about 9,000 properties and further properties of the 43,400 that the distribution network passes, are being connected. TasCOSS believes that gas has the potential to be an important feature of Tasmania’s energy future.

TasCOSS believes that an important issue that the Panel – and the Tasmanian Government – must consider is consumer protection and price regulation for residential consumers of natural gas.

Connection to the natural gas network by Tasmanian households was initially a choice, and remains so for many households. However, this has changed in recent years with the Housing Tasmania policy of replacing wood heaters with gas heating and electric hot water systems, as they fail, with gas water heaters where gas is available. In addition, increasing numbers of private rental properties are being connected to gas. This has not only increased the non-choice take-up of gas use for domestic purposes but has also expanded gas use to a cohort of low income Tasmanians.

We are beginning to see indications of gas customers experiencing hardship with 240 residential disconnections reported in 2001-11 (OTTER 2011, *Tasmanian*

Energy Supply Industry Performance Report 2010-11, p 154) and 1,041 gas customers on payment plans at the end of June 2011 (OTTER, information provided to Customer Consultative Committee, November 2011).

TasCOSS is concerned that consumer protection for gas customers is less robust in Tasmania than for electricity customers on standard tariffs and that gas prices are not regulated. Furthermore, the Tasmanian Government intends not to apply the soon-to-be introduced National Energy Customer Framework (NECF; comprising the *National Energy Retail Law*, *Rules* and *Regulations*) to small gas customers in Tasmania , but will continue to rely on the inadequate (in our opinion) Tasmanian Gas Retail Code for consumer protections.

TasCOSS has argued in other forums that gas prices for small customers should be regulated and that small gas customers should be afforded the same level of consumer protection as residential and small business electricity consumers. We note that the latter could be achieved through the application of the NECF to gas in Tasmania.

We urge the Panel to address these issues in its final report.

TasCOSS congratulates the Expert Panel and its secretariat on the work carried out so far in its review of the Tasmanian Electricity Supply Industry and hopes that the comments and suggestions made in this submission are considered by the Panel and are incorporated in its final report. In particular we hope that the Panel is able to recommend actions to the State Government that will result in greater ongoing affordability of both electricity and gas for Tasmanian residential consumers of those energy sources.

Please feel free to contact Kath McLean at TasCOSS (ph: 6331 0755 or e-mail: kath@tascoss.org.au) if you require any further information or have any questions about this submission.