

Independent Pricing and Regulatory Tribunal
New South Wales

Review of the performance and competitiveness of the retail electricity market in NSW

From 1 July 2016 to 30 June 2017

Draft Report
Energy

October 2017



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Invitation for submissions

IPART invites written comment on this document and encourages all interested parties to provide submissions addressing the matters discussed.

Submissions are due by 7 November 2017

We would prefer to receive them electronically via our online submission form <www.ipart.nsw.gov.au/Home/Consumer_Information/Lodge_a_submission>.

You can also send comments by mail to:

2017 Retail Electricity Market Monitoring Review

Independent Pricing and Regulatory Tribunal

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If you would like further information on making a submission, IPART's submission policy is available on our website.



Contents

1	Executive summary	1
1.1	Competition is continuing to improve	1
1.2	Recent changes in electricity retail prices reflect changes in the costs of supply	2
1.3	Many customers are benefiting from competition	4
1.4	Continued competition should provide the best customer outcomes	6
1.5	Recent changes in gas prices also reflect changes in the costs of supply	9
1.6	List of draft findings and recommendations	9
1.7	How can stakeholders comment on this Draft Report?	10
1.8	What the rest of this report covers	11
2	Context, approach and process for this review	12
2.1	Our approach to the review	12
2.2	Our process for this review	14
2.3	Recent developments in retail energy market	15
3	Changes in electricity retail prices reflect the costs of supply	18
3.1	Overview of draft findings	18
3.2	Recent price changes were consistent with a competitive retail market	19
3.3	Average annual bills for residential customers are at similar levels to 2013-14	23
3.4	The fixed portion of residential bills has increased over time	26
4	Retailers are competing to attract and retain customers	30
4.1	Overview of draft findings	30
4.2	Prices indicate competition between retailers	30
4.3	Increasing product and service variation indicates competition between retailers	36
5	Barriers to entry are low	39
5.1	Overview of draft findings	39
5.2	Number of retailers contesting the market is relatively high	39
5.3	Small retailers' share of the market continues to increase	41
5.4	Retailer views do not consider the barriers to entry and expansion are substantial	42
6	Customers are relatively engaged and active	43
6.1	Overview of draft findings	43
6.2	Customer awareness and confidence continue to improve	43
6.3	Switching rates are relatively high	45
6.4	Customers are relatively satisfied	46
6.5	Some customers do not participate in the market for varied reasons	47
7	Measures to further enhance competition	51
7.1	Overview of draft findings and recommendations	51
7.2	Governments are active in regulating the retail market	52
7.3	Governments should prioritise measures to enhance customer engagement	55
7.4	Protections for customers of residential caravan park customers in embedded	

networks	59
8 Measures to assist hardship customers	61
8.1 Overview of draft findings	61
8.2 Retailer strategies for delivering lower prices to hardship customers	61
8.3 Retailer strategies for increasing awareness of available rebates or market offers	63
9 Take up of digital meters	65
9.1 Overview of draft findings	65
9.2 Retailers plans to inform customers about digital meters	66
10 Gas price increases reflect a competitive market	68
10.1 Overview of draft findings	68
10.2 Changes in gas retail prices	68
10.3 Changes in the underlying costs of supplying gas from July 2017	72
Appendices	76
A IPART’s statutory role	77
B Letter from Minister – 27 June 2017	79
C Letter from the Minister – 22 August 2017	81
D Summary of Stakeholder Submissions	82

1 Executive summary

Since the electricity retail market for small customers was deregulated, the Independent Pricing and Regulatory Tribunal (IPART) has performed the role of Market Monitor in NSW.

The market was deregulated in 2014, when the NSW Government was satisfied competition was sufficient to ensure that electricity retailers could not set prices above the costs of supply without the risk of losing customers to their rivals. Where this is the case, allowing retailers to set prices is likely to result in better outcomes for customers than regulation, because they have better information than a regulator about the costs of supplying electricity to their customers. In addition, competition encourages them to differentiate their products and services through innovation, which can benefit customers.

However, competition is a dynamic process, and its effectiveness in keeping prices in line with the efficient costs of supply can change over time. Therefore, our role as Market Monitor is to review the performance and competitiveness of the state's electricity retail market each year, and report our findings to the Minister for Energy and Utilities (the Minister).¹

This report sets out our draft findings for the year 2016-17. It also sets out draft findings on several additional issues that the Minister asked us to consider as part of this review. These include the changes in electricity and gas retail prices at the start of 2017-18 and whether they reflect efficient costs in a retail competitive market. We have also reported on retailers' strategies to deliver lower prices to hardship customers and manage the delivery of digital meters. We invite all interested parties to make submissions on these findings, which we will consider before we provide our Final Report to the Minister in November 2017.

1.1 Competition is continuing to improve

We found that competition for residential and small business customers in the NSW electricity retail market continued to improve in 2016-17. Each of the key indicators we use in assessing competition in this market improved or remained steady relative to the previous year. For example, the concentration of the market fell and the level of customer activity increased, continuing the trend since price deregulation (Table 1.1). Around one-third of customers moved to a new plan or a new retailer at least once in the year, and the proportion of customers on market offers was 77%.

¹ s234A of the NSW National Energy Law

Table 1.1 Change in key indicators of competition in NSW since price deregulation

Category	Measure	2013	2014	2015	2016	2017
Market characteristics	Number of retail brands/businesses	15/13	20/16	26/22	26/22	26/22
Independent rivalry	Market share of second-tier retailers	7%	7%	9%	11%	13%
Customer activity	Small customers on market offers	63%	69%	74%	77%	
	Residential customers switching company at least once		14%	15%	19%	
	Residential customers switching plan with same company ^a		18%	15%	19%	

^a This is likely to include customers that have switched plans when the prices for their existing offer increased.

Source: 2017 AEMC Retail Energy Competition Review, p 239, AER.

We estimate that electricity retail prices increased by an average of 14% for residential customers, and between 10% and 16% for small business customers at the start of 2017-18. This large price increase reflects the change in the underlying costs of supply – in particular rapidly increasing wholesale costs – and is therefore consistent with a competitive market.

Based on these findings, we consider competition in the NSW retail electricity market continues to develop. We do not consider that it is necessary to undertake a further review of retail costs and margins while the ACCC is undertaking its detailed review of retail electricity markets, including retail costs and margins.²

However, there is scope to make competition more effective by continuing to improve customer engagement and activity in the market particularly for vulnerable and disadvantaged customers. This requires further measures to make it easy for all customers to compare market offers and identify the best offer for their circumstances.

1.2 Recent changes in electricity retail prices reflect changes in the costs of supply

As noted above, we estimate that electricity retail prices for residential customers increased by an average 14% in 2017-18. For small business customers, prices increased by 10% to 16% depending on which network area the business is located in. These price increases were driven by significant increases in the wholesale costs of supplying electricity, which have more than doubled in the last two years.

The ACCC also found that since 2007-08, average residential bills in NSW have increased by around 45%, driven by higher network cost increases.³

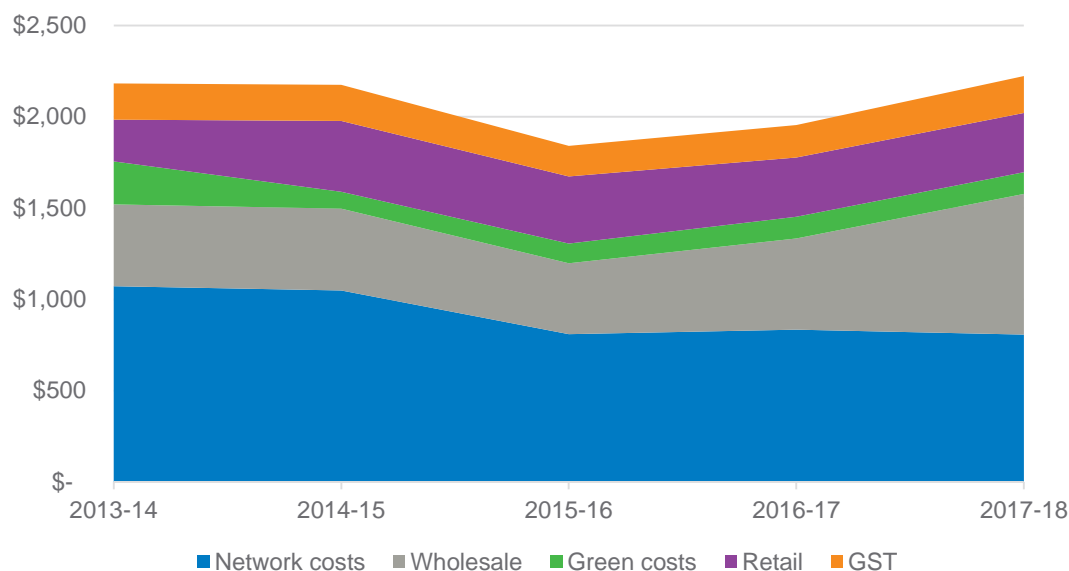
However, the average annual bills for residential customers in NSW are currently around the same as they were in 2013-14 before prices were deregulated, and are slightly lower in

² ACCC, *Electricity supply & prices inquiry*, <https://www.accc.gov.au/regulated-infrastructure/energy/electricity-supply-prices-inquiry>, accessed 16 October 2017.

³ Over the period from 2007-08 to 2016-17. ACCC, *Retail Electricity Pricing Inquiry: Preliminary Report*, 16 October 2017, p 43, <https://www.accc.gov.au/publications/accc-retail-electricity-pricing-inquiry-preliminary-report>, accessed 16 October 2017.

real terms. As Figure 1.1 illustrates, this is because the increases in wholesale costs in 2016-17 and 2017-18 have been largely offset by falling network costs and green scheme costs in 2014-15 and 2015-16. For example, network prices fell by between 12% (Endeavour’s network) and 35% (Essential Energy’s network) in 2015-16 for residential customers.

Figure 1.1 Estimated change in residential bills and costs since price deregulation (6,500 kWh, nominal, GST-inclusive, average across all distribution areas)



Data source: Based on price information provided by retailers, Frontier Economics, *Cost Drivers of Recent Retail Electricity and Gas Prices for Residential Customers in NSW – A Report Prepared for IPART*, September 2017, pp 9-10, AEMC, *2015 Residential Electricity Price Trends Final Report*, 23 February 2017, p 113, ACCC, *Retail Electricity Pricing Inquiry: Preliminary Report*, 16 October 2017, p 43.

After historically low wholesale prices in 2014, the recent increases in these prices were largely the result of reductions in supply. These reductions were due to the retirement and scheduled maintenance of several generators in the NEM, culminating in the closure of Victoria’s Hazelwood coal-fired power station in March this year. The retirement of coal-fired power stations has also meant that more electricity is being supplied by gas-fired power stations. As the wholesale price of gas has increased sharply, this has also contributed to higher wholesale electricity prices.

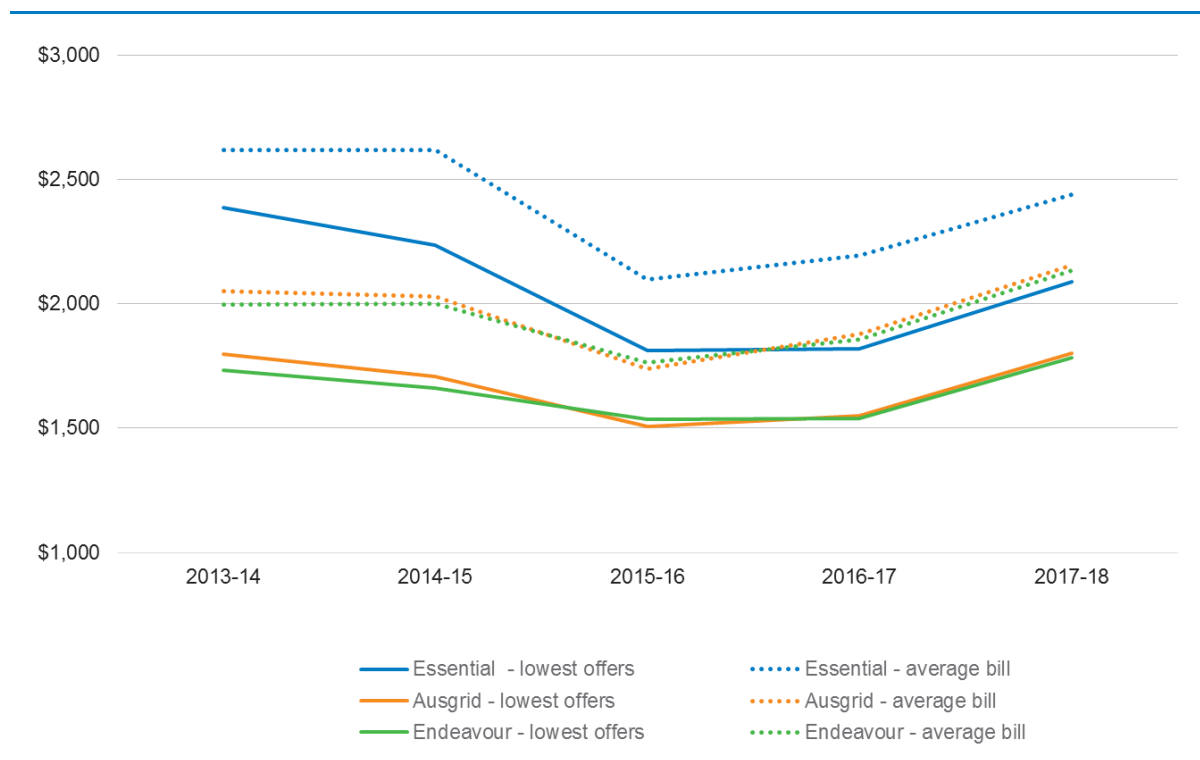
In a well-functioning electricity market, increasing wholesale prices would signal a need for new generation capacity. When investors respond, supply would increase and wholesale prices would fall again. However, continuing uncertainty in the policy environment is hindering this investment. New renewable-energy generators are being built after a period of uncertainty around the renewable energy target (RET). However, there is still reluctance to invest in the wholesale market as the potential for change in policy settings around government subsidies for new generation (including renewable energy), government investment in the energy market, and carbon polices makes it risky for commercial investors.⁴

⁴ *Independent Review into the Future Security of the National Electricity Market*, 9 June 2017, p 29.

1.3 Many customers are benefiting from competition

As mentioned in section 1.2 above, while average retail prices for residential customers increased by 14% in 2017-18, the average annual customer bill in NSW is around the same as it was in 2013-14, before price deregulation (and slightly lower in real terms once the impact of inflation is included). In addition, the lowest offers in the market are around 7% lower than they were before prices were deregulated in real terms (Figure 1.2).

Figure 1.2 Change in average residential customer bills and the lowest offers by network area (6,500 kWh, nominal, GST-inclusive)

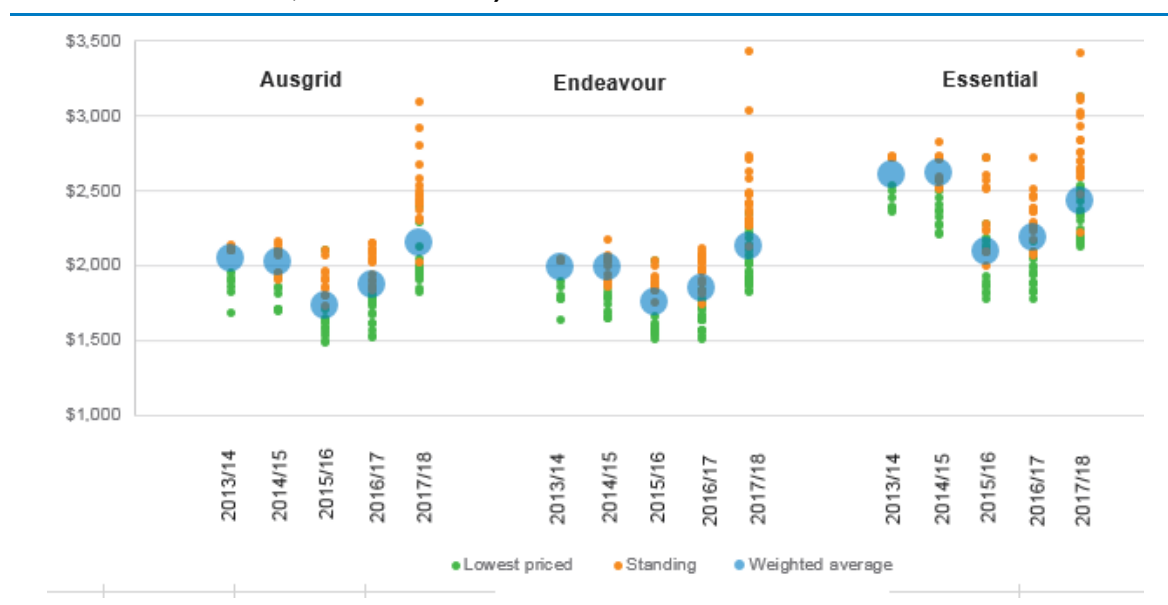


Note: Lowest offers based on the average bottom three offers in the market.

Data source: Information from retailers

However, retailers typically have several different market offers available, which vary significantly in price. A trend of increasing price variation is common in competitive retail markets, and this has become particularly pronounced in NSW from July 2017 (Figure 1.3).

Figure 1.3 Spread of residential offers in the market by network area (6,500 kWh, nominal, GST-inclusive)



Data source: Information from retailers.

The variations in the prices and offers available mean that some customers are paying significantly more than others for the same level of usage.

For example, retailers typically price their standing offers (ie, offers available without signing a contract), higher than their market offers. Since 2013-14, the average price of standing offers for residential customers of the “Big 3” retailers that supply 87% of NSW customers (AGL, EnergyAustralia, and Origin Energy) has increased by around 10% in nominal terms (or 2% in real terms). Similarly, the average increase in the Big 3’s standing offers for business customers increased by 12%.

In 2016-17, 23% of residential customers in NSW were on a standing offer. These customers are paying around 25% more than those on lowest offers in the market.

Price variation is a normal feature of competitive markets. It is observed in most competitive markets (such as airlines, telecommunications, groceries), and often indicates significant competition, rather than lack of it.⁵ It can increase efficiency in markets because it allows retailers to reduce the lowest offers in the markets (and recover more of their fixed and sunk cost from less price sensitive customers), allowing more services to be sold.

⁵ ACCC, Network Issue 63, June 2017, p 10, <https://www.accc.gov.au/system/files/network%20june%202017%20%28D2017-00045379%29.pdf>.

In addition to the potential for lower electricity retail prices, competition can benefit customers by encouraging product and service innovation. This innovation has started to occur, and the range of products and services available has become more varied over the past three years. New products and services currently offered by retailers include:

- ▼ integrated solar PV and battery storage plans
- ▼ bundled energy, data and telecommunications plans
- ▼ plans to contribute an agreed fortnightly/monthly fixed amount towards bills, and
- ▼ options to pre-purchase electricity at discounted rates.

We consider the potential for innovation to benefit customers will continue to grow over time. For example, digital meters will give customers more information and control over their energy usage, and thus increase their ability to benefit from bundled electricity, solar PV and battery storage.

1.4 Continued competition should provide the best customer outcomes

Over the last 12 months, several reviews have considered how outcomes for customers in the electricity retail market can be improved. In Victoria, one recommended that its State Government recommence price regulation because, in its view, customers were paying more as a result of price (and product) deregulation.

However, based on our review, we consider that allowing competition to continue to develop would deliver the best outcomes for customers in NSW. Therefore governments should focus on facilitating increased customer engagement and activity in the retail market to further enhance competition, and ensuring that hardship and vulnerable customers are not paying more than they need to.

1.4.1 Low barriers to entry are the best protection from high prices

In our view, a competitive market with low barriers to entry provides the best protection for customers from higher than necessary prices. In such a market, the incumbent retailers are under constant pressure to offer competitive prices and services, as new entrants can come into the market and outcompete them if they don't.

Our review found that the barriers to entering the electricity retail market in NSW are currently low. In 2016-17, there were 22 retailers and 26 different brands competing for small customers in this market, compared to just 13 retailers and 15 brands in 2013-14.⁶ In addition, although the three largest retailers have the lion's share of the market, smaller retailers have gradually increased their share to 13% in 2016-17 from 7% in 2013-14.⁷

⁶ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 239.

⁷ We note that while the current barriers to entry are low, some retailers have suggested that it may become harder for small retailers to expand in the future, due to the tightening supply in the wholesale market. This may mean that it is increasingly difficult for new retailers to procure wholesale contracts as aging generators are retired, and to the wholesale market becomes more concentrated.

1.4.2 Engaged and active customers increase competitive pressures

The pressure on retailers to offer competitive prices and services are stronger when customers are well-informed, engaged and active in the market. Compared to those in other countries, customers in NSW (and elsewhere in Australia) are relatively engaged in the retail energy market.⁸ However, there is scope to increase the overall level of participation and activity.

As section 1.3 discussed, around 23% of customers do not participate in the market,⁹ and pay more than they need to, and may miss out on other benefits of competition.

For some of these customers, the cost of their time to search for and switch to a better offer outweighs their potential benefit from a lower bill. For these people, not participating or being active in the market is a rational choice. However, for other customers, the challenges of comparing offers and identifying the best offer for their circumstances prevent or limit their participation.

For example, stakeholders submitted that complex and opaque information creates high search costs and lowers customers' ability to engage in the retail market. Discounted offers can also confuse customers because often the highest discounts don't necessarily lead to the lowest bills overall (because larger discounts can relate to higher underlying rates).

While online comparison tool make it easier for customers to compare offers and find the best deals, the AEMC has found that only one in 10 customers is aware of the Australian Government's energy comparison website energymadeeasy.gov.au.¹⁰ In addition, this website is of limited help to the 25% of customers with solar panels, as it does not factor in solar feed-in-tariffs or meter charging into its bill calculations.

1.4.3 Retailers, third parties, and government can take measures to improve customer engagement

To ensure competition continues to develop and deliver better outcomes for customers, retailers need to more actively engage with customers. For example, they need to better help them navigate their market offers effectively and better tailor products and services to their needs.

There is an opportunity for third parties to provide services to help customers find the best offers for their circumstances. For example, for several years the AEMC has made recommendations to make it easier for customers to be given access to their consumption data, which could be provided to third-party services and be used to identify the best offers on behalf of that customer.¹¹

Governments can also help enhance competition by improving customer engagement with the market. By assisting those customers who find it difficult to participate in the retail

⁸ Oxera, *Behavioural insights into Australian retail energy markets – Report for the Australian Energy Market Commission*, 11 March 2016, p 27.

⁹ That is, they remain on standing offers.

¹⁰ Newgate Research, *Consumer research for 2016 nationwide Review of competition in retail energy markets*, June 2016, p 109.

¹¹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 18.

market, to search and switch to a lower offer would mean over time less customers would need to enter hardship programs.

For example, they can take measures to improve the tools available to help customers compare offers and switch retailers easily. We recommend that the AER's energymadeeasy.gov.au web comparison tool should be promoted and be improved. As noted above, the more well-informed and engaged customers are, the more pressure there is on retailers to offer competitive prices and services.

However more 'heavy-handed' options are likely to lead to less efficient outcomes over time, and take away options from customers. For example, reregulating retail prices is likely to reduce the level of engagement and activity in the market (as it is more likely to be seen as a default option for customers). While in the short term, this may lead to lower prices for less engaged customers, reduced activity in the demand-side of the market will lead to less vigorous competition on the supply-side. Over time this is likely to further entrench the market position of the incumbent retailers and dampen the incentives on them to offer lower prices and improve their services. This reduced competition is also likely to stifle the growing opportunities from new technologies to provide innovative energy options, limiting options for customers over the longer term.

1.4.4 Protections for caravan park residents

We are also recommending that the NSW Government investigate the most efficient method to provide electricity customers in residential caravan parks' embedded networks the same consumer protections as provided to customers that can participate in the competitive retail market.

There are around 20,000 caravan park residents in NSW that are being supplied by these private networks. These customers are charged for their electricity by their caravan park owner, rather than by a retailer. Unlike other customers, they are less able to participate in the market to change supplier if they are unhappy with the price they are paying or level of service they are receiving, and they do not have access to the Energy and Water Ombudsman (EWON) if they have a dispute about their bill or service. Many customers living in caravan parks are paying substantially more for their electricity than other customers, even though they are likely to be least able to afford it.

The Australian Energy Market Commission (AEMC) is currently undertaking a review of the regulatory arrangements for embedded networks, however many of the regulations that apply to these residents are state-based, and the AEMC does not have jurisdiction over these.

1.4.5 Retailers, third parties, governments also have a role in helping hardship customers

While competition will lead to the best outcomes for customers in general, one group of customers warrant special assistance. These are vulnerable customers including those in retailers' hardship programs.

We note that retailers are already required by law to have policies and programs for assisting these customers, and to notify them of appropriate government concession programs and appropriate financial counselling services. The AER approves retailers' hardship policies and monitors retailers' performance in implementing their customer hardship policies. The AER is currently conducting a review of retailers' hardship policies with a focus on consumer outcomes.

We found that most retailers have strategies for helping hardship customers to access lower prices. These strategies involve either switching customers who are in their hardship program to contracts with lower prices, or advising these customers that they would save money on their electricity bill if they changed plan. They also use a range of channels to make these customers aware of available rebates or more competitive offers. We will monitor outcomes for vulnerable customers and those in retailer hardship programs to assess whether retailers strategies are ensuring that these group of customers not paying more than they need to.

The NSW Government has also recently announced an Energy Bill Relief Package to help hardship customers that includes introducing penalties for retailers that do not move customers who receive its Low Income Household rebate to a better deal.¹²

1.5 Recent increases in gas prices also reflect changes in the costs of supply

We found that the changes in retail gas prices between June 2017 and July 2017 reflect changes in the underlying costs of supplying gas, and therefore are consistent with a competitive market.

The total cost of supplying gas in early 2017-18 increased by between 6.8% and 7.9% in Coastal NSW and between 12.5% and 20.9% in Country NSW compared to 2016-17.¹³ The main cost driver was higher wholesale gas prices, due to material changes in demand and supply conditions in eastern Australia.

1.6 List of draft findings and recommendations

Draft Findings

- 1 The average bill increase for residential customers in NSW was 14% in July 2017. For small business customers the typical bill increase was between 10 to 16%. These price increases reflect changes in the underlying costs of supplying customers, driven by increasing wholesale costs. 22
- 2 The average bill increase for residential customers in NSW since price deregulation is 2%. This is a real decrease in prices of 5% (once CPI is accounted for). 23

¹² NSW Government, *Energy bill relief package for households and small business*, 3 September, 2017, <https://www.nsw.gov.au/your-government/the-premier/media-releases-from-the-premier/energy-bill-relief-package-for-households-and-small-business/>, accessed 10 October 2017.

¹³ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 47; p 52.

3	The fixed proportion of residential customers' bills has increased by 15% and 22% between 2013-14 and 2017-18 (depending on network area), reflecting how retailers have chosen to recover their costs.	28
4	Standing offers for residential customers have increased by 10% since price deregulation.	33
5	There is evidence of rivalry between retailers and a large range of products and services available to customers. In our view this is consistent with a competitive retail market that is continuing to develop.	38
7	There are no substantial barriers for smaller retailers to enter the NSW electricity market.	42
8	The NSW Government use the National Energy Customer Framework if it requires additional measures to improve or promote customer engagement so as to minimise costs for customers and taxpayers.	58
9	IPART will review issues around the take up of digital meters as part of our 2018 review of the performance and competitiveness of the NSW retail electricity and gas markets.	67
10	The changes in retail gas prices between June and July 2017 reflect changes in the underlying costs of supply, and therefore are consistent with a competitive market.	74

Draft recommendations

1	The AER's energymadeeasy.gov.au web comparison tool should be promoted and be improved so it:	58
	– clearly displays tariff information, ensures tariff information is downloadable in a numeric format, and sets the default bill calculation period equal to a customers' bill period, and	58
	– incorporates the impact of the solar PV units on customer bills.	58
2	The NSW Government investigate the most efficient method to provide electricity customers in residential caravan parks embedded networks the same level of consumer protection as customers that can participate in the competitive electricity retail market.	60

1.7 How can stakeholders comment on this Draft Report?

We are inviting written submissions from stakeholders by 7 November 2017. Page iii at the front of this report provides information on how to make a submission. Late submissions may not be accepted.

We do not have a specific set of questions for stakeholders to comment on. Instead, we invite stakeholders to address any of our draft recommendations and findings, or provide details of additional information that is relevant to our assessment.

We will consider all the issues raised in submissions to our Draft Report, and provide a Final Report to the Minister by 30 November 2017.

1.8 What the rest of this report covers

The rest of this report explains our review and draft findings and recommendations in more detail. It is structured as follows:

- ▼ Chapter 2 outlines the context for the review, and the process and approach we used to reach of findings and recommendations
- ▼ Chapter 3 explains our analysis of the changes in electricity retail prices since price deregulation, including the most recent changes in 2017-18
- ▼ Chapter 4 discusses our findings on the level of rivalry between retailers and prices and the range of products currently in the market
- ▼ Chapter 5 analyses the structure of the market and the barriers to entry and expansion, and rivalry between retailers
- ▼ Chapter 6 presents our findings on customer engagement and activity
- ▼ Chapter 7 discusses what measures Government can take to further enhance competition
- ▼ Chapter 8 focuses on the strategies retailers are using to help hardship customers access lower prices
- ▼ Chapter 9 outlines the progress of the take up of digital meters
- ▼ Chapter 10 explains our findings on how gas prices and costs have changed in 2017-18.

The appendices provide supporting information.

2 Context, approach and process for this review

The NSW Government decided to remove retail electricity price regulation effective 1 July 2014.¹⁴ As part of this decision, it gave IPART a new role to monitor and report annually on competition in the retail electricity market.

This is our third annual report on the performance and competitiveness of the retail electricity market for residential and small business customers. Last year we found that competition for residential and small business customers in the NSW retail electricity market was working well, and that a detailed review of retail prices and profit margins was not necessary.¹⁵

This year, in response to a request from the Minister for Energy and Utilities (the Minister), we have also reviewed electricity and gas price movements into 2017-18, to advise on the drivers of price changes and whether these changes reflect efficient costs in a competitive market.

We also received a second request from the Minister to review retailers' publicly available customer policies, and to consult with retailers and report on their strategies to:

- ▼ deliver lower prices to hardship customers, and
- ▼ manage the timely delivery of digital meters, and communicate this to their customers.

The sections below explain the approach and process we used to perform our role as market monitor and respond to the Minister's additional requests, and then summarise recent developments in the retail electricity market that are relevant to our review.

2.1 Our approach to the review

Our market monitoring role is set out in the *National Energy Retail Law (NSW)* (the Act).¹⁶ The Act specifies the indicators we must have regard to when assessing the performance of the market for small customers, and the information we are able to have regard to.

To conduct the 2017 annual review, we used an analytical approach that ensures we address all the matters we are required to consider, and followed a review process that involved public consultation as well as analysis.

¹⁴ NSW Planning & Environment, Removal of electricity price regulation (deregulation), <http://www.resourcesandenergy.nsw.gov.au/energy-consumers/energy-sources/electricity/removal-of-electricity-price-regulation>, accessed 16 September 2016.

¹⁵ IPART, *Review of the performance and competitiveness of the retail electricity market in NSW - From 1 July 2014 to 30 June 2015 – Final Report*, November 2015, p 1.

¹⁶ *National Energy Retail Law (NSW)*, s 234A. IPART is prescribed by the NSW regulations as the Market Monitor for the purpose of Part 9A of the Act (*National Energy Retail Law (Adoption) Regulation 2013*, cl 8A).

The factors that we must report on that help us assess the performance of the market are set out in Table 2.1.¹⁷ These factors must be considered in combination – no single factor is conclusive in determining whether competition is effective.

Table 2.1 Factors that help us determine whether competition is effective

Factor we must report on	Location of analysis in Draft Report
The participation of small customers in the market and, if the Market Monitor thinks it appropriate, particular groups of small customers	Chapter 6,8
Prices of electricity for small customers in regional areas	Chapter 3,4
Any barriers to entry to or exit from, or expansion in the market	Chapter 5
The extent to which retailers are competing to attract and retain small customers	Chapter 4
Whether price movements and price and product diversity in the market are consistent with a competitive market	Chapter 3

Source: *National Energy Retail Law (NSW)*, s 234A (3).

We are also able to report on any other relevant matters in reviewing the competitiveness and performance of the market.¹⁸ However, in conducting our analysis, the Act limits the information we can consider to:

- ▼ information provided by the AEMC and the AER,
- ▼ any publicly available information, and
- ▼ information provided by a retailer with particulars of the number of market offer customers of the retailer, the market offer prices of those customers, the number of customers on each standing offer price offered by the retailer that has been publicly advertised and those standing offer prices.¹⁹

Because a large number of reviews into competition in the retail market have been recently undertaken or are currently underway, we have had regard to the key themes emerging from these reviews.²⁰ These are described in section 2.3 below.

Based on our assessment of competition, we are also required to report on whether a special review of retail prices and profit margins in the market is required, and if we are of the opinion that it is required, whether there are any actions needed to improve the competitiveness of the market.²¹

¹⁷ *National Energy Retail Law (NSW)*, s 234A (3). IPART is prescribed by the NSW regulations as the Market Monitor for the purpose of Part 9A of the Act (*National Energy Retail Law (Adoption) Regulation 2013*, cl 8A).

¹⁸ Section 234A (3) (h) of the *National Energy Retail Law (NSW)*.

¹⁹ Section 234A (7), (8) of the *National Energy Retail Law (NSW)*.

²⁰ Based on the publicly available reports, in accordance with Section 234A(7) of the *National Energy Retail Law (NSW)*.

²¹ Section 234A(3) (f) (g) of the *National Energy Retail Law (NSW)*.

2.1.1 Electricity and gas price movements in 2017-18

In response to the Minister's request (see Appendix B), we extended our assessment of electricity price movements beyond the reporting period (2016-17) to include the most recent price changes that have occurred. As price movements tend to occur once a year at 1 July, the period we examined was 1 July 2016 to 1 July 2017.

In addition, for the first time, the Minister asked us to assess whether the gas price increases into 2017-18 are consistent with a competitive retail market. The NSW Government deregulated gas prices on 1 July 2017. We will review the retail market for the first time next year after price deregulation has been in place for one year. Therefore our role this year in relation to the retail gas market will be limited to addressing the Minister's request.

To assist us in undertaking these tasks, we engaged Frontier Economics to examine the cost drivers behind the increases in retail electricity prices from July 2017, and quantify the reasonable overall price changes for an efficient retailer. If the price changes broadly reflect the changes in the underlying costs of supply, then we would consider that they are consistent with a competitive retail market.

2.1.2 Hardship customers

In response to the Minister's request to report specifically on hardship customers (Appendix C), we wrote to each of the retailers to ask them about their strategies to deliver lower prices to hardship customers, and what they are doing to make their customers' aware of the assistance available to them. We reported on the retailers' responses.²²

2.1.3 Delivery of digital meters

In response to the Minister's request to report on retailers' processes for managing the timely delivery of digital meters and communicating these processes to their customers, we wrote to each retailer seeking information on these matters. We then reported on their responses.²³

2.2 Our process for this review

In May 2017, we began our review process by releasing an Information Paper, inviting comment on our proposed approach for undertaking our review. We received nine submissions.

We are now inviting stakeholder submissions on this Draft Report. Submissions close on 7 November. Information on how to make a submission is provided on page iii of this report.

²² We have undertaken this review under section 234B of the *NSW National Energy Law (NSW)* in order to consider the information provided to us by retailers.

²³ We have undertaken this review under section 234B of the *NSW National Energy Law (NSW)* in order to consider the information provided to us by retailers.

We will consider all comments from stakeholders before making our Report to the Minister by 30 November 2017. The timetable and key milestones for our 2017 annual report are summarised in Table 2.2.

Table 2.2 Review timetable

Milestone	
Release Information Paper	23 May 2017
Submissions close on information paper	30 June 2017
Release Draft Report	17 October 2017
Submissions close on Draft Report	7 November 2017
Provide Final Report to the Minister	November 2017

2.3 Recent developments in retail energy market

Each year the AEMC conducts reviews of the competitiveness of the retail energy market, and investigates price trends. However, recent events over the last 12 months, has meant that multiple other reviews have been undertaken or are currently underway.

These events include the reliability incidents in South Australia, tightening of generation capacity over the summer months and forecast generation shortages. Around July 2017 retailers announced large increases in both electricity and gas prices – primarily driven by increases in wholesale costs.

The most relevant recent reviews of the energy retail market are outlined below.

2.3.1 The AEMC competition review

The AEMC conducts annual reviews of competition in retail energy markets, both in NSW and other jurisdictions. The latest review concluded in June 2017 and found that competition continues to be effective in the NSW retail electricity market, with some signs of increasing competition since prices were deregulated in 2014.²⁴ The AEMC undertakes surveys of energy customers and retailers as part of its review. We refer to these surveys in various sections of this report.

2.3.2 The ACCC's Inquiry into the competitiveness of retail electricity markets within the NEM

On 27 March the Australian Competition and Consumer Commission (ACCC) was directed by the Federal Government to hold an inquiry into the retail supply of electricity and the competitiveness of electricity retail sector across the National Electricity Market.

The Inquiry will look at the drivers of retail electricity prices over time, including factors at all levels of the supply chain that may affect price, and whether there are options to address price impacts on customers. The Inquiry will consider what can be done to improve the experience of customers in acquiring electricity services. The Inquiry will also examine the

²⁴ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 235.

industry structure, the nature of competition, the representation of prices to customers and any other factors influencing the price of retail electricity services.

The ACCC's Preliminary Report was released on 16 October 2017.

2.3.3 The Independent Review into the Future Security of the National Electricity Market (Finkel review)

In October 2016 the COAG Energy Council commissioned an independent review to examine the current state of the security and reliability of the national electricity market and provide advice to governments on a coordinated, national reform blueprint.

The Final Report released on 9 June 2017 made 50 recommendations to ensure the future security of the National Electricity Market focusing on increasing security, future reliability, better system planning and stronger governance arrangements in the market. The review found that security and reliability had been compromised by poorly integrated variable renewable electricity generators, including wind and solar. This has coincided with the unplanned withdrawal of older coal and gas-fired generators.²⁵

2.3.4 The Independent Review into the Electricity and Gas Retail Markets in Victoria

In November 2016 the Victorian Government commissioned an independent review of its energy markets. The final report provided to the Victorian Government in August 2017 recommended that retailers be required to provide a Basic Service Offer with the maximum price to be regulated by the Essential Service Commission (ESC). The review also concluded that:

- ▼ the retail cost component (including margin) was higher than any other individual cost component, and therefore competition has added additional costs to the market that have not been offset with cost reductions or other benefits and these costs need to be recovered from consumers, and ²⁶
- ▼ market practices such as confusing discounting and retailers not engaging with their customers are leading to poor outcomes to customers.

In response to these findings, the Australian Energy Council²⁷ released a report it commissioned by consultants Oakley Greenwood in September 2017 that found the analysis relied upon on retail costs is likely to be out by a factor of at least 30%.²⁸ However, the Council considered that retailers need to do more to engage with customers and make energy bills easier to understand. We consider issues around engaging customers in Chapter 6.

²⁵ *Independent review into the future security of the National Electricity Market*, 9 June 2017, p 5, 21-27.

²⁶ *Independent Review into the Electricity and Gas Retail Markets in Victoria*, August 2017, p ix.

²⁷ The Australian Energy Council represents 21 major electricity and downstream natural gas businesses operating in competitive wholesale and retail energy markets

²⁸ Oakley Greenwood, *Review of the Thwaites Report and Associated Research*, 19 September 2017, p 2.

2.3.5 NSW Government assistance package

In September 2017 the NSW Government announced that energy rebates would increase by 20 per cent and energy retailers would not be able to charge customers early termination fees, paper bill fees and fees for paying over the counter at Australia Post.²⁹

2.3.6 The Australian gas reservation mechanism

On 20 June 2017, the Federal Government announced that it would implement the Australian Domestic Gas Security Mechanism (ADGSM).

The objective of the ADGSM is to ensure there is a sufficient supply of natural gas to meet the forecast needs of Australian consumers by requiring, if necessary, LNG projects which are drawing gas from the domestic market to limit exports or find offsetting sources of new gas.

²⁹ Gladys Berejiklian, Premier of NSW, *Energy Bill Relief Package for Households and Small Business*, 3 September 2017, http://www.resourcesandenergy.nsw.gov.au/__data/assets/pdf_file/0011/734843/Energy-bill-relief-package-for-households-and-small-business.pdf, accessed 9 October 2017.

3 Changes in electricity retail prices reflect the costs of supply

As Chapter 2 discussed, for this review we extended our assessment of whether the movements in electricity retail prices in 2016-17 are consistent with a competitive retail market to include the most recent changes at start of 2017-18. To provide a bigger picture view, we also looked at all price movements for residential and small business customers since 2013-14, just before prices were deregulated.

In a competitive market, we would expect that price changes broadly reflect changes in the underlying market costs of supplying electricity (see Box 3.1). Therefore, to make our assessment we analysed the changes in the costs of supply to identify the key drivers of the changes in retail prices. In addition, we looked specifically at changes in prices and costs in regional areas, and in fixed and variable price and cost components.

The sections below provide an overview of our draft findings, and then discuss these findings in more detail.

3.1 Overview of draft findings

We estimate that the average retail electricity prices for residential customers increased by 14% in the period from 1 July 2016 to 1 July 2017 (ie, in 2016-17 and the start of 2017-18). For small business customers the typical annual bill increased by between 10% to 16% for the same period³⁰. This increase reflected the change in the cost of supplying electricity, which was primarily driven by wholesale cost increases, which have more than doubled since 2015-16. Therefore, the recent changes in electricity retail prices were consistent with a competitive retail market.

We also found that the average annual residential customer bill at the start of 2017-18 was likely to be at a similar level as in 2013-14. In the period since prices were deregulated, we estimate that the average annual bill for residential customers has increased by just 2% in nominal terms, which is equal to a reduction of 5% in real terms (ie, after adjusting for inflation). This is because the recent increases in wholesale costs were largely offset by decreases in network costs and green scheme costs in 2014-15 and 2015-16.

In regional areas, we found average retail prices for residential customers were higher than in metropolitan areas in 2016-17 and into 2017-18. This reflects the higher costs of supply. However, the difference in prices between regional and metropolitan areas has reduced over the longer term.

³⁰ The increases for small business customers are based on retail prices from the Big 3 retailers (AGL, EnergyAustralia and Origin) for their most common offers.

Box 3.1 Customers' bills are made up of a number of different cost components

Customers' bill are made up of different cost components:

- ▼ Wholesale electricity purchased through the National Electricity Market (NEM).
- ▼ The network costs, which are the regulated costs of transporting electricity from the generators to customers via the transmission and distribution networks, and are set by the Australian Energy Regulator (AER).
- ▼ The cost of meeting 'green scheme' obligations including the:
 - Commonwealth Renewable Energy Target (RET), which requires retailers to purchase:
 - 33,000 gigawatts of additional renewable electricity from renewable energy power stations, such as wind and solar farms, or hydro-electric power stations, under the (Large-scale Renewable Energy Target (LRET)), and
 - Small-scale technology certificates created under the Small-scale Renewable Energy Scheme (SRES)) created by small scale systems, including solar photovoltaic (PV) panels and other small generation systems.
 - NSW Energy Savings Scheme (ESS), which requires retailers to purchase and surrender a certain number of Energy Savings Certificates (ESCs) representing energy savings.
- ▼ Retail costs and margin which retailers incur in performing their retail functions. These costs include customer service (eg, operating call centres), billing and collecting revenue, finance, IT systems, regulatory compliance costs, energy trading costs, marketing costs and an appropriate allocation of corporate overheads. Retailers face a range of risks in supplying electricity, including variations in customer demand and economic conditions, and the retail margins also reflect these risks.

Source: Frontier Economics, *Cost Drivers of Recent Retail Electricity and Gas Prices for Residential Customers in NSW – A Report Prepared for IPART*, September 2017, p 7, Clean Energy Regulator, How the scheme works in *Renewable Energy Target*, 29 March 2017 <http://www.cleanenergyregulator.gov.au/RET/About-the-Renewable-Energy-Target/How-the-scheme-works>, accessed 10 October 2017, IPART, How the scheme works in *Energy Savings Scheme*, http://www.ess.nsw.gov.au/How_the_scheme_works, accessed 10 October 2017.

3.2 Recent price changes were consistent with a competitive retail market

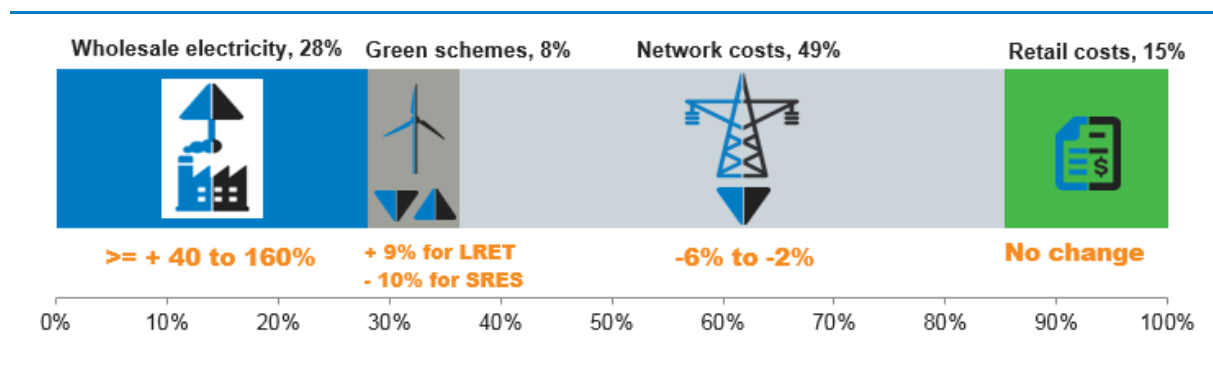
To assess price changes from 1 July 2016 to 1 July 2017, we requested information on retailers' prices for residential and small business customers in each network area in NSW. We used these prices to estimate indicative bills for residential and small business customers. This means our approach provides a snapshot of prices and typical bills implied by these prices as at July 2016 and July 2017. We consider that this information provides an indication of how prices for most customers changed during this reporting period.

We engaged economic consultants Frontier Economics (Frontier) to examine the cost drivers behind the increases in retail electricity prices from July 2017, and quantify the reasonable overall price changes for an efficient retailer. If the price changes broadly reflect the changes in the underlying costs of supply, then we would consider that they are consistent with a competitive retail market.

Frontier has estimated that the overall costs of supply have increased by between 14% and 40%.³¹ As mentioned above, the main driver of the increases in costs is the wholesale price of electricity, which is likely to have more than doubled this year, and now is likely to make up around 40% of customers' bills, up from around 28% in 2016-17. As a result, and because network costs have gone down slightly (-6% to -2%), the proportion of network charges of a residential customer bills has fallen from around 49% to 40% in 2017-18.

Figure 3.1 summarises Frontier's findings, taking the 2016-17 cost proportions as the base year. Frontier's methodology is explained in its Draft Report, and is available on our website.

Figure 3.1 Change in residential electricity costs in 2017-18 based on Frontier's 2016-17 proportion of bills costs



Note: The range for the wholesale cost increases is very large because it includes estimates from three different estimation methods. For more information, see page 15 of Frontier's report.

Data source: Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, pp 9, 15, 21, 26, 30-31.

3.2.1 Wholesale prices have increased

In analysing wholesale electricity costs, Frontier focused on the following two key possible drivers of changes in wholesale energy costs, which are:

- ▼ **Changes in load shape:** Frontier analysed data on the net system load profile for NSW over the last 10 years. Frontier concluded that there is no strong evidence that suggests higher wholesale energy costs are driven by changes in load shape.
- ▼ **Changes in spot and contract electricity prices:** Frontier analysed the difference in wholesale electricity prices in 2016-17 and 2017-18, and assessed what this would mean for the change in wholesale energy costs. Frontier estimated that the change in wholesale energy costs was between 40% and 160%.³²

This large increase in wholesale costs reflects recent retirements of a number of generators. NSW Generators that have closed are Munmorah, Wallerawang C, Redbank and Smithfield. Most recently, Hazelwood, a coal-fired power station in Victoria (which supplied around 20% of Victoria's electricity) closed. Since NSW is connected to the National Electricity

³¹ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, p 33.

³² Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 15.

Market (NEM), events that take place in other states such as power station closures may flow through to affect prices in NSW and other regions in the NEM.

The retirement of coal-fired power stations has meant that higher marginal cost generation plants – in particular gas fired plants – have been setting the market clearing price more often. This is at the same time as gas prices have increased.

The ACCC inquiry into electricity supply and prices is currently examining issues associated with the wholesale market. This includes all wholesale market price, cost and conduct issues and the extent and impact of vertical integration. Findings and recommendations from this inquiry may have implications for future wholesale costs.

In a well-functioning market, higher prices provide a signal to the market to invest in new generation capacity. While new renewables are being built after a period of uncertainty around the renewable energy target (RET), investors have been reluctant to invest in other types of generation due to an extended period of policy uncertainty. Power stations are long-lived assets, and the policy settings around subsidies, government investment in the energy market, and carbon polices can have large impacts on whether investment in generation assets would be profitable over the life of the asset. In the current environment this makes them risky investments for commercial investors.³³

3.2.2 Green scheme costs

To estimate the costs of complying with green schemes, Frontier used a similar approach to that used to estimate changes in wholesale electricity costs. However, since there are no reliable forward prices for green schemes, Frontier used actual spot prices of large scale generation certificates (LGCs) and small-scale technology certificates (STCs) as a proxy for expected certificate prices.

The estimated change to green scheme costs is between -10% and 60%. The change in the cost of complying with the Small-scale Renewable Energy Scheme (SRES) is fairly consistent across the methods used to estimate costs, with a decrease in the cost of complying of around 10%. However, the change in the cost of complying with the Large-scale Renewable Energy Target (LRET) varies depending on the method of estimation used. A current point in time estimate suggests that the change in green costs has increased by less than 10%, while a two-year rolling average suggests a 60% increase.³⁴

Frontier provided possible reasons for the increase in LGC prices from 2015-16 to 2016-17. While large retailers typically obtain the majority of their LGCs through long term agreements such as power purchasing agreements with wind generators, some businesses facing a shortage of LGCs may be acquiring LGCs through the spot market instead, placing upward pressure on LGC spot prices. In addition, there may have been delays in renewable investments in recent years driven by policy uncertainty and this may be reflected in higher spot prices.

³³ *Independent review into the future security of the National Electricity Market*, 9 June 2017, p 29.

³⁴ *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, p 26.

3.2.3 Network costs have decreased

Retailers incur network costs to supply electricity to retail customers. These costs include payments for the use of the transmission and distribution network, which are passed through to customers. We estimate that for 2017-18, network costs make up around 40% of the average customer's total bill.

Frontier calculated the costs incurred by retailers in supplying a typical small retail residential customer in NSW based on the 2015-16 and 2016-17 network prices published by Ausgrid, Endeavour Energy and Essential Energy. Frontier estimated that across the three network areas, network tariffs that for a typical residential customer, network costs fell slightly (between 2% and 6%).³⁵

3.2.4 Retail costs and margin

Retailers incur retail operating costs in supplying electricity to small retail customers. These are the costs that a retailer incurs in supplying electricity to its customers and covering its retail margin. Retail operating costs and retail margins account for a comparatively small portion of the total costs incurred by a retail business.

Frontier notes that there is no clear evidence that retail operating costs and retail margins have changed materially over recent years. They also note there is no publicly available information about how these would likely change from 2016-17 to 2017-18.³⁶ Therefore it has estimated that the retailer operating costs of supplying customers has stayed fairly constant at around \$121 per customer, and the retail margin remains at around 6%.³⁷

However, we note that the ACCC Retail Electricity Pricing Inquiry has found that retail margins in NSW are likely to have increased to around 8% in 2015-16. In addition, they report retail costs of \$235 in 2015-16.³⁸

We do not consider that it is necessary for IPART to undertake a further review of retail costs and margins while the ACCC is undertaking its detailed review.³⁹

Finding

- 1 The average bill increase for residential customers in NSW was 14% in July 2017. For small business customers the typical bill increase was between 10 to 16%. These price increases reflect changes in the underlying costs of supplying customers, driven by increasing wholesale costs.

³⁵ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 31.

³⁶ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, p 31.

³⁷ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, p 8.

³⁸ ACCC, *Retail Electricity Pricing Inquiry: Preliminary Report*, 16 October 2017, pp 39, 43, <https://www.accc.gov.au/publications/accc-retail-electricity-pricing-inquiry-preliminary-report>, accessed 16 October 2017.

³⁹ ACCC, *Electricity supply & prices inquiry*, <https://www.accc.gov.au/regulated-infrastructure/energy/electricity-supply-prices-inquiry>, accessed 16 October 2017.

3.3 Average annual bills for residential customers are at similar levels to 2013-14

The average annual bill paid by residential customers in NSW is currently around \$2,200, for 6,500 kWh of energy usage.

Over the period since price deregulation, we estimate that the average residential bill across NSW has gone up by an average of 2% (Table 3.1). This represents a 5% reduction in bills in real terms. For a typical residential customer using 6,500 kWh, this represents a \$40 increase in customers' bills (or a reduction of \$127 in real terms). Box 3.2 explains how we estimated the average bill across NSW.

Table 3.1 Changes in residential customer bills over time (6,500 kWh, nominal, GST-inclusive, average across all distribution areas)

	July 2013	July 2014	July 2015	July 2016	July 2017	Cumulative
Weighted average typical bill (nominal)	\$2,182	\$2,175	\$1,840	\$1,954	\$2,223	\$40
Price change (nominal)		-0.4%	-15%	6%	14%	2%
Weighted average typical bill (real)	\$2,350	\$2,273	\$1,895	\$1,992	\$2,223	-\$127
Price change (real)		-3%	-17%	5%	12%	-5%

Source: Price information provided by retailers

The contribution that the different costs of supply have made to residential customers' bills have also fluctuated over time (Figure 3.2).

Wholesale costs have risen substantially over the past two years (growing from 20% of costs in 2013-14 (exclusive of carbon) to around 40% in 2017-18). However, network prices have fallen substantially, largely offsetting this increase in wholesale costs. The network cost component now makes up around 40% of customers' bills on average, down from 55% in 2013-14. In 2014-15, the carbon tax was also repealed (which added 9% to bills when it was introduced in 2012).⁴⁰

We note that this price trend may be different in each state. While declining network tariffs has been observed in most jurisdictions in recent years⁴¹, the reductions have been larger in some states compared to others.⁴²

Finding

- The average bill increase for residential customers in NSW since price deregulation is 2%. This is a real decrease in prices of 5% (once CPI is accounted for).

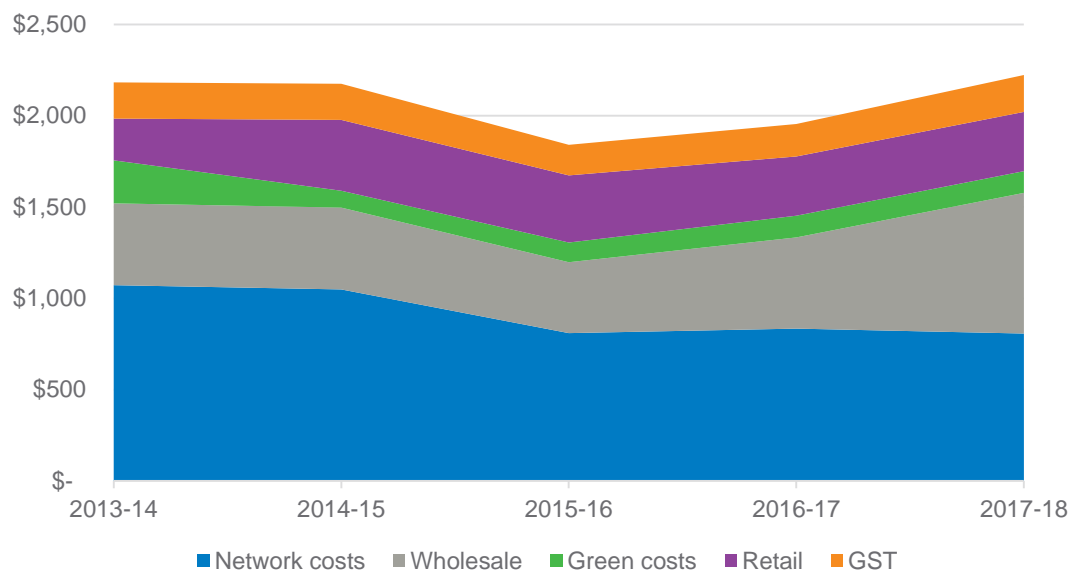
⁴⁰ IPART, Review of regulated retail price and charges for electricity from 1 July 2013 to 30 June 2016, Final Report, June 2013, p 18.

https://www.ipart.nsw.gov.au/files/sharedassets/website/trimholdingbay/final_report_-_review_of_regulated_retail_prices_for_electricity_-_from_1_july_2013_to_30_june_2016.pdf

⁴¹ AER, State of the Energy Market, May 2017, p 130, <https://www.aer.gov.au/system/files/AER%20State%20of%20the%20energy%20market%202017%20-%20A4.pdf>, accessed 13 October 2017.

⁴² AER, State of the Energy Market, May 2017, p 130, <https://www.aer.gov.au/system/files/AER%20State%20of%20the%20energy%20market%202017%20-%20A4.pdf>, accessed 13 October 2017.

Figure 3.2 Estimated change in residential bills and costs since price deregulation (6,500 kWh, nominal, GST-inclusive, average across all distribution areas)



Data source: Based on price information provided by retailers, Frontier Economics, *Cost Drivers of Recent Retail Electricity and Gas Prices for Residential Customers in NSW – A Report Prepared for IPART*, September 2017, pp 9-10, AEMC, *2015 Residential Electricity Price Trends Final Report*, 23 February 2017, p 113, ACCC, *Retail Electricity Pricing Inquiry: Preliminary Report*, 16 October 2017, p 43.

Box 3.2 How we estimated the average residential bill across NSW in each year

Retailers have provided us with their prices for their residential standing offers, their most common offers, and their lowest offers. We also have information on the number of customers with each retailer, and the number of customers' on standing and market offers. However, we do not have information on the prices of every offer in the market, or the number of customers on each. Therefore, when estimating the average residential bill paid by NSW customers, we have had to make a number of assumptions about the number of people paying different prices.

We estimated the average bill for the typical residential consumer by weighting prices by the number of customers on standing and market offers, by retailer, and by the number of customers in each network area, for each year.

For each network area:

1. For customers on standing offers we use the standing offer prices for each retailer's market share (applying the NSW-wide retail market share to each network area) to estimate annual bills.
2. For customers on market offers, we weighted prices by retailers' market shares and we allocated customers to either retailers' lowest offer, their most common offer, or an offer between the most common offer and the standing offer as follows:
 - ▼ 10% are allocated to retailers' lowest offer (and applying the full value of any unconditional and conditional discounts)
 - ▼ 30% are allocated to the most common offer (and applying the full value of any unconditional and conditional discounts).
 - ▼ The remaining customers are allocated to a price equal to the mid-point between the lowest and standing offer prices. This is to account for the range of other offers in the market between the most common offer and the standing offer.

To estimate the average residential bills across NSW, we then weighted the average price for each network area by the proportion of customers in each network area (42% in Ausgrid, 26% in Essential, and 31% in the Endeavour network area).

We consider that these assumptions provide a reasonable estimate of the average residential bill paid across NSW. We tested a range of different assumptions and they led to very similar estimates of average bills. However, we are seeking feedback on this methodology for our Final Report.

3.3.1 The difference between regional and metropolitan electricity residential bills has reduced

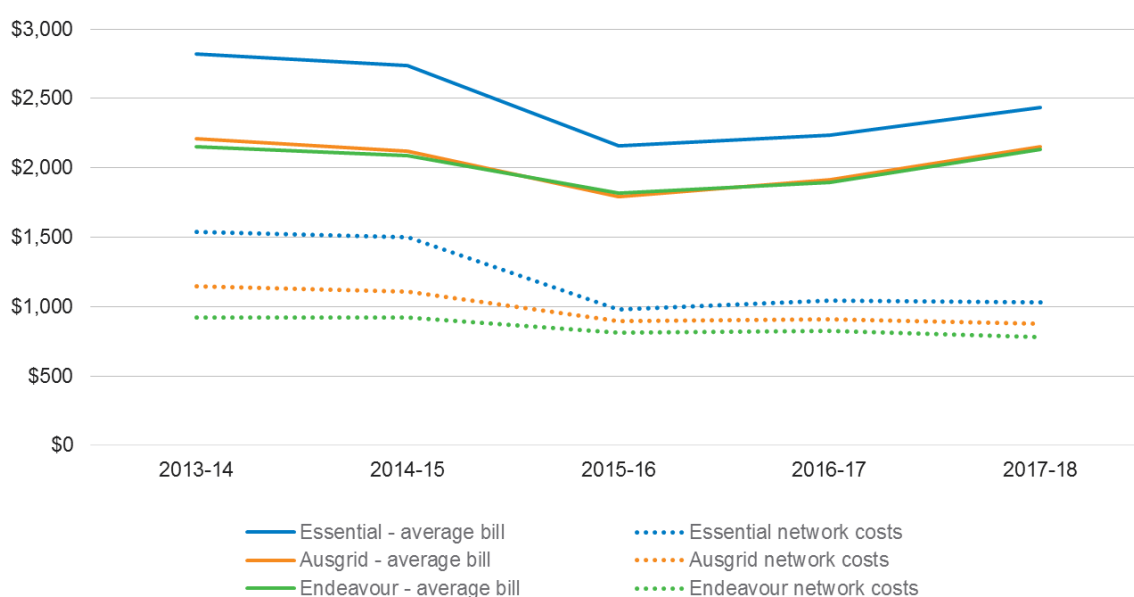
Figure 3.3 shows residential customers' bills and network tariffs by network area. The Ausgrid network supplies most of the Sydney and Newcastle customers, while the Endeavour network supplies customers in South-western Sydney and Wollongong. In our analysis we assume that these customers are in metropolitan areas. The Essential network supplies the remainder of the state, and we consider it to be regional.

We found that for the same level of consumption, residential bills in regional areas remain higher than in metropolitan areas. This is because network costs are currently around 20% higher in regional areas (down from 50% higher in 2013-14).

However, the difference in the residential bills between regional and metropolitan areas has reduced over time. In 2017-18, the average total retail residential bill in regional areas is around 15% higher than in metropolitan areas, compared to 30% higher in 2013-14.

This convergence of residential bills between regional and metropolitan areas is largely due to more substantial network cost reductions in the regional network (Essential), compared to the other networks. On 1 July 2015, network prices for residential customers fell by 12% (Endeavour), 19% (Ausgrid) and 35% (Essential) for residential customers compared to 2014-15.

Figure 3.3 Change in the network costs compared to average retail costs for residential customers by network area (6,500 kWh, nominal, GST-inclusive)



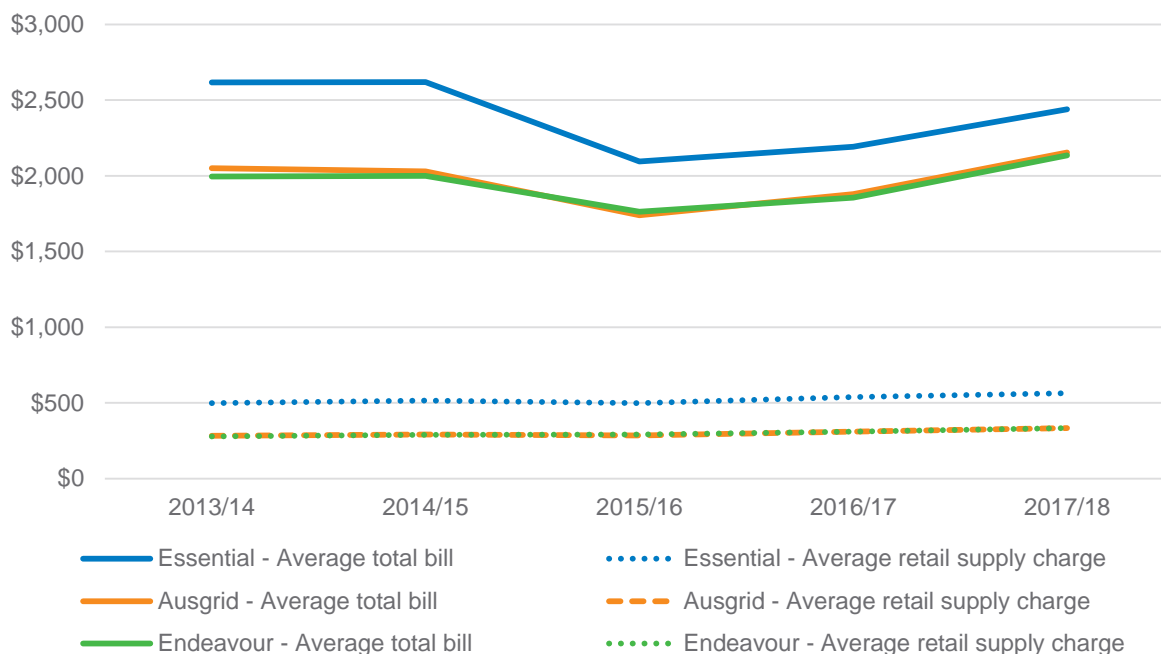
Data source: Information from retailers, network price data.

3.4 The fixed portion of residential bills has increased over time

As well as looking at the total increase in residential customer bills, stakeholders have also asked us to look at the individual bill components. This is because they are concerned that the fixed bill component has risen over time. Unlike consumption charges, customers cannot change this portion of their bill by reducing their electricity usage.

While we have found that residential customer’s total bills have remained at similar levels since 2013-14, the fixed proportion of residential customers’ bills has gone up by around \$50 to \$70, or 18% in the same period (Figure 3.4).

Figure 3.4 Change in the average fixed bill component over time, compared to average total bills for residential customers (6,500 kWh, nominal, GST-inclusive)



Data source: Retail price data.

The main fixed costs components of residential customers' bills are a portion of the network costs, and retail costs. Around 15-30% of residential network charges are fixed (Figure 3.5), while almost all of the retail component is fixed (because billing and marketing costs are the same regardless of how much electricity a customer uses).

The \$50-\$70 increase in the fixed retail bill component does not reflect the change in the fixed network charges, which have fallen by an average of \$14, or 7% (Figure 3.4). Frontier also estimates that there has been little change in the fixed component of retail prices as part of the recent price increases.⁴³

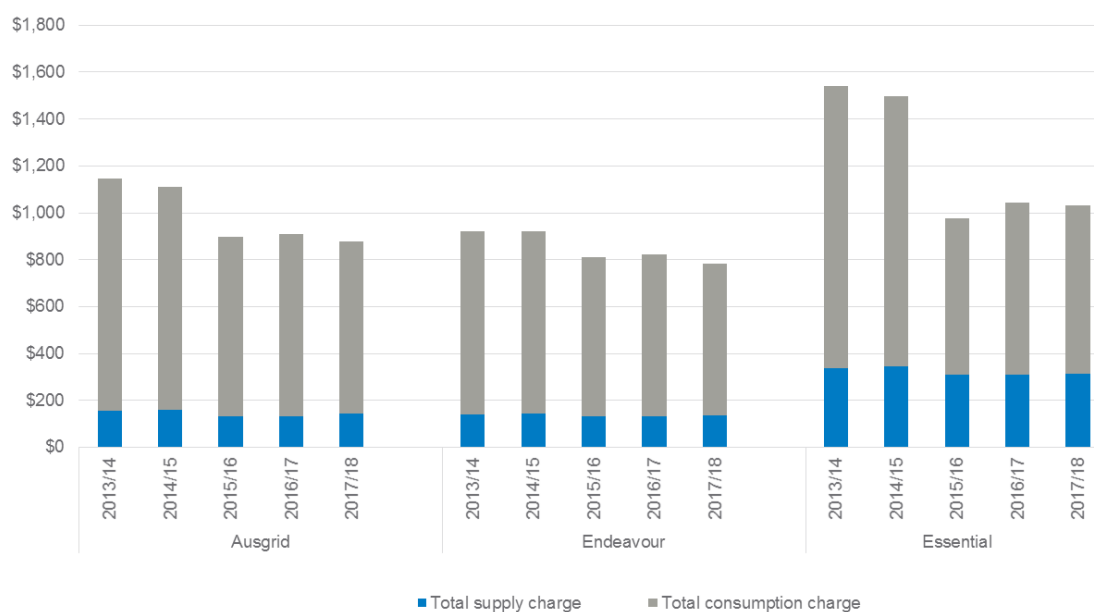
As discussed above, the increase in total costs is primarily a result of increases in wholesale electricity costs. Wholesale electricity costs would typically be considered variable costs and so would be expected to be reflected in an increase in the variable component of retail prices, rather than the fixed component.

However, retailers have discretion over how they recover their costs from retail tariffs. Frontier notes that some retailers may consider the measures they take to manage the risk of wholesale electricity price volatility may represent a fixed cost because many of these arrangements involve capital investments or take or pay contracts.⁴⁴

⁴³ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 33.

⁴⁴ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 34.

Figure 3.5 Change in residential network costs over time, by fixed and consumption charges (6,500 kWh, nominal, GST-inclusive)



Data source: Ausgrid, *Price Lists and Policy*, <http://www.ausgrid.com.au/Common/Industry/Regulation/Network-prices/Price-lists-and-policy.aspx#.Wd4h7FuCzGg>, accessed 12 October 2017, Endeavour Energy, *Our prices*, <http://www.endeavourenergy.com.au>, accessed 11 October 2017, Essential Energy, *Electricity Network Pricing*, <https://www.essentialenergy.com.au/content/Electricity-Network-Pricing-And-Information>, accessed 12 October 2017.

We note that while fixed network charges for residential customers have fallen slightly over the past few years, a new National Energy Rule will result in a larger proportion of network costs being recovered from fixed charges⁴⁵, as network tariffs become more cost reflective. These changes are being phased in from 1 July 2017.⁴⁶

As explained above, the fixed proportion of network charges for residential customers is currently around 16% for metropolitan customers, and 30% for regional customers. Ausgrid has recently consulted on increasing the fixed component from around 16% to 50% or more, and reducing the consumption charges.⁴⁷

Finding

- The fixed proportion of residential customers' bills has increased by 15% and 22% between 2013-14 and 2017-18 (depending on network area), reflecting how retailers have chosen to recover their costs.

⁴⁵ For example, see Ausgrid, *Revised Tariff Structure Statement*, October 2016, p 5 <http://www.ausgrid.com.au/-/media/Files/Industry/Regulation/Network-prices/Amended-Revised-TSS--22-Feb-2017FINAL--AER-amendment--CLEAN.pdf?la=en&hash=6D0913C0330F1E6DBD3D57061634794879EEC0BF>, accessed 15 October 2017.

⁴⁶ AEMC, *Distribution Network Pricing Arrangements*, <http://www.aemc.gov.au/Rule-Changes/Distribution-Network-Pricing-Arrangements#>, accessed 12 October 2017.

⁴⁷ Ausgrid, "The 'Customers at the Centre' Project – Results, Impacts & Implications" in *Presentation of results (by Newgate) and Ausgrid's response (Catherine O'Neill) followed by Q&A/stakeholder discussion*, 12 September 2017, p 3.

3.3 Typical annual bills for small business customers

The typical annual bill paid by small business customers in NSW is currently between \$2,826 (in the Endeavour network) and \$4,753 (in the Essential Energy network) for 10,000 kWh of energy usage. We estimated that for a typical small business customer, retail prices for electricity increased by between 10% to 16% for the period from 1 July 2016 to 1 July 2017 (depending on which network area the business is located in) (Table 3.2).⁴⁸

Table 3.2 Typical bills for small business customers (10,000 kWh, nominal, GST-inclusive, based on offers of the Big 3 retailers)

Network	2013-14 – Regulated tariff	Offer type	2014-15	2015-16	2016-17	2017-18	Change 1 July 17
Ausgrid	\$3,374	Lowest	\$2,788	\$2,696	\$3,100	\$3,585	16%
		Most common	\$2,841	\$2,799	\$3,124	\$3,620	16%
		Standing	\$3,238	\$3,165	\$3,727	\$4,462	20%
Endeavour	\$2,993	Lowest	\$2,328	\$2,219	\$2,432	\$2,826	16%
		Most Common	\$2,462	\$2,368	\$2,453	\$2,855	16%
		Standing	\$2,771	\$2,720	\$2,993	\$3,564	19%
Essential	\$4,567	Lowest	\$3,763	\$3,091	\$3,397	\$3,796	12%
		Most Common	\$3,924	\$3,141	\$3,491	\$3,834	10%
		Standing	\$4,395	\$3,770	\$4,158	\$4,753	14%

Source: Information provided by retailers.

Over the period since price deregulation, the bill for a typical Ausgrid small business customer has increased by 7%, and reduced by 5% for small business customers in the Endeavour network (comparing the most common offers currently in the market to the regulated prices in 2013-14). For small business customers in the Essential Energy network area, the typical bill has reduced by around 16% - driven mainly by large reductions in network charges. Table 3.3 shows that this represents an annual reduction in bills of \$733 for a typical small business customer using 10,000 kWh (or a reduction of \$1,084 in real terms).

Table 3.3 Typical bills for small business customers (10,000 kWh, nominal, GST-inclusive, based on offers of the Big 3 retailers)

Network	2013-14 – Regulated tariff	2017-18 most common offer	Change (\$)	Change (%)
Ausgrid	\$3,374	\$3,620	\$246	7%
Endeavour	\$2,993	\$2,855	-\$138	-5%
Essential	\$4,567	\$3,834	-\$733	-16%

⁴⁸ This is based on the most common offers from AGL, EnergyAustralia and Origin Energy. We note that standing offers in the Ausgrid and Endeavour network areas have increased by 19-20%.

4 Retailers are competing to attract and retain customers

One of the characteristics of a competitive market is strong rivalry between retailers. Where this rivalry exists, retailers attempt to outcompete each other by making more attractive market offers and differentiating their products and services to target different customers' needs.

To assess the level of rivalry between retailers in 2016-17, we examined the range of market offers, products and services available to small customers in NSW, compared to previous years. We also looked at retailers' standing offers, and compared average prices under these offers to those under market offers. The sections below outline our draft findings, and then discuss them in more detail.

4.1 Overview of draft findings

We have found that there is evidence of rivalry between retailers, who are competing on price, products and services. In our view, this is consistent with a competitive retail market that is continuing to develop.

We also found that market offers are becoming increasingly varied. While the lowest market offers are similar to 2013-14 levels before prices were deregulated, standing offers for residential customers have increased by around 10% during this period. This has meant that the gap between the cheapest available offers and the standing offers has increased substantially. For small business customers, standing offers have increased by between 12% over the period.

Product differentiation has continued to increase over the last year. This includes bundling products and services, predictability in billing, transparency in pricing, convenience and control over household usage and renewable energy.

Renewable energy options⁴⁹ and price-based incentives are also continuing to be used to attract customers (for example, bill credits for switching or referring friends who then sign up with the retailer,⁵⁰ pay on time discounts, and predictable billing).

4.2 Prices indicate competition between retailers

Price is the most common way that retailers attract and retain customers. Because customers respond to prices differently, ie, have different demand elasticities, there will inevitably be

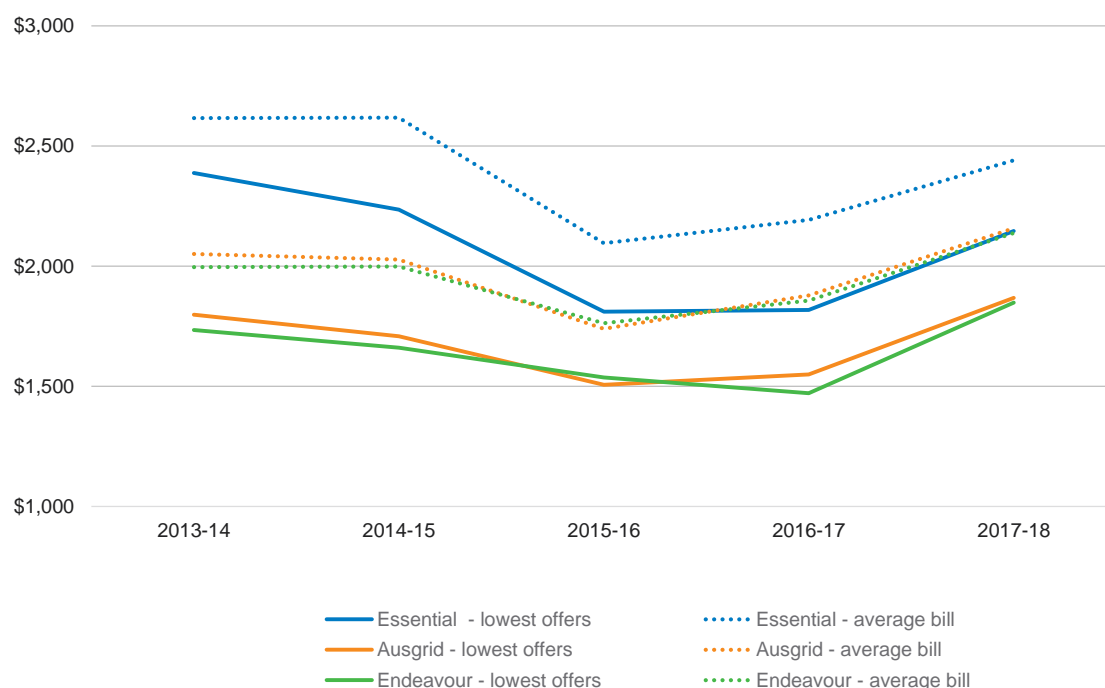
⁴⁹ For example, see EnergyAustralia's offer of carbon neutral electricity, and Enova Energy's 100% Green power offer. <https://www.energyaustralia.com.au/>, accessed 5 September 2017. <http://www.enovaenergy.com.au/about-us/>, accessed 5 September 2017.

⁵⁰ Diamond Energy, *Refer a friend and both receive \$35 credit!*, <http://diamondenergy.com.au/diamond-referral/>, accessed 4 September 2017.

price differentials in the market. We consider price variation is consistent with a competitive retail market, and supports innovation and dynamic efficiency.

We have found that the **cheapest offers** in the market are the same as those available before price deregulation, which is a 7% reduction in real terms. However, this change varies between networks, from a 10% reduction in the Essential Energy network, to a 4% and 7% increase in the Ausgrid and Endeavour networks respectively (real reductions of 17%, 4% and 1% once inflation is accounted for) (Figure 4.1). For small business customers we found similar outcomes.

Figure 4.1 Change in cheapest and average residential offers over time by network area (6,500 kWh, nominal, GST-inclusive)

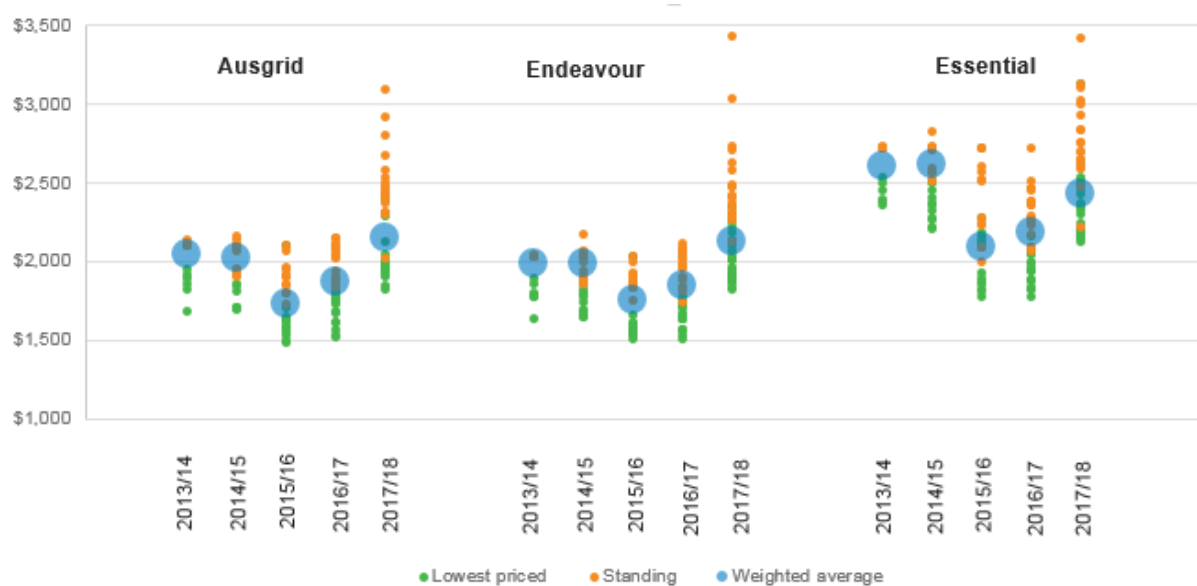


Data source: Information from retailers

4.2.1 Prices have become increasingly varied

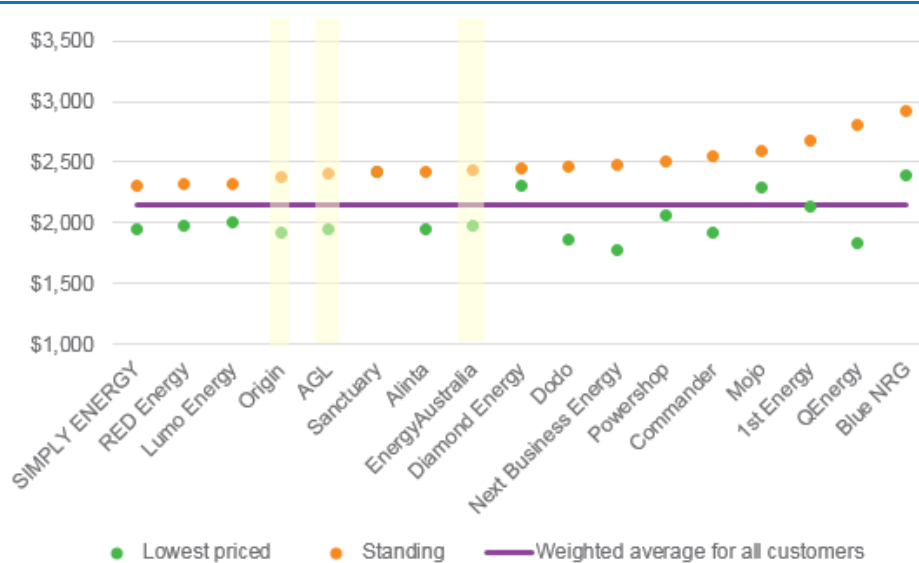
We found that prices have become increasingly varied since price deregulation, and this has become much more pronounced this year (Figure 4.2 and Figure 4.4). As a result, the highest offers in the market in 2017 are significantly higher than the most expensive offers in previous years. Figure 4.3 provides an example of the spread of offers for the Ausgrid network for 2017-18, based on the cheapest and standing offers of each retailer.

Figure 4.2 Spread of offers for residential customers (6,500 kWh, nominal, GST-inclusive)



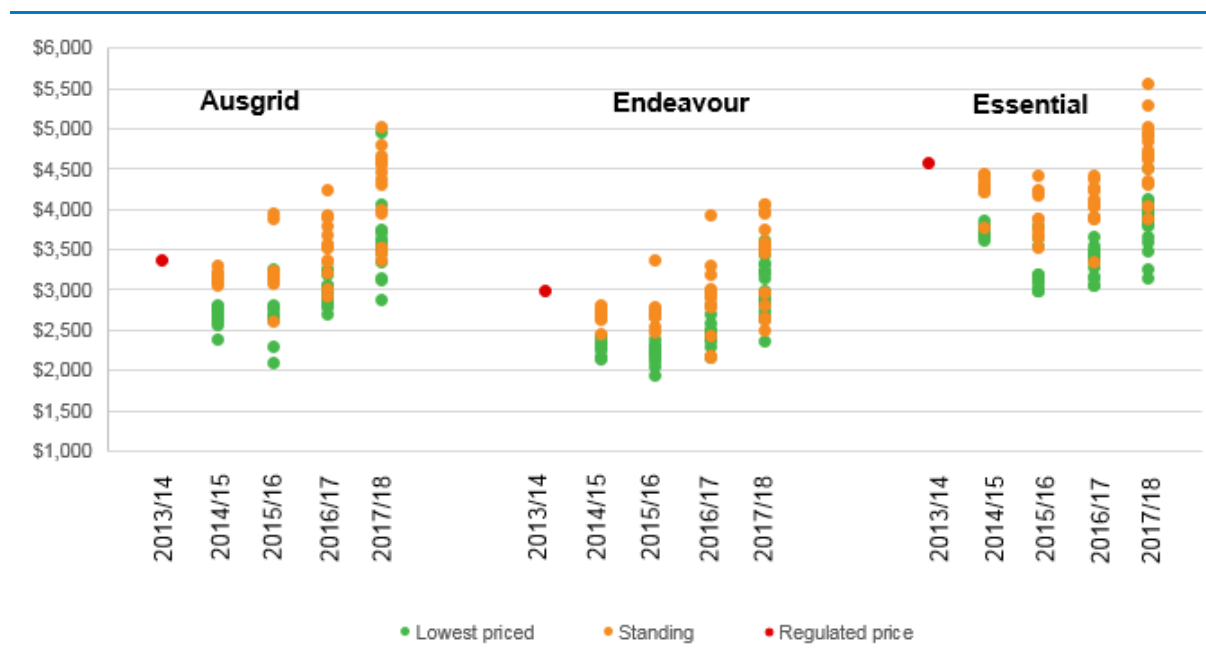
Data source: Information from retailers.

Figure 4.3 Electricity offers for residential customers for 2017-18 (Based on the Ausgrid network, 6,500 kWh, nominal, GST-inclusive)



a Information from retailers.

Figure 4.4 Spread of offers for business customers (10,000 kWh, nominal, GST-inclusive)



Data source: Information from retailer

4.2.2 Standing offers have increased

Figure 4.2 and Figure 4.4 above highlight that between 2016 and 2017, the standing offers have increased substantially. Figure 4.5 shows that for the Big 3's residential customers, standing offers increased by an average of 15% on 1 July 2017, or \$350 for a customer with typical consumption of 6,500 kWh (nominal).

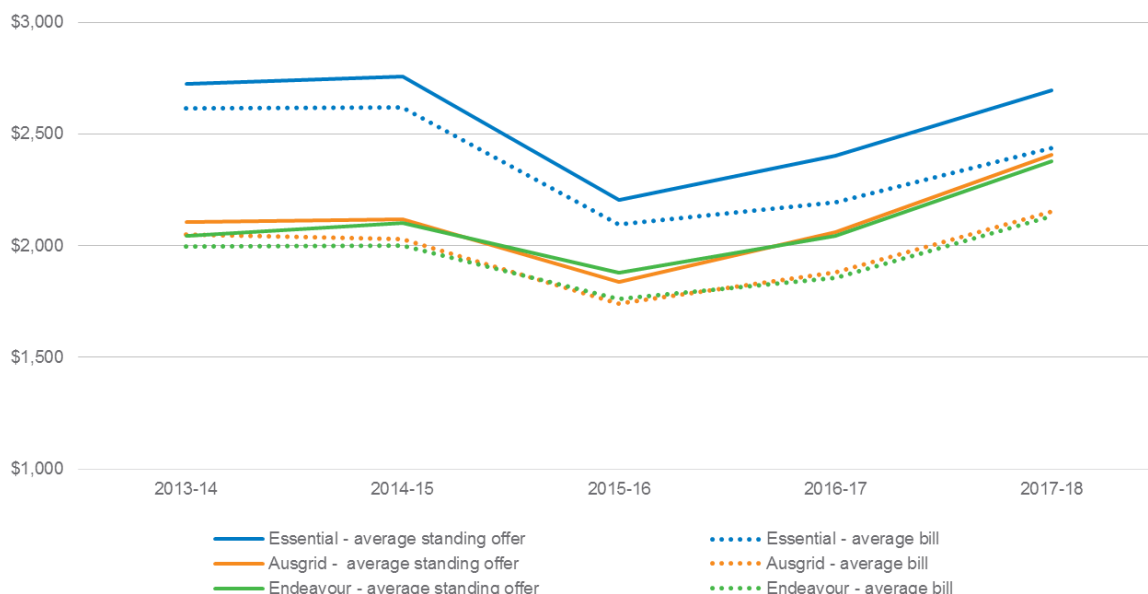
This one-year increase in the standing offer is more than the cumulative increase in the standing offers since price deregulation. Since prices were deregulated in 2013-14, the standing offers for residential customers of the Big 3 have increased by 10% on average across the state (this represents a 2% increase in real terms). For the Ausgrid and Endeavour networks, this is around a \$300 increase, from around \$2100 to \$2,400. The standing offers for the Big 3 in the Essential Energy network fell by around \$30 or 1% over this period, and are currently around \$2,700.

We note that the number of customers on standing offers has fallen over time, so that now around 23% of residential customers are on standing offers (See Chapter 6 for more details).

Draft finding

- 4 Standing offers for residential customers have increased by 10% since price deregulation.

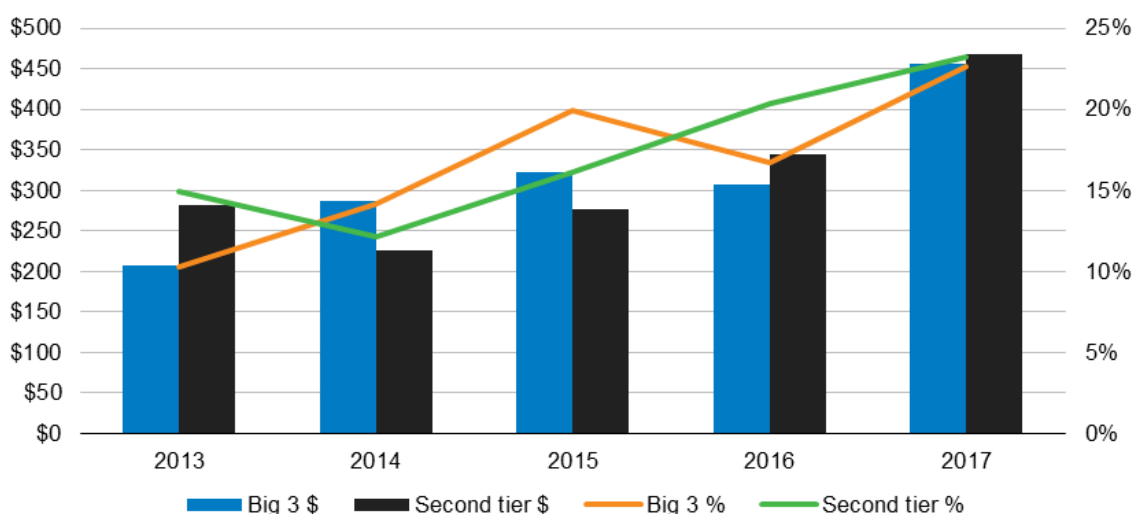
Figure 4.5 Change in the standing offer for residential customers over time (6,500 kWh, nominal, GST-inclusive, based on the Big 3 retailers)



Consistent with these findings, the average **difference** between standing offers and the **cheapest offers** has widened significantly over time.

In 2013, the average difference between the standing offer and the cheapest market offer for residential customers was between \$200 and \$300, or 10% to 15% for a typical customer consuming 6,500 kWh. This has increased to an average difference of around \$460 or 23% (Figure 4.6).

Figure 4.6 Average difference between standing offers and lowest market offer for residential customers (6,500 kWh, nominal, GST-inclusive)



Data source: Price information provided by retailers.

4.2.3 Price variation is a normal feature of competitive markets

The NSW Farmers' Association submitted that the proliferation of market offers by retailers increases search and transaction costs for consumers which creates price opaqueness and limits price competition.⁵¹ It disagrees with our previous conclusions that NSW markets are competitive. It also argued that unlike other markets, significant price differences do not reflect differences in quality and reliability of services.⁵²

Price is the most common way that retailers attract and retain customers. We agree with the NSW Farmers' Association that often price differences do not reflect differences in costs. Price variation in these circumstances is known as "price discrimination," and it occurs because customers respond to prices differently, ie, have different demand elasticities. It is observed in most competitive markets (such as airlines, telecommunications, groceries), and often indicates significant competition, rather than lack of it.⁵³ We consider price variation is consistent with a competitive retail market, and that it supports innovation and dynamic efficiency.⁵⁴

We agree with the NSW Farmers' Association that in some cases differences in prices in these other industries reflect product differences or differences in infrastructure used by service providers, rather than customers' price elasticities.⁵⁵ However, in many cases, differences in prices do not reflect any differences in underlying costs. For example, the price of petrol can be materially different at different petrol stations in the same city, even though the costs of supply are not.

Price discrimination can increase efficiency

Price discrimination often increases efficiency in markets compared to all units being sold at the same price at a constant mark up to the marginal costs of supply to recover fixed costs. By recovering fixed or sunk costs from less price sensitive customers (who will consume the good anyway), businesses can offer lower prices to more price sensitive customers to compete for their business. As more goods are sold at or close to the marginal cost of production, output expands, which increases efficiency.

The closer that goods are sold to the marginal cost of supply to some customers, the more that the fixed costs will need to be recovered by other customers, increasing the level of price variation in the market. This can result in positive distributional effects where businesses recover more of their costs from less price sensitive customers, and these customers are higher income households.⁵⁶

However, because of the large spread of offers in the market, it is also important to understand if there are barriers for customers who would like to be on market offers in

⁵¹ NSW Farmers' Association submission to *IPART Information Paper*, 28 June 2017, p 3

⁵² NSW Farmers' Association submission to *IPART Information Paper*, 28 June 2017, p 5

⁵³ ACCC, Network Issue 63, June 2017, p 10, <https://www.accc.gov.au/system/files/network%20june%202017%20%28D2017-00045379%29.pdf>.

⁵⁴ Although we note that the lack of price variation does not indicate that a market is **not** competitive.

⁵⁵ NSW Farmers' Association submission to *IPART Information Paper*, 28 June 2017, p 3

⁵⁶ Simshauser and Whish-Wilson, *Reforming Reform: Differential Pricing and Price Dispersion in Retail Electricity Markets*, June 2015, p 28.

moving onto them. Customer engagement and barriers to customer engagement is discussed further in Chapter 6.

There are also some vulnerable and disadvantaged customers on higher priced offers. Unlike other markets where participation is discretionary, most customers cannot opt out of purchasing electricity. Therefore we consider that retailers have a role in making sure that these customers are able to engage in the market. Strategies to ensure that these customers do not pay more than they should are discussed further in Chapters 7 and 9.

4.3 Increasing product and service variation indicates competition between retailers

As well as an increasing range of prices being offered to customers, products and services have also become more varied over the past three years, particularly as technology continues to develop.

Some stakeholders have questioned the value of some of the product differentiation in the market that has occurred to date. For example, the NSW Farmers' Association submitted that the differences in price structures are unlikely to represent innovation. It considered that IPART should undertake analysis on consumer sentiment to determine whether consumers view the provision of electricity as a commodity product (ie, do they perceive differences in quality and reliability between retailers), and whether the market is innovative.⁵⁷

In our view product innovation is one of the benefits of competition, but it is only in its infancy. With the take up of digital meters, customers will have the opportunity to get more information and control over energy usage, receive real-time price signals and achieve energy self-sufficiency.

We agree with Origin Energy that these new energy products and services need to be considered when assessing competition in the market, as they are in direct competition with the traditional retail market.⁵⁸

4.3.1 Bundled energy products and services

Retailers are continuing to innovate in repackaging energy services and their pricing model to attract customers. For example, some retailers are offering electricity and gas together, and others are bundling energy with additional products and services such as phone and internet services. For example, Dodo Power and Gas offers consumers the ability to deal with a single company for many of their home services including home phone, mobile, broadband internet, electricity, gas, and insurance.⁵⁹

⁵⁷ NSW Farmers' Association submission to *IPART Information Paper*, 28 June 2017, pp 3-4.

⁵⁸ Origin Energy submission to *IPART Information Paper*, 30 June 2017, p 1.

⁵⁹ Dodo, *About Dodo Power and Gas*, <http://www.dodo.com/power-gas/quick-links/about-dodo-power-gas/>, accessed 5 September 2017.

Bundling electricity with new technologies

Overseas experience suggests that interest in digital energy solutions, combining energy services with telecommunication and solar installation is strong. This industry direction may offer opportunities for utilities, solar installers and telecommunications suppliers to increase their market penetration through bundled products.⁶⁰

Over the last year, more retailers have started to offer digital meters, solar PV, and battery options to their customers, in addition to traditional energy services. For example, EnergyAustralia and Origin Energy offered solar panels, inverter and installation, as well as battery storage systems.⁶¹ This technology allows customers to store energy generated by solar panels to be used at a later date.⁶²

Enova Energy is also planning to develop options to make solar take up attractive to landlords and renters.⁶³

We consider that the opportunities for product innovation will continue to increase over time, as retailers start to bundle electricity with products such as solar and batteries, software is becoming available to capture the value of the energy that is being fed into the grid by households in real time, and issues around the reliability of supply is making customer demand response more valuable at the same time as the take up of digital meters is increasing.

4.3.2 Innovative energy pricing models

Retailers also continue to offer alternatives to the traditional tariff structure to appeal to different market segments. For example, Origin Energy is currently offering its 'predictable plan' aimed at removing 'bill shock'. Customers who value predictability and control over their energy bills can pay an agreed fixed amount on their utility bills each fortnight or month, subject to a fair use policy, with the amount fixed for 12 months.⁶⁴

Powershop offers a pricing model that allows customers to pre-purchase units of energy when it is convenient and offers periodic sales and discounts. This gives customers the option to manage cash flow and smooth out energy costs more evenly throughout the year.⁶⁵ Households fitted with digital meters can further benefit from automatic real-time price signals about their electricity usage from their smart phones.⁶⁶

⁶⁰ According to research conducted by Parks Associates released at the Smart Energy Summit in Austin USA, February 2015: 'Nearly half of homes with broadband in the U.S. are willing to subscribe to a bundle of energy services for about \$USD10 per month. Internet and HVAC maintenance were the most popular services to bundle with electricity services.'
<http://www.greentechmedia.com/articles/read/consumers-hungry-for-bundled-energy-services-survey-finds>, accessed 10 October 2017.

⁶¹ Energy Australia, *Solar Power Systems*, <https://www.energyaustralia.com.au/home/solar-and-batteries/solar-power/solar-power-systems>, accessed 5 September 2017.

⁶² Energy Australia, *Battery Storage*, <https://www.energyaustralia.com.au/home/solar-and-batteries/battery-storage>, accessed 5 September 2017.

⁶³ Enova Energy, *About Enova*, <https://enovaenergy.com.au/about-us/>, accessed 10 October 2017.

⁶⁴ Origin, *Predictable Plan*, <https://www.originenergy.com.au/for-home/campaign/origin-predictable-plan.html>, accessed 10 October 2017.

⁶⁵ Powershop, *Powerpacks – choose your power*, <http://www.powershop.com.au/toolkit/>, accessed 10 October 2017.

⁶⁶ Powershop, *Powershop in your pocket*, <http://www.powershop.com.au/mobile-apps/>, accessed 10 October 2017.

One of the more innovative examples is Mojo trialling the use of demand response by customers by offering them a bill credit to reduce their usage at a time of high wholesale prices. A text message was sent to 500 customers with digital meters in NSW, offering an incentive to those who would turn off power later in the day. Mojo reported that 40% of people agreed to participate within about 30 minutes. The retailer then sent a request for the respondents to switch off appliances. To Mojo, this demand reduction represented \$390 in savings per customer over two hours. Customers received \$25 bill credit for these two hours of participation.⁶⁷

We agree with NSW Farmers' Association that as more of these offers with demand-response features enter the market, new indicators may be required on the availability of service offerings.⁶⁸

Draft finding

- 5 There is evidence of rivalry between retailers and a large range of products and services available to customers. In our view this is consistent with a competitive retail market that is continuing to develop.

⁶⁷ Ecogeneration, Demand response, the opportunity for energy consumers to switch to supply, 21 July 2017, <http://www.ecogeneration.com.au/demand-response-the-opportunity-for-energy-consumers-to-switch-to-supply/>, accessed 10 October 2017.

⁶⁸ Powershop, *Powerpacks – choose your power*, <http://www.powershop.com.au/toolkit/>, accessed 10 October 2017.

⁶⁹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 235.

5 Barriers to entry are low

In any market, there may be economic, legal, regulatory or other barriers that constrain the ability of new retailers to enter the market and/or expand their share of this market. Where these barriers are low, competition will be most effective in protecting customers.

In such a market, the incumbent retailers are under constant pressure to offer competitive prices, products and services, or lose customers to more competitive rivals. In our view, this pressure provides the most effective means of keeping retail prices in line with the efficient costs of supply.

To assess the barriers to entry in the retail electricity market in NSW, we looked at the number of retailers and brands contesting the market and the market concentration in 2016-17, compared to previous years. We also examined retailers' views on barriers to entry, based on a survey commissioned by the AEMC as part of its 2017 retail competition review. The sections below outline our draft findings, then discuss these findings in more detail.

5.1 Overview of draft findings

We found no substantial barriers for smaller retailers to enter the NSW electricity market. There were 22 retailers and 26 brands contesting the market in 2016-17.⁶⁹ While the market is still relatively concentrated between the big three retailers – AGL, Energy Australia and Origin – the trend for smaller retailers to gain market share from the 'big three' retailers has continued in 2016-17.⁷⁰ There are now 26 retailers in the market.

We also found that smaller retailers are able to access exchange-traded derivative products to hedge their risk exposure. However, large vertically integrated electricity businesses in the market and tightening supply in the wholesale market may increase economic barriers, which means that a new retailer to the market needs considerable financial capacity to rapidly gain market share.

5.2 Number of retailers contesting the market is relatively high

The extent to which there are barriers to entering the market will affect how many retailers are competing for customers. In general, the greater the number of active retailers, the stronger is the level of competition in the market.

⁶⁹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 235.

⁷⁰ AER retail performance statistics as at March 2017, <https://www.aer.gov.au/retail-markets/retail-statistics/nsw-small-customers>, accessed 10 October 2017.

As of June 2017, there were 26 retail brands owned by 22 electricity retailers supplying to small retail customers in NSW, which has remained constant since our 2016 review. There were eight gas retail brands owned by six retail businesses.⁷¹ One retailer, Urth Energy, exited the market in February 2017. At the time of entering administration it only had 780 customers across the NEM.⁷² These customers were transferred to alternative retailers.⁷³

Table 5.1 Energy retailers contesting in NSW as at 30 June 2017

	Retailer	Electricity		Gas	
		Residential	Business	Residential	Business
1	Origin Energy	X	X	X	X
2	EnergyAustralia	X	X	X	X
3	AGL	X	X	X	X
	Powerdirect	X	X		
	Actew AGL	X			X
4	Alinta Energy	X	X	X	
5	1st Energy	X	X		
6	Blue NRG	X	X		
7	Click Energy	X	X	X	
8	Commander	X	X		
	Dodo	X			X
9	CovaU	X	X	X	X
10	Diamond Energy	X	X		
11	Energy Locals	X	X		
12	Enova Energy	X	X		
13	ERM Business Energy		X		
14	Red Energy	X	X	X	X
	Lumo Energy ^a	X	X	X	
15	Momentum Energy	X	X		
16	Next Business Energy		X		
17	People Energy	X			
18	Pooled Energy	X			
19	Powershop	X	X		
20	QEnergy	X	X		
21	Sanctuary Energy	X			
22	Simply energy	X	X	X	X

^a Lumo is a subsidiary of Snowy Hydro and is no longer offering electricity to new customers.

Source: Energymadeeasy.com.au

⁷¹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 235.

⁷² AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 235.

⁷³ The 'Retailer of Last Resort' scheme administered by the Australian Energy Regulator provides the arrangements for transferring customers of retailers that exit the market.

5.3 Small retailers' share of the market continues to increase

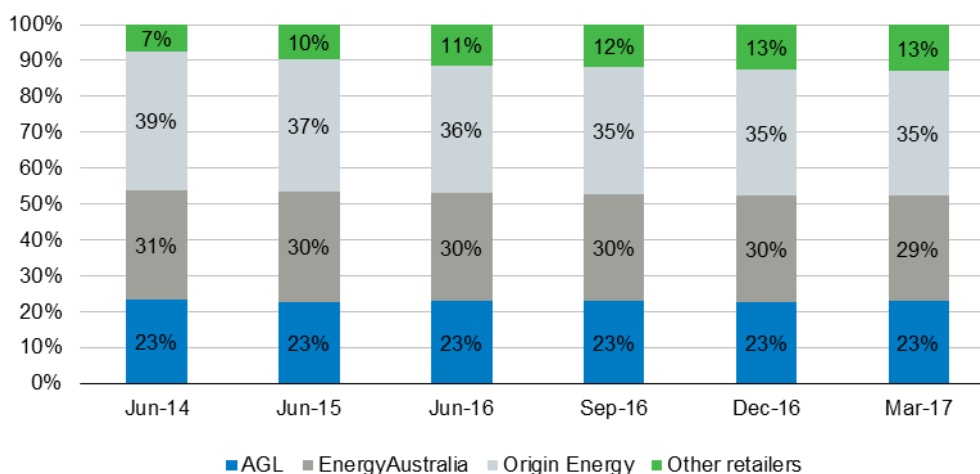
Over 2016-17, the market concentration continued to decrease. Although the retail electricity market remains relatively concentrated,⁷⁴ there is a consistent trend of smaller retailers gaining market share at the expense of the big three retailers in NSW (Figure 5.1).

In June 2014, smaller retailers supplied only 7% of the market for small customers, this has grown to about 13% in the March 2017 quarter.⁷⁵ We expect that it would take some time for a small retailer to build a substantial market share. Snowy Hydro's Red Energy and Lumo brands currently have the highest second-tier market share with around 45% of the second-tier market, or around 5% of the market overall.⁷⁶

As at the end of March 2017, the big three retailers had around 87% share of the NSW electricity market for small customers, which were:

- ▼ AGL (23%)
- ▼ EnergyAustralia (29%), and
- ▼ Origin Energy (35%).

Figure 5.1 Change in electricity retailers' market share for all small customers



Data source: AER Retail performance statistics as at March 2017.

We note that some retailers own more than one retail brand. For example, AGL owns Powerdirect and a share in ActewAGL, and Snowy Hydro owns Red Energy and Lumo (in 2017 Snowy Hydro stopped offering electricity to customers under the Lumo brand). Aside from these examples, there does not appear to be any cross-ownership of the other retailers.

⁷⁴ The extent of concentration in a market can be measured using the Herfindahl-Hirschman Index (HHI), which ranges from close to zero to 10,000. The ACCC considers an index greater than 2,000 indicates a concentrated market. The HHI for the NSW retail electricity market is currently 2,714. It is calculated by squaring the market share of each firm competing in a market, and then summing the resulting numbers. AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 42, 239

⁷⁵ AER retail performance statistics as at March 2017, <https://www.aer.gov.au/retail-markets/retail-statistics/nsw-small-customers>, accessed 10 October 2017.

⁷⁶ AER Retail performance statistics Q3 2016; and AGL, Australian Power and Gas Information, <https://www.agl.com.au/residential/energy-plans/electricity-and-gas-plans/price-and-contract-information/australian-power-and-gas-information>, accessed 12 October 2017.

5.4 Retailer views do not consider the barriers to entry and expansion are substantial

Each year, the AEMC asks retailers to provide their opinions on barriers to entry and expansion in its retailer survey, including the materiality of any barriers, and whether barriers are specific to particular jurisdictions, or to regional and rural areas.

In general, respondents to the most recent survey did not identify substantial barriers to market entry or expansion. However, several retailers commented that the hedging market is tightening with higher wholesale prices. The AEMC reported that:⁷⁷

One retailer did comment however that while hedging products were available, with increasing wholesale prices, the New South Wales hedging market is tightening. Another indicated that the hedging market was becoming tighter as the retailer's scale increased. These are competitive challenges that may limit retailers' ability to expand, but as yet have not impacted this market.

Smaller retailers are able to access exchange-traded derivative products to hedge their risk exposure. However, their future ability to access competitively priced hedging products may become an economic barrier if it requires them to have considerable financial capacity to gain market share. We also note that the ACCC is concerned about the impact that vertical integration may have on standalone retailers' ability to compete.⁷⁸

The AEMC commented that another potential barrier to entry and effective competition noted by a retailer was the logistical difficulties in assuming the responsibility for digital meters in regional New South Wales.⁷⁹ In particular, having responsibility to repair meters on site may add to the costs of serving very remote customers, and discourage retailers from supplying in these areas, reducing competition. While the responsible entity may represent a barrier to entry, a larger take up of digital meters should help facilitate faster switches to new retailers as a meter read (which is occurs to settle accounts with the old retailer), can occur remotely.

One of the main issues raised by retailers that related to multiple jurisdictions was that there was general concern about the level and consistency of regulation. They said that jurisdictional regulations are creating costs and barriers for existing retailers and new retailers to operate. We note that this issue relates mainly to Victoria, due to its own regulatory arrangements, compared with the rest of the NEM, which operates under the national energy retail laws.⁸⁰

The AEMC recommended that jurisdictions harmonise their energy customer protection arrangements to minimise the barriers and costs for traditional and new retailers who operate across the NEM.⁸¹

Draft finding

7 There are no substantial barriers for smaller retailers to enter the NSW electricity market.

⁷⁷ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 52.

⁷⁸ ACCC, *Retail Electricity Pricing Inquiry: Preliminary Report*, 16 October 2017, p 82, <https://www.accc.gov.au/publications/accc-retail-electricity-pricing-inquiry-preliminary-report>, accessed 16 October 2017.

⁷⁹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 52.

⁸⁰ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 50-54.

⁸¹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 51-52.

6 Customers are relatively engaged and active

In markets where competition is working well, we would expect most customers to be engaged and active in the market. For example, they would be aware of the choices available to them, be shopping around for better deals and be satisfied with their participation and experience in the market. And the more well-informed and engaged customers are, the more pressure there is on retailers to offer competitive prices and services.

To assess customer engagement and activity in the retail electricity market in 2016-17, we considered a range of participation indicators, as well as switching rates and satisfaction levels. We also examined the reasons why some customers do not participate in the market, to help us identify potential measures to enhance competition (discussed in the next chapter). The sections below outline our draft findings and then discuss them in more detail.

6.1 Overview of draft findings

Compared to other countries around the world, customers in Australia are relatively engaged in the energy market.⁸² In NSW, we found that customers are relatively engaged and active in the electricity retail market. The level of customer awareness about the choices in the market and confidence in finding information to make choices has continued to improve. Switching rates are relatively high, and most customers appear to be satisfied with their current retailer.

Some customers choose not to participate or be active in the market because they are satisfied with their current retailer, or because the cost of their time to search for and switch to a cheaper deal outweighs their potential benefit from a lower bill. For these people not participating in the market is a rational choice. However, other customers would like to be more engaged, but find it difficult to compare offers and find out if they on the best available offer. Few customers are aware of the Federal Government's energymadeeasy.gov.au comparator website, which can help customers determine the deals that are best for them.

6.2 Customer awareness and confidence continue to improve

Recent consumer research commissioned by the AEMC indicates that 94% of residential customers and 95% of small business customers in NSW are aware they can choose their retailer.⁸³ This research also found that more than 70% of customers are confident that they

⁸² Oxera, *Behavioural insights into Australian retail energy markets – Report for the Australian Energy Market Commission*, 11 March 2016, p 27.

⁸³ Newgate Research, *Consumer research for the Australian Energy Market Commission's 2017 retail competition review*, April 2017, p 104.

can find the right information on energy options.⁸⁴ The levels of awareness and confidence have increased each year since price deregulation occurred (Table 6.1 and Table 6.2).

Table 6.1 Summary of participation indicators for residential customers

Category	Measure	2014	2015	2016	2017
Awareness	Of choice of retailer	90%	89%	92%	94%
	Of choice of plans		81%	82%	86%
Customer activity	Residential customers switching company at least once		14%	15%	19%
	Residential customers switching plan with same company		18%	15%	19%
Information	Confident that they are able to find the right information on energy options		55%	62%	72%
	Awareness of energymadeeasy	11%	16%	9%	13%
Satisfaction	With current retailer	69%	74%	74%	74%
	With customer service ^a		91%	93%	90%
	With the level of market choice	47%	60%	62%	60%
	With value for money ^b	86%	89%	90%	89%

^b Percentage of customers rating the quality of customer service as either fair, good or excellent.

^c Percentage of customers rating overall value for money provided by electricity company as either fair, good or excellent.

Data source: Newgate Research, *Consumer research for the Australian Energy Market Commission's 2017 retail competition review*, April 2017, pp 102-116.

Table 6.2 Summary of participation indicators for business customers

Category	Measure	2014	2015	2016	2017
Awareness	Of choice of retailer	86%	95%	92%	95%
	Of choice of plans		87%	86%	81%
Customer activity	Business customers switching company at least once		17%	15%	16%
	Business customers switching plan with same company		20%	10%	12%
Information	Confident that they are able to find the right information on energy options		45%	68%	72%
	Awareness of energymadeeasy	26%	4%	11%	
Satisfaction	With current retailer	66%	61%	63%	66%
	With customer service ^a		88%	94%	91%
	With the level of market choice	54%	48%	67%	67%
	With value for money ^b	87%	87%	90%	87%

^a Percentage of customers rating the quality of customer service as either fair, good or excellent.

^b Percentage of customers rating overall value for money provided by electricity company as either fair, good or excellent.

Data source: Newgate Research, *Consumer research for the Australian Energy Market Commission's 2017 retail competition review*, April 2017, pp 102-116.

⁸⁴ Newgate Research, *Consumer research for the Australian Energy Market Commission's 2017 retail competition review*, April 2017, p 111.

6.3 Switching rates are relatively high

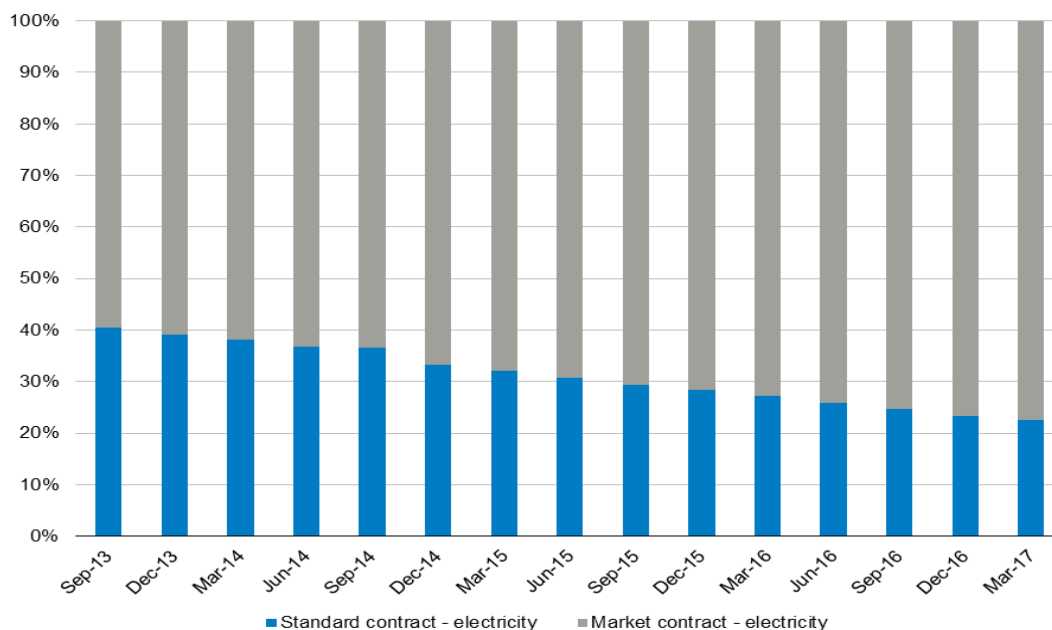
Over 2016-17, one in three residential customers in NSW reported that they actively searched for a better offer, and the same proportion of small businesses also investigated a better offer. This was similar to the search rates in other years.⁸⁵

The percentage of residential customers that actually switched energy company or plan in the previous 12 months increased from 24% to 33% between 2015 and 2017.⁸⁶ 57% of residential customers in NSW reported that they switched retailers and/or plans in the last five years, with 39% of residential customers across the NEM switching provider.⁸⁷

While the Public Interest Advocacy Centre (PIAC) is concerned that less than one-third of those surveyed in NEM states with retail competition had changed retailers in the past 12 months,⁸⁸ the switching rates for electricity providers are higher compared to other products and services. Compared to the 39% of consumers surveyed that switched electricity providers in the last five years, 36% switched car insurers, and 34% switched their mobile providers.⁸⁹

Figure 6.1 shows that 77% of all customers are on a market offer, rather than a ‘standing’ or default offer. This is up from 60% before price deregulation (in September 2013).

Figure 6.1 Proportion of standing and market contracts in NSW



Data source: AER, NSW – Small retail customer contract types, <https://www.aer.gov.au/retail-markets/retail-statistics/nsw-small-customer-contract-types>, accessed 24 July 2017.

⁸⁵ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 105.

⁸⁶ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 105.

⁸⁷ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 87-88.

⁸⁸ PIAC submission to *IPART Information Paper*, 30 June 2017, p 2.

⁸⁹ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p ii.

6.4 Customers are relatively satisfied

When the AEMC surveyed customers in February of this year, they found that there was a relatively high level of satisfaction among electricity customers, both with their level of engagement, and their retailer. We note that the levels of satisfaction might have fallen since then, as prices have risen substantially in the meantime. However, at the time of the survey most residential and business consumers who had switched energy company or plan in the last 5 years reported that they remained happy with both their decision to switch, and their retailer.

High levels of satisfaction were a key reason why customers did not switch plan. For example, among residential customers across the NEM that investigated but chose to remain with their current electricity retailer or plan, reasons given were that:⁹⁰

- ▼ 17% stated that their company/plan had a better discount/cheaper price,
- ▼ 13% remained because they were happy with their current retailer, and
- ▼ 9% said their existing company matched the offer or gave them a better offer.

Similarly, a key reason that customers had not investigated switching retailer, was because they were happy with their current retailer (29% of residential and 25% of business customers who have not investigated switching).⁹¹

The Energy & Water Ombudsman NSW (EWON), which provides an independent dispute resolution service for all retail customers, reported that the overall number of complaints relating to electricity retailers decreased by 25% in 2015-16 compared to the previous year.⁹²

⁹⁰ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 40.

⁹¹ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 39.

⁹² EWON, Annual Report 2015/2016, p 20.

Box 6.1 Customer satisfaction with the energy market

Energy Consumers Australia (ECA) conducts bi-annual nation-wide surveys asking households to rate their levels of satisfaction based on five main criteria, including: value for money, customer service, billing and account options, reliability and faults. It found that NSW households are most satisfied with the reliability of electricity services (75%), followed by billing and account options (67%) and the level of faults (65%). ECA also found that around half of the NSW households are satisfied with the value for money of electricity services, with NSW rating overall value for money higher than all other states.^a

The AEMC found that in relation to satisfaction with their retailer:

- ▼ 74% of residential customers and 66% of small business customers responded that they were very or somewhat satisfied with their current electricity retailer,⁹³
- ▼ 67% of residential consumers and 61% of small business customers rated the overall quality of customer service provided by their electricity retailer as good to excellent, and ⁹⁴
- ▼ 62% of residential customers surveyed rated value for money provided by their electricity retailer as good to excellent. Around a quarter thought they were getting fair value from their retailer. Approval ratings from small businesses declined, with 49% reporting obtaining good to excellent value from their retailer, down from 59% in the previous survey.⁹⁵

^a Satisfaction is measured based on percentage of Australian households giving positive ratings of 7 out of 10 or higher.

Source: Energy Consumers Australia, *Energy Consumer Sentiment Survey*, June 2017. Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 116-117.

6.5 Some customers do not participate in the market for varied reasons

Not all customers are actively engaged in the market. For some customers this is a rational choice because the search costs involved in finding the best offers outweigh the benefits.

Our view is that competition is working if you can get a lower price by shopping around. A number of competitive markets demonstrate this. For example, customers can make substantial savings by shopping around when buying flights, consumer electronics, insurance, cars and mobile plans. However, some customers would like to be more engaged, but find it difficult to compare offers.

6.5.1 For some customers it is a rational choice not to participate

As noted above, many customers do not participate in the market because they are satisfied with their current retailer. For other customers, the cost of their time to search for and switch to a cheaper deal outweighs their potential benefit from a lower bill. For these people not participating in the market is a rational choice.

⁹³ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 112-113.

⁹⁴ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 114-115.

⁹⁵ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 116-117.

While the AEMC found that the main motivation for customers to switch retailer or plan was to reduce their bill,⁹⁶ customers said that to seriously consider switching retailer or plan, they wanted to save an average of \$388 per year on their electricity bill and small business customers wanted to save about \$796 on their yearly electricity bill.⁹⁷

One of the main reasons that around 40% of customers had not investigated switching was because they didn't have time (22% for business customers, and 15% for residential customers). Similarly, 14% of residential and 10% of business customers felt it was too much hassle or couldn't be bothered.⁹⁸

6.5.2 Some customers find it difficult to compare offers

We note the finding by the AEMC that 8% of residential customers across the NEM reported that the reason they investigated switching offers but did not, was because it was too confusing.⁹⁹ While 72% of residential customers surveyed in NSW were confident that they could find the information required for them to select the best offer for their circumstances, this leaves 28% of customers who are not confident that they will be able to find the required information.¹⁰⁰ Customers also thought the process is more complex than comparing and selecting other services, such as home/car/health insurance, internet and telecommunication plans, or banking services.

Several stakeholders submitted that complex and opaque information creates high search costs and lowers the ability of consumers to engage. The NSW Council of Social Service (NCOSS) concluded that a significant proportion of vulnerable customers are not aware what deal they are on, that different deals exist, how to compare deals, and what is required to ensure that they are not paying more than is necessary.¹⁰¹ The NSW Farmers' Association suggested that search costs are being deliberately "inflated by market participants to ensure that the cost of participating outweighs benefits."¹⁰²

We consider that as competition in the retail market continues to strengthen, customers' searching and switching costs would be expected to continue to reduce as retailers will strive to make their offers as visible and easy to access as possible.

Discounting can be confusing for customers

As shown in Chapter 4, price is the most common way that retailers attract and retain customers, and they often do this by offering discounts. However, the largest percentage discount does not necessarily represent the lowest priced offer, as the reference rate can vary across retailers and plans.

⁹⁶ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 38.

⁹⁷ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, pp 46-47.

⁹⁸ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 39.

⁹⁹ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 40.

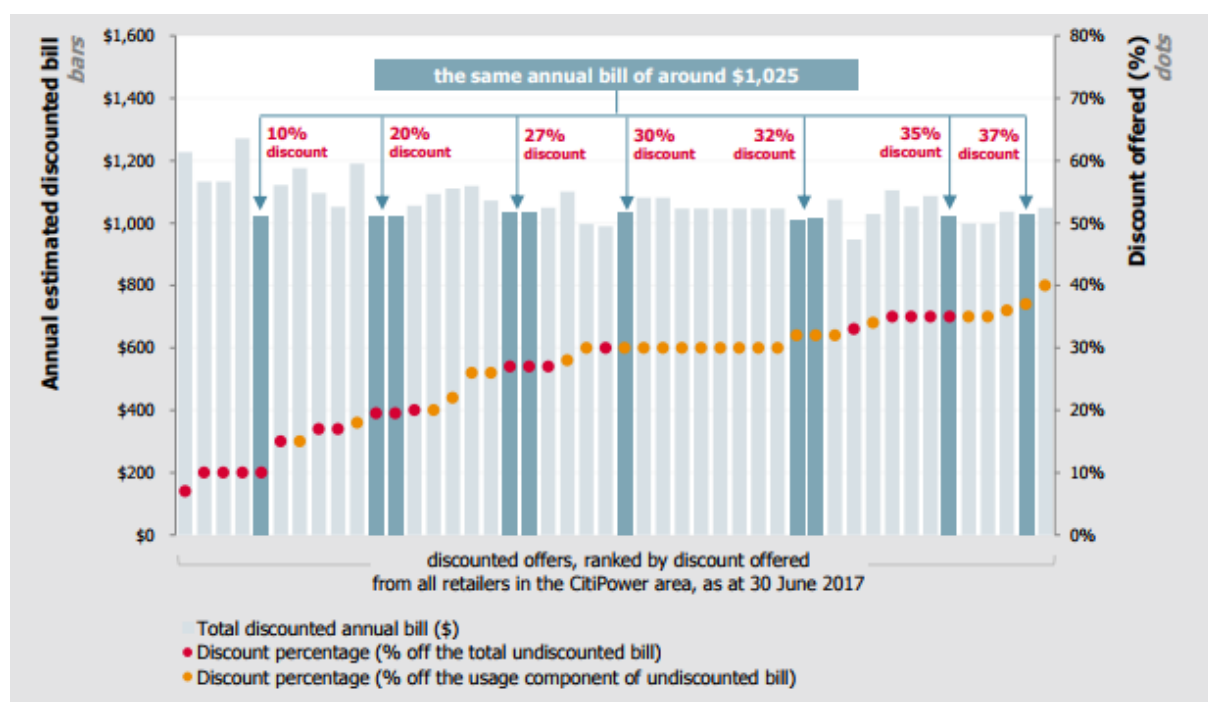
¹⁰⁰ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 111.

¹⁰¹ NCOSS submission to IPART's 2017 Retail Electricity Market Monitoring Review, 29 June 2017, p ii.

¹⁰² NSW Farmers' Association submission to IPART Information Paper, 28 June 2017, p 304.

For example, in its recent market update, the Victorian Essential Services Commission (ESC) found that offers with very different discounts – 10%, 20%, and 37% - resulted in almost the same annual bill (\$1020 to \$1030 for 4,000 kWh of consumption) (Figure 6.2).¹⁰³

Figure 6.2 Different discounted offers could end up with the same annual bill (extracted from ESC Victorian energy market update)



Data source: Essential services commission, *Victorian energy market update – April to June 2017 with audit findings*, 26 September 2017, p 6, http://www.esc.vic.gov.au/wp-content/uploads/2017/09/victorian-energy-market-report-april-june-2017-update-20170926_v2.pdf, accessed 16 October 2017.

Not many customers are aware of the independent online comparator website

Because electricity offers are made up of a number of different tariff components, including a supply charge, different consumption charges that sometimes vary by time of day, and discounts, which can be applied to some or each of these components, it can be very difficult to compare offers without online comparator tools.

The Australian Energy Regulator (AER) administers the independent energymadeeasy.gov.au website, which allows customers to search for the offer that provides the lowest bill. However, the AEMC found that only 13% of customers in NSW are aware of the energy made easy website.¹⁰⁴

While the energymadeeasy.gov.au website is a useful tool for customers to find better energy offers, the NSW Farmers’ Association submitted that the website fails to cover all offers available, and it can still be difficult to identify the best offer. In particular, the NSW

¹⁰³ Essential services commission, *Victorian energy market update – April to June 2017 with audit findings*, 26 September 2017, pp 5-6, http://www.esc.vic.gov.au/wp-content/uploads/2017/09/victorian-energy-market-report-april-june-2017-update-20170926_v2.pdf, accessed 16 October 2017

¹⁰⁴ Newgate Research, *Consumer Research for the Australian Energy Market Commission’s 2017 Retail Competition Review*, April 2017, p 107.

Farmers' Association said it was difficult to compare single-rate offers to time-of-use offers.¹⁰⁵ We also note that for the 25% of customers with solar panels, comparing offers using the website is further complicated since the estimated bills do not factor in house consumption from solar PV units, solar feed-in-tariffs, the costs of meter installation or ongoing metering charges.

We note that in addition to the energymadeeasy.gov.au website, retailers can also increase awareness through commercial comparator websites.

In its report for non-profit organisation GetUp!, Carbon and Energy Markets (CME) notes that commercial switching sites only include offers from a subset of retailers.¹⁰⁶ Nevertheless, we consider these sites can encourage customers to engage in the energy market, and can also offer substantial savings to customers that might not otherwise have switched retailer. As more customers use these commercial switching sites, competition between retailers on these platforms would also intensify, and we would expect the range and value of offers available to improve over time.

Customers are not always aware when they are no longer on the best offers

One reason that some customers may not participate in the market is because they are not aware that they are no longer on a competitive offer. Retailers can vary the prices that they charge at any point in the contract (subject to any contractual limitations), and they are not required to notify customers of price changes until their next available bill.¹⁰⁷

The Combined Pensioners and Superannuants Association submitted that because retailers can vary the price of electricity at any point during a fixed-term contract unilaterally, customer choice is redundant.¹⁰⁸

¹⁰⁵ NSW Farmers' Association submission to *IPART Information Paper*, 28 June 2017, p 5.

¹⁰⁶ CME, *Australia's retail electricity markets: who is serving whom? – A report prepared for GetUp!*, August 2016, p 10.

¹⁰⁷ National Energy Retail Rules, Version 8, Part 2, Division 7, s 46(3) and (4).

¹⁰⁸ CPSA submission to *IPART Information Paper*, 30 June 2017, p 4.

7 Measures to further enhance competition

While we consider the findings outlined above indicate that competition in the NSW electricity retail market is consistent with a competitive retail market, we considered whether there are measures government could take to make it work even better.

We also specifically considered whether greater government intervention in the market would help to improve outcomes for customers, as one review has recently recommended in Victoria (see section 2.3.4).

The sections below outline our draft findings and recommendations, then discuss them in more detail.

7.1 Overview of draft findings and recommendations

Competition should drive the best outcomes for customers in the retail electricity market. We consider that there is a role for governments to help enhance competition by improving customer engagement in the market, which will place more pressure on retailers to offer competitive prices and services. Competition also creates incentives for product and service innovation.

On the other hand, the reintroduction of regulated prices is likely to lead to less efficient outcomes by entrenching the market position of the incumbent retailers, and dampening incentives to offer lower prices and better products to consumers. Over the longer term, customers are likely to be left worse off.

Similarly, introducing requirements for how retailers can present their market offers for 'typical customers' could stifle innovation by under-emphasising the non-tariff elements of offers (for example, bundling with batteries and solar). This could be misleading and leave 'non-typical' customers worse off.

Any NSW Government measures that improve customer engagement in the market should be implemented through the National Energy Customer Framework (NECF). This framework regulates the sale and supply of electricity to retail customers, and was developed by State, Territory and Commonwealth Governments to streamline the manner in which the electricity retail market is regulated, through a single regulatory framework.

We are recommending that the NSW Government investigate the most efficient method to provide electricity customers in residential caravan parks' embedded networks the same consumer protections as provided to customers that can participate in the competitive retail market. IPART would be well placed to undertake such a review.

7.2 Governments are active in regulating the retail market

Although electricity prices were deregulated in NSW in 2014, there is still a large number of rules and regulations that retailers have to follow when supplying small customers with electricity.

In July 2013, the NSW Government adopted the National Energy Customer Framework, which sets out consumer protections and operates alongside the Australian Consumer Law to protect small energy customers in their electricity supply arrangements.

However, the existence of price differentials and concern over lack of customer engagement has led some governments and regulators to consider greater action in electricity retail markets in addition to the rules under the National Energy Customer Framework. For example, proposals are currently being considered in Victoria to re-introduce a form of price regulation, and introduce more rules around the ways that retailers can engage with their customers.¹⁰⁹ Other reviews and stakeholders have expressed support for standard comparator rates.

In our view, these measures would hamper competition, stifle innovation and remove options from customers, and eventually leave customers worse off. Box 7.1 explains that when similar measures were introduced in the UK in 2009 they were removed when the UK Competition and Markets Authority (CMA) found that they had not benefited customers.

Box 7.1 Retailer requirements in the UK

In the UK, the Competition and Markets Authority (CMA) found that similar requirements introduced in 2009 by Ofgem made customers worse off, and were eventually removed. These included:

- ▼ a ban on complex tariff structures
- ▼ a limit of four tariffs per meter type
- ▼ limits on bundling electricity with other services, and
- ▼ discounts needed to be precise monetary amounts continuously applied on a daily basis, could not be applied to rate structure, and had to be consistent throughout the UK and for all types of contracts.

Source: Competition and Markets Authority (CMA), *Energy Market Investigation*, Final Report, 24 June 2016, p 41-42.

7.2.1 The National Energy Customer Framework

The National Energy Customer Framework, introduced in NSW in 2013 replaced most state-based rules that were different in each jurisdiction.¹¹⁰ For example, it governs consumer protection measures, mandatory minimum terms and conditions for market retail contracts

¹⁰⁹ *Independent Review into the electricity & gas retail markets in Victoria*, August 2017, https://engage.vic.gov.au/application/files/7415/0267/4425/Retail_Energy_Review_-_Final_Report.pdf, p xii, accessed 10 October 2017.

¹¹⁰ NSW has made limited modifications to the National Energy Retail Rules for NSW customers, for example. It requires that retailers must waive late fees if the customer receives the low income household rebate. <https://legislation.nsw.gov.au/~view/regulation/2013/168/historical2014-07-01/part4>

for all small customers, retailer hardship policies and limitations on disconnections, including processes to follow and restrictions on when disconnections can occur.¹¹¹

As well as ensuring that all customers, regardless of where they live, receive the same level of consumer protections, a consistent set of rules across most states and territories reduces the operating costs for retailers, resulting in more competitive prices for consumers.¹¹²

On the other hand different sets of rules between states and territories can discourage retailers from entering other retail markets because there are costs involved with understanding and complying with each different set of regulations, increasing barriers to entry. In turn, lower competition can put less downward pressure on prices, and result in less innovation in different markets.

7.2.2 Regulated prices would hamper competition

In our view, reintroducing regulated prices in NSW is likely to lead to less efficient outcomes over time. Regulated prices can tend to become the default option for many customers, reducing the level of customer engagement as the gains from switching fall in the **short term**. Some of these customers would be paying more than they otherwise would be compared to if they searched for alternatives.

More problematically, is that in the longer run, a less active demand-side of the market leads to less vigorous competition on the supply-side. This is likely to further entrench the market position of the incumbent retailers and dampen the incentives to offer lower prices and improve their services. In the long run, this is likely to result in prices that are higher than they otherwise would be, and new products and services that better meet customer needs are not developed and introduced into the market.

7.2.3 Mandating standard comparator rates would make some customers worse off

Recent reviews and commentary on the electricity market has suggested that ‘standard comparator rates’ could deliver better customer outcomes by making it easier for customers to compare offers and participate in the market.¹¹³ For example, the Grattan Institute and the Thwaites report both recommended presenting offers in terms of a ‘typical’ customer’s bill. The proposal has received some support from the Big 3 retailers. In their submissions to our Information Paper, NCOSS and the NSW Farmers’ Association also expressed support for a standard comparison rate.¹¹⁴

¹¹¹ Australian Government Department of Environment and Energy, *National Energy Customer Framework*, <http://www.environment.gov.au/energy/markets/national-energy-customer-framework>, accessed 11 October 2017.

¹¹² Australian Government Department of Environment and Energy, *National Energy Customer Framework*, <http://www.environment.gov.au/energy/markets/national-energy-customer-framework>, accessed 11 October 2017.

¹¹³ Grattan Institute, *Price shock: is the retail electricity market failing consumers*, March 2017, <https://grattan.edu.au/wp-content/uploads/2017/03/Price-shock-is-the-retail-market-failing-consumers.pdf>, p 31, accessed 9 September 2017, and *Independent review into the electricity and gas retail markets in Victoria*, August 2017, p xi.

¹¹⁴ NSW Farmers’ Association *submission to IPART Information Paper*, 28 June 2017, p 3; and NCOSS *submission to IPART Information Paper*, 30 June 2017, p 31.

However, we consider that a mandate on retailers to express offers in terms of ‘typical’ customer bills could limit competition to the detriment of many customers. Over the longer term, it could also stifle innovation and hamper the adoption of technology that could lower energy costs, resulting in higher energy prices for all customers.

It would be more difficult for ‘non-typical’ customers to identify good offers

Presenting offers in terms of bills for a ‘typical’ customer creates a trade-off between the ease of comparison on the one hand, and relevance to the specific circumstances of the customer. For example, the consumption profile and level of a ‘typical’ household with solar panels and a battery is very different from an identical household with neither.

By limiting the presentation of offers to ‘typical’ customers, it might make it *more* difficult for ‘non-typical’ customers to find the best offers for them. Importantly, a non-typical customer might not realise how their particular circumstances would differ from that of the ‘typical’ customer.

Wholesale energy costs would be higher than necessary

By limiting the available pricing options (eg, time-of-use tariffs) and innovative product offerings (eg, digital meters and automated demand response), efforts to reduce peak consumption would be hampered. As a result, the cost of peak-energy would be higher than necessary.

We note that stifling innovation would most benefit the vertically integrated retailers who are the major owners of generation assets, and make their largest revenues in peak periods. Therefore, they stand to lose the most from the adoption of demand management solutions.

It would be more difficult for retailers to compete for ‘non-typical’ customers, or on non-price aspects

Offers not targeted at ‘typical’ customers would compare poorly, even if they were attractive offers for ‘non-typical’ customers (see Box 7.2). This would also be the case for offers that included non-price elements, such as bundling with other services or energy savings or demand management technology. Many such offers would likely be withdrawn, limiting product innovation and options available to ‘non-typical’ customers.

Smaller retailers would struggle to compete, and incumbents’ market shares could be entrenched

By making it more difficult to compete for ‘non-typical’ customers and on non-price elements, the innovation and competitive edge offered by new retailers would also be diminished. Further, through intensified price-competition for ‘typical’ customers, smaller retailers might struggle to compete against the larger incumbents that benefit from economies of scale. In turn, this would result in fewer new retailers entering the market, less switching to smaller retailers, lower competitive pressure and the entrenching of the incumbents’ market shares.

Box 7.2 Example of offers that might be withdrawn as not targeting the “typical” customer

This example shows how three offers for a “typical” household that consumes 6,000 kWh per year might compare under a regulated typical customers profile. There are two time-of-use (TOU) tariffs and one flat anytime tariff, as shown below.

Unit	TOU 1	TOU 2	Anytime
Supply charge (c/day)	80	80	90
Peak (c/kWh)	58	45	36
Shoulder (c/kWh)	16	28	36
Off-peak (c/kWh)	9	22	36

To arrive at the comparison rate or bill for the TOU tariffs, the regulator must assume a “typical” consumption profile. In this example, we have assumed a typical consumption profile as shown below, along with actual consumption profile for two hypothetical customers.

Consumption period	Regulated “typical” profile	Customer 1 (C1) actual	Customer 2 (C2) actual
Peak	60%	45%	50%
Shoulder	25%	30%	25%
Off-peak	15%	25%	25%

Using the regulated “typical” profile to estimate annual bills for each tariff are shown below. The table also shows the actual bills for the two hypothetical customers, and the lowest bill in each case is shown in green. As shown, the anytime tariff would be the lowest *advertised* bill, but customer 1 would receive a lower annual bill under the TOU 1 tariff, while customer two would have a lower bill under the TOU 2 tariff.

“Typical” vs actual bills	TOU 1	TOU 2	Anytime	Saving vs lowest advertised
“Typical” bill advertised	\$2,701	\$2,530	\$2,489	N/A
C1 actual	\$2,281	\$2,341	\$2,489	\$208
C2 actual	\$2,407	\$2,392	\$2,489	\$97

In this case, a retailer might choose to withdraw offers like TOU 1 and TOU 2, as they would advertised as more expensive for the “typical” customer.

Source: IPART calculations.

7.3 Governments should prioritise measures to enhance customer engagement

We consider that competition is the best way to drive down electricity retail prices, as different suppliers compete for customers. Competition also creates incentives for retailers to better tailor their products to customers’ needs, and sell electricity in new ways – including bundling it with solar panels or battery storage – much like mobile phones are often sold with phone services and data in the telecommunications industry. In the longer

run, this will result in more efficient outcomes and better products and services for customers.

However, we think that there is a role for governments to improve customer engagement in the retail market, because the more well-informed and engaged customers are, the more pressure is on retailers to offer competitive prices and services. In addition, by assisting vulnerable and disadvantaged customers who may find it difficult to participate in the retail market, to search and switch to a lower offer would mean over time less customers would need to enter hardship programs.

As discussed in the sections above, introducing more rules about the types of offers that retailers can provide, the prices that they can charge, and how they are required to communicate with customers would stifle innovation and limit options for customers.

As discussed in Section 7.2.1, any additional measures should be introduced consistently across states and territories under the National Energy Customer Framework to minimise costs for customers and taxpayers.

The ACCC is currently undertaking a national inquiry into the supply of retail electricity and the competitiveness of retail electricity prices. As part of its inquiry, it has been asked to review any impediments to consumer choice, (including transaction costs, a lack of transparent information, or other factors) and the impact of diverse customer segments and different levels of consumer behaviour, on electricity retailer behaviour and practices.

There is no ‘silver bullet’ or single solution to concerns about the comparability of energy offers and customer engagement. However, some of the proposals that have been submitted to this review and other reviews are outlined below, including:

- ▼ promoting and enhancing the energymadeeasy.gov.au online comparator website
- ▼ providing customers with better access to and control over their usage data,
- ▼ requiring retailers to inform customers when their prices change,
- ▼ removing unnecessary information from bills, and
- ▼ establishing a database of customers who have not recently switched.

We will further consider whether additional measures are needed to improve customer engagement for our Final Report. If we consider additional measures are needed, we would make recommendations for the NSW Government to consider through the National Energy Customer Framework.

7.3.1 Promoting and enhancing the energymadeeasy.gov.au online comparator

As Chapter 6 discussed, customers can find it very difficult to compare offers without online comparator tools. This is because electricity offers are made up of several different tariffs, including a supply charge, a range of consumption charges that sometimes vary by time of day, and discounts that can be applied to some or each of these charges.

The Australian Energy Regulator (AER) provides an online comparator tool, energymadeeasy.com.au. However, the AEMC found the awareness of this tool to be as low

as 13% in NSW.¹¹⁵ We also note that the tool is of limited help to the 25% of customers with solar panels, as it doesn't account for customers' consumption from PV units, feed-in tariffs and metering arrangements, which can affect the overall bill outcome for solar customers.

In its recent report, the AEMC recommended steps to improve the usability of the energymadeeasy.gov.au tool and increase customers' awareness of the tool so as to encourage further customer participation in the retail energy markets.¹¹⁶ In its submission to our Information Paper for this review, the NSW Farmers' Association expressed its support for this recommendation.¹¹⁷

7.3.2 Providing customers access to and control over their data

For several years the AEMC has recommended that customers be given access to their consumption data, which could be provided to third-party services and be used to identify the best offers on behalf of that customer.¹¹⁸ This was also one of the key recommendations from the Finkel review and the Thwaites review.¹¹⁹

7.3.3 Requiring retailers to inform customers when their prices change

Several reviews have recently recommended that retailers should be required to inform customers:

- ▼ when their prices change, and the likely bill impacts of the change
- ▼ when their discounting period concludes
- ▼ what other deals they offer.¹²⁰

These recommendations were also supported by some stakeholders in response to our information paper.¹²¹ NCOSS submitted that retailers should be required to directly inform customers in writing prior to the end of their current deal and tell them what the end of the deal will mean for them if they do not do anything.¹²²

¹¹⁵ Newgate Research, *Consumer Research for the Australian Energy Market Commission's 2017 Retail Competition Review*, April 2017, p 107.

¹¹⁶ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 16-17.

¹¹⁷ NSW Farmers' Association submission to IPART Information Paper, 28 June 2017, p 3.

¹¹⁸ AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 18.

¹¹⁹ *Independent Review into the Future Security of the National Electricity Market*, June 2017, p 143, and *Independent Review into the electricity & gas retail markets in Victoria*, August 2017, https://engage.vic.gov.au/application/files/7415/0267/4425/Retail_Energy_Review_-_Final_Report.pdf, p xii, accessed 10 October 2017.

¹²⁰ Grattan Institute, *Price Shock, Is the retail electricity market failing consumers?*, March 2017 <https://grattan.edu.au/wp-content/uploads/2017/03/Price-shock-is-the-retail-market-failing-consumers.pdf>, p 33, accessed 9 October 2017; AEMC, *2017 Retail energy competition review*, Final Report, 25 July 2017, p 17; and *Independent review into the electricity and gas retail markets in Victoria*, https://engage.vic.gov.au/application/files/7415/0267/4425/Retail_Energy_Review_-_Final_Report.pdf, p xi, xii, accessed 10 October 2017.

¹²¹ CPSA submission to IPART Information Paper, 30 June 2017, p 4; NCOSS submission to IPART Information Paper, 29 June 2017, p 31.

¹²² NCOSS submission to IPART Information Paper, 29 June 2017, p 31.

We note the Australian Government recently indicated it will seek a change to the national electricity rules to require retailers to inform customers when the discount period is about to end, and the bill impact of this.¹²³

7.3.4 Removing unnecessary information from bills

Customer bills can be difficult to navigate as they contain a large amount of information relating to all of the different bill components. The Thwaites review found that there is an opportunity to simplify some of this information by requiring retailers to present all charges inclusive of GST.¹²⁴

All businesses must present a GST-inclusive price to their customers. However, retailers also choose to present the GST-exclusive rates because they appear lower than the GST-inclusive rates. No retailer has an incentive on its own to remove GST-exclusive rates because there is a chance that it will then appear to compare poorly to other retailers who present GST-exclusive rates. However if all retailers are required to present all charges on a GST-inclusive basis, no retailer would be disadvantaged.

7.3.5 Establishment of a database of customers who have not recently switched

The AEMC found that 50% of households in the NEM had not changed their retailers or contracts in five years. In 2016, the UK Competition and Markets Authority (CMA) made the decision to create a database of customers who have not switched energy offers in three or more years, and give retailers access to this database.¹²⁵

Draft finding

- 8 The NSW Government use the National Energy Customer Framework if it requires additional measures to improve or promote customer engagement so as to minimise costs for customers and taxpayers.

Draft recommendation

- 1 The AER's energymadeeasy.gov.au web comparison tool should be promoted and be improved so it:
 - clearly displays tariff information, ensures tariff information is downloadable in a numeric format, and sets the default bill calculation period equal to a customers' bill period, and
 - incorporates the impact of the solar PV units on customer bills.

¹²³ Prime Minister of Australia, *A Better Deal for Australian Families*, 9 August 2017 <https://www.pm.gov.au/media/2017-08-09/better-deal-australian-families>, accessed 9 August 2017

¹²⁴ *Independent Review into the electricity & gas retail markets in Victoria*, August 2017, p 56, https://engage.vic.gov.au/application/files/7415/0267/4425/Retail_Energy_Review_-_Final_Report.pdf, accessed 9 October 2017.

¹²⁵ CMA, *Modernising the Energy Market*, 24 June 2016, p 8, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/531204/overview-modernising-the-energy-market.pdf, accessed on 12 October 2017.

7.4 Protections for customers of residential caravan park customers in embedded networks

Another national energy market review that is currently underway is a review of the regulatory arrangements for embedded networks. This review is being undertaken by the Australian Energy Market Commission (AEMC).

Embedded networks are private networks which serve multiple premises. They are connected to a distribution or transmission system in the national electricity market through a central connection point. Common examples of embedded networks include shopping centres, retirement villages, apartment complexes and caravan parks. These customers are charged for their electricity by the owner of the network (such as a caravan park owner), rather than by a retailer.

In its Draft Report, the AEMC found that compared with standard supply customers, embedded network customers receive less consumer protections.

The AEMC held a roundtable with stakeholders representing caravan park residents, who have experienced particular problems with being supplied in an embedded network area. For example, caravan park owners are able to charge their customers' standing offer rates, even though the park owners pay the distributor much lower rates.¹²⁶ As discussed in Chapter 4, standing offer rates are 25% higher than market offer rates on average. Therefore, many customers living in caravan parks are paying substantially more for their electricity than other customers, even though they are likely to be least able to afford it.¹²⁷

There are around 20,000 caravan park residents in NSW that are being supplied within an embedded network.¹²⁸ Unlike other customers, these customers are less able to change supplier if they are unhappy with the price they are paying or level of service they are receiving.

The AEMC is currently reviewing the regulatory arrangements for these networks. Its draft recommendations are for the existing regulatory framework for embedded networks to be changed to improve the alignment of the regulation of retailers and network service providers for standard supply customers and embedded network customers.

¹²⁶ AER, Applicable conditions for exemption class R4, <https://www.aer.gov.au/retail-markets/retail-exemptions/classes-of-retail-exemption-applicable-conditions/applicable-conditions-for-exemption-class-r4#condition-7---pricing>

¹²⁷ AEMC, *Review of regulatory arrangements for embedded networks*, Draft Report, 12 September 2017, <http://www.aemc.gov.au/getattachment/08fa7747-e165-4bd6-9691-d43e82c2213e/Draft-report.aspx>, accessed 9 October 2017.

¹²⁸ The Caravan, Camping & Touring Industry & Manufactured Housing Industry Association of NSW Ltd (CCIA), Submission on Issues Paper, Access to Dispute Resolution Services for Exempt Customers, June 2017, https://www.aer.gov.au/system/files/Caravan%2C%20Camping%20%26%20Touring%20Industry%20%26%20Manufactured%20Housing%20Industry%20Association%20of%20NSW%20submission%20-%20Access%20to%20dispute%20resolution%20services%20for%20exempt%20customers%20-%2013%20July%202017_0.pdf, accessed 12 October 2017.

However, the AEMC does not have jurisdiction for many important parts of the regulatory framework. It cannot change the state-based arrangements, such as those in NSW which do not provide embedded network customers access to EWON's dispute resolution services.¹²⁹

We are recommending that the NSW Government investigate what changes to the state based regulatory framework are required to ensure electricity customers in caravan parks' embedded networks receive the same level of consumer protection as customers that can participate in the competitive retail market. IPART would be well placed to undertake such a review.

Draft recommendation

- 2 The NSW Government investigate the most efficient method to provide electricity customers in residential caravan parks embedded networks the same level of consumer protection as customers that can participate in the competitive electricity retail market.

¹²⁹ AEMC, *Review of regulatory arrangements for embedded networks*, Draft Report, 12 September 2017, <http://www.aemc.gov.au/getattachment/08fa7747-e165-4bd6-9691-d43e82c2213e/Draft-report.aspx>, p vi, accessed 9 October 2017.

8 Measures to assist hardship customers

As Chapter 2 discussed, as part of this review, the Minister asked IPART to report on retailers' strategies to deliver lower prices to hardship customers. In response to this request, we wrote to all electricity retailers operating in NSW to request information on their strategies and the methods they used to raise their customers' awareness of the assistance that is available to reduce electricity bills.

The sections below provide an overview of our draft findings and then discuss them in more detail.

8.1 Overview of draft findings

We found that all retailers have strategies to improve outcomes for hardship customers that include informing those in their hardship program of the concessions and rebates available to them. These strategies also involve either switching customers who are in their hardship program to plans with lower prices, or advising these customers that they would save money on their electricity bill if they change plans.

Retailers use a range of methods to raise their customers' awareness of the assistance measures available, including contacting them directly and providing information through community support groups.

However governments and retailers should assist vulnerable and disadvantaged customers who may find it difficult to participate in the retail market to search and switch to a lower offer as this would mean over time less customers would need to enter hardship programs.

8.2 Retailer strategies for delivering lower prices to hardship customers

Retailers currently use a range of strategies to deliver lower energy bills to their hardship customers. The most common strategy, used by all retailers, is advising these customers of available government rebates and concessions. Other strategies include:

- ▼ advising customers of cheaper tariff plans that are available,
- ▼ proactively moving customers to cheaper tariff plans,
- ▼ providing financial assistance such as debt relief or bill credits,
- ▼ establishing payment plans, or weekly, fortnightly or monthly billing, and
- ▼ not charging late payment fees.

Table 8.1 Retailer strategies for assisting customers experiencing financial hardship

Strategy	Retailers
Proactively moving hardship program customers to cheaper plans	AGL, Powerdirect, Alinta, Click Energy, CovaU, EnergyAustralia
Advising customers of cheaper tariff plans that are available	ActewAGL, Alinta, Diamond Energy, Enova, Powershop, Momentum Energy, Lumo Energy, Red Energy, Sanctuary Energy
Advising customers of available rebates/concessions	All Retailers
Providing financial assistance such as debt relief/ funds towards energy vouchers/bill credits/freezing price increases for hardship customers	ActewAGL, AGL, Powerdirect, EnergyAustralia, Origin, Momentum, Lumo Energy, Red Energy
Approaching concession card customers and assisting them to move to a lower priced contract, or advising them of rebates that are available.	AGL, Powerdirect
Assisting customers to apply for grants and concessions	Alinta, Enova, Momentum
Guaranteeing pay on time discounts/other discounts/ where the customer has entered into a payment plan.	1st Energy, Origin, Powershop, Simply Energy
Advice on reducing usage	1st Energy, ActewAGL, Alinta, EnergyAustralia, Enova, Dodo, Commander, Origin, QEnergy, Lumo Energy, Red Energy, Sanctuary Energy
Weekly/fortnightly/monthly billing and/or payment plans	1st Energy, AGL, Powerdirect, CovaU, EnergyAustralia, Energy Locals, Enova, Mojo, Origin, Pooled Energy, Sanctuary Energy, Simply Energy

Source: Retailer responses to IPART

The Combined Pensioners and Superannuants Association (CPSA) submitted that electricity retailers should be required to notify recipients of the Low Income Household Energy Rebate of the best value plan available to them and provide support to switch plans. CPSA also noted that it occasionally receives calls from pensioners who are not aware of this rebate and have not been receiving it. Given the vulnerability of these customers, CPSA submitted that electricity retailers should determine a customer's eligibility at the point of sign up.¹³⁰

The NSW Council of Social Service (NCOSS) submitted that retailers should be required to put all Low Income Household Energy Rebate recipients, hardship customers and customers on payment plans onto a 'best deal', or develop special low cost deals for this cohort.¹³¹

There are already quite stringent requirements in relation to retailers' hardship policies and programs. Under the National Energy Retail Law, all retailers are required to have a hardship policy. The AER must approve these policies and monitor the retailer's performance in implementing it.¹³²

¹³⁰ CPSA submission to *IPART Information Paper*, 30 June 2017, p 6-7.

¹³¹ NCOSS submission to *IPART Information Paper*, 29 June 2017, p 31.

¹³² National Energy Retail Law (NSW) No 37a, Division 6.

Before it approves a hardship policy, the AER must be satisfied that the retailer has processes to:

- ▼ review the appropriateness of a hardship customer's market retail contract,
- ▼ identify customers experiencing payment difficulties due to hardship, including identification by the retailer and self-identification by the customer,
- ▼ provide an early response to customers in hardship,
- ▼ allow flexible payment options (including payment plans and Centrepay) for the payment of energy bills by hardship customers, and
- ▼ identify, and notify customers of, appropriate government concession programs and appropriate financial counselling services.

The National Energy Retail Law also requires that retailers notify hardship customers of appropriate government concession programs and appropriate financial counselling services. The AER is currently conducting a review of retailers' hardship policies with a focus on early detection and consumer outcomes. In addition, the NSW Government recently announced an Energy Bill Relief package,¹³³ which imposes penalties on retailers who do not move rebate recipients to a better deal (see Box 8.1).

We consider that retailers' strategies, plus the existing requirements and announced penalties, should help to ensure customers experiencing financial hardship benefit from competition. We will monitor outcomes for vulnerable customers and those in retailer hardship programs to assess whether retailers strategies are ensuring that these group of customers not paying more than they need to.

8.3 Retailer strategies for increasing awareness of available rebates or market offers

Retailers communicate to customers via a range of channels to make them aware of available rebates or more competitive offers. Some of the ways that retailers increase awareness of rebates or better market offers include:

- ▼ having telephone discussions with new customers about concessions, government rebates and how to ensure a customer is on the best available offer,
- ▼ providing community support groups with information to distribute to members detailing ways hardship customers can access assistance in paying their energy bills,
- ▼ approaching concession card customers and assisting them to move to a better contract, or advising them of rebates that are available,
- ▼ assisting customers to apply for grants and concessions,
- ▼ providing information on bills, websites and letters regarding available rebates, and
- ▼ proactively identifying customers in potential hardship to provide information on available assistance.

¹³³ http://www.resourcesandenergy.nsw.gov.au/__data/assets/pdf_file/0011/734843/Energy-bill-relief-package-for-households-and-small-business.pdf, accessed 4 October 2017.

For example, Enova commented that it regularly reviews its customers' payment history for indicators that a customer needs assistance under its hardship program. If this review indicates that a customer needs assistance then Enova contacts the customer directly and provides advice on access to government rebate schemes. CovaU uses its bills to provide information regarding hardship and rebates and prompts the customer to contact them for assistance.

In its submission to the Information Paper, the Public Interest Advocacy Centre (PIAC) commented that when retailers are ineffective at communicating with their customers, this adversely impacts low-income and vulnerable consumers, who are least able to afford higher electricity costs. These customers may also find it difficult to engage in the market due to being less financially literate, having a language barrier, a disability or being on a hardship plan or prepayment arrangement that limits their ability to change retailers.¹³⁴

As discussed in Chapter 7 there is a role for Government and retailers to assist vulnerable and disadvantaged customers who may find it difficult to participate in the retail market to search and switch to a lower offer as this would mean over time less customers would need to enter hardship programs.

Box 8.1 NSW Government Energy Bill Relief Package

On 3 September 2017, the NSW Government released its Energy Bill Relief Package for Households and Small Business. The package contained a number of measures aimed at vulnerable and hardship customers, and included changes to rebates. Some of the measures contained in the package that were aimed at these customers included:

- ▼ increasing the Low Income Household rebate from \$235 to \$285 and the Family Energy Rebate from \$150 to \$180
- ▼ penalties for retailers who don't move rebate recipients to a better deal
- ▼ discounts for up to 23,000 concession cardholders to save up to 50% on the cost of upgrading old fridges and TVs to energy saving models, saving each household on average around \$200 a year, and
- ▼ energy saving upgrades for up to 16,500 public housing clients to assist the state's most vulnerable, with participating households to save an average of around \$360 per year on their bills.

Source: Gladys Berejiklian, Premier of NSW, *Energy Bill Relief Package for Households and Small Business*, 3 September 2017, http://www.resourcesandenergy.nsw.gov.au/__data/assets/pdf_file/0011/734843/Energy-bill-relief-package-for-households-and-small-business.pdf, accessed 4 October 2017.

¹³⁴ PIAC submission to IPART Information Paper, 30 June 2017, p 2.

9 Take up of digital meters

In NSW, most residential and small business customers still have 1950s-style electricity meters that have limited functionality. As a result, most customers have limited information available to them from which to make informed decisions about their electricity use and costs.

From 1 December 2017, new rules will come into force across the NEM which mean that networks will no longer have responsibility for metering services. Customers can choose to arrange the meter replacement through their retailer or directly from registered metering providers. Introducing competition among installers is designed to promote innovation and lead to investment in advanced meters that deliver services valued by customers at a price they are willing to pay.

Digital meters, and the energy products and services this technology enables, allow customers to make decisions about how and when they use electricity, and manage the costs of those decisions. This should enhance retail competition.

As part of this review, we consulted with retailers about their processes for managing the timely delivery of digital meters and how the delivery is being communicated to their customers. The sections below outline our draft findings and then discuss them in more detail.

9.1 Overview of draft findings

Most retailers told us they have put in processes for managing the take up of digital meters including arrangements with installers to be ready to deploy digital meters in a timely, safe and effective manner. Most plan to publish easily accessible information about digital meters on their websites with FAQs, and to train their frontline staff to discuss customers' options around digital meters. Most retailers also plan to distribute marketing material to customers in early 2018.

Some retailers acknowledged there had been problems with the delivery of digital meters for Solar Bonus Scheme customers after this scheme closed at the end of 2016, and they had applied lessons learned from this experience in preparing for the broader delivery of meters to customers.

Given the recent problems with the delivery of digital meters for solar bonus customers and the important role that digital meters can play in the retail market, we propose to review issues around the take up of digital meters as part of our 2018 review of the performance and competitiveness of the NSW retail electricity and gas markets.

9.2 Retailers plans to inform customers about digital meters

Retailers indicated they propose to use a range of strategies to inform customers about the delivery of digital meters, and will select communication methods to suit their customers' needs and preferences. For example, several retailers propose to raise customer awareness about the benefits of installing digital meters, such as:¹³⁵

- ▼ enabling remote meter readings, thus removing the need for estimated bills and onsite meter reads,
- ▼ providing customers with more energy information, which can help them manage their electricity usage,
- ▼ enabling innovative products and services, which can give customers more choice and control of their electricity consumption, production and export (where the customer has solar panels and/or battery storage),
- ▼ allowing remote connection and disconnection services, making it easier, more efficient and cheaper to move properties, and
- ▼ allowing the early detection of supply issues, including as a result of blackouts, system-failure and critical power management faults.

Retailers also plan to communicate to customers about the timing of stages associated with the installation process as well as providing specific communications for consumers with anticipated issues for installation, such as reliable access to communications networks or remedial work required to meter boards and how that may be undertaken.

Retailers generally acknowledged there were problems with the delivery of digital meters for former Solar Bonus Scheme (SBS) customers. Some retailers are still resolving outstanding meter installations. Importantly retailers advised they have attempted to contact SBS customers who are yet to receive a digital meter via phone or leaving behind cards at the time of an incomplete installation.

EWON received many customer complaints about poor customer service associated with changing meters for former SBS customers. Customers complained about inadequate communication about how long they would have to wait for a meter to be installed. EWON also received many complaints about some retailers that offered a free digital meter as an incentive for customers to switch retailers, but then failed to install the digital meter.

Poor retailer communication around the waiting time for digital meters to be installed increased customers frustrations and concerns as former SBS customers were responding to marketing campaigns to switch retailers to obtain a better deal.

Given the recent problems with the delivery of digital meters for solar bonus customer and the important role that digital meters can play in the retail market we propose to review issues around the take up of digital meters as part of our 2018 review of the performance and competitiveness of the NSW retail electricity and gas markets.

¹³⁵ Requires remote communications to be enabled. Customers can elect not to have remote communications enabled on their digital meter at the time the digital metering is being installed. Some retailers may charge for digital meters without remote communications and some products or services may not be available.

Draft IPART finding

- 9 IPART will review issues around the take up of digital meters as part of our 2018 review of the performance and competitiveness of the NSW retail electricity and gas markets.

10 Gas price increases reflect a competitive market

When the NSW Government deregulated retail gas prices from 1 July 2017, our role as Market Monitor was expanded to monitor the performance and competitiveness of the gas market. We will make our first annual report to the Minister by 30 November 2018, which will cover the year 2017-18.

However, as gas retail prices increased by around 5% to 16% at the start of 2017-18,¹³⁶ the Minister asked that we analyse these price increases and consider whether they are consistent with a competitive market, as part of this review. The sections below outline our draft findings then discuss them in more detail.

10.1 Overview of draft findings

We found that the changes in retail gas prices between June and July 2017 reflect changes in the underlying costs of supplying gas, and therefore are consistent with a competitive market. These costs have increased by 6.8% to 11.8% in coastal NSW and by 12.5% to 20.9% in country NSW since 2016-17.¹³⁷

The main driver of this increase was higher wholesale gas prices, due to material changes in demand and supply conditions in eastern Australia.

10.2 Changes in gas retail prices

To assess whether the price changes from July 2017 are consistent with a competitive market, we measured changes in annual bills from June 2017 to July 2017 based on information retailers provided on their prices. We then analysed changes in the main underlying costs of supplying gas over the same period.

10.2.1 Price changes from June 2017 to July 2017

We compared estimated annual bills for a typical residential customer based on the major retailers' prices in June 2017 and July 2017 for coastal and country NSW. Estimated annual bills for country customers are higher than those for coastal customers, due to the higher average annual consumption in country NSW (Figure 10.1 and Figure 10.2).

Customers on standing offers had the highest bills. For the Big 3 retailers, customers' bills increased by between 6% and 9% for coastal customers¹³⁸ and by between 6% and 15% for

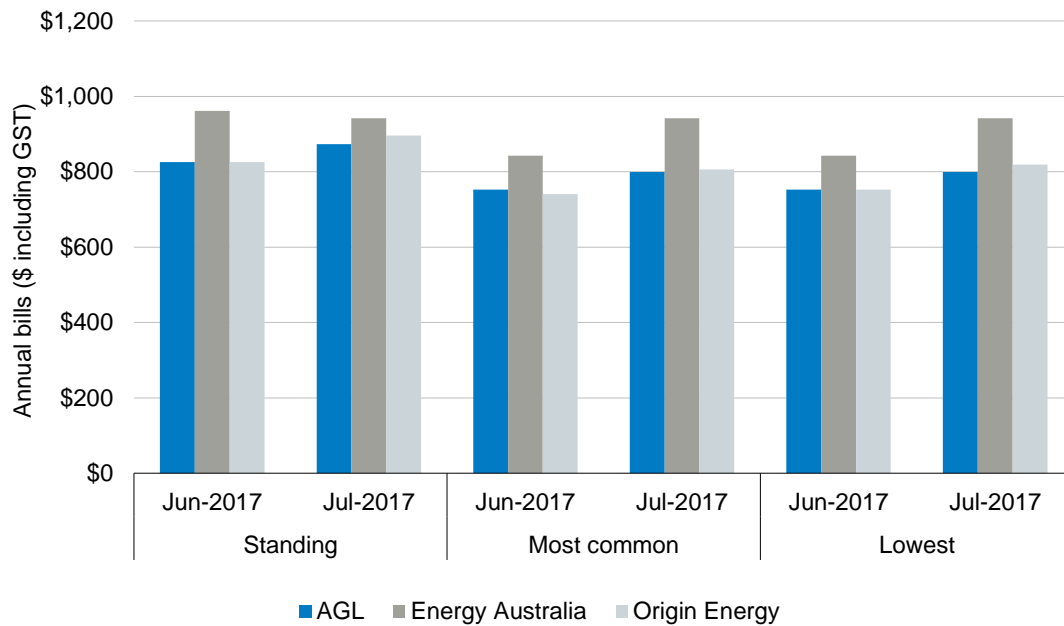
¹³⁶ For the Big 3 retailers in Coastal and Country NSW. Where retailers supply gas in different network areas in Country NSW, annual bills are averaged within each retailer.

¹³⁷ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 53.

¹³⁸ Except for EnergyAustralia for which standing offer prices decreased by 2%. Bills are calculated based on annual consumption of 20 GJ.

country customers.¹³⁹ The bills of customers on the lowest market offers increased by similar amounts (between 6% and 12% for coastal customers and between 5% and 16% for country customers).

Figure 10.1 Estimated annual gas bills for typical residential customers on standing offers, most common market offers and cheapest market offers in coastal NSW (Nominal, GST-inclusive)

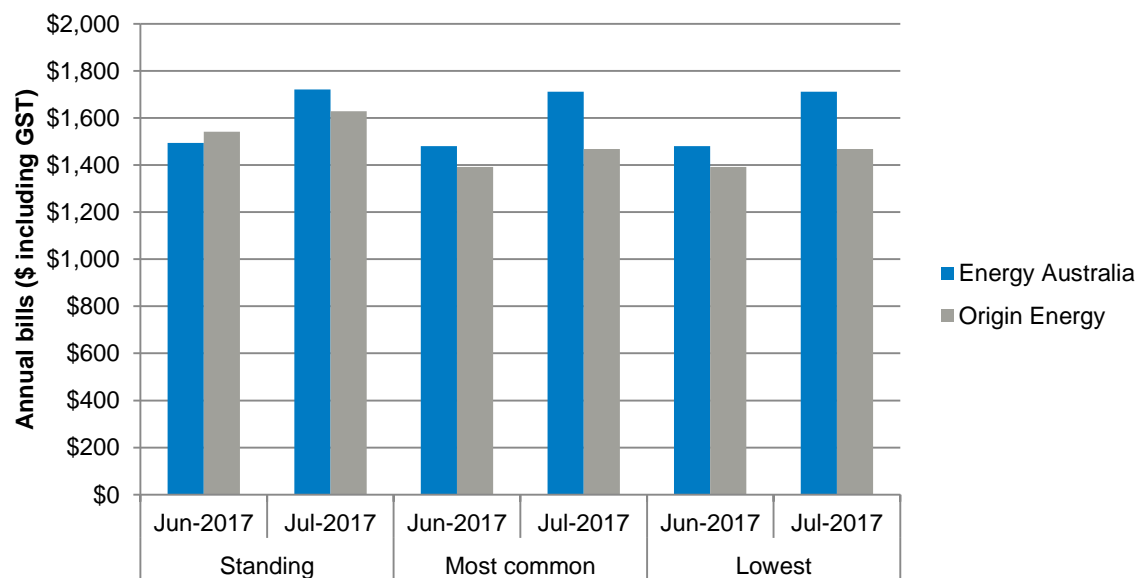


Note: Bills are calculated based on annual consumption of 20 GJ, taking into account all available conditional and non-conditional discounts.

Data source: Gas retailers and IPART calculations

¹³⁹ Bills are calculated based on annual consumption of 45 GJ.

Figure 10.2 Estimated annual gas bills for typical residential customers on standing offers, most common market offers and cheapest market offers in country NSW (Nominal, GST-inclusive)

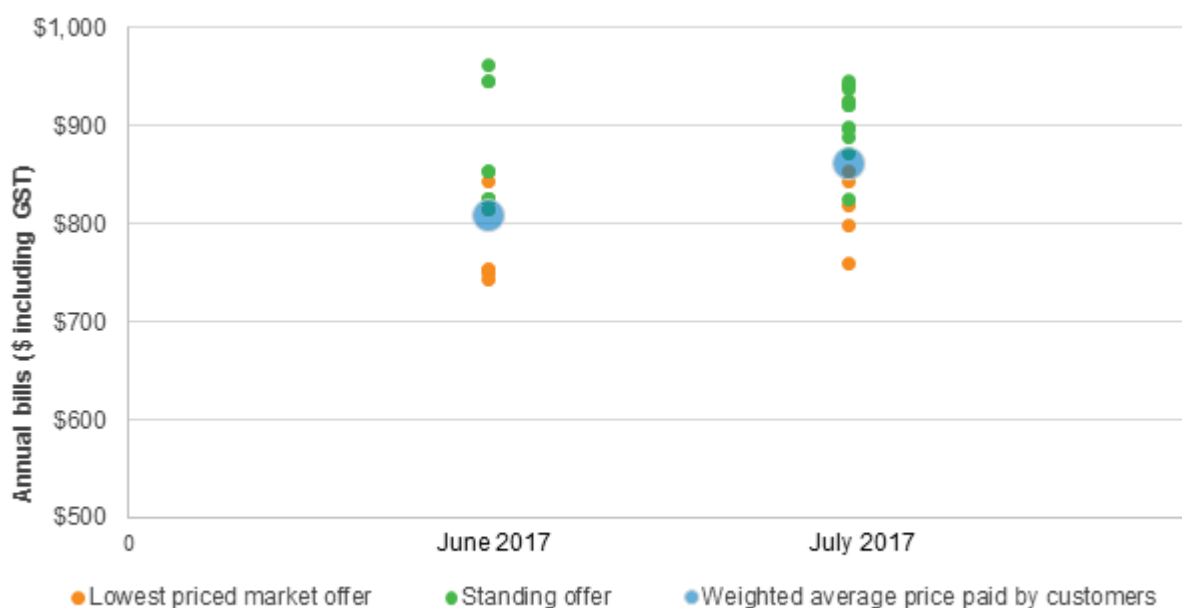


Note: Bills are calculated based on annual consumption of 45 GJ, taking into account all available conditional and non-conditional discounts. EnergyAustralia and Origin have offers in various network areas in Country NSW. Annual bills are averages within each retailer.

Data source: Gas retailers and IPART calculations.

Similar to our findings in the retail electricity market, there seems to be a wide variation in retail gas prices in coastal NSW (Figure 10.3). There is less intense competition in country NSW, with only one or two active retailers and a few different market offers for customers to choose from. However, the range of discounts available is not materially different to those offered to coastal NSW.

Figure 10.3 Annual bills for coastal NSW customers (Nominal, GST inclusive)



Data source: Gas retailers and IPART calculations.

The increases in the estimated annual bills between coastal and country NSW are similar (when weighted by the number of customers on standing, most common and cheapest offers) (Table 10.1). We estimate that between June 2017 and July 2017, retail gas prices increased on average by around 6.6% to 6.8% for coastal and country customers.

Table 10.1 Average gas retail bills (Nominal, GST inclusive)

	June 2017	July 2017	% change
Coastal NSW	\$809	\$862	6.6%
Country NSW	\$1,453	\$1,552	6.8%

Note: Coastal NSW includes the Jemena network area and Country NSW includes all other areas of NSW. We used annual consumption of 20 GJ for Coastal NSW and 45 GJ for Country NSW. Weighted average annual bills are calculated as explained in Box 3.2. Retailers' market shares for Coastal customers are from the AER's retail statistics and those for Country customers are from IPART's household survey results for the Riverina area.

Source: Price information provided by retailers.

10.3 Changes in the underlying costs of supplying gas from July 2017

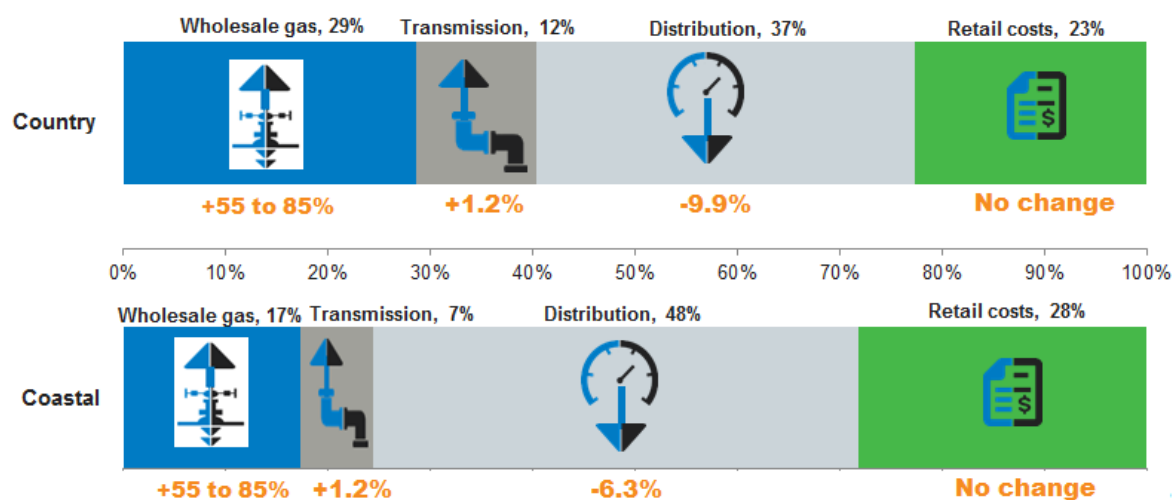
Retailers incur a number of different costs to supply gas, including:

- ▼ **wholesale gas costs**, which are the costs that retailers face in procuring the gas that they supply to their customers,
- ▼ **network costs**, which include payments for the use of the transmission pipelines and the distribution network, and
- ▼ **retail costs**, which include the costs that a retailer incurs in operating its retail business to supply gas to its customers (ie, retail operating costs), and the return that it requires to attract the capital needed to provide a retailing service (ie, retail margin).

We engaged Frontier to examine the changes in these costs from July 2017 and estimate reasonable overall price changes from 2016-17 to 2017-18 for an efficient retailer.

Frontier estimated that the total costs of gas supply increased by between 7% and 12% for coastal customers and by between 12% and 21% for country customers. This was primarily due to a substantial increase in wholesale gas costs (Figure 10.4).¹⁴⁰ As wholesale gas costs represent a bigger proportion in the total bill for country customers, the material increase in wholesale gas costs has a bigger impact on these customers than on coastal customers.

Figure 10.4 Changes in gas supply costs by cost category in 2017-18



Data source: Frontier Economics, *Cost Drivers of Recent Retail Electricity and Gas Prices for Residential Customers in NSW – A Report Prepared for IPART*, September 2017.

¹⁴⁰ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 53.

10.3.1 Wholesale gas costs have increased materially

Frontier found that wholesale gas prices in NSW have increased substantially by around 55% to 85% from June to July 2017. Changes in demand and supply conditions in eastern Australia are the largest contributor to these price increases. For example:

- ▼ the commencement of LNG exports at Gladstone, Queensland has tripled the demand for gas in eastern Australia within a few years
- ▼ gas production capacity has increased by less than expected compared to when construction of the LNG projects commenced due to:
 - lower than expected gas production from Queensland's coal seam gas fields
 - the abandonment or delay of new developments as a result of state government policies restricting or preventing the development of certain gas projects, and
 - a reduction in gas production from a number of existing projects including from the Cooper-Eromanga basin and Victoria's offshore gas basins.¹⁴¹

The combined effect of these supply and demand trends has been a tightening of the supply-demand balance for gas in eastern Australia and an increase in the marginal opportunity cost of supplying gas. This has resulted in higher prices.¹⁴² Additionally, there have been a number of recent inquiries into the gas sector in eastern Australia, with these inquiries suggesting a lack of competition has exacerbated this pricing pressure.¹⁴³

10.3.2 Network costs

Network costs, which include the transmission and distribution costs, account for 55% and 49% of the total gas supply costs for coastal and country areas, respectively. Frontier found that the distribution costs have decreased by 6.3% for coastal customers and by 9.9% for country customers. However, transmission costs increased slightly by 1.2% for all customers.¹⁴⁴

10.3.3 Retail costs

Retail costs, which include retail operating costs and retail margins, account for 28% and 23% of the total gas supply costs for coastal and country areas, respectively. Retail costs represent a bigger proportion in the total costs for gas retailers than for electricity retailers. This is because retail operating costs represent the same, fixed amount for both electricity and gas, even though gas bills tend to be smaller than electricity bills.

Frontier found no clear evidence to suggest that retail costs changed materially between 2016-17 and 2017-18. It did not quantify a percentage change in the retail costs from 2016-17 to 2017-18 for an efficient retailer.¹⁴⁵

¹⁴¹ Frontier Economics, *Cost drivers of recent retail electricity and gas prices for residential customers in NSW – A report prepared for IPART*, September 2017, p 45; pp 47-48.

¹⁴² *Ibid*, p 48.

¹⁴³ *Ibid*, p 48.

¹⁴⁴ *Ibid*, p 49.

¹⁴⁵ *Ibid*, p 51.

Frontier's full Draft Report is available on our website www.ipart.nsw.gov.au.

Draft finding

- 10 The changes in retail gas prices between June and July 2017 reflect changes in the underlying costs of supply, and therefore are consistent with a competitive market.





Appendices

A IPART's statutory role

National Energy Retail Law (NSW) No 37a

234A—Market Monitor

(1) In this Part, the Market Monitor is the person prescribed by the NSW regulations as the Market Monitor for the purposes of this Part.

(2) The Market Monitor is to monitor the performance and competitiveness of the retail electricity market and the retail gas market in New South Wales for small customers.

(3) The Market Monitor is to report annually to the Minister on the performance and competitiveness of each of the retail electricity market and the retail gas market in New South Wales for small customers, including on the following matters –

(a) the participation of small customers in each market and, if the Market Monitor thinks it appropriate, particular groups of small customers;

(b) prices of electricity or gas for small customers in regional areas;

(c) any barriers to entry to or exit from, or expansion, in each market;

(d) the extent to which retailers are competing to attract and retain small customers;

(e) whether price movements and price and product diversity in each market are consistent with a competitive market;

(f) if the Market Monitor is of the opinion that it is required, steps necessary to improve the competitiveness of each market;

(g) whether there is a need for a detailed review of retail prices and profit margins in each market;

(h) any other matters the Market Monitor thinks appropriate.

(4) An annual report is to be prepared for each year commencing on 1 July.

(4A) The first annual report for the retail gas market is to be for the year commencing 1 July 2017.

(5) The annual report is to be provided to the Minister not later than 30 November following the end of the year to which the report relates.

(6) The Minister is to lay the annual report or cause it to be laid before both Houses of Parliament of this jurisdiction not later than 30 days after receiving the report.

(7) In preparing an annual report, the Market Monitor is to have regard only to the following—

- (a) information provided by the AEMC and the AER;
- (b) any publicly available information;
- (c) information provided by a retailer under subsection (8).

(8) The Market Monitor may, by notice in writing served on a retailer, require the retailer to provide particulars to the Market Monitor of the number of market offer customers of the retailer, the market offer prices of those customers, the number of customers on each standing offer price offered by the retailer that has been publicly advertised and those standing offer prices.

B Letter from Minister – 27 June 2017



Don Harwin MLC

Minister for Resources, Minister for Energy and Utilities,
Minister for the Arts, Vice-President of the Executive Council

V16/4095#15
BN17/3679

Dr Peter Boxall AM
Chair
Independent Pricing and Regulatory Tribunal
PO Box K35
HAYMARKET POST SHOP NSW 1240

27 JUN 2017

Dear Dr Boxall

Thank you for the opportunity to make a submission in relation to the Independent Pricing and Regulatory Tribunal's (IPART) 'Information Paper – 2017 NSW retail electricity market monitoring' consultation.

As highlighted in the paper, IPART previously found that electricity market competition is working and is delivering better outcomes for customers than if prices remained regulated. I am keen to ensure this continues and that the innovative range of electricity products and services that is emerging better meets the needs of customers.

IPART's role as market monitor throughout this process has been essential in monitoring competition and supporting consumer confidence in the electricity market.

The electricity market transition to clean energy, along with the opening of the east coast gas market to exports, has driven wholesale electricity and gas prices sharply higher over the last 12 months. This is expected to result in higher retail electricity and gas prices especially from July 2017.

The Australian Competition and Consumer Commission (ACCC) is already undertaking two reviews to examine retail electricity prices and the Australian gas market. Therefore, I ask that IPART undertakes a review of electricity and gas price movements into 2017-18, to advise on the drivers of any price changes and whether any such changes reflect efficient costs in a competitive market.

While this is outside the current electricity market monitor role which is reviewing 2016/17, I consider this critical to provide NSW households and businesses with independent advice on what is driving changes in energy prices. As you may be aware, the electricity and most gas network charges will be lower in 2017-18.

Should you have any further questions in relation to this matter, please contact Ms Katharine Hole, Executive Director, Energy Strategy, at the Division of Energy, Water and Portfolio Strategy on 9338 6634.

Yours sincerely



Don Harwin MLC
Leader of the Government in the Legislative Council
Minister for Resources
Minister for Energy and Utilities
Minister for the Arts
Vice-President of the Executive Council

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C Letter from the Minister – 22 August 2017



Don Harwin MLC

Minister for Resources, Minister for Energy and Utilities,
Minister for the Arts, Vice-President of the Executive Council

V17/8144#1

Dr Peter Boxall AO
Chair
Independent Pricing and Regulatory Tribunal
PO Box K35
HAYMARKET POST SHOP NSW 1240

22 AUG 2017

Dear Dr Boxall

I am writing to engage the Independent Pricing and Regulatory Tribunal (IPART) to undertake further work under the Retail Energy Market Monitoring 2017 review.

This additional work is to focus on retailer customer service as major transformations take place. As you would be aware, the electricity market transition to clean energy, along with the opening of the east coast gas market to exports, has driven wholesale electricity and gas prices sharply higher over the last 12 months. This has resulted in higher retail electricity and gas prices from July 2017. Concurrently, many customers are voluntarily transitioning to digital meters to help them manage their energy bills and make the best use of their solar systems.

In this context, affordability and customer service become critical components of ensuring customer engagement with the competitive energy market is a positive experience. I am keen to ensure that retailers are helping hardship customers in particular secure the best outcome possible. I held a retailer roundtable in May this year to set out Government expectations about good customer service practices including communications with customers. Therefore, I ask IPART to report on retailers' strategies to deliver lower prices to hardship customers, through consultation with retailers, and review of their publicly available customer policies.

A second key issue consumers are raising with me is around the installation of digital meters. Therefore I am also asking IPART to consult with retailers and report on their processes for managing the timely roll-out of digital meters and how the roll-out is being communicated to their customers.

I would appreciate if IPART would report on both these matters as part of the ongoing 2017 review, and no later than 30 November 2017.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Don Harwin'.

Don Harwin MLC

Leader of the Government in the Legislative Council
Minister for Resources
Minister for Energy and Utilities
Minister for the Arts
Vice-President of the Executive Council

D Summary of Stakeholder Submissions

We received 9 submissions to our Information Paper.

Table D.1 Issues raised by stakeholder submissions to Information Paper

Issue	Stakeholder Responses	Stakeholder
Price Increases/ Affordability	Electricity prices have increased substantially in recent years and will have a large impact on customers.	CPSA, p 1. PIAC, p 1.
Competition	Competition is not delivering better outcomes for customers, often due to lack of customer engagement, particularly among vulnerable customers.	CPSA, p 6. NCOSS, p i-ii. NSW Farmers' Association, p 3. PIAC, p 2.
	Differences in price structures do not represent innovation	NSW Farmers' Association, p 4.
	IPART should undertake analysis on whether consumers perceive differences in quality and reliability between retailers, and whether the market is innovative.	NSW Farmers' Association p 3
	New indicators are required to assess availability of new services such as demand response and behind-the-meter activities.	The Australian Energy Council, p 1-2.
Customer engagement	Retailers should be required to inform customers immediately of variations in the price of electricity, or inform customers prior to the end of their current deal to make them aware of impacts if they do not do anything	CPSA p 4. NCOSS, p 31.
	It is difficult to determine the best offer using the energymadeeasy.gov.au website, particularly for comparing single-rate offers and time-of-use offers.	NSW Farmers' Association, p 5.
	Transaction and search costs are high due to the large number of offers available which makes it difficult to compare offers and limits price competition	NSW Farmers' Association, p 5.
Hardship/ Vulnerable Customers	Low income and vulnerable customers have been particularly affected by recent price rises and had limited ability to engage in the retail market. These customers were not receiving the benefits of competition and were likely to be on uncompetitive standing offers.	CPSA, p 5-6. NCOSS, p ii. PIAC, p 1-2.
	Outcomes for vulnerable customers should be examined as one of IPART's indicators.	PIAC, p 2.
	Retailers should be required to notify recipients of the Low Income Household Rebate of the best plan available to them and provide support to switch plans.	CPSA, p 6.
Rebates/ Government Assistance	Retailers should proactively identify whether customers are eligible for rebates or assistance, or whether rebates should automatically be applied to low income customers.	CPSA, p 7. NCOSS, p 31.
	The Low Income Household Energy Rebate should be set as a percentage of the overall bill, rather than an overall rate.	CPSA, p 6. NCOSS, p 27 .
	Rebates and assistance such as the Family Energy Rebate and Emergency Accounts Payment Assistance should be	NCOSS, p 25.

reviewed and improved to increase awareness, ease of access, and ensure they are better targeted.
