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Ms Sarah Proudfoot
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Dear Ms Proudfoot

Submission to AER Issues Paper – Regulating Innovative Energy Selling Business Models under the National Energy Retail Law

EnergyAustralia is pleased to provide this submission to the Australian Energy Regulator’s Issues Paper on the regulation of innovative energy selling business models under the National Energy Retail Law (the Issues Paper).

EnergyAustralia is one of Australia’s largest energy companies, providing gas and electricity to over 2.6million household and business customers in NSW, Victoria, Queensland, South Australia and the Australian Capital Territory. EnergyAustralia owns and operates a multi-billion dollar portfolio of energy generation and storage facilities across Australia, including coal, gas and wind assets with control of over 5,000MW of generation in the National Electricity Market.

The emergence of new business models based on technological developments is creating challenges for regulators across many industries who must balance the need to maintain adequate consumer protections with the promotion of innovation and competition. Examples include the commercial passenger vehicle and hospitality industries where companies such as Uber and AirBnB are challenging incumbent market participants who are subject to more significant regulatory obligations.

The energy sector in Australia is somewhat different in that it receives particular attention from policymakers, regulators and other stakeholders; this reflects the importance for households and business of reliable and safe energy supply. It is perhaps the most heavily regulated sector of the economy and it is clear that regulation is often the default response on the part of policymakers and some stakeholders to actual and perceived problems.

As such, market participants are subject to a substantial number of industry-specific obligations over and above the protections afforded to customers through Australian Consumer Law. The most notable example is the National Energy Customer Framework (the NECF), which is a relatively recent initiative and was introduced following extensive consultation by the Ministerial Council on Energy (now COAG Energy Council). Energy businesses, and retailers in particular, have and continue to invest substantial resources in developing and maintaining systems and processes to ensure they are aware of and compliant with their NECF obligations.

Any loopholes or opportunities within the overarching framework that are available to either a subset of incumbents or to potential entrants have the potential to undermine the policy intent of the NECF – and other industry-specific obligations – and to disadvantage those market participants that have invested substantial resources in compliance functions.

Looking forward, regulatory frameworks influence the investment decisions of incumbents and potential entrants so the AER must carefully consider how to construct a regulatory framework that does not bias against or in favour of specific market participants or technologies, i.e. that is competitively neutral and contributes to dynamic efficiency. Similarly, the potential treatment of innovative energy sellers also raises important issues of good practice in ongoing regulatory administration. The transparent and consistent treatment of all market participants within a stable regulatory environment contributes to efficient outcomes over the longer term. In contrast, a reactive, ad hoc approach can inadvertently favour specific technologies or market participants.

Regulatory frameworks that involve differential treatment for some market participants can also exacerbate the impact of existing distortions. Current distortions include volume based (rather than more cost reflective) network tariffs, which subsidise distributed generation outside of peak consumption periods and consumption during peak periods, and direct subsidies for solar (i.e. feed-in tariffs).

In summary, EnergyAustralia encourages the AER to consider not only the current but the potential scale of emerging business models. Its decision will set the tone of the regulatory framework over the short to medium term and have important implications for the evolution of the energy market, particularly in an environment of rapid technological change. The short time that elapsed between the release of the AER's final guideline for the regulation of *alternative* energy sellers and the release of the Issues Paper on *innovative* energy sellers presumably illustrates the rapid emergence of new business models and the limitations of previous regulatory models.

Moreover, it is very difficult for regulators to predict the precise timing, form and impact of technological developments. Consideration must be given to ensuring that innovative energy sellers are not delivering energy under a different standard from licensed sellers with the unfortunate effect of lowering protections for customers.

The remainder of this submission focuses on those issues to which the AER should give careful consideration:

- Minimum customer protections that should apply irrespective of the mechanism through which energy is sold.

- Regulatory neutrality and cost differentials between incumbents and potential entrants.
- Importance of good regulatory practice, both in terms of design and ongoing administration.

Recommended minimum consumer protections

EnergyAustralia emphasises the importance of maintaining an appropriate level of customer protections, irrespective of the mechanism through which customers obtain energy. Energy markets are evolving at a rapid pace and emerging technologies will be capable of providing the entire energy solution for an increasing proportion of residential and small business customers within a relatively short period of time. Indeed, it is conceivable that some customers will completely disconnect from the grid, moving away from the provision of energy by licensed distributors and authorised retailers.

Therefore, EnergyAustralia views the following as the minimum consumer protections and determinants of the customer experience that should apply to the sale of energy, irrespective of the mechanism through it is sold and in addition to protections under Australian Consumer Law:

- Information provision, energy sellers should be required to provide a clear statement of the terms and conditions of their commercial arrangement with customers (including pricing, effective interest rates and repayment terms) and to obtain explicit informed consent to offer or vary arrangements. This obligation should also include a clear statement about the regulatory obligations of respective entities with whom the customer has a commercial arrangement.
- Privacy obligations, noting that a small business with an annual turnover of \$3 million or less is a small business operator and so not covered by the Privacy Act under the current Australian Privacy Principles.
- Specific obligations to manage hardship and the appropriate handling of debt.
- Limitations on the ability of energy sellers to recover unbilled amounts beyond a prescribed timeframe (i.e. restrictions on backbilling).
- Prohibitions on disconnections, including appropriate arrangements for life support customers and obligations to follow certain procedures – such as a positive obligation to ensure there is continuity of supply – prior to disconnecting their service.
- Measures to promote competition, such as prohibitions on technical or other elements of commercial arrangements that limit a customer’s choice of retailer. This is important where the alternative or innovative service provider has some form of commercial arrangement with an authorised retailer.
- Access to alternative dispute resolution mechanisms, such as Ombudsman schemes and the subsequent need to ensure that complaints are registered against the appropriate entity (i.e. complaints against an ‘innovative’ seller should not be recorded as complaints against the authorised retailer).
- Maintenance of records and obligations to provide customers and authorised third parties with access to consumption (i.e. to mirror the recent AEMC decision to facilitate customer access to data).
- All energy sellers should provide existing mandatory reporting to the regulator as currently applicable to authorised retailers and deemed essential to providers of an essential service. Some of which covers, hardship, disconnection and regulatory breach reporting.

A further obligation that would inform retail market analysis going forward is formal reporting requirements about the scale and form of more innovative selling mechanisms. This would facilitate the ongoing assessment of their significance (for example, in terms of market share or volume of energy sold) and the extent of effective competition in retail markets; this is not readily available under current arrangements.

This information would be an important input to formal reviews of retail markets, including the AEMC's annual Retail Competition Reviews, the AER's own *State of the Energy Market* reports and similar market monitoring by state regulators. We note the AEMC's definition of retail markets, as outlined in its *Approach Paper* for its 2015 Review of Retail Competition, only captures energy sold by authorised retailers; this is likely to reflect the lack of reliable information about the scale and form of alternative sellers and will become an increasingly significant analytical gap going forward.¹

Regulatory neutrality and cost differentials

EnergyAustralia is concerned about the potential cost differentials that regulatory models might create and their consequential implications for competition and dynamic efficiency. EnergyAustralia acknowledges the AER is seeking to adopt a proportionate regulatory response to the emergence of new business models. However, this will potentially create significant differences in regulatory obligations and by implication, differences in cost structures between competing market participants.

Limitations on retailers' commercial flexibility such as reduced ability of retailers to recover costs or manage risk— particularly in areas such as billing and disconnections, for example — are other outcomes of the current regulatory framework.

The cost of compliance is driven by all aspects of regulatory administration, namely:

- initial assessment and approval to operate;
- scope of regulatory obligations;
- systems and processes to ensure the business is aware of and complying with all applicable regulations;
- applicable penalty regime and treatment of breaches, noting that the NERL states that AER 'may deal with a breach of a condition imposed under this section as if it were a breach of the Rules';
- ongoing obligations associated with monitoring and compliance (including reporting obligations), and enforcement activity.

¹ See AEMC (2015) *Retail Competition Review, Approach Paper*, 18 December 2014, Sydney for a more detailed discussion of market definition.

In addition to the cost of regulatory compliance, the emergence of these business models will reduce the volume of energy sold by authorised retailers so the unit cost of regulation – and the relative disadvantage for incumbents – may increase substantially. Furthermore, the flow of energy to or from grid-connected customers may become less certain, which can create challenges for network businesses.

These issues have the potential to significantly distort the energy market over the longer term. The AER needs to ensure it does not penalise those entities who continue to sell energy through conventional channels or confer an unfair advantage on operators of specific technologies.

Regulatory administration

Irrespective of whether the AER chooses to authorise innovative energy sellers as retailers or issues exemptions with conditions, the Issues Paper fails to address numerous issues of regulatory administration. For example, it is unclear how the AER will assess applications from different types of innovative energy sellers. This includes operating models and technologies that haven't yet emerged and to which the AER does not refer in the Issues Paper.

The Issues Paper also refers to 'relative flexibility and adaptability' and that the AER has 'wide discretion in relation to the types of condition we can impose on an individual exemption'. Furthermore, the AER acknowledges it has commenced this process in response to the emergence of new service offerings, while its consultation on the regulation of 'alternative energy sellers' reflected the increasing number of solar power purchase agreements in the market in 2013 and 2014.

We recognise that this reflects the considerable discretion that the NERL grants the AER with respect to the authorisation and exemption framework. This includes the ability of the AER to respond to emerging issues in energy markets, such as the increasing importance of solar power purchase agreements and now, combined solar and storage solutions.

However, the absence of a transparent approach that is clearly articulated, well publicised and consistently applied is contrary to principles of good regulatory practice and will only create uncertainty for incumbents and potential entrants about the competitive environment in which they operate. The use of arbitrary triggers or different forms of regulation depending on actual or potential scale (however it might be measured) could create further complexity and uncertainty.

Therefore, EnergyAustralia recommends that any decision by AER to establish a framework for the exemption of 'innovative energy sellers' should be accompanied by publication of clear guidance on the assessment and approval, and monitoring framework for such entities.

Finally, we agree with the AER that the NERL and its binary approach to the sale of energy (i.e. either by an authorised retailer or an exempt party) is ill suited to the direction in which energy markets are likely to go in near future so any immediate outcome of this consultation process will represent a second-best outcome.

As such, we recommend a more fundamental review of the NERL with a view to developing a framework for the medium to longer term that encourages efficient consumption and investment in energy markets and which is indifferent to the mechanism or business model through which energy is supplied to residential and small business customers. We anticipate that the Energy Market Reform Working Group's consultation on the regulatory implications of new products and services in the electricity market is the mechanism through which this issue will be considered in more detail.

Any review of the NERL should recognise that energy customers are increasingly empowered by technological developments and have far greater control over their consumption and generation, particularly in terms of their form and timing. This suggests that policymakers might consider reducing the reliance on industry-specific regulation to achieve desirable outcomes as energy markets evolve.

Recommendation

In summary, EnergyAustralia recommends the following for the regulation of innovative energy sellers:

- Exemptions with strict conditions that incorporate the recommended minimum consumer protections outlined above.
- Preparation of clear guidance by the AER relating to the administration of its proposed regulatory framework. This should include processes for assessment, approval, monitoring and enforcement, reporting obligations)
- Review of the NERL with a view to establishing an overarching legislative framework that is better suited to the evolving energy market.

If you require any further information with regard to this submission, please contact me on 8628 1479 or via email at geoff.hargreaves@energyaustralia.com.au.

Yours sincerely,



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