National Irrigators' Council

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Ms Lyn Camilleri
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Dear Ms Camilleri

Re ACCC guidelines on the Prohibiting Energy Market Misconduct Bill

The National Irrigators' Council (NIC) seeks to provide comment on issues that have seen policy and regulatory change in recent times, and on further issues that we view as requiring adjustment. This is to properly reflect a fairer electricity generating and distribution system that delivers electricity in an affordable, efficient and sustainable manner to consumers with a regulated tariff structure and pricing system, characteristic of a competitive market.

We recognise the challenges during this period of transition and the technical innovations required to meet these challenges. This includes an energy market design with the adoption of renewable technologies, creating an increasingly dynamic system.

These challenges notwithstanding, we do seek to highlight that during our long standing participation in energy policy and regulatory advocacy, we have been up against a regulatory bias which appears to put returns ahead of the national interest and interests of consumers. In our case, the interest of agriculture industries struggling to operate in a competitive market in providing food and fibre for Australia and for export.

NIC is supportive of several of the recommendations of the ACCC inquiry report *Restoring electricity affordability and Australia's competitive advantage* tabled in July 2018 and we continue to monitor progress on several key recommendations. In our view, the report represents a starting point and basis for much needed regulatory reform in key areas.

While we are not in a position to provide detailed comment on the ACCC proposed new remedies and processes provided in the *Treasury Laws Amendment Prohibiting Energy Market Misconduct Bill 2019 (*which the Australian parliament passed in November 2019), we are broadly supportive of the Bill's intentions which focus on any misconduct under the Bill's guidelines.

We note the Bill is designed to prevent certain conduct in parts of the electricity supply chain:

- The wholesale market, whereby electricity generators produce electricity that is supplied into the electricity grid and distributed to customers. This can be done through a spot market, such as that which exists for the NEM.

- The financial (or hedging) contract market, whereby electricity generators, electricity retailers and some end users enter into derivative contract arrangements to manage price risk arising in the wholesale market. Other entities, such as financial intermediaries and speculators, may also engage in this market.
- The retail market, whereby electricity is supplied to most end users of electricity (such as residential and small business consumers) through retail contracts.

The ACCC guidelines will relate to Schedule 1 of the Bill only.

Schedule 1
NIC notes that the ACCC will be responsible for enforcing the new prohibitions, and will issue guidelines setting out the approach to the ACCC's enforcement role.

Unfortunately, without access to the resources to provide more expert comment ,NIC is not in a position to provide comment on the issues listed for consultation set out in Attachment A, and the processes and remedies that might be included in the guidelines. We note that the guidelines will include examples of conduct that the ACCC considers unlikely to breach the prohibitions and examples of conduct that are likely to breach the prohibitions.

We note Schedule 1 describes three sources of additional compliance costs and additional legal costs for businesses operating in electricity retail, contract and wholesale markets, seeking to comply with information gathering notices issued by the ACCC.

We would be **strongly opposed** to any costs incurred by electricity businesses seeking to comply with the bill and ACCC information gathering notices, being passed on to consumers. This might include potential legal costs incurred by electricity retailers and generators seeking advice to support their understanding of the new regime to ensure their businesses are compliant.

Background and general comments
NIC has broadly supported the efforts by Government, via key decisions and Government related inquiries, to deliver a fairer policy and regulatory environment for consumers participating in the NEM and to enable businesses to properly compete from a more stable business footing. We strongly supported the removal by Government of the **Limited Merits Review** (LMR). On first impressions this is delivering better outcomes for consumers whereby decisions made by the AER are no longer subject to merits review of the Australian Competition Tribunal, or any state or territory body.

Disappointingly however, there has been no progress on recommendation 11 of the ACCC report (July 2018) in relation to the **RAB write-down**, recommending that:

> *The governments of Queensland, NSW and Tasmania should take immediate steps to remedy the past over-investment of their network businesses in order to improve affordability of the network.*

We have long advocated a rule change through the AEMC to change the way electricity networks' regulated asset base (RAB) is calculated.

In our submission to the **AER on profitability measures for regulated gas and electricity network businesses** in December 2017, we argued for systemic change to deliver greater fairness, transparency and competition. We highlighted the disparity where agriculture users were forced to operate in a market environment lacking genuine competition, and an environment that was dominated by generators and transmission and distribution infrastructure owners, focused on maximising their returns.

We recommended to the AER that the rate of return methodology be fundamentally changed to ensure a reasonable rate of return commensurate with the secure monopoly position of network owners and to ensure a departure from the 'gold plating' of assets. We suggested the AER adopt a performance measurement framework to enable an accurate assessment of the profitability of regulated electricity and gas businesses, comparable to that of other ASX entities.

During the catastrophic energy failure in South Australia in September 2016 and February 2017, we highlighted the absence of competition in that state that saw blatant gaming on the **spot market** which was struggling to cope with the transition to renewables. Consumers were exposed to the spot market volatility when they were unable to secure quotes from retailers for fixed term contracts and where loopholes under market governance arrangements were enabling price gouging by network businesses. The evidence was clear where industry profits were running parallel to soaring prices.

We note the series of examples provided in the Bill's Explanatory Memorandum where it could be assessed that there had been misconduct. In particular we note the example (2.11) provided and circumstances where it would be assessed that a gentalier had failed to make a reasonable adjustment to its retail prices, as its wholesale costs of procuring electricity had been artificially inflated. This is against the background where (for example) there had been a substantial reduction in market-wide wholesale spot prices and in the case where a gentalier realises it may need to make a reasonable adjustment to its prices to reflect this reduction, and then has sought to avoid doing so. Instead of adjusting its retail prices, the gentailer instead uses accounting methods to shift its profits to its generation arm, such that the retail arm appears to be paying a much higher spot price than it actually is.

NIC welcomed the **ACCC proposal to implement a class exemption for small business** to collectively bargain which will be an enabler for many in the agriculture sector. The exemption is designed to provide legal protection for: businesses with an annual turnover of less than $10 million in the preceding financial year to collectively bargain with customers or suppliers; and all franchisees to collectively bargain with their franchisor regardless of their size or other characteristics, without them having to apply to the ACCC.

In our submission on this matter supporting the proposal, we further recommended that the proposed class exemption should be available to collective bargaining groups with a threshold annual turnover of less than $20 million in the preceding financial year. We believe this will allow irrigators to form energy buying groups in order to negotiate better value from retailers and networks across the NEM.

In the development of our 2017 **submission to the ACCC inquiry into retail prices**, NIC and the Agriculture Energy Taskforce engaged Sapere Research Group to assist with the submission. Sapere confirmed that at every level of the electricity market *'costs, prices and profits across much of the sector, and at multiple points across the supply chain, exceed efficient costs, prices and profits'.*

The Sapere report showed that *'despite being subject to price/revenue regulation, network costs, profits and prices also appear to be excessive'.* And noted: '*There is evidence of substantial excess network capacity across many parts of the NEM. We have not been able to identify a corresponding reduction in the allowed cost of capital to accompany risk transfer associated with the move to the RAB roll-forward method for setting the RAB at the start of the following price period (replacing the* *previous method which included provision for asset optimisation). Consequently, it appears that network prices incorporate the double effect of excessive returns on an excessive asset base'.*

In our submission to the **2017 Finkel review**, we suggested network service providers were seeking to increase the proportion of their bills, recovered through fixed charges. Some have argued for this on the basis that 'fixed costs should be recovered through fixed charges'. We believe there has been confusion between sunk (historic) costs and (current) fixed charges. There is no basis in the theory of electricity pricing for sunk costs to be recovered through fixed charges. Raising fixed charges reduces the ability of our members to reduce their electricity bills by consuming less. It also negatively impacts the economics of distributed generation relative to grid-supplied electricity (which is exactly why the networks are raising fixed charges).

We understand that the AEMC intends to make changes to the National Electricity Rules to mandate that tariffs should be 'cost reflective'. It is yet unclear what this will mean in practice, but we are concerned that networks will use 'tariff reform' as an opportunity to undermine the prospects for energy efficiency and distributed generation, both of which are competitive threats to their business. We encourage this review to examine the anomalies within network tariffs, which should be designed to ensure that irrigators and other businesses in non-congested parts of the network are not forced to meet the costs of network investments made to overcome congestion in other parts of the network.

NIC key messages
As part of our key aims and objectives to achieve a more competitive environment for the agriculture sector, NIC is seeking:

- **16 cents/kWh maximum:** a price ceiling for electricity of 8 cents/kWh for electrons and 8 cents/kWh for supply;
- **Implementation of the ACCC Retail Electricity Pricing inquiry recommendations** including those relating to network costs.
- **A NEM rule change** to optimise the Regulated Asset Base (RAB)
- **Introduction of irrigator tariffs:** recognising that irrigation demand is <u>not</u> driving critical peak loads on hot days;
- **Genuine competition:** a properly functioning market with competition at all levels;
- **Local networks:** removing network barriers to sharing of local energy generation on local networks;
- **Reducing the barriers** to connecting on-farm generation to the grid;
- **Policy certainty:** a stable energy policy that is technology-neutral, market-based and economy-wide, delivering affordable, reliable and secure energy;

NIC acknowledges that our comments are broad, however we do see this measure as being a positive part of a long and complex process of trying to create an electricity market that is genuinely competitive and operates in the national interest. We commend these comments to you.

Yours sincerely

Steve Whan
CEO