12 November 2017

Dear Australian Competition & Consumer Commission

Re: Retail Electricity Pricing Inquiry Preliminary report - 22 September 2017

Firstly thank you for sending the preliminary report and providing an opportunity to comment. I have read through the 176 page report and it is evident that a lot of work has been put into this report.

In response I would like to present a new approach to the problem to clarify what the real problem is and in addition provide some specific comments on the content of the report.

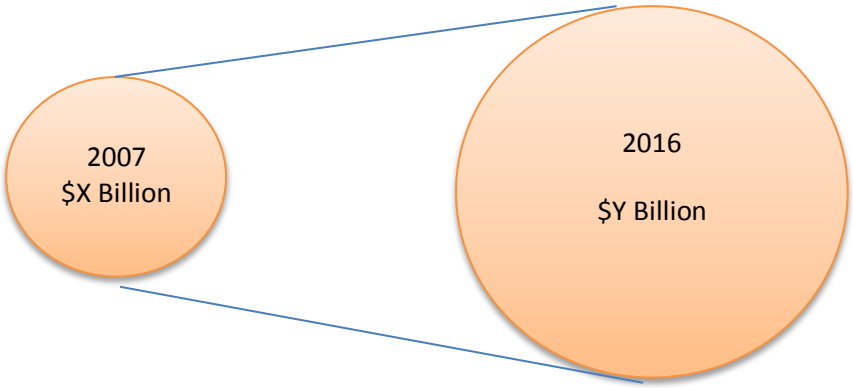
A new approach

What is very evident is a large part of the report is focused on the specifics of the pricing which is only the symptom of the underlying problem and not the problem itself. From a consumers' perspective I would like to have the real problem addressed, which will in turn ultimately resolve the pricing issue in an efficient and cost effective manner. Furthermore, despite there being an expectation that this report will provide measurable, realistic and concrete recommendations and associated expected outcomes, I.e. if you implement recommendation X you should expect a reduction of price by Y% in year 1 and Z% in year 2 and so on, the report's recommendations are unqualified and do not provide a sense that they will significantly lower the current prices, nor benefit consumers.

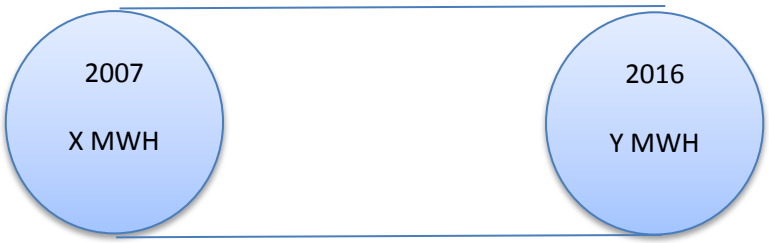
So what is the real problem? The real problem is the dollar value of the economic pie associated with the electricity industry which has grown in real terms by about 100% in the last 10 years despite the amount of electricity consumed remaining relatively flat. This means that somewhere in the supply chain companies are earning well above the expected/normal returns for a utility industry and the so call controls and safeguards are not working and the market is not working.

So how can this be shown? Firstly you need to start with a macro-economic view of the market in terms of dollars and in terms of MWh consumption. This should be relatively easy to do as you already have the consumption data in MWh, CPI data and the value the consumption. It is noted that in your report you have shown only the consumption side which is only half of the picture. Showing the full picture of the market will clearly demonstrate that the problem is that the dollar value of the market has increase disproportionately with the natural increases due to CPI, wages growth, new connections and changes in usage. The result of this disproportionate increase is that we are paying a higher price per unit of electricity. See illustration below.

Growth of the electricity market in dollars



Growth of Consumption in MWH



Once you have this, calculate a pricing benchmark to form a basis for what prices should be today. To do this you can use, the base market size in dollars in 2007, inflation, connection growth, consumption growth and importantly general efficiency gains by the supply chain. Do not use the wholesale electricity prices over the period because they are a symptom/result of the underlying problem and will skew your results. Additionally you might question the use of efficiency gains, but this is a normal expectation when running a business and is commonly used in both the private and public sector when setting budgets. I suspect once you have calculated the benchmark pricing for 2017 you will probably find that in real terms it is probably only a percent or two of annual growth, which is fairly standard in the utility industry. This benchmark should then be made part of the qualitative objectives in the report's recommendation.

Now that you have validated the fact that consumers are paying double for the same amount of electricity in real terms (i.e. inflation adjusted), the question needs to focus on which segments of the supply side are taking what proportion of the inflated pie. This should not be

that hard to do as the costs associated with Transmission and Distribution are regulated by the AER, electricity costs for the market are easily attainable from AEMO and AER, and Government subsidies passed onto the market are available from the Federal and State governments along with the costs associated directly with the AER and AEMO. The remaining part of the economic pie is the retailer's costs.

From this macro-economic segment based data you should be able to clearly identify which segments of the supply chain are the issue. From here the next step is to correlate your micro-economic analysis with this macro view and identify which controls or markets are not working.

Reading your report I can see that you found it a challenge to try to obtain a clear picture using micro economic analysis from the retailer's financial statements etc. This is natural due to vertical integration in the supply chain and creative financial accounting (c.f. recent revelations from the Paradise Papers regarding one of the large French companies involved in our power generation who syphoned off 1 billion dollars and then claimed $250 million from tax payers because they were struggling economically)

Finally with the list of ineffective controls and market failures it should be simple to put together a list of concrete measurable options and expected quantifiable outcomes to address the real root cause of the inflated price increases. Additionally measures should be suggested on how to normalise the prices, in the short term, back down to the levels they should be at.

<u>Specific comments on the details of the report</u>

- The Executive summary is full of a lot of padding and it not really a summary. You do not have to have all the preamble about why you are doing the report. The executive summary should start with factual statements such as "Our extensive analysis has validated that prices have increased by X % over inflation and are well in excess of ……", "This has caused considerable economic hardship etc…." "The root cause of the price increase is …….","Our short term recommendations to address this are…a,b,c,….", "Our long term recommendations are……","The expected outcomes from these recommendations are …
- The macro-economic analysis showing the close 100% price increase over the last 10 years based on CPI and the international comparison, in Figure 1.8 on page 24, does not match your cost stack analysis of only a 40+% increase for the same period. You need to join the dots here using a real sample from historical pricing plan data from the major retailers. You will see that the 100% increase is much closer to the mark.
- In your various analysis of price it is not clear what you are actually looking at. Is it the overall costs as seen by the consumer? Is it just the electricity price (cents per KWh)? You need to make sure all your definitions of price are consistent throughout the entire document and make sure that they have direct relevance to what a consumer sees on their bill. I.e. it needs to be shown in terms of Daily Supply Charges, Electricity costs (cents/KWh), GST, Feed in Tariffs, Government subsidies, Discounts. You might also look

at changing wording such as demand to consumption. Your report must be relevant to the consumer in terms relevant to them.

- Some of your tables, for example table 1-1 on page 14, whilst factual, does not portray the fact that some of the prices have been "artificially" adjusted due to State specific regulation. The table leaves readers with an impression that the market is not working given that all the states use the NEM to buy the electricity. You are better off using a graph over time that shows how various market changes such as regulation have had a direct impact on prices. Another example is Figure 1.1 on page 11. The true height of the graph has been truncated to emphasise that Roof top PV is significant when in reality it is not because it only contributes to a mere 3%. I.e., if you put the full height graph in you would virtually not see it. Again you are attempting to mislead the readers.
- The cost stacks do not appear to reflect reality. For example using your average NSW bill of $1,533 in 2017 and the daily supply charge (which is supposed to contain the transmission and network costs which are fixed per connection and a large component of the retailers administration fix costs) of $1.05 currently from Dodo, you will see that it only equates to 25% of the bill and not the 49% shown on page 39. It is a similar story for the other states.
- Since a lot of the report is focused on the cost stacks using a waterfall chart, I suggest you validate each one with the median standard offer and market offer prices from each of the leading 3 retailers in 2007 with the similar data in 2016 or 2017. You can also do it for the years in between as well to provide even a clearer picture similar to the analysis done in Figure 1.7 on page 24. What I expect you will see is that whilst the overall cost of the Standard offer will be higher the year on year percentage increases will be comparable between the two. Note the AER would not provide me with the historical pricing data when I requested so I cannot do it myself. The non-disclosure by the AER is also a problem and smells like protectionism.
- The report discusses pricing for small, medium and large enterprises yet it is not clear what their definitions are and on spec it appears that they are not consistent in the report as you have used extracts from other sources each with its own definition. Some appear to be based on consumption other on revenue and others on the number of employees. To give credibility to your work you need to use a consistent definition.
- Retail margins based on EBITDA Figures 2.38 and 2.40 on pages 72 and 75 appear that they are supposed to represent the same thing yet the figures do not correlate.
- You might want to include a look at further upstream beyond the power generators to the gas and coal supply chains as these also have an impact on the prices.
- The recommendations in section 5 are not quantified (no numbers, dates or numeric targets), vague and do not indicate any reduction in pricing, just a moderation of pricing. This suggests the ACCC considers it fine for the supply side to continue to rip off the consumers albeit moderately going forward. It should be noted that the term, moderation of pricing, does not represent a reduction in price but a slowing of price growth. This is not the outcome the majority of consumers are expecting as it clearly sends the wrong message to the supply side. With the final report only due out next year you need to send

a message to the supply side now that prices need to be reduced back to the benchmark pricing.

- There is no recommendation suggesting the reregulation of pricing, nor of moving away from a market based industry to what we had before the privatization of assets and the creation of the NEM. The recommendations seem focused on pursuing an open market despite the fact that the sheer nature of the assets and the dynamics of the participants do not lend themselves to a functioning open market. All you have to do is look at how solar customers have been ripped off by the retailers because solar producers are unable to fully participate in the market and are price takers.

In summary, your report needs to move away from the symptoms and focus on the fundamental issue of an inflated market created by the supply side. The report needs to attack the issue from a macro-economic perspective so you can see the wood from the trees. The details of the micro-economic analysis needs to be match up with the overall macro-economic picture. Consistency of terms and relevance of those terms to the consumer is essential. The final concrete qualified recommendations need to address solving the root cause and normalising the pricing back to the benchmark in the short and long terms. These recommendations should not be around band aid solutions that for example prop up an inefficient market without the goal of fixing it, nor should they continue to protect the companies who have extracted well and beyond their fair share. Broader options such as the de-privatisation of some if not all of the supply side segments should also be looked at as the stability, security and cost effectiveness of our electricity is a sovereign issue. This includes looking at ensuring that our energy resources such as gas are used firstly to supply the domestic market at a close to cost price and not at inflated global prices. Yes, this will have an initial impact on our trade balance but we are already seeing a significant negative impact because domestic businesses cannot keep the machines running and lights on due to the high cost of electricity. Overall you will find this type of strategy will have a positive effect on our economy and trade balance. We should not buy into the argument that this will impact foreign investment as we have seen that this foreign investment has created very few jobs, has produced little in the way of tax revenue, pillaged Australia's resources at very cheap prices and through complex financial arrangements extracted billions of dollars from Australia.

Although not mentioned in the report I have a real concern about the conflict of interest between the ACCC and the AER. There is a commercial arrangement between the ACCC and the AER whereby the ACCC is providing a number of services to the AER. With a business relationship in place I believe this restricts the ACCC in expressing critical comments regarding the AER's regulation or lack thereof, of the market participants such as the Transmission and Distribution companies. It also potentially restricts the ACCC from putting forward recommendations directly levelled at the AER and their management. We can even see evidence of this light handed approach in the report in section 5.2 paragraphs one and two where it is portrayed that the AER are improving and they need more regulation. You really have to ask the question why the AER has let it go on for so long and not done anything about it and what qualified measureable improvements have they made.

Lastly, whilst I understand that there is a degree political bias or pressure from interested parties in these reports I sincerely hope the ACCC does the right thing and present an unbiased report that will help Australia get out of this mess we are in and help put some balance back into the energy market as it is a critical utility that is used by every Australian and is essential for all Australian businesses current and future.

Regards,

Martin Vizjak