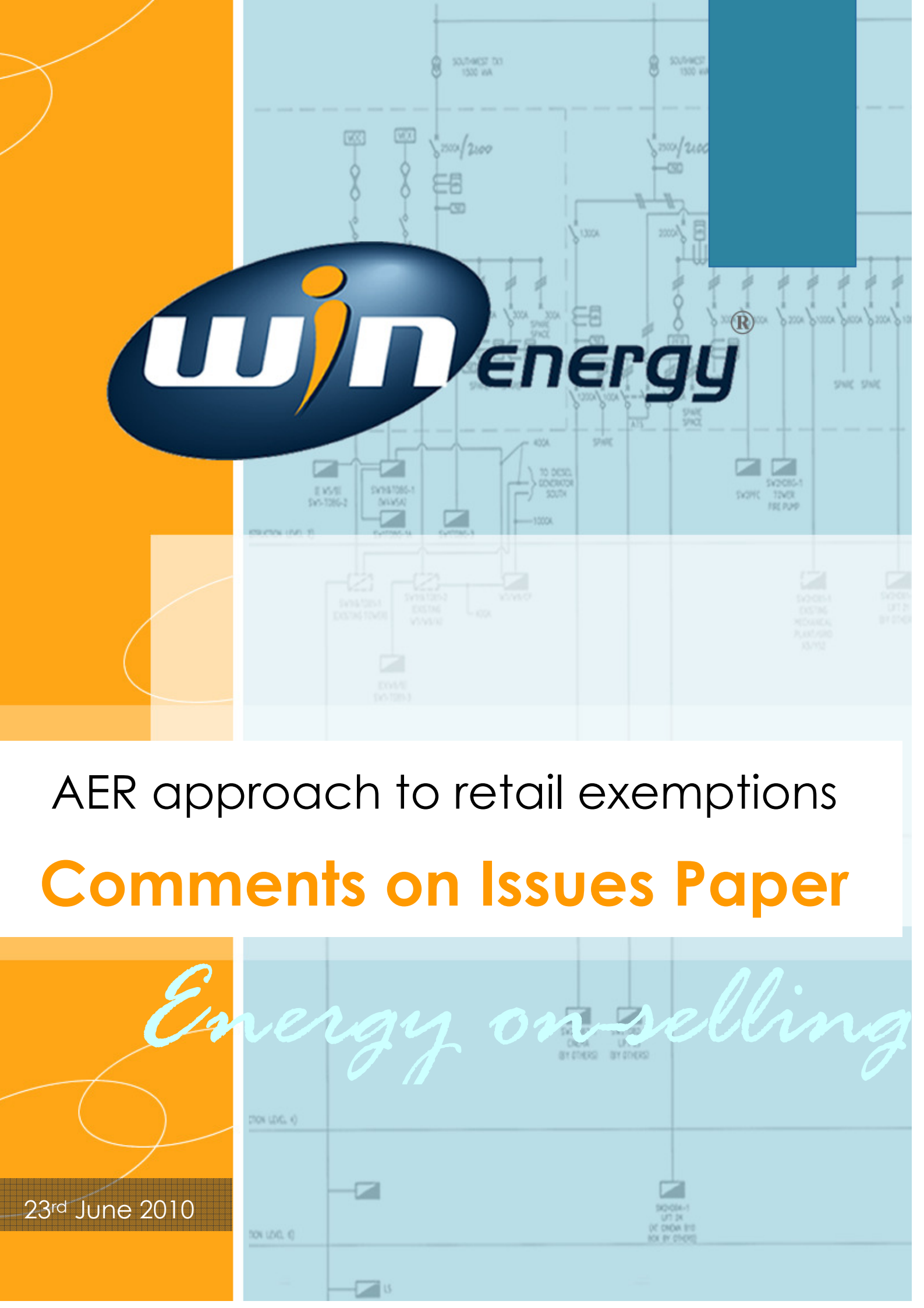

AER approach to retail exemptions

Comments on Issues Paper

Energy on-selling

23rd June 2010

1 BACKGROUND

Since it inception in 2005, WINenergy has specialised exclusively in the establishment and operation of Embedded Networks for electricity. Typically we undertake this activity as an agent of the property owner or the owner's corporation. Our perspective on the AER issues paper "AER approach to retail exemptions" is firmly rooted as an organisation who exclusively works in this market segment.

At a few sites we bill for water and gas, but only as a billing agent. We do not have hands-on perspective pertaining to the on-selling of gas.

With regards to electricity we operate 70 sites and we have a further 18 contracted sites in implementation. We have about 80 sites in our forward sales book that are likely to be contracted in the next 24 months. All of our sites are "grid connected". We operate sites in Qld and NSW, but the majority of our sites are in Victoria.

Our clients are large funds and property trusts who own shopping centres. We also service property developers who either build and "run" properties, or hand them over to owners' corporations.

Our fundamental business is the supply of metering and the management of data and billing in privately owned embedded networks. Electricity is resold at a rate that is substantially lower than a conventional supply arrangement.

Whilst WINenergy's activities are considered niche in nature, they are predicated on:

- Increased competition,
- End-user cost reduction,
- More comprehensive energy management and
- Excellence in service delivery.

In delivery of its services, WINenergy complies with all relevant state legislation, distribution codes and pricing policies as appropriate and operates under contract to blue chip organisations.

In producing monthly electricity bills for about 7000 customers we have adopted and adapted the following procedures:

- All consumption is metered
- Type 4 or Type 5 interval meters (complaint with metrology code) are used exclusively
- Meters are read monthly and bills are based on actual not estimated consumption
- Where requested, we probe meters and supply customers with interval data for a modest fee.
- Customers are presented with an industry compliant bill that details tariffs, consumption, green house gas emission and graphical usage comparisons.
- Customers are offered a broad range of payment options
- With the exception of our client sites in Qld, customers are always offered choice and given the ability opt out of the EN.
- Our internal customer service centre adheres to complaint handling procedures.
- We comply with industry disputation procedures and our customers have access to and use VCAT for more complex cases.
- Payment plans are provided for genuine hardship cases including small business owners
- There is a formal disconnection procedure for non-payment.
- We offer customers a discount to the published tariffs of the local default retailer and endeavor to beat the best genuine offer that the customer can get from a retailer.

2 PROFIT

The economics of EN is well understood. The aggregate price of energy to all customers is greater than the cost of the bulk energy purchased at the gate meter. This margin can then be applied to:

- Payment of any capital in establishing the EN (e.g. switchboard modifications and metering)
- Operation of the EN (meter reading, billing, customer service, collections)
- Cheaper energy to the consumers
- Profit

The onselling margin is a combination of getting a bulk price for consumption, and achieving a beneficial arbitrage between network tariffs. It is acknowledged that discussions about distribution exemptions are outside the scope of the current AER review, however the involvement of LNSP's in the establishment of EN's and in the ongoing tariffing of EN's goes to the very heart of pricing. Ultimately the energy that is onsold has network tariffs inherently embedded in it.

What is a concerning trend is introduction of punitive tariffs for EN gate meters by some distributors. The cost of servicing a single large customer from a network point of view is lower and is reflected in the network tariffs applied. EN tariffs applied by LNSP's are higher than for single customers with the same load profile yet there is significantly less work involved in the on-going servicing of a site that is converted to an EN. The viability of EN's is totally dependant on the behaviour of the LNSP's.

To ensure that the beneficial arrangement provided by EN's are realised, the regulatory framework needs to preclude the application of punitive EN tariffs.

3 IGNORANCE IS BLISS – WHAT THEY DON'T TELL YOU AT SCHOOL

Working daily in the establishment of imbedded networks has given us a "school of hard knocks" education that can't be gained from a text book.

One of the challenges in establishing an EN is the lack of standards and procedures within the existing market participants (retailers and distributors). The act of establishing an EN demands that distributors and retailers make the appropriate entries in the market system. As it is not a core activity for them, they do it in a best endeavours basis. This is complicated by the fact that prior to the conversion of many of the large shopping centres to EN's, the LNSP's have taken very little interest in the on-site metering and have very poor records of what is inside the meter cupboards. The approach to paperwork, procedures and inspection is different for each distributor.

Typically we spend the first 3 months after a site goes live trying to rectify MSATS records via email requests. The inconvenience to consumers is significant and double billing is a frequent occurrence.

There is a significant need to create a category for EN operators as registered participants in the energy market so that they take responsibility for this work.

4 CONTEXT OF OUR RESPONSE

It is useful for us to state our operating procedures because when it comes to specifically answer some of the questions in the issues paper, you will be able to understand the view point of our responses. Indeed, it is anathema to us that unmetered consumption is on-sold or that energy is billed as a line item on rental invoice. We believe that the consumer should have choice and should not be disadvantaged by onselling.

Most of our experience is with electricity rather than gas.

5 RESPONSE TO QUESTIONS

Q1: Do stakeholders agree with the AER's interpretation of what constitutes the sale of energy?

We agree but note that there remains an outstanding need to address the selling of bulk hot water.

Q2: Are there any other matters that should be included in the Exempt Selling Guidelines?

The comment on page 13 of the issues paper is very accurate:
It may be difficult to distinguish between distribution issues and retail issues in these embedded network situations.

AEMO "Embedded Network Guidelines" and procedures such as the "Allocation of Embedded Network Codes (August 2009)" require that MSATS is correctly and accurately updated to reflect the configuration of the EN.

> *The LNSP of the parent NMI has the key role in entering the change requests into MSATS. MSATS must be updated in an accurate and timely manner. (section 5 AEMO "Embedded Network Guidelines")*

The issue in summary is that LNSP's do not satisfy this obligation and the inability of an embedded network operator (ENO) to even view MSATS makes the correction and update process unwieldy.

If ENO's were recognised as registered participants with access to market systems (MSATS) and data, the ENO will have the ability to obtain Tier 1 and Tier 2 customer meter data from licensed MDPs and forward this to relevant parties. The ENO should be able to provide approved metering to both Tier 1 & 2 customers, thus alleviating the requirement for the LNSP to provide metering and meter reading services to Tier 2 customers of an EN.

This would ultimately be beneficial to consumers by:

- The elimination of lengthy and obstructive processing delays by an incumbent distribution network operator when a new embedded network is established,

(In the majority of cases LNSP's do not have processes to cope with the establishment of an EN and rely on work processes and practices outside their normal work activities which are prioritised against the more normal work requests where processes exist)

- Timely and accurate maintenance of consumer records,
  (In brown-field sites records are usually not maintained with any accuracy by the LNSP. Alterations, moves and changes are invariably not kept up to date)
- Improving service delivery,
- Removal of discriminatory EN tariffs , and
- Maintaining sustained low consumer energy rates.

Q3: Are there other particulars and information relating to exempt sellers that should be included in the public register?

The type of meter should be recorded. This would ensure some visibility of the penetration of smart meters within embedded networks.

The management arrangement for the site should be recorded as to whether it is owner operated or operated by an agent.

There should be a general statement that the exempt seller is entitled to collect "Use of System" charges from all connections down stream of the Gate Meter at the same rates & charges as those which would have applied to each connection if they were a market participant.

Q4: Is the apparent growth in onselling problematic, and if so, why?

To a certain extent we have been instrumental in some of that growth. We see the growth continuing because there is an increased awareness of EN's stemming from successful reference sites that have given property owners confidence.

Property owners have a right to the financial rewards of energy on-selling because they own the infrastructure which delivers electricity to tenants down stream of the Gate Meter.

The risk of customers becoming stranded can be minimised by the implementation of industry best practises. Furthermore, by ensuring that EN's

are profitable it will be attractive for another operator to take over an EN in the event of insolvency.

One of the challenges associated with the growth is the requirement for established standards and procedures within the existing market participants. The act of establishing an EN demands that distributors and retailers make the appropriate entries in the market system. As it is not a core activity for them, they do it in a best endeavours basis. There is a significant need to create a category for EN operators as market participants so that they take responsibility for this work.

It appears that as a response to the growth of ENs, some LNSPs have developed EN tariffs which may be deemed to be anti-competitive and unfair. EN connections should have the right to select the most appropriate network tariff applicable to general market participants, not be restricted (or penalised) by being forced on to higher-priced EN tariffs.

Q5: Is it appropriate for the AER to impose no conditions on large customers of exempt sellers (as is the case for large customers of authorised retailers), or should they be provided with basic customer protections where the existing arrangements prevent them from choosing their own retailer?

All customers within an EN should be afforded the same customer protections as those who use licensed retailers. Large consumers of power (above 160 MWhrs) will typically sign unbundled supply contracts and be protected by contract law.

Q6: Should the AER impose a condition on onsellers selling to large customers to ensure that they do not hinder or prevent the customer from choosing their own retailer?

We believe that in most instances customers should be able to choose their own retailer. Even though an EN can offer cheaper energy than retailers, large customers who may have national buying leverage can get prices that can't be beaten. It is unjustifiable to force them to take energy from the EN to their commercial detriment. In cases where customers within an EN purchase electricity from a Licensed Retailer, then a subtraction must take place and business to business data exchanged between the retailer and the EN.

WINenergy does not agree with the statement on page 17 of the issues paper

Within a particular building, each meter may have been assigned a unique identifier for wholesale market purposes. If this is the case, customers within that building will be able to choose their own retailer. The AER considers that it will generally not be appropriate to grant a retail exemption (and particularly a deemed or registrable exemption) to an onseller where all customers have access to a retailer of choice. Onselling in these circumstances is unnecessary and deprives customers of some protections under the Retail Law and Rules.

In the instance of a brownfield conversion of a site to an EN, all tenants will have market meters to start with. A marketing campaign is conducted to assess the popularity and potential take-up of tenants. If there is sufficient popularity by tenants choosing to opt into the EN, then the market meters are removed and replaced by meters belonging to the EN. This is only for customers opting in. Other customers retain their NMI and status as children of the NEM. On face value, the above paragraph runs counter to this practise.

Q7: How important is it for customers in onselling situations to have access to choice of retailer?

We believe that choice of retailer is a fundamental right of the consumer. The imposition of competitive market tension can act to ensure that some of the financial benefits emanating from the operation of ENs are passed on to consumer.

Q8: Once network configuration/metering issues are addressed, are there any other impediments to exempt customers having access to choice of retailer for electricity?

The ongoing business to business arrangements for management of child meters needs to be in place.

Q9: Where gas is only used for limited purposes, how important is it for customers in onselling situations to have access to choice of retailer for gas?

In this case, choice of retailer is not justified.

Q10: What core customer protections should exempt sellers be required to provide for their small customers?

We agree with the customer protection outlined in the issues paper detailed in Attachment 1. We agree that payment plans and hardship schemes

should be enabled. In addition to the provisions suggested, we believe that customers should be able to access interval data on request.

Q11: Are the core protections proposed in the draft categories of deemed and registrable exemptions attached to this paper appropriate?

Yes

Q12: Do stakeholders agree with the requirement for exempt sellers to notify the AER, and their customers, of the possibility of disconnection?

This is reasonable

Q13: Are there any conditions which the AER could impose which might help to mitigate the risk of an exempt seller failing and leaving its customers without supply? Would it be appropriate for the AER to do this?

It is important that the economics of an EN stacks up and that regulatory regime and distribution tariffs continue to allow profitable EN operations. We note the comments on page 26 of the Issues Paper.

The AER does not consider it unacceptable for an exempt seller to earn some level of profit which reflects the efficiencies attributable to exempt sellers versus the cost of administering the onselling arrangements (economic profit), but a balance should be struck between the level of profit earned and the prices charged to customers.

Profitable EN's provides the best chance of continuity of supply.

If an EN operator is unable or unwilling to pay the retailer for supply to the gate meter, then the retailer should have the option of taking over all the customers of the EN.

Q14: To what extent can the protections found in hardship policies be applied to customers of exempt sellers operating under deemed and registrable exemptions?

Hardship policies are in the best interest of the customer and accord with industry best practices. Deemed and registrable exemptions should accord with best practises.

Q15: In jurisdictions where the Ombudsman or dispute resolution schemes do not extend to exempt sellers, what dispute resolution processes should the exempt seller provide to its customers?

The guidelines for dispute resolution that apply to licensed retailers (particularly timing and notification processes) should apply to EN customers and operators. In Victoria VCAT has provided an avenue for customers to have complaints resolved when direct discussions have failed. This is a reasonable process and one which is transparent and binding on all parties. The Ombudsman process covers all non EN customers and seems to work. There is a belief by LNSP's that failures in their networks that cause damage or loss to customers in embedded networks are not their responsibility and they have refused to compensate EN customers. Subsequent lodgement of the claim with the Ombudsman has seen the LNSP's pay compensation but as an exception rather than the rule.

Our clients who own shopping centres have tenancy relationships with the end consumers. If a tenant has a dispute over energy, they may possibly also have one over rent. The energy disputation process should not preclude the shopping centre owner pursuing dispute resolution avenues pertaining to leasing.

Q16: Should exempt sellers operating under an individual exemption be required to base their dispute resolution processes on Australian Standard AS ISO 10002-2006, as amended and updated from time to time?

Yes

Q17: Should this requirement be extended to exempt sellers operating under a deemed or registrable class exemption, or to all exempt sellers selling to more than a certain number of customers? Why or why not?

Yes. Customers should not be disadvantaged by being in an EN. However, in the instance of unmetered gas described in question 9 a dispute resolution regime is possibly not required.

Q18: What sort of tests should the AER use to determine whether the sale of energy is incidental to a business?

The conversation on page 25 requires clarification. WINenergy does not agree with the statement:

The AER may consider the 'incidental selling' factor in conjunction with the factor which explores whether the exempt seller is intending to profit from their selling arrangement. A landlord selling energy to its tenants at cost is more likely to be considered an incidental activity by the AER. However, structuring the selling arrangement with the intention of making a profit from it may indicate that it is a core business activity in its own right. This could be inferred, for example, from the onseller setting its own tariff structure. In these circumstances it may be more appropriate for the onseller to seek a retailer authorisation.

This runs counter to the conversation elsewhere in the paper that a profit motive is "not-unreasonable". Many EN's deliver measurable profits to the owners. The above paragraph would imply that a large shopping centre which accounts for the onselling as a profit centre would be required to attain a retail authorisation. It is also commonplace (and desirable) for exempt sellers to set their own tariff structures. This is means by which consumers within an EN get cheaper energy.

The final test on p25 pertaining to resources is also fraught with difficulty. It is very common to outsource the onselling operation (and is the core or our business) without it becoming a core part of the exempt sellers business.

Q19: Is the approach taken to the 'incidental' requirement in the categories of deemed and registrable exemptions appropriate?

Yes. We accept that persons who are not covered by a class exemption should seek an individual exemption.

Q20: Are there any additional circumstances to those identified above (and in other parts of this issues paper) that would warrant the AER issuing an exemption rather than a Retailer Authorisation?

No.

Q21: How should the AER judge an exempt seller's profit intentions?

We think it is healthy to make a profit and is necessary to ensure customer protection and service levels do not decline because they are in an EN. In fact it may be the preferred method of providing customer service and connection to the market.

With respect to the commentary on administration fees, we agree that meter reading, billing and payment processing costs must be recovered as part of the energy tariff. However, we believe that the EN operator must be able to charge ancillary fees in the same manner as Retailers. Deposits, connection and disconnection fees, special meter reads etc, should be included on energy invoices as separate line items as long as that practice is consistent with the retail practice in the jurisdiction. Additional services available from WINenergy such as the provision of interval data and consumption analysis reports must be able to be separately charged. If all of these ad hoc services have to be bundled into the tariff, then there will be a lack of transparency in pricing.

Q22: Will the proposed pricing protections adequately protect exempt supply customers?

If choice is offered to the consumer then market forces will set reasonable tariffs. We agree that prices must not be higher than the published prices of the local default retailer. Indeed when exercising the principle that consumers should share in the efficiencies of the EN, then prices within the EN should always be at a significant discount.

Q23: What additional information might the AER have regard to when considering the significance of the energy likely to be sold by an exempt seller?

We agree that the exempt selling activities are insignificant in relation to the national markets in terms of volume of energy. However the number of consumers being serviced by EN's will continue to grow and these consumers cannot be disregarded or ignored by the national energy market. In particular, greater efficiencies are needed to accommodate some the non-standard aspects of EN's within the market settlement process.

Q24: Will the obligations imposed through proposed exemption conditions (see attached) and existing state/territory tenancy legislation be sufficient to avoid requiring the exempt seller to obtain a retailer authorisation?

The proposed obligations should avoid the need for retailer authorisations. However, as we note in response to Q35, some tenancy legislation precludes

a rational treatment for the charging of the energy component of hot water unless the exempt seller is a licensed retailer.

Q25: Are there any instances where state/territory tenancy and related legislation comprehensively addresses onselling, such that the conditions proposed in the attached draft determinations of deemed and registrable exemptions should not be applied?

Not that we know of, however it is desirable to have uniform nation-wide regime.

Q26: What methods might the AER adopt to determine the costs of obtaining a retailer authorisation compared to the benefits to customers of being serviced by a retailer rather than an exempt seller?

If the industry best practises are followed there is not necessarily any benefit for the consumer if the EN owner is an authorised retailer.

Very few EN owners could possibly justify seeking a retail license given the fiducial requirements of registration not to mention the administrative burden. In the context of electricity, there is no logic in an EN owner applying for retail authorisation unless it make commercial and sense for that owner to purchase power from the national market. This is most unlikely.

An appropriate national registration process for EN operators is however worthy of consideration.

Q27: Should the AER create a class of deemed exemption for persons engaged in the sale of unmetered energy where that is not prohibited by jurisdictional legislation? If yes, what conditions should be attached to that exemption? Should it be limited to existing dwellings and those that are currently in the planning stages?

Non metered consumption should be avoided wherever possible

Q28: Are there situations where it may be appropriate for the AER to grant an individual exemption to a new development that does not allow for individual electricity metering of dwellings?

No. Premises within new developments should have individual meters.

Q29: In what situations would it be appropriate for the AER to grant an individual exemption to a new development that does not allow for individual gas metering of dwellings?

It would be appropriate where the building has a centralised hot water system, heated by gas, and hot water meters are used to measure the consumption. Obviously a heating factor would need to apply to this consumption. Best practise would be for gas to individually metered in new developments.

Q30: Are there concerns about situations where there is no meter, and the consumer is not billed separately for electricity/gas? Although the consumer 'pays' for the energy indirectly (most likely through higher rent or body corporate fees), are stakeholders aware of particular concerns regarding vulnerable consumers?

This places an undue onus on Owners Corporations and creates the potential for unfair distribution of charges/costs to occupiers either through higher rent or Owners Corporation fees.

Our understanding of the Residential Tenancy Legislation (such as in Vic) is to protect tenants by ensuring billing of utilities is only achievable if the utility is metered. Despite this, there is a practise of apportioning the costs of unmetered consumption on a lot liability basis. This is at least transparent and better than being bundled into Owners Corporation fees.

This question also impinges on the challenges associated with charging for hot water consumption where the energy component is not metered but the water is metered.

Q31: Are stakeholders aware of situations where there is no meter, but customers pay an itemised charge for electricity/gas on terms negotiated as part of the purchase or leasing arrangement?

Yes. Gas only.

Q32: Would electricity metering that is not compliant with national metrology procedures suffice in situations where it would be expensive to retrofit an existing dwelling?

No. Meters must be compliant and should be type 4 or 5 meters in our opinion. The expense of retrofit should be funded by the profit attained from onselling. This is another benefit of enabling a profit incentive in EN's.

Q33: Is it appropriate for the AER to require energy suppliers in off-grid networks to seek individual exemptions?

Yes. This is an opinion only. We are not involved in off-grid networks.

Q34: Are pricing protections necessary for off-grid customers? If so, what conditions could the AER impose on off-grid suppliers to limit energy prices?

We are not involved in off-grid networks.

Q35: What other seller related factors might the AER consider in addition to those outlined in the Law?

1 Distributors

As stated elsewhere, the regulatory treatment of distributors is inevitably linked with onselling. Whether by accident or design, the LNSP's seem to frustrate the establishment of EN's.

We believe there is a case to isolate their influence over EN's by devolving responsibility for child meters within the EN to the ENO. It would make sense that the law provides for an operator to deliver services from where the LNSP's responsibilities stop at the customer premises (i.e. the low voltage terminals in the sub station). Considering that the downstream portion of the distribution network is not owned by the LNSP and the responsibility to upgrade and/or manage this portion is the responsibility of the owner, then the ENO should manage all meters.

2 Hot Water Billing and Tenancy Acts

There is a significant issue with respect to hot water billing to tenants in residential units in Victoria which causes a great deal of frustration and additional costs to Owners Corporations and has an unfair cost recovery process. While the intent of the Residential Tenancy Legislation is to protect

tenants, it creates an inconsistent approach to hot water billing dependant on whether the seller is a retailer or the body corporate.

> Retailers – can read water meters and apply a heating factor to determine the cost of gas or electricity to heat the amount of water used.
>
> Owners Corporation – under the Residential Tenancy Legislation the specific energy utility has to be metered before a tenant can be charged for hot water even though the water is metered.

This situation arises in very many high rise residential buildings and has caused a great deal of frustration and additional cost to establish a fair and reasonable approach to cost recovery and allocation on a user pays basis. In fact, a fair and reasonable approach has not been found to resolve this issue and the current tenancy legislation appears to be at odds with the intent of the AER issues paper.

Q36: What specific customer characteristics or circumstances make it appropriate for them to be served under an exemption rather than a Retailer Authorisation?

The fundamental characteristic for customers serviced in an EN under an exemption order is where the price offered to them is better than they can achieve from a Retailer. In some instances a large customer may get better pricing from a Retailer, but choose to stay in the EN because of superior service or data provision. Another circumstance is where the EN metering is used for energy reporting and energy efficiency initiatives.

Q37: What other customer related factors might the AER consider in addition to those outlined in the Law and those discussed in section 4.2.3?

None

Q38: Do stakeholders agree with the AER's registration threshold of 25 premises with a single site? Why or why not?

This seems reasonable. We have some sites with less than 25 premises but we choose to register them.

Q39: Do stakeholders agree with the AER's proposed Class 1 deemed exemption? Why or why not?

The intent of this category is to impose some conditions and guidelines without the impost of registration. This is reasonable. However, in our experience, sites of less than 25 small customers are rarely large enough to commercially operate as embedded networks.

As a matter of principle we feel that consumers should have choice of retailer. We need to understand the arguments as to why this should be waived for this class of exemption.

Q40: Do stakeholders agree with the conditions outlined in the attached draft determination that will apply to this class of deemed exemption? Why or why not?

The exempt seller does not have to offer choice of retailer. The fixed costs of operating a small network presumably need to be recouped. There is a risk that energy needs to be onsold at a price higher than market. If one applies the principle that consumers should not be financially disadvantaged by an EN, then some governance is required to ensure that "locked in" consumers are not being charged more than if supply was from a licensed retailer.

The other provisions outlined are consistent with industry best practices and should be applied to this class of exemption. There is a risk that the costs of compliance may mean that the EN is no longer financially viable.

Q41: Do stakeholders support the AER providing a blanket exemption (the Class 2 deemed exemption) to cover situations where energy is passed through without a separate charge? Why or why not?

Q42: Do stakeholders agree with the AER's proposal for this exemption to be issued without conditions?

The method of apportionment of energy cost should be transparent to the consumer.

Q43: Do stakeholders agree with the AER's proposed Class 3 deemed exemption? Why or why not?

Yes

Q44: Do stakeholders agree with the AER's proposed Classes 4 and 5 deemed exemptions? Why or why not?

The distinction between Class 4 and Class 5 registrable EN's could be confusing as many EN's have both large and small customers.

Q45: Do stakeholders agree with the conditions outlined in the attached draft determination that will apply to small customers under the Class 4 deemed exemption? Why or why not?

As a matter of principle we feel that consumers should have choice of retailer. We need to understand the arguments as to why this should be waived for this class of exemption.

Q46: Do stakeholders agree with the AER's proposed classes of registrable exemptions? Why or why not?

Yes

Q47: Is the approach of allowing a transitional deemed exemption that will be replaced by a registrable exemption appropriate? Will the proposed expiry date allow sufficient time for the relevant exempt sellers to register?

The issues paper suggests a 3 year window for transitional deemed exemptions to be becomes registered. It would be preferable for participants to operate within a registered framework as soon as practicable.

Q48: Should individual exemptions be time-limited?

From the point of administrative simplicity we would prefer that they are not time-limited. If they are time limited, then an efficient renewal system is warranted.