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Inquiry into Energy Efficiency
Productivity Commission
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Productivity Commission Draft Report

esaa welcomes the opportunity to comment on the Productivity Commission's Draft Report on Energy Efficiency. The energy industry believes that energy efficiency improvements can result in more efficient investment in energy supply infrastructure and have a valuable role to play in reducing greenhouse gas emissions.

As a general observation, esaa commends the Commission for its comprehensive and largely robust analysis of the barriers to the uptake of energy efficiency improvements and of existing government programs to address these. In addition, esaa broadly agrees with many of the Commission's conclusions regarding policies and programs currently proposed by government.

esaa is not convinced, however, that it is necessary to put the National Framework for Energy Efficiency (NFEE) process 'on hold', while existing programs that are generally recognised as being effective are reviewed. Fine-tuning and streamlining of programs should be possible while maintaining the momentum of the overall policy development process.

esaa would like to comment on two key issues of particular relevance to the energy industry: the role of energy market reform (coupled with complementary policies) and the need for a cohesive national greenhouse gas policy framework.

Energy market reform

esaa agrees with the Commission's support for further energy price reform and sees the removal of retail price controls as a priority. While the industry recognises that cost reflective pricing alone is unlikely to lead to significant increases in energy efficiency for smaller consumers, the removal of price controls is still a necessary first step. Deregulation of retail prices will further enable retailers to develop more innovative pricing options for customers, helping to reduce peak demands and the need for inefficient investment in supply infrastructure.

The Commission supports the removal of price caps only once effective competition has been established and sees price regulation as an important check on the potential for market power in some regions of the NEM. However, the draft report points to the potential for anti-competitive behaviour in the generation sector as grounds for retaining retail price controls to protect end users. esaa disagrees with this reasoning because the imposition of retail price caps simply places increased financial pressure on retailers, which are essentially price-takers. If government or regulators have concerns related to interconnection constraints, gaming or barriers to entry these should be directly addressed via competition regulation or wholesale market reform and not by retaining retail price controls.

esaa supports the removal of retail price controls wherever effective retail competition is evident. There is evidence to suggest that competition has been steadily increasing in the states where full retail contestability (FRC) has been introduced. For example, in its March 2005 Statistical Report, the Essential Services Commission of South Australia reported that in the two years since the introduction of FRC around 34 per cent of the South Australian small customer base had completed transfers to electricity market contracts. A similar transfer rate has been reached in Victoria (where FRC was introduced in 2002). In June 2004, the Victorian Essential Services Commission concluded that:

“competition has now, or will have soon, developed to a stage at which it can be relied on in the majority of cases to discipline attempts to exercise market power by raising prices above efficient costs. As competition continues to strengthen, consideration can be given to progressively rolling back the current retail price arrangements and, ultimately, to their elimination, leaving price setting to the competitive marketplace.”

There is also a danger that if retail price caps are set too low, they will not allow sufficient headroom for retailers to offer competitive prices, which discourages transfers and acts as a disincentive to new entrants. The retention of price caps that do not allow for full recovery of costs thus has the potential to further delay the emergence of a fully competitive market.

esaa reaffirms the view outlined in its original submission that complementary policies will be needed in tandem with more cost reflective prices. In some cases effective education campaigns will be required to increase the public's understanding of the implications of energy consumption. End users must be made more aware of the real costs of their usage, including the cost of investing in energy supply infrastructure and the cost of environmental externalities, especially greenhouse gas emissions. In order to be effective, such campaigns require significant government funding commitments, sophisticated marketing strategies and must be ongoing (which has not been seen in the energy efficiency field in Australia).

In other cases, it is likely that direct regulation will be necessary. esaa believes that minimum energy performance standards are warranted where the purchase decision is highly influenced by emotive considerations, where the split incentive problem arises, and where replacement occurs infrequently due to long asset lives and high up front costs. Similarly, for building standards, while fine-tuning of existing programs may be necessary, standards are likely to be needed because the same issues will act as significant barriers that cannot be overcome by information

provision alone. In both these cases it is important that policies and programs are nationally consistent to minimise costs for the industries involved.

National greenhouse policy

ESAA strongly agrees that piecemeal greenhouse policies are costly and often ineffective. The energy industry has called for a consistent national approach that provides a long term policy framework, including a long term greenhouse gas abatement target. Participants must be allowed to choose from the full range of abatement options to ensure least cost compliance.

The current fragmentation of greenhouse policy creates uncertainty about the future and can thus threaten timely investment in the energy sector. While it is likely that specific energy efficiency policy measures will be needed, these should be developed as part of a cohesive national strategy (such as that being developed under NFREE).

As the Commission has noted, there is a need for the clarification of energy and greenhouse policy objectives. Some policies may be warranted for their wider social and environmental benefits, in particular greenhouse gas reductions, even though their private benefits are less clear. If households or firms are really being required to make certain expenditure decisions as a way of achieving low cost greenhouse emissions reductions this should be explicitly recognised rather than overstating the private cost-effectiveness of the policy.

ESAA agrees with the Commission's assessment of the practicality of a national energy efficiency target. There are likely to be less costly and more effective means of addressing the barriers to energy efficiency improvements, and these should be pursued before any such scheme is considered.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Brad Page', with a stylized, cursive script.

Brad Page
Chief Executive Officer