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18 November 2013

Dr Peter Boxall, AO
Chairman
Independent Pricing and Regulatory Tribunal
PO Box Q290, QVB Post Office
QVB Post Office NSW 1230

By email: ipart@ipart.nsw.gov.au

Dear Dr Boxall,

Early Termination Fees – Electricity – Draft Report

AGL Energy welcomes the opportunity to comment on the Independent Pricing and Regulatory Tribunal (IPART)'s Draft Report on Early Termination Fees (the Draft Report), October 2013. In September 2013, AGL had provided a submission to the Issues Paper as well as confidential cost information.

AGL supports the approach IPART has taken in the Draft Report to determine the range of costs to establish the base ETF cap. In the Draft Determination, IPART has determined the base ETF cap on the basis of costs which a retailer would avoid if the customer had not signed the market contract. On this basis, customer acquisition costs are included. AGL considers that this approach conforms to the Terms of Reference which requires IPART to consider "... the retailer's reasonable costs of giving effect to the early termination of a market retail contract ..." and "... any potential impacts on consumer prices and on competition in relevant retail markets".

To be cost reflective, it is reasonable that customer acquisition costs are recovered from customers who terminate early. AGL notes that in the 2013 review of regulated retail prices[1], costs attributable to customers who terminate early were not included[2]. If these costs are not recovered from customers who terminate early, they will have to be recovered from all other customers.

However, AGL proposes for IPART's further consideration, a few points on the setting on the base ETF cap.

Acquisition cost

The costs associated with acquiring customers were assessed to be $83 per customer (2013/14$). AGL understands that this is based on the average of channel costs based on data provided by retailers. AGL uses a range of channels with some channels costing over $200 per acquisition excluding door to door marketing channels. In AGL's view, for the purpose of setting a price cap, the upper range of channel costs should be used instead of average costs. As retailers are likely to utilise the extent of the various channels differently, setting the ETF at the average benchmarked

[1] Review of regulated retail prices and charges for electricity from 1 July 2013 to 30 June 2016, Electricity – Final Report, June 2013, IPART
[2] In the 2013 review, it is implied that customers remain at least 4 years with a retailer as the customer acquisition costs are assumed to be recovered over 4 years

costs will risk setting the ETF that is too low. There is little risk in setting the ETF too high as retailers will balance the need to recover costs and the deterrent impact of the ETF on customers signing on to the market contracts.

Market segments

IPART has pointed out that the two most significant costs were sales channel costs relating to acquiring customers and the cost of bad debts (relating to losing customers).

In the Draft Determination, IPART has set the base ETF cap for small customers which include residential and small business customers. The acquisition cost and bad debt for small business customers are likely to be materially higher than those for residential customers. In AGL's experience, in some sales channels, the cost to acquire a small business customer can be 70% to 100% higher than for a residential customer. In relation to bad debts, as the typical bill for a small business customer is about 40% higher than a residential bill[3], it is reasonable to expect certain costs to be correspondingly higher. Therefore, AGL considers that there is merit in considering the base ETF cap separately for residential and small business customers.

Financial modelling assumptions

In the Draft Determination, IPART has assessed the base ETF cap to be $130 for the first year and $45 in the second year. Although AGL understands that this is a result of the modelling assumptions, AGL is concerned with the difference between the ETF in the first and following years. Preferably, the fee in the following year should not be less than half the fee in the first year.

If you have any questions in relation to this submission, please contact me on (02) 9921 2221 or mgoh@agl.com.au.

Yours sincerely,

Meng Goh
Manager Regulated Pricing

[3] 2013 review, p 6-7