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Dr Peter Boxall
Chairman
Independent Pricing & Regulatory Tribunal
Level 8, 1 Market St
Sydney, NSW

Submitted online at www.ipart.nsw.gov.au

Dear Dr Boxall

Submission on the Issues Paper - Early Termination Fees: regulating the fees charged to small electricity customers in NSW

EnergyAustralia welcomes the opportunity to make a submission to the IPART Issues Paper on the Early Termination Fees (ETFs) that apply to small electricity customers in NSW (Issues Paper).

In previous submissions to IPART, we've commented on the health of competition in the NSW electricity market, and we fear that the introduction of regulated ETF caps will undo some of the advances that have been made previously. A highly competitive market provides long-term benefits to customers. But, the introduction of regulated base ETF cap threatens discounts and price levels and may reduce the range of products and services offered by retailers. Either of these impacts would result in a worse outcome for customers.

The National Energy Customer Framework already mandates that ETFs must only include a reasonable estimate of costs resulting from early termination and must not include the costs based on lost supply or lost profits. These requirements closely align to the Terms of Reference set by the NSW Government who are seeking to provide additional customer protections and reduce barriers for customers switching retailers. Although a regulated base ETF cap may be lower than what customers would have otherwise paid, it is not clear to us that an ETF cap will provide the broad protection that customers experience in highly competitive and deregulated markets. It is also not clear that customers are excessively hindered in switching between retailers currently.

Under the new legislation enacted by the NSW Government, retailers can recoup the costs of any upfront incentives, but the ETF will be capped at a level determined by IPART. If the regulated ETF cap is set only to cover a minimal set of administration costs, then retailers are highly likely to not invest in retention activities to the same degree. For example, ongoing discounts, loyalty rebates and service offers will become less generous and less common. We argue that these customer retention activities are a key driver of customer satisfaction and, therefore, that a base ETF which does not allow for these costs will have negative consequences for customer outcomes in the NSW electricity market.

Any potential impacts to competition can be mitigated to some degree by ensuring that the regulated base ETF cap is not set 'too low' and still allows retailers some flexibility in how they structure their offers. We believe that the base ETF cap for customers who terminate early should include the costs that the retailer would not have incurred had the customer not signed the contract. This cap should therefore include the substantial costs that retailers incur during the customer acquisition process that cannot be recouped if the customer leaves too soon. These costs include:

- Acquisition and marketing costs – where these are direct and attributable to customers;
- Cost of direct investments made on behalf of the customer, including ongoing incentives;
- Energy purchase portfolio adjustment costs; and
- Administrative costs – associated with gaining or losing a customer or making adjustments when the customer terminates early.

Separately, we will also provide confidential details of the costs above to allow IPART to benchmark and determine a reasonable base ETF cap.

If you would like more information on this submission, please contact me on (03) 8628 1242.

Yours sincerely

Melinda Green
Regulatory Manager - Pricing

EnergyAustralia submission to IPART on the Early Termination Fees Issues Paper

September 2013

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1. Costs included in early termination fees

1.1. Cost recovery through existing ETFs

1. What types of costs do retailers typically seek to recover through their current ETFs?

As part of recent changes to the National Energy Retail Rules, the NSW Government has decided to cap the amount of the base level of the ETF for electricity contracts.[1] However, the Act will still allow retailers to recoup the pro rata amount of any 'upfront inducement' or incentive for customers who terminate early. Retailers commonly include early termination fees (ETFs) as part of energy contracts so they are able to recover some of the significant costs incurred in signing up customers who leave early.

The categories of costs that we seek to recover through our current ETFs are consistent with IPART's assessment:

- acquisition and marketing costs (where directly attributable to any particular customer);
- cost of direct investments made on behalf of the customer, including non-upfront inducements;
- energy purchase portfolio adjustment costs; and
- administrative costs – associated with gaining or losing a customer or making adjustments when the customer terminates early.

IPART note that they *"did not find a clear relationship between the level of the ETF and other features of the offering, such as upfront inducements or the ongoing discounts."*[2] This is not surprising. As discussed by IPART, ETFs can differ significantly between retailers, because costs to acquire customers are highly variable and because retailers all have different cost structures. In addition, retailers are likely to not recover all the costs listed above in their ETFs as customers may be put off signing up to a retail offer that has a particularly high ETF. It is also more difficult to collect a very high ETF from customers who terminate early than it would be to recoup a smaller amount. So while an ETF can be a deterrent to customers leaving a retailer before the end of the contract (or fixed benefit term), the retailer has to balance the level of the fee with any potential negative impact on customer acquisitions and the ability of the retailer to recover the full ETF.

These factors exist in a competitive market where there is no cap on ETFs (see later discussion in section 3.3). If a restrictive cap is placed on ETFs then it's likely that all retailers will set their fees at the cap level and this will limit competition for this element of the offer.

[1] The National Energy Retail Rules as modified by the *National Energy Retail Law (Adoption) Regulation 2013*, and which apply in accordance with the *National Energy Retail Law (Adoption) Act 2012 (NSW)*.

[2] IPART, Issues Paper, page 12

1.2. Costs to be included in the base ETF cap

2. Which costs, consistent with the terms of reference, can be included in the base ETF cap?
   - Which costs would a retailer avoid if the customer had not signed the contract?
   - Which costs would a retailer avoid if the customer completed the contract term?
   - Of these costs, which (if any) relate to lost supply and lost profit?

1.2.1. Interpretation of 'giving effect to early termination'

IPART has considered how to interpret the requirement in the Terms of Reference to assess *"a retailer's reasonable costs of giving effect to the early termination of a market retail contract"*.[3] It's appropriate that IPART are considering the following interpretations:

1. The costs the retailer would avoid had the customer not signed the contract
2. The costs incurred if the customer did not complete the contract term

When a customer terminates early, the majority of these costs have already been incurred during the 'sign-up' process, although there are some other smaller expenses associated with the termination process. When a retailer sets an ETF, they hope:

- to signal to the customer the retailer's cost of the customer leaving early (to discourage the customer from leaving early); and
- to be able to recover their reasonable costs (if the customer does leave early).

Retailers expect to retain customers for the length of the contract period and so a retailer will attempt to win another customer when a customer terminates early. That is, giving effect to the early termination of one customer is directly linked to acquiring another.

The consequences of replacing customers who terminate early are that a retailer with more 'early terminating' customers will also incur higher total costs in acquiring new customers. Therefore, in our view, the costs of giving effect to an early termination are coupled to the costs associated with acquiring a new customer. As such, we suggest that the interpretation under point 1 is the most appropriate.

At the high level, retailers enter into contracts (each for a certain period) to hedge the purchase of energy for customers. It is costly for a retailer to be significantly over- or under-hedged and so we always try to maintain and adjust hedge volumes to reflect forecast customer load. Optimising our hedge position minimises overall energy costs, which enables us to give customers better offers. This factor also drives retailers to replace lost customers.

IPART state that in considering their preferred interpretation of 'the reasonable costs of giving effect to early termination' may depend on which has the least distortionary effects on competition. Excluding the costs of signing up a customer who terminates early in this definition would mean that retailers are less able to recover the sign up/set up costs. Thus, without finding another way of recovering these costs, then retailers will be less able to fund the acquisition of a new (replacement) customer.

[3] IPART, Issues Paper, page 37, Appendix A

The offsetting unrecovered sign-up costs is likely to involve limiting the value and type of discounts, rebates and other non-recoverable inducements and investments that go into the retail offer. We contend that the consequences of these limitations will have a negative effect on competition. Therefore, it is in the interests of customers that 'the reasonable costs of giving effect to early termination' should be interpreted as 'the costs the retailer would avoid had the customer not signed the contract' (interpretation 1).

1.2.2. Categorisation of costs that can be included in the base ETF cap

In table 1, we've listed the categories considered by IPART as 'the costs the retailer would avoid had the customer not signed the contract'.[4] Alongside each category, we've provided a more detailed description of the specific costs and a brief assessment of which we believe are suitable for inclusion under the Terms of Reference.

Table 1: Assessment of the inclusion of costs in the base ETF cap

Cost category	Description of costs included within each category	Can be included?
Acquisition and marketing costs	1. Sales commission costs for external channels	Yes
	2. Direct marketing costs – e.g. the costs of sending a direct mail offer to the customer on request, or visiting the site as part of a home energy audit)	Yes - although these are currently very low
	3. General sales overheads and marketing campaign costs	No – costs are incurred regardless
Cost of investments made on behalf of the customer	4. Non-upfront inducements (provided to the customer sometime after they initially sign up) - e.g. loyalty rebates, discounts, free services, etc.	Yes – these are direct investments made on behalf of the customer
	5. Other direct investments made behalf of the customer – e.g. for the supply of a metering service, etc.	Yes
	6. New systems, tools and services for all customers	No – these are not incremental costs
Energy purchase portfolio adjustment costs	7. Gains or losses on the energy purchase portfolio position	Yes
	8. Energy portfolio adjustment transaction costs	Yes
Administrative costs of gaining a new customer	9. Administrative quoting costs for some external sales channels	Yes
	10. Costs of sending offer confirmation packs to customers after the quote is accepted	Yes
	11. Costs of processing new customer 'transfer in' and setting up the customer's account	Yes
Administrative costs of finalising a customer account (following early termination)	12. Calling the customer to encourage them not to terminate early	Yes
	13. The costs of final billing a customer (including final billing a customer on a bill-smoothing arrangement or a payment arrangement)	Yes
	14. Costs of late payment and bad debt	Yes

Costs relating to 'lost supply' or 'lost profit'

The majority of the costs are operational costs and cannot be deemed to be revenue or profits of any kind. Except for cost 7 (in table 1), none of the costs that we've listed for inclusion in the base ETF cap contains an amount that could be considered the costs of 'lost profit' or 'lost supply'.

[4] IPART, Issues Paper, Table 3.1, page 18

Cost 7 arises from the gains or losses made when the energy purchase portfolio position is adjusted when the customer leaves, and may be considered a type of revenue. However, given the systematic bias in contracts being below the purchase price at the time the retailer loses the customer,[5] then this will be (on average) a cost, not a form of revenue or profit (see section 2.4).

Neither is cost 7 a cost of lost supply. If a retailer enters a contract to provide energy to a customer, the cost of lost supply in our view, would be the future costs of the retailer continuing to pay the unadjusted hedge contract amount for the remainder of the contract period (as if the customer hadn't terminated early). If the retailer adjusts the hedge contract when the customer leaves early, then the retailer can avoid the ongoing cost of supply under this contract. However, the retailer crystallises a loss when making this adjustment (as noted above). Importantly, this loss relates to the difference in hedge position, rather than the cost of continuing to supply energy to the customer. The costs of energy supply from the pool price purchase costs would not be incurred once the customer moves to another retailer, however this does not nullify the hedge costs as the contract taken out by the retailer is still in place. Therefore, we believe that cost 7 also meets the requirements outlined in the Terms of Reference for inclusion in the ETF cap.

[5] IPART, Issues Paper, page 25

2. The level and range of relevant costs

2.1. Introduction

3. What level and range of costs could be reasonably associated with giving effect to early termination?

In the sections below, we discuss the costs in table 1 that should be included in the base ETF cap and describe the components of each cost in more detail. Although there is no quantitative data included here, as part of our submission to this review, we will be providing IPART with confidential data in support of the cost categories in table 1 to show the level and range of these costs.

2.2. Customer acquisition costs

- What is the range of the customer acquisition costs (excluding upfront inducements) that retailers could reasonably avoid if the customer had not signed the contract?

Acquisition and marketing costs can be classified into three main types:

- sales channel commission costs;
- direct, incremental marketing costs associated with a specific sales approach to a customer; and
- general sales overheads and marketing campaign costs.

The first two cost types are suitable for inclusion in the base ETF cap as they are direct costs that escalate for every additional customer signed up. However, the third type of cost is not appropriate as these are a type of overhead cost that we incur for investing in broad level sales and marketing activities, *"but which are not attributable to acquiring a specific customer"*.[6]

The structure of the contacts that we have with our external sales channels usually specifies the amount of commission per customer signed up. The commission amount may vary depending on the type of sale made and may include other types of incentive payments. Sales channel commission costs per sale are significant and make up a large proportion of the customer acquisition costs that IPART assessed as part of their recent retail review.[6]

IPART mention in the Issues Paper that acquiring a dual fuel customer may lower the overall customer acquisition costs per fuel.[6] This lowering effect can arise for some internal channels through reduced overheads as we have spent less time and resources in signing up both fuels. However, we do not see any reduction in costs for our external channels as the commission payments for electricity and gas sales are additive and do not differ if the sales channel sells one or two fuels to a customer.

In the Issues Paper, IPART also suggest that inducement costs can be a substitute for direct sales acquisition costs and that sales commission payments may include amounts for

[6] IPART, Issues Paper, page 22

advertising and other marketing costs. However, the amounts we will provide to IPART are commission amounts alone and do not include inducement costs or overheads.

Another type of direct and incremental costs that retailers can face is a marketing cost associated with contacting a specific customer to make a sale. At times, we may run a campaign that encourages customers to call us to discuss the offer, or may possibly arrange an appointment with the customer (e.g. for a home energy audit). Although the costs of the original marketing campaign would be considered to be overheads, any other customer-specific costs incurred as part of signing the customer up are direct costs attributable to each sale. We are currently not carrying out this type of activity in any significant amount, but believe it's appropriate that this cost type to be recognised as a valid component in the base ETF cap for retailers who do market in this way, or who may be carrying out this type of activity when IPART reviews the cap in two years' time.

2.3. Investments made on behalf of the customer

- What is the range of investments made on behalf of customers, such as incurring energy-purchase related costs that retailers could reasonably avoid if the customer had not signed the contract?

We consider that there are also three broad types of costs for investments that retailers make on behalf of customers:

- non-upfront inducements – that is, an item of value to the customer mentioned at the time of customer sign-up to encourage the customer to accept the retail offer, but which is delivered sometime later in the contract rather than 'upfront' (e.g. later than the receipt of the first bill);
- contracts entered into on behalf of the customer – e.g. for the supply of a metering service – these differ from inducements in that they are not used as a selling point to induce a customer to accept a retail offer; and
- investments in new and improved retail systems, tools and services.

Each type of cost is discussed in more detail below.

Non-upfront inducements

Upfront inducements are specifically excluded from consideration as a cost component of the base ETF cap by the Terms of Reference. These usually include any monetary rebates, magazine or football team subscriptions and tickets provided soon after the customer signs up.

However, not all inducements discussed at the point of sale are delivered soon after the customer signs up. Such 'non-upfront' inducements include:

- loyalty rebates
- discounts
- free green energy
- electronic billing (this may be provided through a separate contractual arrangement)

- ongoing payment of subscriptions or memberships
- anniversary gifts – e.g. annual solar panel cleaning, in house display, book voucher, etc.

These types of inducements are an investment that the retailer makes to retain the customer. They are a direct and incremental cost to the retailer and therefore should be included in the assessment of the price level for the base ETF cap. Sometimes retailers may enter into a contractual arrangement with external parties to offer some of these inducements to customers.

Determining the value of these investments across all retailers may be difficult as this category of costs will vary significantly over time and between retailers. To not include an amount for non-upfront investments however, would discourage retailers from offering non-upfront inducements (or would limit the value of the inducement).

If retailer offers were structured to focus more heavily on upfront inducements rather than ongoing or later benefits, then the sales and marketing focus would transfer to the acquisition of accounts rather than retention. This would also drive retailers to continue to compete on the basis of 'churning' or continually acquiring new customers rather than retaining existing customers. We believe that customer outcomes are better where markets also place considerable focus on retention activities.

Other direct investments made on behalf of the customer

The examples that IPART give in the Issues Paper for investments made on behalf of the customer fit into a category where they are neither an inducement (as above) or an investment of fixed cost made on behalf of a large group of customers (as below). For example, a retailer may have to engage with a service provider to offer metering services to the customer or provide the customer with referrals to financial counsellors and other hardship assistance.

These investments do not have the same perceived value to the customer and so are not an inducement mentioned at the point of sale. However, they do have a direct cost that varies in line with the number of customers for whom the investments are made, and so they fit the criteria for inclusion in the base ETF cap. Their inclusion in the base cap also assists in creating awareness of the costs of investments made to assist customers in financial hardship.

Systems, tools and process investments

Investments in new and updated systems, tools and processes are high-level investments. That is, they are investments made on behalf of all customers where costs do not escalate based on customer take up and which are normally seen as an overhead. These types of costs do not appear to be appropriate to consider as an investment for the purposes of setting the base ETF cap.

2.4. Energy purchase portfolio adjustment costs

- What energy-purchase related costs do retailers face in adjusting their portfolio if a customer terminates early?

The Issues Paper clearly outlines the two types of energy-purchase related costs that retailers bear when a customer terminates early.[7] These are the:

- gains and losses on the energy purchase portfolio position that arise when the retailer adjusts their hedging arrangements following early customer termination; and
- transactional or administrative costs of adjusting the energy purchase portfolio position following early customer termination.

Gains and losses on the energy purchase portfolio position

While it could be seen that customers terminating early could lead to both retailer gains and losses when adjusting their hedge position, the current market conditions will produce a net loss based on the systematic bias of contracts being lower in value when sold than when purchased. Financial realisation of these changes in value is triggered by the customer's early termination and so is directly attributable to the customer. Earlier, we outlined our reasons why this cost category is not a form of lost supply or profit (see section 1.2.2). Thus, we believe it is appropriate to consider this cost in the base ETF cap.

The estimation of this cost is complicated as futures contracts for later periods are typically higher in price today than closer to the start of the contract period. We suggest that a good proxy for this cost would be to calculate the value of the swaption premium and multiply this by the average usage of a NSW electricity customer. The resulting value represents is the value of the risk that a retailer accepts in signing up a customer for a longer period without being certain that the hedge arrangements for later periods will be required. We will provide details of the swaption calculations to IPART along with our other data.

Transactional or administrative costs of adjusting the energy purchase portfolio

Similar to the gains and losses that result from adjustments to the hedge position, the associated transactional costs are also a direct and incremental cost of the customer's early termination. These costs have historically been lower in total than the costs arising from losses in the energy purchase position. The types of costs we incur in this category include:

- brokerage fees;
- exchange fees; and
- costs of settlements resources who carry out these adjustments.

[7] IPART, Issues Paper, pages 25-26

2.5. Administrative costs

- What is the range of administrative costs that retailers could reasonably avoid if the customer had not signed the contract?
- What is the range of costs for closing an account and what proportion relates to early termination?

2.5.1. Administrative costs incurred by the retailer when a customer signs up

The direct costs faced by a retailer that are attributable to a customer sign up are:

- administrative quoting costs for some external sales channels;
- costs of sending offer confirmation packs to customers after the quote is accepted; and
- costs of processing new customer 'transfer in' and setting up the customer's account.

Of these costs, the offer confirmation packs and the costs of processing new accounts are applicable to each sale we make. The administrative quoting costs are only incurred for customers who sign up via certain channels. Further details on the level of these costs will be provided confidentially to IPART.

2.5.2. Administrative costs incurred by the retailer when a customer terminates early

For customer termination, there are also a range of direct and incremental costs that retailers incur. These are listed below and further details on cost ranges will be provided to IPART:

- calling to attempt to retain the customer by offering greater discounts or improved product features;
- costs of final billing a customer (including final billing a customer on a bill-smoothing arrangement or a payment arrangement); and
- credit related costs of late payment and bad debt associated with the final bill.

3. The impacts an ETF cap on prices and the competitive market

4. What are the impacts of the introduction of a base ETF cap for consumer prices and the competitive market in terms of:
   - The potential responses of customers and retailers to the introduction of a regulated base ETF?
   - The potential impacts these responses will have on electricity prices and the level of competition in the retail electricity market?
   - The implications of setting the base ETF cap either 'too low' or 'too high'?
   - The experience in other jurisdictions where ETFs are regulated?

3.1. Potential responses of customers and retailers to an ETF cap

Whether customers take the opportunity more often to switch retailers under an ETF cap is uncertain. On one hand, a barrier to switching may be removed; on the other, customers may pay less attention to the ETF than in the past and continue to switch at the same rate (all other factors being equal). It is likely that ETFs will feature less prominently in customers' minds at the time they are choosing between retail offers as:

- customers could perceive that 'all ETFs are the same anyway' (and depending on the price level of the ETF cap, it's possible that ETFs will all be the same); and
- that more fixed term contracts may include an ETF than they do currently.

We agree with IPART's synopsis of possible retailer responses to the introduction of an ETF cap. Retailers are likely to respond in different ways. It is highly probable that retailers will structure their retail offers differently – to have lower discounts, lower overall rebates and free services and other add-ons. Some may reduce their level of marketing and sales activity, while others may become more selective in which customers they acquire on offers with higher unrecoverable costs. The more generous offers may not be available to all customers – for example, they may only be open to existing customers or those whose profile suggests a low likelihood that they will terminate their contract early.

In addition, different customers value the elements of an energy offer differently. Some customers focus purely on the per MWh/MJ rate, while others are attracted to discounts and special offers. Other customers value the certainty of a fixed price, which is generally offered with an ETF where a customer chooses to leave before the end of the contract period. Having a variety of offers allows us to cater to a diverse range of customer preferences. Limiting ETFs may reduce this variety.

Another response to the introduction of an ETF cap is that the implementation diverts retailers' resources to changing systems and processes and ensuring ongoing compliance. This can take time, people and money away from implementing other changes that could have greater benefits customers. Although it may seem like a simple change to alter the value of existing ETFs to the new regulated cap amount, it is not. The changes are more complex as they require us to separately manage the customers who sign up on the new contracts with an ETF

cap, and to restructure our product sets, establish processes for calculating the pro rata amount for any upfront inducement[8]

3.2. Potential impacts of an ETF cap on electricity prices and level of competition

The response of retailers to a base ETF cap that does not allow them to recover the costs that they will incur in having customers terminate early will be to limit their product and service offerings in some way. That is, innovation will be constrained and retailers will shift the value of product offers around so they can still attract and retain customers - and make a profit.

The effect on electricity prices in isolation is difficult to predict, but we would expect that discounting would decrease, or that offers would be restricted so that more of the value provided to customers qualifies as an upfront inducement, which is recoverable if the customer terminates early. This would limit the interest of retailers in investing in ongoing service provision to customers such as electronic billing, meter data services, energy efficiency services, etc. (for example, see the list of non-upfront inducements in section 2.3). These services are used to retain customers are unsurprisingly the ones that drive customer satisfaction with their retailer. If these were unable to be recovered then it would also shift the focus of competition between retailers more to the upfront inducements and therefore to acquisition instead of retention. When a retail market does not as actively try to retain customers, then there is a risk that customer outcomes will suffer.

For these reasons, we contend that a restrictive ETF cap would have a negative effect on competition and the long-term interests of customers.

3.3. The implications of setting the ETF cap either 'too low' or 'too high'

IPART has indentified the major issues associated with having the ETF cap set 'too low' and clearly outlines their concerns on the negative consequences for customers if retailers' flexibility is reduced.[9]

Under a low regulated ETF cap, customers would have a lower barrier to switching and not face the cost-reflective price of switching before the end of the contract term. If more customers were to switch early due to lower switching barriers, then retailers' total costs could be driven up. In effect, all customers would be bearing the costs of customers who terminate their contract early, and these costs would be higher than they are today. This is clearly not a positive step for competition.

On the other hand, IPART suggest that setting the ETF cap 'too high' also creates risks, however we disagree that this would occur in practice. ETFs are already effectively capped by the competitive market. Retailers are required to disclose ETFs up front when making a sale and in the Energy Price Fact Sheets published on the retailers' and regulator websites. Customers will baulk at signing up to a contract with an exorbitant ETF (i.e. where the value is out of line compared to their expected electricity costs) and will easily find a better deal

[8] If the pro rata amount of the inducement has to be determined to a quarterly, monthly or even a smaller time period, this will add an extra task to the usually largely automated final bill creation process. In Victoria, the pro rata inducement amount can be calculated on an annual basis, which is far easier and cheaper to automate. The same concerns were raised in the Essential Services Commission review –Early Termination Fees Compliance Review: Final Decision, Dec 2006, page 8

[9] IPART, Issues Paper, page 31

elsewhere even if this were to occur. The current base ETFs are not exorbitant[10] and, excluding upfront inducements, do not even cover the customer acquisition costs that IPART assessed as part of their recent retail review.[11]

Unless retailers can still realistically recover their reasonable costs and compete under the base ETF cap, we believe that there will be a longer-term detrimental impact to competition. These effects may not be seen immediately due to the way that the ETF cap will be introduced for new customers, and could be clouded by other major factors that affect competition. However, the fact remains that regulating a key product element (and revenue source) and making a charge less cost-reflective will have a detrimental effect on competition and the long-term interests of customers.

A consumer awareness campaign to assist customers to understand more about their options would be useful regardless of the amount of the ETF cap amount. We do not understand why IPART suggest that a consumer awareness campaign may be required if the ETF cap is set at a level that allows retailers to recover a reasonable proportion of the costs for early termination. Retailers are already competing on ETFs and so there would be little difference in the options that customers already have.

3.4. The experience in other jurisdictions where ETFs are regulated

In Victoria, the Essential Services Commission has set the ETF cap at $20.[12] This cap level is too low and is designed to allow retailers to recover only a limited range of administrative costs. There are some important differences in Victoria that stimulate competition, product innovation and customer outcomes. The prime differences being that price regulation was removed in 2009 and that there has been a large investment in smart metering technology that allows retailers to increase and tailor the range of services and offerings to customers. Retailers have therefore been able to find other ways to compete whilst still being offering a relatively expansive product range.

However, there are many who also suggest the range of retailers' offers is limited compared to what they would expect to see in a competitive market with a large number of new entrant retailers. Arguably, product differentiation may be greater in Victoria if it weren't for the low cap on ETFs, the continued high burden of non-price regulations and the need to adapt systems and processes to operate effectively in readiness for the large portion of customers on smart meters.

[10] IPART, Issues Paper, Table 2.1, page 12

[11] IPART, Issues Paper, Table 4.1, page 22

[12] Essential Services Commission, Energy Retail Code, Version 10, May 2012, clause 31