SHOPPING CENTRE
COUNCIL OF AUSTRALIA

Inquiry into Inset (or Embedded) Electricity Networks

Submission by the

Shopping Centre Council of Australia

21 February 2013

TABLE OF CONTENTS

Executive Summary

Although puzzled by the reasons for this *Inquiry into Inset (or Embedded) Electricity Networks*, announced on 18 December 2012, the Shopping Centre Council of Australia (SCCA) welcomes the opportunity to provide a submission.

This submission outlines how inset schemes operate across our member's shopping centres, noting the Inquiry's "business to small business" context and addressing the three key areas of examination noted in the Terms of Reference: (1) pricing arrangements for different networks and customers, (2) the methodology employed to determine pricing; and (3) the ability for inset customers to purchase electricity from other providers. We have focussed on the provision of electricity to retail tenants for their consumption on their premises (as a service) as distinct from the provision of electricity to common areas which is recovered from retail tenants (as an outgoing).

The Commissioner would be aware that inset schemes continue to be a regulated activity, with regulatory responsibility transferring from the Essential Services Commission of South Australia (ESCOSA) to the Australian Energy Regulator (AER) from 1 February 2013 as part of the SA Government's adoption of the National Energy Customer Framework (NECF). A principal focus of regulation has been, and continues to be, 'reselling' and 'pricing' arrangements, particularly in relation to small electricity customers (who consume less than 160MWh per annum) and who do not have access to their electricity provider of choice. Until 1 February 2013, the operation of inset schemes was principally guided by the ESCOSA's *Electricity Reselling Arrangements in South Australia (November 2003)* and occasional pricing updates.

While no Issues Paper has been released which would have provided transparency and a clear articulation of areas of concern, we understand a concern relates to circumstances where inset scheme customers do not have access to their electricity provider of choice. The ESCOSA guideline referenced above provides that inset scheme operators must provide an inset customer with access to their electricity provider of choice if they entered into a lease agreement after 1 January 2003, or the premises commenced construction on or after 1 October 2000. The AER has noted that given the time that has passed since 1 January 2003 (when 'full retail contestability' was introduced for small electricity customers) it is unlikely that many inset scheme customers would no longer have access to their provider of choice. In any case, the ESCOSA guideline provides pricing protections for such customers through the setting of a maximum charge, referencing the AGL Standing Contract Price. In circumstances where customers do have access to their electricity provider of choice, pricing is established through a commercial agreement.

We must highlight our concerns with the basis of the Inquiry which appears to be a handful of misconceptions and unsubstantiated allegations against inset scheme operators, potentially raised through the Energy Consumers' Council (on which the SCCA is not represented). The Government has called for "facts, figures, data, examples and documents" in submissions, but hasn't produced any information about the basis of the Inquiry or the issues.

We request that the Commissioner notes our concerns in his final report to the Minister.

We do not raise this point lightly. In announcing the Inquiry, and based on previous public statements, Minister Koutsantonis has effectively accused the operators of inset schemes of improper conduct, including "anti-competitive behaviour", "inappropriate use of the imbalance of bargaining power" and the methods used to determine electricity pricing. A review of the past three (publicly available) Energy Consumer Council Annual Reports provides no further clarification on the issues driving the Inquiry, with each report having the same general conclusion in relation to inset schemes as follows: "the Council will closely monitor future developments in this area".

We are also further puzzled about the need for an Inquiry given the operation of inset schemes remains the subject of extensive regulation, including recent new regulations. With regard to the Minister's comments noted above, we hope our members are not being accused of any improper conduct given that they simply complied with long-standing Government requirements.

We further note that regulatory responsibility for inset schemes was transferred to the Australian Energy Regulator (AER) on 1 February 2013. In fact, the transition to the AER framework was announced at the same time as the announcement on the Inset Scheme Inquiry. This raises questions about the future role of the SA Government with inset schemes. We would be concerned about the introduction of additional and potentially duplicative requirements through additional regulation, guidelines or an industry code of conduct.

The basis of the Inquiry is also confusing given that government and council imposed statutory charges have a much more significant impact than electricity costs. By way of example, for neighbourhood shopping centres, the industry benchmark cost for local council rates is $18.42/m2 of Gross Lettable Area of Retail (GLAR), while land tax is $16.96/m2. Water and sewerage rates are $8.16/m2. A comparison of these costs with the electricity cost benchmark of $5.39/m2 highlights that the lowest statutory charge is 50% higher than the cost of electricity and land tax and council rates are more than 200% higher. It is therefore difficult to understand why the Government has singled out electricity costs to be the subject of an Inquiry. We would urge the Commissioner to investigate these statutory taxes and charges; particularly given they are provided by monopoly providers and have no equivalent 'price protections' in place for businesses. We recently addressed some of these issues in our submission to the SA Parliament's *Economic and Finance Committee's Tax Inquiry* which is available on the Committee's website.

Because of the recent commencement of the AER framework, our submission covers the pre and post 1 February 2013 regulatory arrangements, but we have tried to focus on the current AER arrangements.

We sincerely hope the Inquiry will be approached in an objective manner and that claims from small businesses and retailers will be transparent, analysed and critiqued. We remain sceptical about the basis of the Inquiry. A fair inquiry cannot be conducted with the operators of inset schemes being asked to respond to vague and unsubstantiated accusations and allegations about their conduct. This is particularly the case where companies have operated inset schemes in accordance with long-standing SA Government requirements, and now the AER's requirements, which the SA Government endorsed on 18 December and brought into effect on 1 February.

We also hope the Inquiry will acknowledge the fact that inset schemes reflect a significant capital and operational investment from shopping centre owners and developers, and they are entitled to operate these networks on commercial terms within the parameters of relevant regulation.

We would welcome discussing this submission with the Commissioner. Our contact details, including a list of our members who operate in South Australia, are provided at the end of this submission.

1. What is an inset scheme?

This section provides a general description of inset schemes.

General

There are two aspects to the operation of inset schemes: (i) the physical operation of an inset network built into a property which permits the distribution of electricity (essentially the operation of a mini electricity network), and (ii) the onselling of electricity using that inset scheme. The Inquiry appears to be focusing on this second category – namely the onselling of electricity using inset schemes, rather than the first category (although this is not clear from the Terms of Reference) and therefore we will primarily respond in relation to this second category of onselling.

It is important that the Commissioner understand that under this second category, the price of electricity sold using that network consists of not only the electricity commodity price, but also network access charges (imposed on an onseller by the network distributors) and environment and other charges (imposed on an onseller as a consequence of government regulation).

The onselling of electricity using an inset scheme also requires the operator of that scheme, generally the owner of the property, to have invested substantially in physical components such as switchboards, cabling, gate meters, common area meters, 'child' and 'orphan' meters (as in individual meters used for retail tenants), and transformers. As such, it represents a substantial capital investment by the owner of a property where an inset scheme is located. It also encompasses the operational activities such as meter reading, billing, the provision of customer service as well as general maintenance activities. If anything happens to the inset scheme's physical network, it is the responsibility of the owner to rectify that network and take the risk in that investment. Additionally, in order to ensure that an onseller has electricity to onsell, they typically enter into long term forward purchase contracts with electricity retailers where the purchase price for the electricity commodity is set over the term of the contract, with applicable network and environmental and other charges added on by the electricity retailer.

Regulation

Inset schemes and electricity onselling are highly regulated activities.

In South Australia, up to 1 February 2013, inset schemes were operated in accordance with relevant legislation, policies and guidelines including the *Electricity Act 1996*, *Electricity (General) Regulation 1997 (Regulation 6 (3)-(9))* and guidance issued by the ESCOSA including its *Electricity Reselling Arrangements in South Australia Advisory Bulletin (November 2003)*. Since 1 February 2013, inset schemes are operated under a combination of regulations including the *Electricity Act 1996 (SA)*, the *National Energy Retail Law (South Australia) Act 2011*, and associated regulations. The onselling of electricity using inset networks is now the responsibility of the AER. As such, the operation of inset networks has for a significant period of time been recognised as a legitimate part of the electricity network and a legal aspect of the business of shopping centre owners and operators.

In accordance with relevant laws, inset schemes are able to be operated pursuant to certain exemptions, which exempt the operators of inset schemes from the requirement to be: (1) a registered network service provider (i.e. network exemption) and (2) an authorised electricity retailer (i.e. retail exemption), subject to compliance with certain conditions. The right to be exempt recognises that inset schemes are incidental to, and not core business of, the operators of such schemes such as shopping centre owners and managers. The AER framework has three broad exemption classes: (1) deemed exemptions, (2) registrable exemptions, and (3) individual exemptions, within which there are a number of situation specific exemptions. Our members typically rely on the following deemed and registrable exemptions to permit the operation of their inset networks:

- Retail class D7 & Network class D7 - Landlords or lessors passing on common area energy costs to premises in commercial developments
- Retail class R1 & Network class R1 - Metered energy onselling by commercial/ retail landlords or lessors to small customers

- Retail class R5 & Network class R5 - Metered energy onselling to large customers

All of these exemptions impose conditions on the onseller or network operator, which are outlined in the AER's *Network Service Provider Exemption Guidelines* and *Exempt Selling Guidelines*, and include conditions which relate to issues such as:

- The right of customers to access to electricity provider of choice.
- Metering arrangements.
- Dispute resolution.
- General customer protections.

The AER also recognises that in South Australia the majority of inset scheme customers are likely to have access to retailer of choice, and that only a limited subset of consumers would not have such access.

In the case of shopping centres, the price at which a landlord can sell electricity in inset schemes also relates to the *Retail and Commercial Leases Act 1995*, through the disclosure and recovery of electricity for common areas as an operating expense or outgoing.

RECOMMENDATIONS

1. **The Commissioner acknowledges that inset schemes are a legitimate part of the electricity network.**
2. **The Commissioner acknowledges that inset schemes represent a substantial capital and operational investment by shopping centre owners which they need to operate on commercial terms.**
3. **The Commissioner acknowledges that the operation of inset schemes remains the subject of government regulation, including customer protections for inset scheme customers.**

2. Terms of reference

We are pleased to respond to the Terms of Reference.

2.1 Pricing arrangements currently in place for different inset networks and for different inset customers.

The pricing arrangements currently used by our members generally reflect the regulatory requirements pre 1 February 2013, as given the timing of this Inquiry and the legislative changes to energy regulation in South Australia and the commencement of the AER framework. These pricing arrangements reflect the different treatment of inset scheme customers required under previous legislation, which is broadly differentiated into the following two areas:

2.1.1 Small customers/large customers

- Small customers – who consume less than 160 MW-hours of electricity per annum; and
- Large customers – who consume 160 MW-hours or more of electricity per annum.

It is worth noting that the SA Government maintained its 160MWh small/large customer threshold in transferring the regulation of inset schemes to the AER, whereas the AER default threshold is 100MWh. This means that more businesses are treated as small electricity consumers (and therefore subject to 'small customer' protections as set out in the conditions to the on selling exemptions referred to above) than would otherwise be the case under the AER framework.

2.1.2 Date of entry into a lease

In South Australia, since 1 January 2003, inset scheme operators have been required to provide inset customers with access to an electricity retailer of choice if:

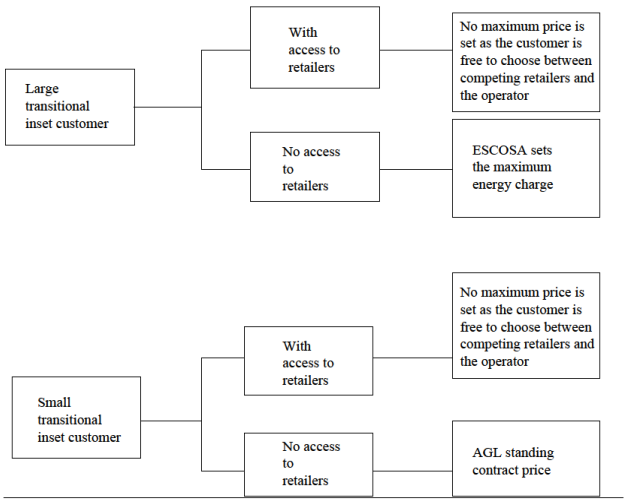
- The operator and inset customer entered into a lease agreement after 1 January 2003 (inset customers who entered into a lease prior to 1 January 2003 are referred to in the regulations as "transitional inset customers"), or
- The premises commenced construction on or after 12 October 2000.

The requirements noted above were introduced (through ESCOSA guidelines) when 'full retail contestability' was introduced in South Australia for small electricity customers on 1 January 2003. Under this regulatory regime, those tenants who did not have access to retailer of choice had the price at which the landlord could sell them electricity capped by ESCOSA at the applicable AGL SA Standing Contract price

Given the introduction of full retail contestability over ten years and the time period for most retail leases, there are very few retail tenants who do not have access to an electricity provider of choice.

The pricing arrangements under the previous ESCOSA framework (which to a large extent are the pricing arrangements implemented by our members) are best summarised by an illustration from the ESCOSA's *Electricity Reselling Arrangements in South Australia (November 2003)* (page 10) as follows:

Figure 1. ESCOSA sets the maximum charge for large and small transitional customers without access to their retailer of choice.



Other and more specific pricing arrangements are outlined in the ESCOSA guideline.

Pricing arrangement example

To give an example of a recently monthly charge (pre 1 February 2013) for a small inset scheme customer, a mobile phone retailer was charged the AGL *General Supply 126M* tariff. This retailer consumed around 2,100kWh and was charged around $720 (excl. GST). It is important to note that electricity tariffs are not simplistic. The AGL Tariff 126M is structured into a retail and network component; winter and summer tariff periods; and inclining consumption tariffs.

AER Exempt Selling pricing arrangements

Under the AER *Exempt Selling Guidelines* (December 2011), there is no similar 'price protection' in place for small customers who do not have access to retailer of choice. However the AER issued in November 2012 a set of revised draft guidelines for consultation in, which are yet to be finalised, which contain a revised condition 7 to be applied to a number of classes of exemption, which provides:

> *Where access to choice of retailer for a customer is not available, an exempt person must not change the exempt customer tariffs higher than the standing offer price that would be charged by the relevant local area retailer for new connections, if the local area retailer were to supply that quantity of energy directly to the premises of the exempt customer. (This condition applies if immediate access to Full Retail Contestability is not available, that is, where the customer must pay for and negotiate a new connection and pay for associated infrastructure).*

We have no objection to the proposed revised condition 7, and are awaiting the finalisation of these revised guidelines to determine whether current pricing arrangements will be subject to further change.

We were involved in the development of the AER's exemption guidelines. As our members are organisations that operate across a number of jurisdictions, we support the national approach to the regulation of inset schemes to improve certainty, consistency and efficiency. As we outlined earlier, we would have major concerns if the SA Government re-introduced its own requirements through additional regulation, guidelines or an industry code of conduct. If there was merit in making proposed changes, we strongly these would best be considered under the AER framework.

2.2 Methodology employed by inset operators to determine pricing of electricity delivered through their inset network.

As noted in the previous section, the methodology employed by our members to determine pricing is consistent with ESCOSA and AER guidelines, and each member does to independently and without consultation without other members.

2.3 Ability for inset customers to purchase electricity from providers other than the operator of the inset network.

The SA Government introduced changes to inset schemes with the introduction of 'full retail contestability' for small electricity customers on 1 January 2003. As outlined in ESCOSA's guidelines, inset customers who entered into a lease after 1 January 2003, or where the premises commenced construction on or after 1 October 2000, have been able to purchase electricity from their electricity provider of choice.

Most of our member's retail tenants – particularly specialty tenants - entered into leases after 1 January 2003. They therefore have access to their electricity provider of choice. It is our member's experience that most retail tenants have chosen to remain as customers within inset schemes, and there are few complaints or disputes. The AER has noted that based on the time that has passed since 1 January 2003, the inability for a retail tenant to access their electricity provider of choice "is unlikely to apply to many customers today".

In a practical sense, if a retailer wants to access their retailer of choice, the following steps are followed:

- The tenant approaches centre management and informs them in writing that they want to leave the inset scheme.
- The tenant arranges for a child National Metering Identifier (NMI) to be installed, and enters the market to purchase electricity from their provider of choice (e.g. AGL, Origin Energy).
- The owner enables the installation of a child NMI.
- The tenant's usage is then deducted from the property owner's electricity account.
- The tenant is billed their raw energy from the retailer and is billed a separate ESCOSA shadow network tariff from the property owner.

Some of our members include information relating to the provision of electricity within inset schemes as part of their disclosure statement and information to prospective retail tenants. This includes an information sheet which provides a summary of inset schemes and a retail tenant's right to access an electricity provider of choice which is either one of the local area electricity providers (e.g. AGL, Origin Energy, ERM) or the inset scheme operator (e.g. the shopping centre owner or manager).

RECOMMENDATIONS

4. **The Commissioner acknowledges that pricing arrangements have, and continue to be, largely set by government regulation.**
5. **The Commissioner acknowledges that small electricity customers have been able to access their electricity provider of choice where they have entered a retail lease since 1 January 2003.**
6. **That the Commissioner acknowledges the disclosure of information about inset schemes to prospective retail tenants.**
7. **That the Commissioner recommends the continuation of the AER framework for the regulation of inset schemes in South Australia.**

3. Other issues

As noted in a previous section, government and council imposed statutory charges have a much more significant impact than electricity costs. By way of example, for neighbourhood shopping centres, the industry benchmark cost for local council rates is $18.42/m2 of Gross Lettable Area of Retail (GLAR), while land tax is $16.96/m2. Water and sewerage rates are $8.16/m2. A comparison of these costs with the electricity cost benchmark of $5.39/m2 highlights that the lowest statutory charge is 50% higher than the cost of electricity and land tax and council rates are more than 200% higher. It is therefore difficult to understand why the Government has singled out electricity costs to be the subject of an Inquiry. We would urge the Commissioner to investigate these statutory taxes and charges; particularly given they are provided by monopoly providers and have no equivalent 'price protections' in place for businesses. We recently addressed some of these issues in our submission to the SA Parliament's *Economic and Finance Committee's Tax Inquiry* which is available on the Committee's website.

RECOMMENDATIONS

8. The Commissioner immediately investigates the impacts of government and council imposed taxes and charges on shopping centre owners and their retail tenants.

4. Contacts

The Shopping Centre Council of Australia represents Australia's major owners, managers and developers of shopping centres.

Our members have ownership interests in 15 shopping centres and independent management of an additional 40 shopping centres in South Australia. These companies include AMP Capital Investors, Charter Hall Retail REIT, Colonial First State Global Asset Management, DEXUS, Federation Centres (formerly Centro Retail Australia), ISPT, Lend Lease, Precision Group, Savills, Westfield Group and the Westfield Retail Trust. These shopping centres incorporate around 100 major retailers and 2,000 specialty retailers.

Contacts

The Shopping Centre Council would be happy to discuss any aspect of this submission. Please do not hesitate to contact:

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ATTACHMENT 1: SOUTH AUSTRALIAN SHOPPING CENTRES UNDER SCCA MEMBER OWNERSHIP

- Centro Hilton
- Centro Kurralta
- Centro Arndale
- Centro Mount Gambier
- Centro Colonnades
- Wharflands Plaza
- Myer Centre
- Castle Plaza Shopping Centre
- Elizabeth Shopping Centre
- Southgate Plaza
- Adelaide Central Plaza
- Port Canal Shopping Centre
- Westfield Marion
- Westfield West Lakes
- Westfield Trea Tree Plaza