1/30/2015

Submission to the

South Australian Power Networks Proposal 2015 – 2020

Prepared by the

South Australian Financial Counsellors Association in collaboration with twenty agencies that employ Financial Counsellors in SA

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SAFCA Submission to the Australian Energy Regulator

SAPN Proposal 2015 – 2020

Introduction

The South Australian Financial Counsellors Association has collaborated with some twenty agencies that employ financial counsellors and other stakeholder bodies in this state to prepare a submission to the Australian Energy Regulator (AER). This submission states and gives evidence for our position that there should be no increase to the South Australian Power Networks (SAPN) revenue as they propose. Instead, significant reductions should be pursued. This consortium includes some of the State's largest employers, who operate across a diversity of service areas.

SAFCA and its consortium agencies submit to the AER that thousands of South Australian households are in financial distress and do not have the capacity to pay their energy bills. In our view, the SAPN 2015-20 Regulatory Proposal provides a level of service that is unaffordable and, in the absence of changes to the South Australian Electricity Concession arrangements, must be pared back to a more prudent proposal that can be afforded by the *whole* community.

The SAFCA consortium's view is that the cost of electricity distribution in South Australia must return to levels that existed during the 2005-10 Regulatory Period and prior to the effects of the Global Financial Crisis (GFC).

South Australian households have endured steep electricity price increases during the current 5-year regulatory period that have not been matched by increases in the community's capacity to pay. As will be shown in this submission, SA has some of the National Electricity Market's least affordable electricity and, as a result, has above average levels of debt and disconnections. Financial counsellors support many thousands of households each year to manage their energy bill debts and are of the view that prices should be falling to reflect the fact that SAPN's costs have also reduced.

This submission provides comment on key financial parameters of the SAPN proposal and gives evidence to support the consortium position that the cost to consumers of electricity distribution in SA is too high and should be reduced.

The Role of Financial Counsellors

Financial counsellors provide information, support and advocacy for people in financial difficulty. They offer their services free of charge to their clients and provide impartial advice. Financial counsellors are at the coal face working with people in financial distress.

Financial counsellors play an integral role in negotiating hardship program applications for clients. It is common for clients to have attempted this themselves and to contact a financial counsellor only after they were unable to negotiate reasonable and sustainable payment plans. Financial counsellors are also the "gatekeepers" for the state's Energy Electricity Payment Scheme (EEPS), processing around 1000 applications each year[1].

SAFCA Member Survey

SAFCA surveyed the collaborating agencies as part of preparing this submission. The survey responses reflect the provision of case management/financial counselling assistance to over 14,000 clients in 2013-14. A similar number, around 15,000, are also provided with self-help information via the Helpline (1800 007 007). The survey responses indicate that around 60% of clients (approx. 9,000) assisted by a financial counsellor in 2013-14 had a debt with an energy company[2].

SAFCA Survey results

- Number of clients surveyed; 14,000
- Number with Utility debt: 10,500
- Number with electricity debt: 8,680
- % with utility debt: 75%
- % with electricity debt: 62%

Compared to the scale of debt and hardship shown below in Figure 1 below, the scale of financial counselling activities is very significant; thousands of households each year that get caught up in debt and face disconnection from their electricity supply are supported by financial counsellors.

The SAFCA consortium is therefore very well positioned to provide some insights into *capacity to pay* for energy from the household budget that may not align with what SAPN have assessed as the community's *willingness to* pay (WTP) in the 2015-20 Regulatory Proposal.

Case Study: The Role of Financial Counsellors

Sam and his wife presented to Emergency Relief Services requesting help with budgeting. Sam stated that he was being harassed by 2 separate energy providers looking for 2 separate payment amounts and he could not afford to pay either bill. Sam was referred to a financial counsellor who was able to contact both energy providers and clarify which energy provider Sam was currently connected to and organised for relevant concessions to be applied to his account.

The financial counsellor completed an income and expenditure statement and discussed Sam's current energy usage. The financial counsellor organised for Sam to be placed on the hardship programme with fortnightly payments of $120 to cover current usage. Payment deductions were organised through CentrePay. The financial counsellor was able to ascertain that the other energy provider who was chasing Sam had passed the debt on to a debt collector. The financial counsellor obtained relevant documentation from the debt collector and negotiated fortnightly payments of $20 to an agreed amount to satisfy the debt.

[1] From the DCSI Annual Report 2012-13 *"Support is also provided through the **Emergency Electricity Payment Scheme** which provides a one-off payment of up to $400 to eligible South Australians. During 2012-13, the scheme received 1084 applications, resulting in 849 payments being granted."*

[2] Respondents include Uniting Communities, AnglicareSA and Salvation Army. Approximately 3 in every 4 people had a Utility Debt of some sort and 62% reported an energy debt.

Energy and Hardship in South Australia

South Australian households are afforded energy specific consumer protections as part of the National Energy Customer Framework (NECF). The NECF requires energy retailers to operate an approved Hardship Program where households are protected from disconnection if they meet the requirements of a repayment plan. As at the end of June 2014, around 8,000 South Australian households were participating in a retailer's electricity hardship program.

The Australian Energy Regulator (AER) reported that in 2013-14, residential energy customers owed $30m to energy businesses. At any one time, 38,000 electricity customers owed approximately $25m – around $650 each[3]. As shown in Figure 1, across the four quarters of 2013-14, about 80% of these were engaged in some sort of repayment plan (20% were participating in a retailer hardship program, 60% in an arrangement outside of the hardship provisions).

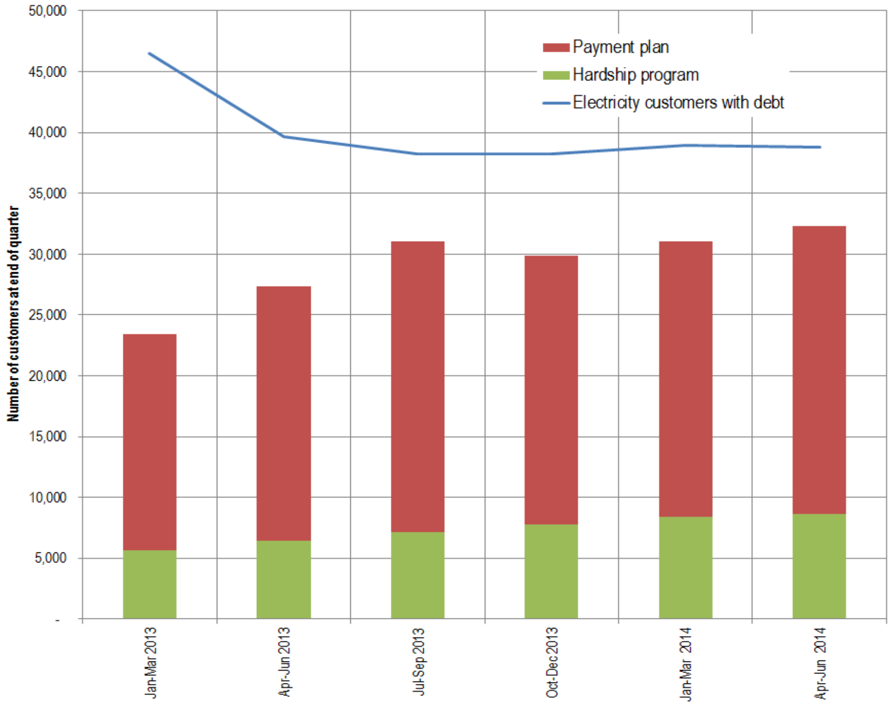


Figure 1: Numbers of SA households with electricity debts and repayment arrangements (2013-14) Source: AER

Figure 1 also illustrates two key trends since the commencement of the National Energy Customer Framework in SA (January 2013):

- The number of households engaged in retailer hardship programs has been increasing. This is likely due to increased awareness and accessibility rather than any increase in underlying demand – illustrated by the slowing rate of increase (and heading for around 10,000 customers per annum)

[3] The AER also reports 15-20,000 gas customers with a combined debt of around $5m in 2013-14. It is understood that there is some overlap between these counts – i.e. some customers may appear in both the electricity total and the gas total so combining the two totals would overstate the number of customers in debt.

- The total number of households (approx. 38,000) and the total amount of money owed (approx. $25m) appears to be relatively stable across the four quarters of 2013-14 – suggesting that arrangements under the NECF have 'stabilised' and that the figures are representative of a continuing systemic problem.

> **Case Study: Hardship**
>
> Bill has work history but over last 12 months has been unable to secure full-time work – currently in receipt of Newstart Allowance (sickness) and suffering some mental health issues. He has cut back on expenses as far as possible but his electricity bill has continued to escalate. Disconnection was imminent but Ombudsman intervened – now on 'last chance' from electricity supplier. Account is in excess of $2,000 therefore Emergency Electricity Payment Scheme not available to him. He has found it necessary to seek emergency food assistance.
>
> The financial counsellor contacted the electricity provider and established Bill's power usage. In order to meet ongoing supply cost and pay something towards outstanding debt Bill was asked to pay $140 per fortnight which is unaffordable. Made temporary hardship arrangement for $100pf. Longer term, unless Bill is able to find work, unfortunately he will still be in serious financial difficulties and at risk of having electricity supply cut.

How does SA compare with other jurisdictions?

In order to demonstrate that South Australian households have reached or exceeded their capacity to pay, the following illustrates how we compare to other NEM jurisdictions. We acknowledge that debt and disconnection is present in all jurisdictions but wish to highlight the relatively high levels of hardship in SA. According to the AER[4]:

> *"South Australia has an above average number of customers on payment plans with a high level of debt"*

South Australia also has the **highest disconnection rate** among those reporting to the AER under the NECF and second only to Victoria across all states as shown in the following table from the Victorian Essential Services Commission[5].

[4] AER Board Member Jim Cox contained in AER media release 25 Nov 2014 "AER Retail Market Performance and Affordability Report - South Australia highlights" available from www.aer.gov.au/node/28525

[5] Source: AER Retail Performance Data and Essential Services Commission 2014, *Energy Retailers Comparative Performance Report – Customer Service, 2013-14*, December 2014

TABLE 4.2 DISCONNECTIONS, BY JURISDICTION — RESIDENTIAL ELECTRICITY
Per 100 customers, 2009-10 to 2013-14

Jurisdiction	2009-10	2010-11	2011-12	2012-13	2013-14
Victoria	0.59	0.77	1.02	1.07	1.47
New South Wales	0.60	0.61	0.80	0.83	1.03
ACT	0.56	0.26	na	0.05	0.17
South Australia	0.66	1.01	1.35	1.50	1.37
Queensland	0.90	1.22	1.16	0.94[a]	1.31[a]
Tasmania	0.59	0.51	0.08	0.46	0.68
Western Australia	0.39	0.90	0.87	0.72	0.97

[a] The Department of Energy and Water Supply calculated this ratio, based on information published by the Queensland Competition Authority. Queensland data may be marginally higher than reported, because the small market customer numbers include both small residential and small business customers.

na – Not available.

Data sources: Independent Pricing and Regulatory Tribunal (NSW) (IPART), Essential Services Commission of South Australia (ESCOSA), Economic Regulation Authority (WA) (ERA), Department of Energy and Water Supply (Qld) (DEWS), Australian Energy Regulator (AER).

Figure 2: Residential Electricity Disconnection Rates in Australia (2009-10 to 2013-14) Source: ESCV

South Australian households also endure some of the nation's highest electricity and gas prices[6]:

Figure 3.2: Annual electricity and gas bills (6500 kWh and 24 000 MJ pa), June 2013 and 2014

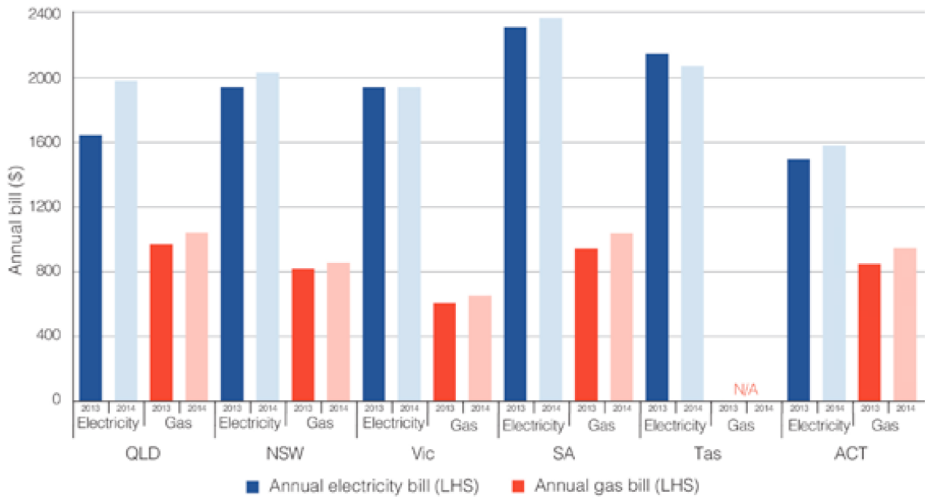


Figure 3 Comparative Annual electricity and gas bills for the same level of consumption in each jurisdiction (June 2013 and June 2014) Source: AER

The AER State of the Energy Market Report 2014 shows that, after Tasmania, South Australians have the least affordable electricity in the national market[7]:

[6] Source: AER Annual Report on the Performance of the Retail Energy Market 2013-14 page 40
[7] Source: AER SOEM 2014 figure 5.6

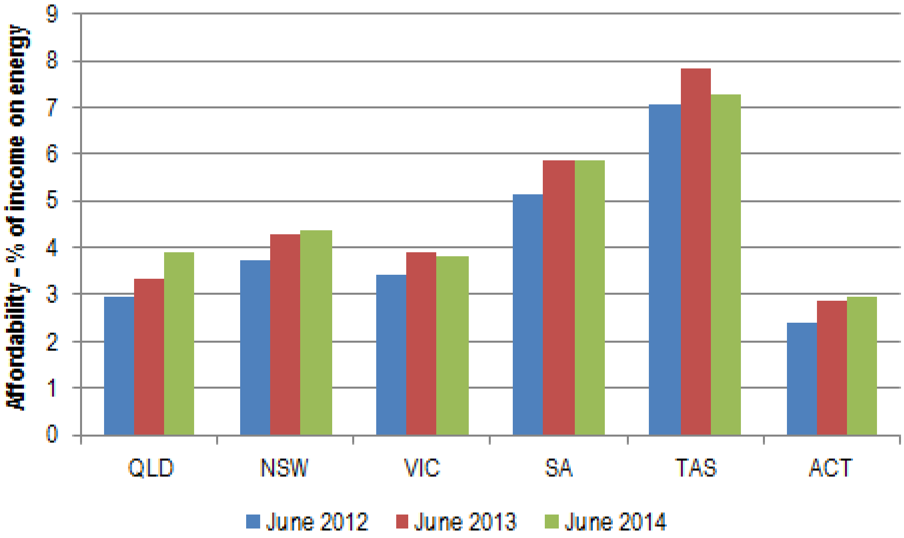


Figure 4: Affordability expressed as % of disposable income spent on dwelling energy (June 2012, 13, 14) Source: AER

The AER State of the Energy Market Report 2014 also shows how the Adelaide retail electricity price index has increased 85% above inflation since the start of the National Electricity Market in 1998[8]. The majority of this increase though has been since June 2010 - the start of the current SAPN regulatory period. The SAFCA consortium is well aware that distribution charges are only one part of these prices rises. However the intent is not to allocate blame but to highlight the context of rapid price rises that present genuine challenges to many in the community – especially those clients of SAFCA members.

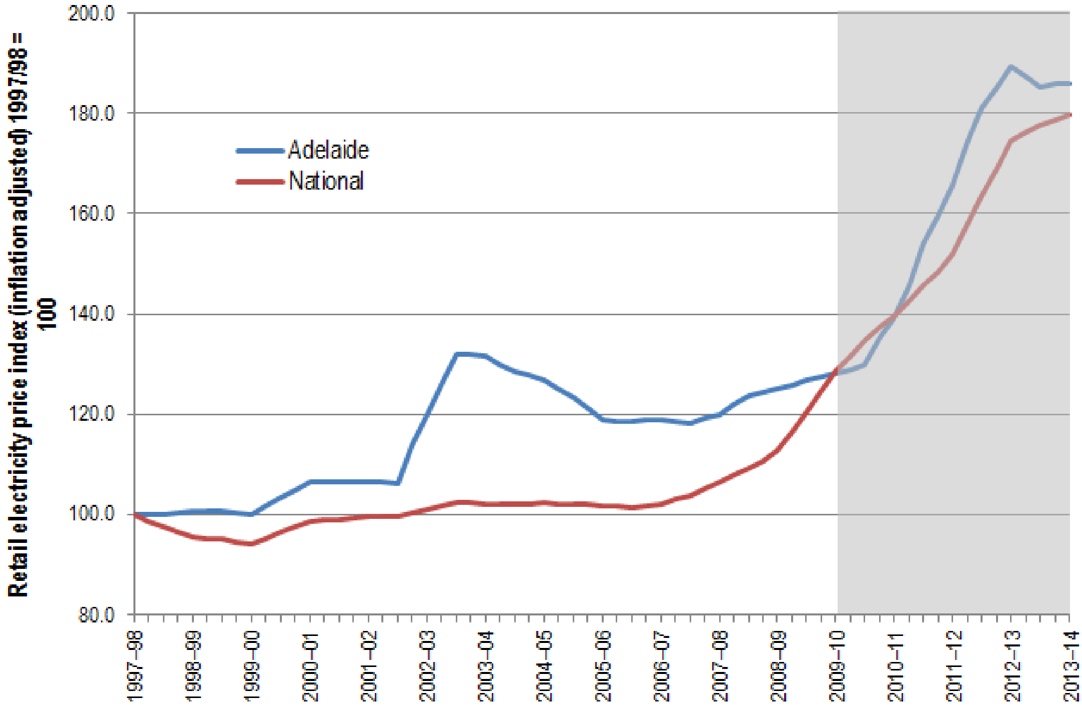


Figure 5: Retail electricity price index (inflation adjusted) Adelaide and Australia 1997/98=100 Source: AER based on ABS

[8] Source: AER SOEM 2014 figure 5.4

In summary, South Australian households have endured steep electricity price increases during the current 5-year regulatory period that have not been matched by increases in the community's capacity to pay. SA has some of the NEM's least affordable electricity and, as a result, has above levels of debt and disconnections. Financial counsellors support many thousands of households each year to manage their energy bill debts and are of the view that prices should be falling to reflect the fact that SAPN's costs have also reduced.

Case Study: Disconnections

Sandra was disconnected 2 months ago. She called the Telephone Financial Counselling for help to get reconnected and to gain assistance to pay fines she had received over the past 2 months from the police for starting fires in the back garden. Sandra lived in suburb of Elizabeth and was making fires in the back garden to do her cooking. She did not know that she was not allowed to make a fire in the back garden initially, but when faced with the option of a fine or cooking to feed her children she choose to feed her kids. The repetitive police attendance to her home was the catalyst for Sandra's contact for help.

Sandra has gone to extraordinary lengths to remove the necessity of gas or electricity. Sandra explains how she puts her washing in a barrel of water with soap and rolls it up and down the road outside her house to wash her clothes. Sandra has implemented many other drastic money saving initiatives to reduce her energy consumption. Sandra's electricity bill was $385. Sandra received help with an Emergency Electricity Payment to get reconnected to her energy provider and was put on a fortnightly payment plan to reduce the risk of further disconnection.

The National Electricity Objective

The AER has stated that it would like to hear views on how the National Electricity Objective (NEO) is best reflected in their determination[9]. In relation to electricity distribution, the NEO can be paraphrased as; *promoting efficient investment in, and efficient operation and use of electricity* [distribution] *services for the long term interests of consumers with respect to price, quality, safety, reliability and security of supply*.

SAPN's record in terms of quality, safety, reliability and security of supply is impressive and there is little doubt that SAPN is a well-run, efficient business. However, the element that we wish to challenge is that of *price*. In our view, the long term interests of consumers mean a strong focus must be placed on what constitutes *prudent* expenditure and not just what can be argued as *efficient* expenditure. The National Electricity Rules require that only the expenditure needs of a *prudent operator* can be approved[10] and *prudence* is a requirement of the AER Better Regulation Guideline "*Expenditure Forecast Assessment Guideline for Electricity Distribution (November 2013)*".

In summary, we believe that the NEO will be best reflected in the AER's Determination by emphasising *prudence* as well as efficiency.

[9] AER Issues Paper p38
[10] NER clauses 6.5.6(c), 6.5.7(c)

Comments on Key Financial Aspects of the SAPN Proposal

Context

The SAFCA consortium notes that this regulatory proposal is being presented based on the previous regulatory period 2010-2015 which was established at a time of substantial uncertainty in global financial markets, in part as a result of the Global Financial Crisis. At this time capital was expensive and in limited supply and the AER responded to SAPN and other network business requests for significantly higher financing allowances than for the previous period.

The perceived impact of the GFC on the cost of capital was the key driver in SAPN receiving a much greater revenue allowance in this current regulatory period (2010-2015) than it earned in the 2005-2010 period. SAPN have acknowledged that the cost of capital is now lower but instead of a reduction in revenue, is proposing an expansive expenditure program that will offset the lower costs of capital and, in effect, hold revenues and prices relatively constant in real terms over the 2015-2020 period. In our view there are too many households without the capacity to pay current electricity prices for this to be accepted.

We consequently do not accept that increasing capital expenditure by a half and operating expenditure by a third as proposed is either warranted or prudent.

The SAFCA consortium strongly asserts that the cost of electricity distribution in South Australia should return to levels that existed during the 2005-2010 Regulatory Period and prior to the effects of the Global Financial Crisis (GFC); reducing distribution costs for the typical household from the current $672 by a third to less than $500 pa (Figure 6).

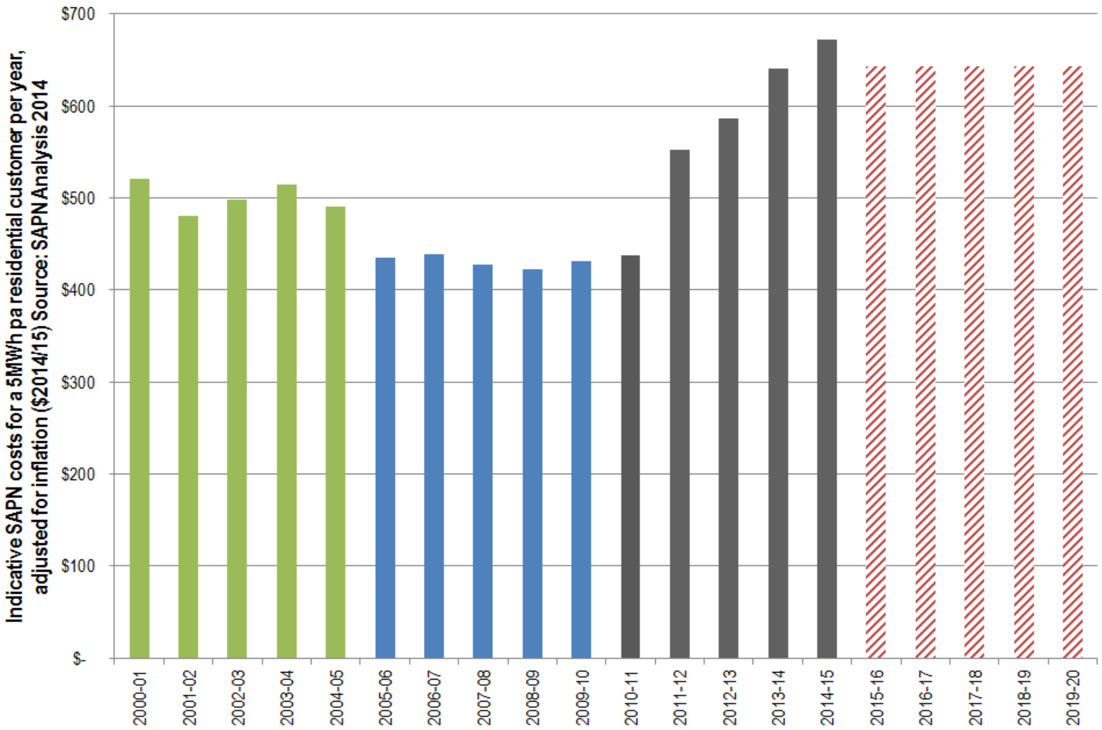


Figure 6: Annual Electricity Distribution costs for a typical 5MWh residential customer since 2000-01 and projected to 2020 ($204/15) Source: SAPN

Some SAFCA members and parties to this submission have been involved with the last two regulatory proposals from South Australian Power Networks / ETSA Utilities and have heard many of the same arguments proposed for 2015-2020 in the past two regulatory proposals. In particular, SAPN / ETSA Utilities has continued to advocate strongly through regulatory proposals that they have an ageing 'fleet' and that substantial upgrading of the network is needed so therefore capital expenditure must go up significantly.

We note that in the last regulatory period where the same arguments for the need for increased replacement expenditure (REPEX) were mounted, SAPN has underspent the allowance from the Regulator. This underspend over the past regulatory period certainly reduces the veracity of the argument this time around. We do not accept that there is a need for greater replacement expenditure over the 2015-20 regulatory period.

Weighted Average Cost of Capital (WACC)

We understand that the most significant factor affecting the prices consumers pay for electricity is the return on investment that is made by the network business to operate the network. Two significant factors in considering the SAPN regulatory proposal are therefore the WACC - weighted average cost of capital and the size of the Regulated Asset Base (RAB). The incentive for network businesses is to maximise their regulated return on capital and to maximise the size of the RAB. SAFCA is convinced that SAPN has overstated the WACC and seeks to increase the size of their RAB beyond reasonable levels. We consider these in turn.

The following key parameters are proposed by SAPN with regards to their rate of return:

Overall WACC	7.62
Return on Equity	10.45
Return on Debt	5.74
Gearing	60%
Equity Beta	0.82 (if using Sharpe Lintner CAPM model; Beta=0.91
Gamma	0.25
Required return on the market portfolio	11.15%
Benchmark credit rating	BBB

We observe that SAPN is seeking return on capital both through equity and debt that are out of kilter with prevailing market conditions and are based much more on trying to lock in the very high rates that were allowed in most recent regulatory period, set in the context of the GFC. However, for the 2015-2020 regulatory period it is clear that capital for safe investment is relatively cheap and certainly much cheaper than it was at the height of the global financial crisis. It is this context that must be understood in considering SAPN proposed rates of return.

The AER Issues paper asks two questions regarding rate of return;

- *Do you consider departures from the rate of return guidelines are justified?*
- *In particular do you have any comments on the departures on the rate of return guideline proposed by SA POWER NETWORKS?*

The SAFCA consortium is aware that there was extensive stakeholder engagement in developing guidelines through the AER Better Regulation Programme through the duration of the 2013 calendar year. Consumers and network business were actively involved with these discussions with, we suggest, the largest number of meetings and greatest attention being given to rate of return. This led to rate of return guidelines being proposed and subsequently accepted by the AER board and published. SAFCA is acutely aware of the active involvement of network businesses in both developing rate of return guidelines and also in considering benchmarking both for category analysis and broader econometric modelling.

We do not consider there is any justification for SAPN, or any other network business, to depart from the rate of return guidelines that were published by the AER December 2013.This rate of return was based on a full calendar year of consultation, debate and active consideration by key stakeholders, including network businesses.

We are also concerned that SAPN has embellished the extent of risk associated with capital raising for a regulated energy business in Australia. We recognise that these are very safe businesses with a regulated return on a protected asset base which provides great certainty for investors, particularly at a time when global interest rates are exceedingly low.

Currently American official interest rates are 0.25% (confirmed at meeting of US Fed, 17th December 2014) European interest rates are 0.05%, UK Interest rate is 0.5% and Japanese official interest rates are 0.0%[11]. These very low interest rates mean that global capital is readily available and cheap. SAPN is a safe business with reliable regulated returns that would have easy access to cheap global capital. Their prudent, rolling capital raising will be at very low rates, benefits of which must be passed through to consumers who have borne the burden of high interest rates in the past.

Consequently, it is unreasonable for SAPN to be proposing a return of 11.15% and to be proposing a BBB basis of risk for their financing. Similarly, their Beta proposals, whether for their own model where they propose Beta of 0.82 or a Beta of 0.91, applied to the Sharpe Lintner CAPM model, are simply way of out of kilter with current realities. We believe that a Beta of the order of 0.55 is much more in line with regulator sentiment in other jurisdictions internationally and with prevailing market conditions.

The AER's most recent paper[12] considering estimate for beta states "During both the 2009 WACC review and now we considered the empirical estimates support a range of 0.4 to 0.7. In the 2009 WACC review, we adopted a point estimate of 0.8 (slightly above the range of empirical estimates). In this issues paper, we propose to lower our point estimate from 0.8 to 0.7 because we now have greater confidence in the reliability of the empirical estimates" We argue that the midpoint of the range 0.4 – 0.7, namely 0.55 is a better point estimate for equity beta.

We regard the proposal from SAPN that their required return on the market portfolio should be 11.15% as being substantially higher than prevailing financial conditions would suggest as prudent. We can assure SAPN that any money that is held by SAFCA consortium clients in their bank accounts is not returning 11.15%.

[11] http://www.tradingeconomics.com/united-states/interest-rate
[12] AER: Better Regulation Equity beta issues paper October 2013

Figure 7 shows the nominal WACC for a comparable regulatory environment, the Uniting Kingdom and then shows the comparable WACC for both the AER's recent NSW / ACT draft determinations and for the SAPN proposal. The SAPN proposed WACC is considerably higher than for the UK and is also meaningfully higher than the AER's draft determination for NSW and ACT, which may yet be shown to be higher than necessary.

Returns on both equity (10.45) and debt (5.74) are also considerably higher than overseas regulatory decisions for comparable businesses and higher than low risk businesses in Australia are likely to be expecting. Similarly, the SAPN proposed benchmarking credit rating of BBB, fails to adequately recognise the low risk for capital raising for a business with a guaranteed, ie regulated income.

SAFCA urges the AER to revise the proposed WACC to a significantly lower level, more in keeping with prevailing financial conditions.

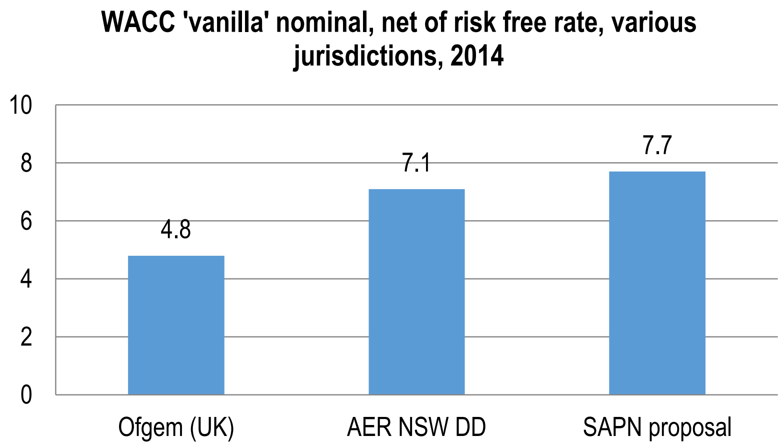


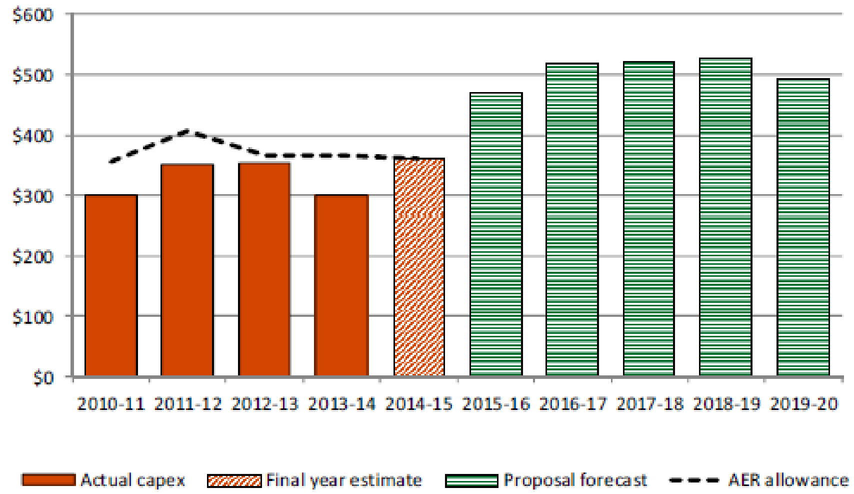
Figure 7: WACC 'vanilla' nominal (adjusted to a common risk free rate) Source: Consumer Challenge Panel, Bruce Mountain presentation, AER Forum 10/12/14[13]

Capital Expenditure Program (Capex)

Despite spending less than was approved for the current regulatory period, SAPN is proposing a drastic increase in capital expenditure as illustrated below. This is at a time of declining electricity demand in South Australian markets, so a surge in expenditure is a situation we regard as completely unreasonable.

[13] SAPN proposal restated to be consistent with AER Risk Free Rate in NSW Draft Decision of 3.55%, compared with 5.74 return on debt from SAPN proposal, used in table 1

Figure 2 **Capital expenditure ($million, 2014–15)**



Source: AER capex allowance is drawn from the PTRM determined by the AER for the 2010–15 period as varied by the Australian Competition Tribunal (the Tribunal). Actual capex is drawn from SA Power Networks' submitted RFM. Proposed capex is drawn from SA Power Networks' submitted PTRM.

Figure 8: SAPN current and proposed Capital Expenditure programs. Source: AER Issues Paper Figure 2

This expenditure program would significantly increase the size of the regulatory asset base (RAB) and lock in future prices which would be unnecessarily high and completely unsustainable should the cost of capital return to GFC levels (for higher risk financing). This seems particularly inappropriate and imprudent given SAPN's own assessment of the future need for electricity distribution:

> [Regulatory Proposal p51] *"There is little doubt that the confluence of customer, technological, market, economic and regulatory changes now underway will drive a period of change in the distribution sector that is unprecedented."*
>
> *[p 231] "The 2015–20 RCP will be a period that will see the most significant and transformative change in the distribution sector since the establishment of the NEM."*
>
> [p306] *"… the risk of electricity network businesses has changed dramatically in the very recent past… Essentially our business is confronted with two possible future scenarios, one in which we evolve and survive and the other in which our network progressively becomes redundant."*
>
> [p307] *"… it calls into question whether customer disconnections from the grid might be significant enough to put at risk the viability of the whole regulated price recovery system."*

In our view, and particularly against the uncertainty outlined above, the long term interest of consumers is most likely to be met by more prudent expenditure proposals.

SAPN used its relatively modest real RAB growth from 2005 to 2013 as evidence of its "prudent investment in our network" (see figure 4.7 below at page 42 of the RP). However, the proposed capital expenditure program would increase the value of the RAB by around 47%[14] (approximately 30% in real

[14] AER Issues Paper p 16

terms) see figure 9 below. The proposed capital expenditure for 2015-20 totals nearly $2.5 billion over 5 years[15] and represents an increase of around 50% on the 2010-15 regulatory period[16].

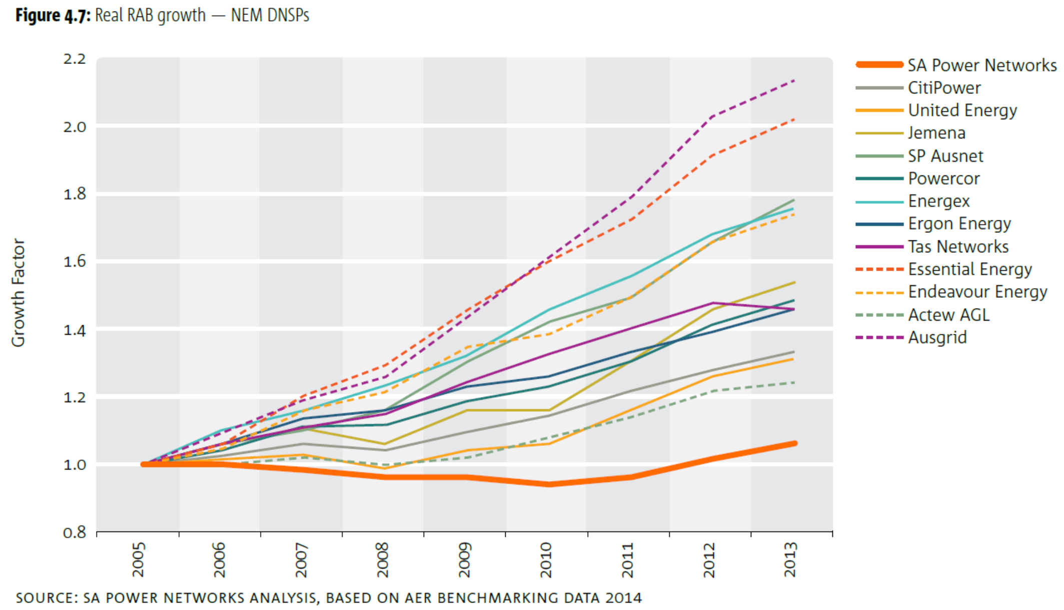


Figure 8: SAPN Analysis of the real growth in the RAB of Electricity Distributors in the National Electricity Market. Source: SAPN RP Figure 4.7

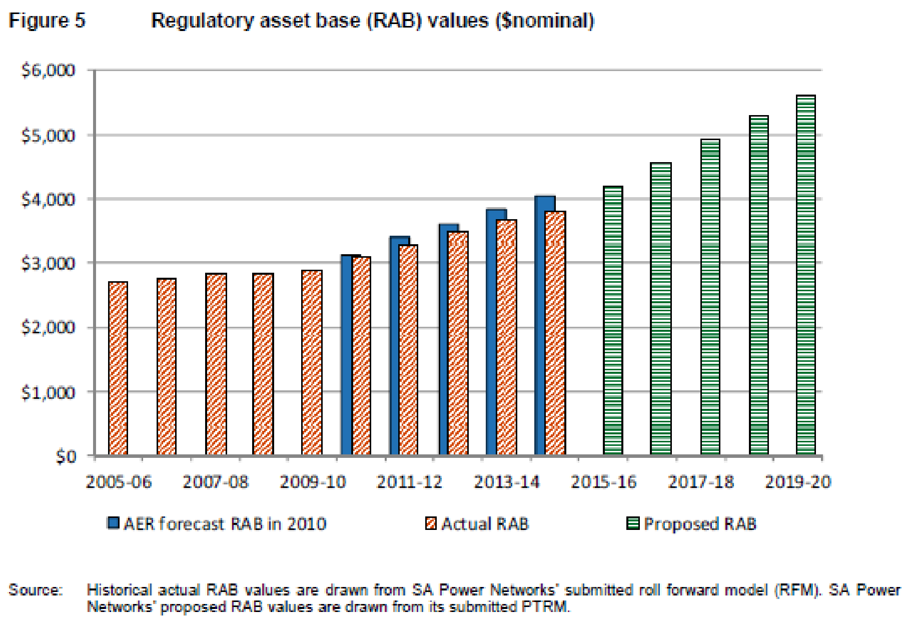


Figure 9: SAPN historic and proposed Regulatory Asset Base. Source: AER Issues Paper Figure 5

We are very concerned that the substantial increase in RAB proposed, 47% over the 5 years to 2020 and 97% over the decade sets up a very high opening RAB for the 2020-25 regulatory period, which cannot be in the long term interests of consumers.

[15] Regulatory Proposal Table 20.4 p 179
[16] AER Issues Paper p 11

In summary, the SAFCA consortium does not accept that such a dramatic increase in the Capex can be considered to be how a prudent operator should respond to such an uncertain future. The National Electricity Rules require that only the expenditure needs of a *prudent operator* can be approved[17] and *prudence* is a requirement of the AER Better Regulation Guideline "*Expenditure Forecast Assessment Guideline for Electricity Distribution (November 2013)*". On this basis, the AER should reject the proposal as not meeting the expenditure criteria.

Operating Expenditure Program (Opex)

The following figure 11 is taken from the AER discussion paper and clearly shows the substantial increase in Opex that SAPN is seeking in its 2015-20 proposal.

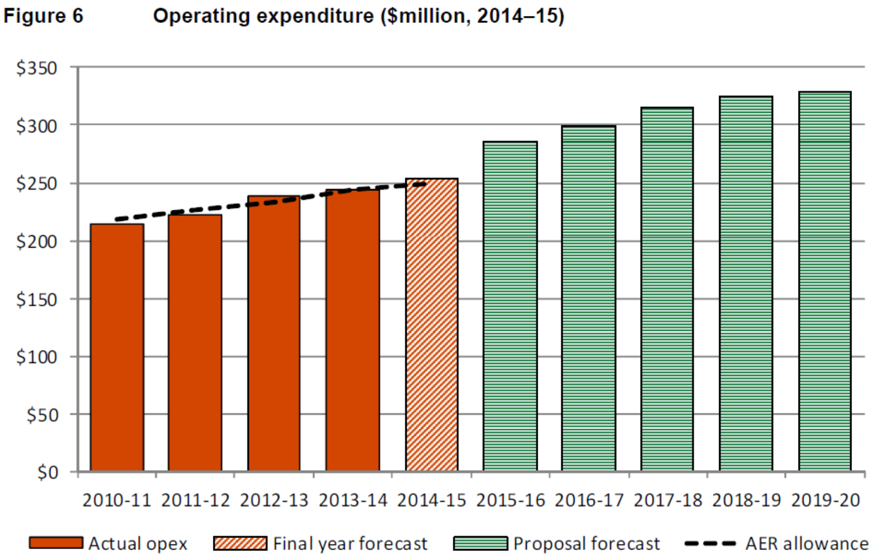


Figure 11: SAPN current and proposed Operating Expenditure. Source: AER Issues Paper Figure 6

SAFCA sees no reason for an increase in operating expenditure over the duration this regulatory period, given that demand is falling, that SAPN is a long established business, and that newer technologies should be increasing efficiency of operation rather decreasing efficiency.

We also note that in a period of declining demand, SAPN is seeking to increase both Capex and Opex over the life of this regulatory period, so there is not even a trade - off between and Capex and Opex which would be expected. If Capex were to increase then it would be expected that operating costs would diminish or if there was a reduction in capital expenditure, then there might be some argument for operating costs increasing. However, for SAPN to propose increases of substantial amounts over the next 5 years is simply unreasonable.

We note that considerable costs are being allocated to vegetation management. Whilst we certainly recognise the importance of vegetation management, and of responding to realistic risk of bush fires, we do not see evidence to support the level of expenditure for vegetation management that is included in SAPN's proposal.

[17] NER clauses 6.5.6(c), 6.5.7(c)

Profit

Chapter 17 of the SAPN Proposal is titled 'Service-price trade-off' and discusses the 'regulatory bargain' that seeks to balance the objectives of consumers and the interests of SAPN. The aim being "… *a **reasonable commercial return** in providing services to customers at an agreed standard*" (p157, emphasis added). We accept the need for a reasonable return.

Information presented by Consumer Challenge Panel member Mr Bruce Mountain on the profitability of SAPN compared to its sister company in the UK[18] (and the financial statements of SAPN published by 49% owners Spark Infrastructure) [19] suggest that SAPN's profitability may be well beyond our notion of a "reasonable commercial return".

While we accept that the levels of profit may be regarded by the AER as an indicator of relative efficiency of a business compared to the benchmark, in our view, if a business is returning substantially higher profits than is regarded as reasonable elsewhere then there is no doubt in our mind that customers are paying too much and economic efficiency has been harmed. We strongly urge the AER to have regard to profit levels of SAPN in the context of their efficiency, and in particular, its proposed income tax for 2015-20 now almost three times as much as AER allowed for the current period.

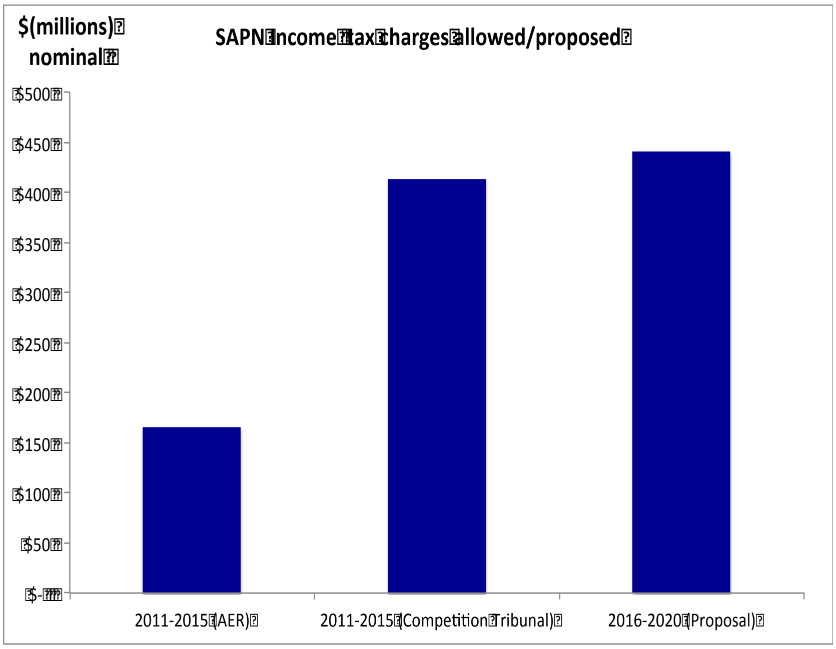


Figure 12: SAPN Income Tax Allowance, current and proposed Source: Consumer Challenge Panel, Bruce Mountain presentation, AER Forum 10/12/14

For 2011 to 2013 financial years inclusive, SAPN financial statements show that it has received tax credits of $4.2m, yet it is unclear how much tax SAPN are paying, indeed if they are paying any tax in Australia at all. Transparency is very important in assessing SAPN claims and consumers have a right to understand if there is a difference between the hundreds of millions provided to SAPN for tax

[18] In 2012 UK Power Networks (majority owned by CKI), also a regulated electricity network business achieved profit before interest and taxes of £711m for delivering electricity to about 8 million entities, a cost per connection of $161 per connection. In 2012/13 SA Power Networks achieved a profit of about $710 per connection. This suggests a profit rate for SAPN of about 4 times its UK sibling. Source: Consumer Challenge Panel, Bruce Mountain presentation, AER Forum 10/12/14

[19] http://sparkinfrastructure.com/investor/reports/fact-books reports calendar year results for SAPN for 2013 and 2012 that report Underlying Profit after Tax of over $360m on turnover (75% regulated) of just over $1,100m in each year.

liabilities and the tax actually paid. If SAPN is paying significantly less tax than AER expected in the past regulatory period, then the 2015-20 determination must deal with this. High profits, indeed higher than profits of comparable businesses elsewhere, do not indicate a company acting in the best interests of consumers, particularly with regard to prices that customers have to pay.

SUMMARY

In summary, the SAFCA Consortium's position is that:

- the cost to consumers of electricity distribution in SA is too high and should be reduced;
- thousands of South Australian households are in financial distress and do not have the capacity to pay their energy bills. In our view, the SAPN 2015-20 Regulatory Proposal provides a level of service that is unaffordable and must be pared back to a more prudent proposal that can be afforded by the *whole* community;
- thousands of households each year that get caught up in debt and face disconnection from their electricity supply. South Australia also has the highest disconnection rate among those reporting to the AER under the NECF and second only to Victoria across all states;
- the National Electricity Objective (NEO) will be best reflected in the AER's Determination by emphasising *prudence* as well as efficiency;
- the cost of electricity distribution in South Australia must return to levels that existed during the 2005-2010 Regulatory Period and prior to the effects of the Global Financial Crisis (GFC);
- we urge the AER to revise the proposed WACC to a significantly lower level, more in keeping with prevailing financial conditions;
- we do not accept that such a dramatic increase in the capital expenditure can be considered to be how a prudent operator should respond to such an uncertain future;
- we see no reason for an increase in operating expenditure over the duration this regulatory period, given that demand is falling, that SAPN is a long established business, and that newer technologies should be increasing efficiency of operation rather decreasing efficiency;
- high profits, indeed higher than profits of comparable businesses elsewhere, do not indicate a company acting in the best interests of consumers, particularly with regard to prices that customers have to pay;
- SAPN's profitability may be well beyond our notion of a "reasonable commercial return".

The SAFCA Consortium thanks the Australian Energy Regulator for the opportunity to comment of SA Power Network's proposal and trusts that this representation on behalf of the South Australian's who are struggling with high electricity prices will be considered. Please find additional case studies in Appendix 1 that further illustrate the plight of our clients.

Appendix 1 Further Case Studies

1. Ahmadi – a married father of three who did not speak English attended a financial counselling appointment with a financial counsellor. Through the use of a translator the financial counsellor was able to support Ahmadi with his financial issues, which were mainly due to his electricity account.

   Ahmadi and his family had lived at their property for a number of years with the same utility company. As bills would come in he would pay the amount that was said to be owed without question and without checking the details due to his lack of English.

   Prior to Ahmadi making contact with the service, he had received an electricity bill in his wife's name rather than his own. Ahmadi tried to contact the utility company to ask why they had received a bill in his wife's name when previously all accounts had been in his name and neither Ahmadi nor his wife had asked for it to be changed. No explanation was provided and due to the language barrier nothing was resolved. When Ahmadi attended his appointment it was identified that the family had actually received a number of bills for the same quarter but different amounts and different account numbers and names.

   The financial counsellor made contact with the utility company who they said that they have not done anything wrong and all the bills were correct. They also demanded an outstanding amount to be paid as Ahmadi had switched providers due to the issues he had been experiencing and therefore had a debt.

   The financial counsellor placed a complaint with the Ombudsman. After lengthy investigation the accounts that had been paid twice were traced down and transferred all into one account. A record of this was sent to the financial counsellor to explain to Ahmadi. During this time the outstanding amount was sent to a debt collector while investigations were taking place with the utility company. The financial counsellor contacted the debt collector and asked for a hold until a resolution was reached. Eventually the correct amount owing was identified and Ahmadi agreed to pay it on a reasonable payment plan per fortnight.

2. Amber, a sole parent, is a 32 year old mother of three young children. She does not work and her income comprises of Centrelink's Parenting Payment Single and Family Tax Benefit A&B and Child Support. She suffers from mental health issues. She lives in Mount Gambier and struggles to maintain her mortgage repayments and other living expenses.

   Amber attended a financial counselling service as she had a number of debts, including arrears of $1700 in a payment plan with her electricity provider.

   The financial counsellor liaised with the electricity provider and arranged a payment plan of $110 per fortnight which addressed Amber's electricity usage. The financial counsellor applied for and Amber was granted an EEPS payment of $400 which was applied directly to the electricity account.

   Throughout all negotiations, the provider was extremely good to deal with via an appointed account manager. Amber undertook to make a lump sum payment of $500 when she received her Family Tax Benefit reconciliation payment in July 2013. The electricity provider matched Amber's payment of $500.

   With the payment plan in place, the $400 EEPS payment, Amber's $500 and the provider's matching $500 payment, in July2013 the debt was paid in full.

3. Jane is a 45 year old woman who is the sole income provider for her family. She is married and has 2 children both aged 11. Her husband has mental health issues that have prevented him from working since 2003. She came to see a financial counsellor for advice on her family's budget.

   Jane earns 65,000 per year. She has a mortgage of $1500 per month and she budgets for every expense throughout the year and uses a spreadsheet to record her spending to ensure she stays on track. Jane sees herself as fortunate to be purchasing her own house as she has watched the rents of the houses next door to her increase from $210 per week to $385 per week over the last few years. One house recently rented for $410 per week she exclaims!

   Jane reports the cost of living has gone up so much over the last 5 years that she has gone from paying bills when they arrived to having a budget and making every effort to keep bills within her budget. Jane reports her food and utility bills have all doubled and yet they have had to reduce the amount of meat they now purchase or energy they consume. Meat is now limited to sausages or mince and shopping daily for the meat specials to decide on dinner that night – no more fortnightly shopping as she cannot afford to purchase meat at normal prices nor can she afford any food wastage. Jane buys necessities like toilet paper only when it is on special and stocks up on things like that. Jane says she is often confronted with the choice to buy healthy or to buy cheap and make the dollar go a bit further.

   Jane is amazed at the thought that she used to earn enough to provide for her family needs but now she has removed Private Health Insurance, exercise classes, kids extra curriculum activities, holidays, and going to the movies from family life. Jane does not want to be ungrateful and realises there are others worse off. The increased cost of living is out of her control and the only action she can take is to cut expenses. Jane gives an example: her Emergency Services Levy arrived recently and it increased over 400%. Jane exclaims "It was $90 and now it is over $400 – it was a shock, it's the same with the utilities, they just keep going up and up, where I am expected to find the extra money from?"

   Much to Jane's surprise is her utility bills. Jane annually checks the market to get a better deal of her utilities and is annoyed at needing to change companies every year to save money but confirms it is worthwhile because the $20 per month savings add up throughout the year.

   Jane explains that she uses buckets to save water, she no longer uses the flush button on the toilet but tips the collected water from the buckets to flush the toilet and has done so for about 4 years now. Her washing process has now changed to collect the water to use in the toilet. Jane cannot remember the last time she allowed herself or her kids to have a bath. Her water use is that of a single person living in a unit but yet her bill has not decreased much because the supply charges, and levies on her bill are not within her control. Jane states her Water Bill is usually around $110 per quarter and $97 of that is the supply charge.

   Jane explains that her house has energy saving equipment through a variety of schemes that have provided light bulbs and other gadgets for the home. However, the reality of living throughout winter is not a comforting one. No longer is anyone allowed to put the heater on, she gets blankets out and her and the kids walk around the house rugged up throughout winter so as not to use any heating. Jane says that she looks out for bubble wrap and stores it to cover the windows throughout winter. When her kids complain about being cold her response is to give them a cuddle to warm them up. But, her concern is as they get older this strategy will not work! (Jane giggles) and says, “I am lucky to go to work in winter where the office is at least warm”.

Jane proudly talks of her $2 purchases – solar lights. She puts them out in the morning before going to work and brings them in just before dark. The lights provide just enough light to get around the house for the family at night without needing to use any electricity or candles. This is just one example of many, many, changes Jane and her family have made to reduce living costs.

Jane explains how she and her family have changed the way they live to reduce their electricity consumption and yet even having implemented these changes, her energy bill has still doubled due to price rises. Jane’s concern is that any action she takes to gain support to deal with increased living costs will affect her future credit rating. However, as Jane is not a Centrelink recipient Jane is not eligible for any financial support or any concessions.

Jane is very much in control of her finances and is clearly very competent. She has taken actions to reduce her utility consumption. Jane is one of many responsible clients who have taken actions to lower consumption and are still struggling to understand and reduce utility expenses.

This submission has been approved and supported by the following agencies:

South Australian Financial Counsellors Association Inc

Aboriginal Legal Rights Movement Inc

AC Care

Anglicare SA

CareWorks SA

Centacare Catholic Family Services Country SA

Central Community Legal Service SA

Consumer Credit Law Centre SA

Lifeline South East

Lutheran Community Care

Marion Life Community Services Inc

Northern Community Legal Centre

Relationships Australia SA

The Salvation Army

St Vincent de Paul Society (SA) Inc

UCare Gawler

UCare Kapunda

Uniting Care Wesley Bowden

Uniting Care Wesley Country SA

UnitingCare Wesley Port Adelaide

Uniting Communities