Market Segmentation and Domestic Electricity Supply in Victoria

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Abstract

If the observations of unregulated and recently deregulated essential services were to hold for electricity reform, we could expect to see market segmentation of household customers. This is a corporate strategy aimed at the acquisition of attractive customers and the avoidance of unattractive customers. It is a function of market relations and commodification. Some markets already segment and assign unattractive customers to ‘residual’ markets, ‘sub-prime’ markets or ‘markets of last resort’. Residual markets tend to involve market abuse by suppliers because these customers lack market power. It is possible therefore to suggest that segmented markets are characterised by simultaneous competition and monopoly. The implications for the supply of essential services, such as electricity, are profound. This research sought to identify whether there is evidence of emerging segmentation of the domestic electricity market in Victoria.

In practice, few essential services areas are completely deregulated. The history of segmentation in the US insurance and lending industries provides valuable insights into markets, market failure and social protections. Taking this history and the more recent experiences of reforms in the US, the UK and Australia, it has been possible to identify three models of social protection: ‘universal service’, a ‘civil rights’ model, and a ‘market’ model. The Victorian reforms reflect some elements of each of these. The social protections included in the reform package both encourage and present barriers to market segmentation. At the time of the research, some elements of the safety net arrangements and customer inertia (born out of negative attitudes to competition) have acted to inhibit segmentation. Customer inertia in its own right poses questions for the efficacy of competition policy.

The key understanding that is gained from this research is that both civil rights and socio-economic entitlements (social rights) are required to prevent markets in essential services acting upon and exacerbating inequality. This suggests that universal service, as a model of social protection, is most likely to ameliorate the impacts of inequality.
Acknowledgements

I would like to acknowledge a number of people who have supported and encouraged my research. Firstly, a number of individuals and one organisation in particular literally made it possible through their generous financial support for the costs of the survey work. Mostly they have asked to remain unsung but I am delighted that I can acknowledge at least one, Timothy Fegan. Thank you.

The Institute for Social Research also provided me with a three-year scholarship that was internally funded. The granting of this scholarship recognised not so much any previous academic contribution on my part but my engagement in the public policy debates around privatisation and competition policy. Recognition of this work has been very important to me. Much of this, of course, can be attributed to my primary supervisor Professor David Hayward whose enthusiasm for my research never seemed to wane. Equally Dr Peter Love, my other supervisor, was supportive and engaged with the arguments. A special thanks goes to Professor Denise Meredyth whose detailed feedback made a significant difference to the final outcome. A huge advantage of being at the Institute is that the postgraduate students are housed together and it made so much difference. I had fun.

Thesis ideas of course do not come out of nowhere. I owe a good deal of my knowledge about the electricity industry to John Dick from the Energy Action Group. I had innumerable conversations with two Melbourne financial counsellors, Barry Duggan and Esther Gregory, whose coalface experience of a number of markets reinforced the direction I was taking. The encouragement and support of US economist and consumer advocate Dr Eugene Coyle has also been important.

Finally, David Hudson edited the thesis with remarkable patience and good humour.
Declaration

This thesis contains no material which has been accepted for the award of any other degree or diploma, except where due reference is made in the text of the thesis. To the best of my knowledge, this thesis contains no material previously published or written by any other person except where due reference is made in the text of the thesis.

Mr David Hudson edited this thesis. The editing addressed only style and/or grammar and not its substantive content.

Signed…………………………………………

Dated…………………………………………
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<td>ABS</td>
<td>Australian Bureau of Statistics</td>
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<tr>
<td>ACA</td>
<td>Australian Consumers Association</td>
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<td>AFCO</td>
<td>Australian Federation of Consumer Organisations</td>
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<td>BOZO</td>
<td>brings only zero outcomes</td>
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<td>CPO</td>
<td>consumer protection obligation</td>
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<td>CSO</td>
<td>community service obligation</td>
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<td>DB</td>
<td>distribution business</td>
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<tr>
<td>ESC</td>
<td>Essential Services Commission</td>
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<td>EWOV</td>
<td>Energy and Water Ombudsman Victoria</td>
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<td>FRC</td>
<td>full retail competition</td>
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<tr>
<td>GBE</td>
<td>government business enterprise</td>
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<tr>
<td>GFC</td>
<td>Gas and Fuel Corporation</td>
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<td>GTE</td>
<td>government trading enterprise</td>
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<tr>
<td>HEAS</td>
<td>Home Energy Advisory Service</td>
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<tr>
<td>HVC</td>
<td>high-value customer</td>
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<tr>
<td>kWh</td>
<td>kilowatt hour</td>
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<td>MUT</td>
<td>maximum uniform tariff</td>
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<tr>
<td>NCP</td>
<td>National Competition Policy</td>
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<td>NESB</td>
<td>non-English-speaking background</td>
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<td>ORG</td>
<td>Office of the Regulator-General</td>
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<td>OSOE</td>
<td>Office of State Owned Enterprises</td>
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<tr>
<td>PAC</td>
<td>Public Authorities Contribution</td>
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<tr>
<td>POLR</td>
<td>provider of last resort</td>
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<tr>
<td>PPM</td>
<td>prepayment meter</td>
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<tr>
<td>SECV</td>
<td>State Electricity Commission of Victoria</td>
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<td>URG</td>
<td>utility relief grant</td>
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<td>USO</td>
<td>universal service obligation</td>
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PREFACE

This thesis is the outcome of the researcher’s long-standing interest in essential services, especially utilities. This interest grows out of employment in the area and a community concern with both the radical reforms to utilities that have occurred in Victoria over the past ten years and the related social issue of the persistence of fuel poverty.

The thesis is concerned with the possible emergence of customer segmentation, exclusion and/or exploitation of vulnerable and disadvantaged domestic consumers in the new Victorian electricity market. In particular, it questions the degree to which corporate marketing and customer strategies exclude particular customer groups because they lack economic value and associated market power.

The possibility of vulnerable customers failing to obtain supply or being subject to higher than necessary prices – where the product is an essential service and there is no reasonable opportunity for substitution – would be likely to mean that some of them would have periods without supply, or forfeit some other essential item. In either case, persons in these households could experience harm, such as poorer health from lack of heating or going without food.

My central argument is that ‘redlining’ is an example of market segmentation, and the history of redlining and the associated concept of residual markets demonstrate that market segmentation is based on exclusion and exploitation and is therefore not economically efficient. Market segmentation through redlining exacerbates existing social and economic inequalities.

Research for the thesis drew on an existing, albeit limited, literature, my own experience in employment around issues of fuel poverty, and a mail-out survey of 576 households across Victoria. My personal experience not only provided the ability to access data and reports not publicly available, but also meant I could draw on related personal research and writings in the area, most notably the report Bleak House which is to be published in 2006.
The thesis is not concerned with privatisation. While privatisation and marketisation are very much related in terms of the reforms to the Victorian electricity industry, the thesis proposes a phenomenon relating specifically to the operation of markets that is independent of ownership issues.

The thesis is comprised of four parts. In addition to introducing the subject, Part 1 provides a guide to the more specialised terms and concepts used throughout. In Chapter 2 I discuss the methodological approach employed in the research. Part 2 has three chapters. In Chapter 3 I trace the development of domestic supply of electricity in Victoria leading up to the reforms of the 1990s. This is an important prologue because it demonstrates that, as far as electricity supply goes, economics and politics are deeply entwined and possibly inseparable. This context sets the scene for an analysis of the subsequent struggle over reform and assists our understanding of the traditional argument for monopoly supply and universal service that is explored later. While it may appear to be something of a digression, the claim to a right of supply at an affordable price has had a highly significant impact upon public policy. Recognition of this claim gives unanticipated insights into the role and impact of governmental action on market segmentation.

In Chapter 4 I provide an outline of the neo-liberal vision through a review of the public policy literature, and the key changes undertaken by the Kennett government. I give particular attention to the shift from universal service obligation as a form of social protection to the adoption of community service obligations (CSOs). This was important not merely because universal service offended neo-liberal prescription of what constituted economic efficiency, but because it allowed government to address some of the political opposition to market reform.

Not everyone welcomed market reform of the Victorian electricity industry. Chapter 5 shows that the struggle involved varying levels of dissent. Whilst a relatively small body of literature was produced, the opponents of the neo-liberal vision of the market managed to modify the proposed model in significant ways. This opposition was made up of two distinct groups reflecting two further understandings of market relations and social protection. The conflict between these positions reveals the deficiency of pursuing a consumer rights model based predominately on civil rights.
Having given some history of electricity supply and of the reforms of the past decade, I turn in Part 3 to the traditional and non-traditional arguments against competition and the market. In Chapter 6 I examine the traditional economic arguments about the nature of the supply side of the electricity industry and why it has certain attributes that mean, in practice, it may be unsuitable for competition. I then discuss in detail the characteristics of domestic electricity customers in Victoria. Demand-side characteristics are important in establishing why and how the market can be segmented, and also why certain kinds of protections such as targeted assistance in the form of CSOs will not necessarily provide safeguards.

In Chapter 7 I address non-traditional arguments against the market. This chapter provides a detailed exploration of market segmentation. It includes a description of commodification and its role in the process of segmentation. I examine redlining as a long established, albeit illegal, practice in the US as an example of segmentation and economic discrimination. Residual markets are described, along with their relationship with consumer safety nets in the deregulated electricity markets. Segmentation and some implications for economic theory are canvassed. Chapter 8 specifically focuses on electricity deregulation and liberalisation, with reference to the US, UK and Victorian experiences. Prepayment meters are highlighted as an example of a residual market in Chapter 9. Chapter 10 brings together the different understandings of market relations, social and consumer protection and electricity in three basic models of protections, explaining how the lack of accounting for market segmentation undermines both the neo-liberal argument for market reform and the new consumerist model of social protection.

In Part 4 I turn to the results of my investigation into the possible emergence of customer segmentation, exclusion and/or exploitation. Chapter 11 focuses on those households who it may be expected could be harmed by market segmentation. I was also aware that I needed to consider the possibility that there may be little immediate change with full retail competition (FRC) or that the changes may be different from those anticipated. Accordingly, the investigation sought to ensure that an explanation could be offered for alternative findings. Chapter 12 covers the impact of customer attitudes, customer inertia and the legacy of social democratic and new consumerist influence on the reform process.

Chapter 13 presents my conclusions.
PART 1: INTRODUCTION

Chapter 1: Introduction

1.1 Introduction

In this chapter I provide an outline of the central argument of the thesis that redlining and residual markets are examples of market segmentation, and as such can be used to demonstrate that competition in an essential service such as electricity achieves neither economic efficiency nor equity. The terms ‘redlining’, ‘residual markets’ and other terms and concepts that may be novel to the reader are explained here to help guide later discussion. Context for the research is also provided through a brief explanation of the significance of the Victorian electricity industry reforms. Limitations to the scope of research are also indicated.

Marketing literature and observations of other essential services markets suggest that competitively supplied domestic electricity customers are likely to be subject to corporate strategies that differentiate between those with different economic and social profiles. Different marketing strategies will be used for different profiles, including potentially those customers whose income and usage attributes make them unattractive. In marketing literature this is known as ‘market segmentation’. Using a statewide survey of households, this research set out to identify the possible emergence of market segmentation within the recently deregulated domestic electricity market in Victoria. Market segmentation of essential services is of interest because of the potential negative impacts upon low income and other disadvantaged domestic customers.

One particular form of market segmentation is redlining, a term coined to describe certain types of exclusion from markets, particularly of minorities. Colton’s (1997) concept of residual markets, which is concerned with exploitation in markets, is also an example of market segmentation. By relating market segmentation to redlining and residual markets, the research is able to draw on historical market and policy failures and extrapolate the policy issues to newly emerging essential service markets.
The research plan recognised the potential for very little to occur in the early years of the market. Deregulated electricity markets elsewhere had experienced high levels of customer inertia. I found that customer inertia was widespread but, unlike previous research, I identified that Victorian households are cynical in regard to the purported benefits of competition and this determined their response to the market. This has important policy implications.

Customer inertia, along with an unanticipated extension of the consumer safety net arrangements, worked to inhibit market segmentation during the period under examination. The extension of the safety net effectively prohibited retailers from shedding customers on any scale. The corollary of this change in policy was a shift in attention to the role and impact of consumer safety nets. Analysis of Victorian government regulation and overseas examples revealed the pivotal role of government in creating the conditions for segmentation, both in the context of a market and as the outcome of regulation. The UK was the most thoroughly segmented domestic customer base examined, but this segmentation occurred prior to competition and the lifting of price controls. While I had worked with the assumption that competition drives segmentation, it became evident that segmentation strategies will be adopted by profit driven commercial businesses, even publicly owned monopolies, unless there are countervailing policies or regulation that provides consumers with certain rights.

The history of the State Electricity Commission of Victoria (SECV) illustrates this point. For long after its establishment, the SECV adopted practices whereby domestic customers served the needs of the utility rather than the other way round, despite equity impacts being apparent. It took until the 1980s in Victoria before the social correlates of energy usage (the welfare function) of electricity service was officially acknowledged and policy changes made to reflect this understanding. A key contention of social reformers such as Kiers (1983) was that utilities redistribute wealth by being quasi taxation collectors. When utilities fail to account for capacity to pay, this taxation is highly regressive. I provide a lengthy historical overview of the SECV because the characteristics and attributes of both the supply side of the industry and of the demand side have so much bearing on the issue of electricity as a form of welfare.
Not surprisingly, the most extreme neo-liberal reformers of the 1990s wanted to strip out all the perceived vestiges of welfare. Theirs was a claim that a commercially focused utility delivering an essential service is neutral in regard to equity, as competition would drive prices to reflect the cost of supply. I argue that market segmentation, to the contrary, reflects market abuse of one segment of customers, which does not result in cost-reflective prices and is not economically efficient. The rent derived from this exploitation is then used to cross-subsidise the attractive customers, which also voids the efficiency principle that is the justification for market reform. Accordingly, competition in essential services where customers cannot avoid the residual market does not result in cost-reflective pricing but in a quite perverse economic outcome and considerable injustice.

Given this insight, it became necessary to establish what kinds of rights are necessary to prevent segmentation acting upon and exacerbating existing inequalities. What rights the customer, or the citizen, should have in a market was highly contested throughout the reform process. Chapter 5 identifies three ideological models – neo-liberal, social democratic and ‘new consumerism’ – each of which has a particular view regarding rights as the foundation of their arguments. Each is critiqued in the light of market segmentation and the experiences of redlining and residual markets in the US.

A key understanding gained from this research is that both civil rights and socio-economic entitlements (social rights) are required to prevent markets in essential services acting upon and exacerbating inequality.

The lack of attention given to market segmentation in market reform proposals and in the academy represents a serious oversight for both public policy outcomes and economic theory. Moreover, the economic discrimination central to segmentation not only raises questions for economic theory, but for equal opportunity policies and social regulation more generally.

1.2 Redlining and residual markets: What do they mean?

The underlying arguments for and against market reform of electricity in Australia, New Zealand, the UK and the US have largely been identical. In the US, however, a unique argument was being accepted by many legislatures intending to deregulate that provisions
needed to be made to prevent redlining in domestic energy markets. Redlining in the US context had traditionally referred to discrimination against minorities in the delivery of specific services such as insurance and mortgage lending. It was generally regarded as locality specific. The effect of redlining is exclusion from the market. The earlier deregulation of telecommunications and gas in the US had exposed redlining as not being peculiar to the above markets but a more general phenomenon of unequal treatment in markets. Legislatures which accepted the need for measures to prevent this discrimination included what we in Australia would regard as equal opportunity provisions in their deregulation laws. In addition to the typical categories such as race, gender, age, disability and religious affiliation, these laws also had prohibitions on discrimination on the basis of (low) income and source of income.

Chief amongst the proponents for redlining provisions was economist and lawyer Roger Colton. Colton (1997) drew attention to where redlining was irrational discrimination (for example, race prejudice) and where it was rational. By rational, he meant that it had an economic basis. Equal opportunity laws address the former by seeking to prevent certain actions. However, addressing service exclusion in a low-income minority neighbourhood may require the use of remedies intended to promote specific actions by an industry, such as community reinvestment schemes because the exclusion results from an economic decision. The term ‘redlining’ has tentatively entered the debate in the UK in the wake of privatisation and deregulation, and the term ‘service exclusion’ sometimes appears as a component of the broader concept of ‘social exclusion’ (National Consumer Council 2005, Gordon et al. 2000, Richardson and Le Grand 2002, Scullion and Hillyard 2005, Bramley and Ford n.d.). Neighbourhood renewal projects in the UK reflect the promotion of private sector action or community reinvestment.

1 The National Consumer Council (2005) in the UK provides the following definition:

Market-based exclusion affects those who are already the most disadvantaged in terms of their income, employment, health and life chances. It means that they find it hardest to access even the basic goods and services – heat, light, health services, banking facilities – they need to live in modern society. It also means that they may end up paying more than their better-off counterparts for these goods and services – even though they often don’t meet their needs – despite having little, if any, money to spare. Frequently, the factors associated with market-based exclusion combine to ensure that the most vulnerable people in our society, who face the hardest daily struggle to get by, have little time, money or energy to improve their situation. They become trapped in a cycle of poverty which is hard to survive and even harder to escape.
Colton (1997) also drew attention to how previous action such as the federal Fair Access to Insurance Requirements laws intended to promote service inclusion in the US had resulted in access to service being delivered on the basis of discriminatory terms and conditions. In addition, in essential service markets, the characteristics of particular sub-groups of customers meant that competition effectively did not work for them. That is, they had ‘neither the resources not the ability to make competition work’ (Colton 1995d: n.p.). This lack of market power on the part of customers correspondingly provides too much market power to suppliers. It required, in his view, public regulation to curb the ‘abuses which such power portends’ (Colton 1995d: n.p.). He called this part of the market the ‘residual market’, and cited as examples rural residential consumers and, for insurance, high-risk households or drivers.

In summary, Colton alerted policy makers to the limitations of voluntary essential service markets because unregulated providers are likely to exclude some customers and exploit others. Moreover, he warned that regulation intended to remedy these problems needed to avoid replicating these outcomes.

Despite Colton’s insights on the existence of residual markets, his proposition is not particularly developed. He appreciated, for example, that the affected customers were rationed because their demand exceeds the supply available to them. This, however, goes back to the exclusion issue. He thought that the exploitation he observed more often resulted from there being no sellers ‘engaged in active rivalry for the business of these households’ (Colton 1995d: n.p.). The market power issue he refers to is a classic case of market failure: too few suppliers. Yet observations made by others such as Alwitt and Donley (1996) suggest that there can be a robust number of suppliers in these markets, and that these markets can be big business. In seeking evidence for this, I found that market reform of various essential services had generated sufficient observations of unequal economic treatment that did not relate to insufficient numbers of suppliers. In addition to this, marketing literature revealed the application of new information technology to market segmentation as allowing highly differentiated treatment of customer segments (Hallberg 1995, Berry and Linoff 1997, Clancy and Shulman 1991, McDonald and Dunbar 1995, Stewart 1996). ‘Choice’ can be regarded as contingent not only on corporate strategies intent on shaping consumer preferences, but increasingly on the result of data mining and related marketing research targeting specific customer segments. It could be
expected that corporate strategies would be employed to acquire attractive customers whilst at the same time shedding those that are unattractive. Customer segmentation’s most simple objective is to sort profitable customers out from the unprofitable, but it has also allowed firms to effectively charge what were once regarded as low and/or unprofitable customers more. Knights, Sturdy and Morgan (1994) argue that regulatory changes to stimulate competition have been a major factor in promoting segmentation.

Redlining and residual markets can therefore be more clearly understood as market segmentation. Technological change has revealed that geography, in terms of it being possible to delineate spatial distribution of wealth, was being used as a method of segmenting mortgage and insurance markets. Information technology has provided marketers with significantly more powerful tools. Understanding the market segmentation of customers also permits us to better locate and define the residual markets. These form where consumption is essential or involuntary and are closely associated with services that have traditionally been considered network services (gas, electricity, water, banks and telecommunications) or pooled risks (insurance and credit). The residual market is a market segment comprised of customers that, due to the essentiality of the good or service, can be subjected to market abuse. Why rivalry between firms does not undermine the exploitation of residual market customers is something that deserves urgent attention.2

The residual market can be distinguished from the HVC (high-value customer) segment and the BOZO (brings only zero outcomes) or excluded segment.

While Colton understood that the non-discretionary nature of essential services meant that some of these consumers could be exploited, I have argued that it is not necessarily a lack of suppliers that causes this. In this sense I have redefined the meaning of ‘residual market’, establishing that government intervention can also result in segmentation. I distinguish this outcome by use of the term ‘provider of last resort’ (POLR) and note that the discrimination involved can be either positive or negative. Unfortunately in Victoria the liberalisation has meant that vulnerable consumers are subject to state sanctioned safety net arrangements that constitute the negative form of POLR. Just as Florio (2004) identified exploitation arising from regulation and liberalisation in the UK, I have been able

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2 Generally higher prices are justified on actuarial grounds, yet if customers manage to pay these premiums, it would seem logical that they could afford the cheaper standard rates.
to demonstrate that regulation, aimed at mimicking the market, contributes to discriminatory practices by retailers.

In the UK, payment methods and associated technologies were instrumental in segmenting the customer base even before supply was deregulated. Prepayment meters (PPM) mean the poorest consumers pay the most for supply. This constitutes the residual market. Market segmentation of essential services customers affects not just the vulnerable and disadvantaged, but could also mean that attractive customers are cross-subsidised. This undermines the argument that competition engenders economic efficiency. In his discussion of the distributional impacts on households, Florio (2004: 259) makes it clear that the domestic price increases that resulted from tariff rebalancing in the UK constituted for many small customers ‘social hardship’ that was ‘unnecessary for an improvement in allocative efficiency’.

The reaction to redlining in the US offers an insight into the nature of civil, political and social rights and markets. Redlining resulted in legislation such as the Community Reinvestment Act and the Fair Access to Insurance Requirements laws to protect the civil rights of minorities. In the wake of telecommunications and gas liberalisation (and the emergence of redlining in these industries), electricity consumer advocates moved quickly to have anti-redlining provisions included in reform legislation. As part of this, provisions were made to protect customers from discrimination on the basis of income or income source. This was new. It made it clear that, in an era of pervasive credit scoring, poor economic status could not be used as the basis for denial of service or discriminatory service. This is very much an anti-segmentation measure. It uses civil rights to give effect to a socio-economic entitlement. In addition to this, many states in the US also required cross-subsidisation of disadvantaged customers. The general effect of this set of civil rights is universal service. These civil rights are being bound with socio-economic entitlements because it requires both to prevent the discriminatory impacts of segmentation.

Implicit in this US reaction to market outcomes is a view that the purported actuarial basis for discrimination is not only unfair but based on wrongful assumptions. While I have not tested this (it is a large enough question to warrant a separate piece of research), my lengthy discussion of fuel poverty highlights how consumer disadvantage arises from the
combination of vulnerability factors and supply features (the characteristics of a particular market). If products are tailored to vulnerable customers, perceived risks (such as default on payment) can be addressed. This is what Alwitt and Donley (1996) mean by re-balancing the act of exchange. Commodification, however, is the means by which market power can be asserted. Limits on market power are limits on commodification.

I also argue that compensatory welfare transfers are also subject to the impact of segmentation. Many have argued that lump sum tax transfers are preferable to cross-subsidies. This policy option fails to account for segmentation and market abuse and, indeed, rewards firms which engage in market abuse. This is not to say that transfers aimed at improving income security are not warranted. Rather, there is a need to recognise that these are only one part of a package of measures required to overcome the mismatch between customer needs and the supply features of essential services industries. Segmentation acts upon the perceived risks associated with inequality, therefore a package of measures needs to address both actual inequalities and perception of risk. The neo-liberal approach allows retailers to avoid responsibility for the social costs of energy supply. The market model therefore socialises these costs on the one hand through income support, and privatises them on the other in that households assume the costs of rationing, disconnection, higher prices etc.

As the section on fuel poverty shows, many households are not in a position to manage these costs. Tenants, for example, are hard-pressed to address building thermal efficiency. A crude response would suggest that retailers assume a greater share of the social risks because, if they did, the root causes of fuel poverty or inequality would become the focus of their attention. What is essential here is the recognition that domestic consumption of electricity is ‘ordinary’ but the relationship between supplier and customer is ‘extraordinary’ (Shove and Chappells n.d.). It is this relationship that permits the mitigation of fuel poverty or can be its cause. Utilities do not occupy a neutral position in regard to the distributive impacts of the supply/consumption relationship. As has been indicated, the market model is flawed because segmentation establishes that the goal of economic efficiency (welfare) is undermined by market abuse. The compensatory social welfare measure – the CSO – cannot efficiently overcome this. The alternative is to pool all the risks together, as occurs with universal service, so that the customers’ vulnerability
factors and the industry's supply features are addressed together, recognising the relationship between the two.

These lessons are not confined to utilities but are applicable across banking and finance, telecommunications, housing, health, insurance and education, and the first question society needs to ask is whether access to essential services should be dependent on discriminatory premiums.

1.3 The significance of the Victorian reforms

The Victorian electricity industry has been revolutionised over the last decade as a result of two distinct but related policies, privatisation and market liberalisation. For 75 years, electricity had been largely supplied by the SECV, a state-owned vertically integrated monopoly.3 It mined the brown coal deposits in the La Trobe Valley, built hydro-dams, built and run a high voltage transmission system and the lower voltage distribution system, and provided the retail interface with customers. Within this institutional arrangement, Victoria had been rapidly electrified.

The Kennett Coalition (Liberal/National) government (1992-99) undertook the disaggregation4 and privatisation of the SECV. It also introduced competition for larger industrial and commercial customers. The final stage of the reforms, ‘full retail competition’ (FRC) – the extension of the market to small customers such as households – commenced on 13 January 2002, under the Bracks Labor government. With the establishment of wholesale and retail markets, the electricity industry is now characterised by multiple private competing firms in both generation and retail supply.

FRC permits all customers to choose their retail supplier. These purchase wholesale energy from generation companies or from a ‘spot’ market and have it transported by the transmission and distribution businesses (the ‘poles and wires’ companies) to the point at which it is consumed. The separation of generation from transmission/distribution and from

3 While the SECV supplied retail services to most of the state, there were also eleven municipal distribution/retail systems that purchased wholesale energy from it.
4 This involved separation of each of the business units – generation, transmission, distribution and retail – from each other. Generation and retail were further split so as to form competing firms. Transmission was left as a single monopoly, and distribution carved into five geographically based franchises that were expected to ‘compete by comparison’.
retailing permits competition in those areas of the industry where it is possible to have a number of firms (generation and retailing). The monopolies (transmission and distribution) are regulated, but provided with incentives that are intended to mimic the market.

The Kennett government argued that competition would result in retailers offering innovative price/service mixes tailored to individual customer needs (OSOE 1994a, 1994b, Smith 1994). Competition and choice would place pressure on retailers to price their products to reflect underlying costs of supply, thereby delivering significant efficiencies and, eventually, cost savings to be shared by customers and shareholders.

Victoria and New South Wales were the first states to extend competition in electricity to the household level, with South Australia following later, but not all agreed that there were benefits in pursuing competition to this extent. Queensland, for example, initially rejected it, while embracing competition for larger electricity users (Beattie 2001).

The shift in Victoria from regulated tariffs, terms and conditions to a private market and minimal consumer protection was a radical policy change. It involved the abandonment of universal service objectives, the dismantling of the maximum uniform tariff that had meant that households paid the same rate regardless of locality, and the erosion of some measures aimed at preventing disconnection from supply due to an inability to pay. The Electricity Industry Act 2000 envisaged the formal abandonment of an obligation on retailers to supply households. Yet little empirical work was undertaken to see whether the reforms could in practice deliver the outcomes theorised or whether or not the market was something that people wanted. Neither the Commonwealth (which introduced National Competition Policy) nor the Kennett or Bracks governments in Victoria undertook studies to address these issues. There are strong theoretical grounds on which to argue that the electricity industry has characteristics that limit the extent to which the ideal of competition can be realised. Coyle (2000) argues, for example, that undifferentiated commodities in capital-intensive industries require very specific pricing strategies centred on maximising volume of sales. This necessitates price discrimination, which in turn assumes the presence of market power – something that is supposed to be the antithesis of the

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5 ‘Tariff’ refers to the schedule of charges for electricity. A tariff is mainly comprised of an energy charge (the actual electricity used) and a contribution to the cost of transporting the electricity to the point of sale.
neoclassical concept of perfect competition. That electricity is an undifferentiated commodity remains an undeniable fact. So while customers may be able to choose between companies (brands) offering different prices and terms and even bundling with other services, the only real difference in the product is price (Humphrey 2002).

It would have been useful for policy makers to explore the many ramifications of the full commodification of such an essential service, and who the winners and losers might be in a competitive market. There was little debate about what the loss of universal service could mean. This concept was simply supplanted by the neo-liberal notion of CSOs and the encouragement to think of consumer rights in terms of procedural fairness rather than economic justice (Ernst 1994a).

1.4 Limitations to the scope of the research

There is a very large global literature on deregulation and privatisation. It is interested in issues regarding the benefits or otherwise of divestiture of public assets, productive efficiency of plant, labour efficiency, unionisation, environmental performance, earnings, the wealth transfers of certain sale models such as public floats, quality of supply, market abuse by generators, network regulation, asset valuation methodologies, third party access and the like. Even where the literature is concerned with deregulation rather than privatisation it concentrates almost exclusively on generation, transmission and distribution. Retailing is often covered only in the context of industrial and commercial supply rather than domestic supply. When domestic supply is mentioned, it is the franchise (pre-competition) arrangements that are discussed (for example, Ernst 1994a). This arises

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6 National Competition Policy (NCP) reforms removed the price discrimination clauses from the Trade Practices Act, and reference is made to the ‘benefits’ of Ramsey pricing – the discrimination to which Coyle refers. Ramsey pricing involves charging those with the least elastic demand the highest rates. This may be acceptable for a publicly owned and vertically integrated industry, but for a private disaggregated industry there is less justification, considering that in a market context it is an abuse of market power. The NCP reforms retained the market abuse provisions of the Trade Practices Act. In my mind there is an inherent contradiction in advocating perfect competition on the one hand but advocating market abuse when it cannot be achieved.

7 Each electron is identical. Generator sources can differ between gas (various types), coal (black or brown), hydro, wind, wave etc. This means that electricity supply can be distinguished by who produced it. For example, electricity can be marketed as ‘green’, meaning fewer greenhouse gases are produced as externalities. However, consumption of green energy is hypothecated as all electrons go into a common pool (the transmission network). Reliability is not relevant to the retail market as it is a function of the regulated networks.
in part because of the relatively small number of jurisdictions that have fully liberalised, and the recent period in which this has occurred.

Therefore privatisation literature per se is not relevant to this thesis as the focus is on markets in essential services. As mentioned, some essential services in some countries have always been delivered via markets, and it is observations from these markets that have prompted concern that segmentation will occur in newly created essential services markets. In addition, some electricity industries, as in the US, have long had a mixture of ownership. Privatisation has not been an issue there. That being said, the conduct of privatisations can have significant impact upon the efficacy of any future market. Spoehr (2003), for example, describes the problems that have arisen out of the privatisation of the South Australian electricity industry as a result of the government seeking to maximise the sale price of assets. Florio (2004: 226) describes the increase in domestic prices in the UK prior to privatisation as a ‘dowry’ paid to the new owners. Price increases prior to divestiture in Victoria also occurred. Even Florio tells us little about domestic consumer impacts subsequent to the lifting of price caps in the UK in 2002. This is partly due to the gap in time between privatisation and market liberalisation. He did observe, however, that the changes before 2002 were not the result of privatisation but of regulation and liberalisation: a ‘sophisticated system of fine-tuned tariffs and consumer exploitation has replaced old systems of cross-subsidies and uniform tariffs’ (Florio 2004: 260).

Lessons from the generation sector may have some applicability for domestic supply. Spoehr (2003) and Finn (2003) claim that generators have engaged in market abuse in South Australia. Such abuse, Finn notes, is not illegal under the Trade Practices Act 1974 as the National Electricity Code was authorised by the Australian Competition and Consumer Commission. He suggests that market abuse by generators in the national electricity market challenges classical economic theory because new entrants, rather than imposing discipline upon incumbents, collude with them. There may be specific features in some markets that mean all firms will adopt the same seemingly non-competitive behaviour. This may be relevant to segmentation.

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8 The Victorian government clawed back the excess profit through franchise fees. The increased prices permitted future regulated price cuts that were budget neutral for both the government and the retailers. Moreover, it left prices sufficiently high at the opening of the market that ‘competition’ would ensure that they would decline.
As Quiggin (2003) explains, ‘electricity markets face a tension between the short-term function of electricity prices in allocating a scarce and non-storable resource and the long-term function of providing appropriate investment signals’. There are unresolved issues about the way domestic demand creates risks for the broader electricity industry, how these are managed currently and how they might be managed in a fully liberalised system. Quiggin notes that privatisation and deregulation have meant that one set of risks has been swapped for another, and argues that the costs and benefits have not been fully assessed. The lack of assessment of FRC is a case in point. Sheil (2000) also explored the issue of risk, arguing that privatisation creates new social, economic and environmental risks. In his book on the performance of corporatised and commercialised water entities in Australia, he says that government has never been able to shed responsibility for essential services like water and electricity. Indeed, privatisation of essential services results in governments facing a moral hazard in which they are trapped into accepting the private owner’s arguments about prices and investment. This is a salient point, given the history of the Victorian government’s response to price rises for the deemed and standing offer customers. McDonell (2004: 83) describes the ‘de facto residual and ineradicable risk attendant upon a government’s obligation in a modern society to assure the supply of electricity to all, households and businesses alike, as an essential service, and like other essential services’ as the ‘sovereign risk of universal service’.

Sheil’s most significant contribution was to establish the dangers of uncritically adopting private sector performance measures for the management of essential services such as water. He argues that the use of market proxies meant that managers had a ‘set of abstractions derived from fictionalised assumptions about the productive facts of the infrastructure’ that could not authentically reflect the condition and capacity of the vital resources for which they were responsible (Sheil 2000: 156). The same issue of poor data and poor analysis informs Walker and Walker’s (2000) critique of Australian privatisations. King and Maddock (1996) also point to the apparent tension between competition theory and its application in their criticism of the access regime established by the Competition Policy Reform Act. In Victoria, the market model assumes that domestic retail pricing will be competitive and prices will be cost-reflective. According to this model, the existence of

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9 The Victorian government gave itself reserve pricing powers but has been reluctant to use them. Facing politically unpopular annual price increases, it eventually negotiated a four-year price path with retailers.
multiple suppliers by definition means that prices cannot move from under-recovery (under
the former monopoly) to over-recovery (in the market). This thesis seeks to test, in a small
way, whether this is true in practice, given empirical observations of other markets. So
while it is in substantially different territory to writing on privatisation (in particular), it can
be characterised as following a line of inquiry that runs through much of the work that
critiques privatisation and liberalisation.

1.5 Terms and concepts used

There are a number of key concepts used in this research. The first is that electricity is an
essential service. Electricity and gas (as domestically consumed 'energy') and water share
an important attribute: consumption is non-discretionary. Energy and water are life-giving
and are required for human survival. In developed parts of the world, utilities also share
the attribute that production and supply is via vast infrastructure networks that provide
economies of scale. These industries are, accordingly, usually monopolies. Yet even in
wealthier nations, some households consume less energy than is regarded as necessary
for a reasonable standard of welfare. This phenomenon is known as fuel poverty within the
Australian, UK and US literature.

Fuel poverty may reflect lack of income, poor thermal quality of housing, inefficient
appliances, lifecycle stage or regressive tariffs (Kiers 1983, Backman et al. 1987, Day
1985). It may manifest as rationing, accumulation of debt or under-consumption of other
essentials such as food. Difficulty in maintaining payments and the requirement of some
governments that utilities provide flexible payment arrangements means that these
customers are often viewed, rightly or wrongly, as expensive to serve. The fuel-poor and
rural customers, as well as others who may be regarded as disadvantaged in some way
(for example, having high energy needs related to medical conditions), have traditionally
been guaranteed supply at affordable prices by explicit universal service obligations or
other public policies to the same effect.

Universal service places an obligation on utilities to supply all customers regardless of
income or locality. Sometimes this may mean supplying at a reduced rate, which may
involve substantial cross-subsidies between different customer classes or sub-groups. Government may provide income supplements to some customers to ensure they can afford the utility service. In other cases, as in Victoria in the late 1980s, tariff structures are mandated to ensure that low-consumption, low-income customers can afford at least a lifeline amount of electricity. Universal service in effect posits access to affordable supply of electricity as a right. This type of right is often associated with the concept of social citizenship.

Social citizenship argues that, in addition to civil and political rights, citizens are entitled to socio-economic rights that ensure them a basic level of welfare (Marshall 1950, Esping-Andersen 1990). It is usually linked with the rise of the welfare state. Social rights within welfare states have been delivered in the form of welfare goods such as health, housing and education that were made available on a universal basis. The welfare state and social citizenship grew out of reactions to, and experience of, markets.

The liberal idea of the market is premised on the existence of many buyers and sellers and voluntary transactions. Individual exchanges reflect aggregate outcomes of all exchanges. This is because price, service and quality are determined by individual sellers seeking to gain market share in an environment in which they are unable to exercise market power because they have no more influence over outcomes than any other seller. Customers are able to ‘choose’ between competing products and services, but likewise cannot exercise market power. This ‘competition’ results in prices reflecting costs, or a situation of ‘Pareto optimality’ (Keen 2001, Johnson and Rix 1991).

The use of markets to set prices which, in turn, reflect aggregate demand and supply stands in contrast with other possible values, such as the need for sustenance. The direct relationship between production and consumption is abstracted in a market. The serving of human needs is replaced with the requirement to serve a commercial interest. This results in the commodification of goods and services.

Market segmentation has traditionally been concerned with differentiating specific groupings from the general mass of customers who may be more interested or more willing to pay for particular products. Increasingly it serves the purpose of identifying and separating out attractive (profitable) customers from unattractive (unprofitable) ones in
each market for customer acquisition or avoidance. The use of sophisticated information technology and data mining enables the process to be incredibly precise. This type of segmentation is not new but has been limited in many industries in the past by public ownership and regulation. It is best known in the US insurance and mortgage lending industries where it is closely associated with racial discrimination.

In the US, the exclusion of potential insurance and home loan customers on the basis of race and locality is known historically as redlining, reflecting the practice of suppliers literally mapping in red pen the localities they would not serve. With the deregulation of electricity, many states have included anti-redlining provisions in their reform legislation. Redlining has also served to highlight exploitation of certain customer segments. Colton (1995b) observed that public policy effort directed at addressing redlining frequently resulted in the formation of residual markets, that is, markets of last resort, characterised by consumers who have no market power and are accordingly likely to be subject to exploitation. These markets appear to exhibit little competition between suppliers, although specific ones such as payday lending (short-term unsecured loans) are highly profitable (Alwitt and Donley 1996). The credit industry, for example, has its own term for this segment: the sub-prime market (Consumers Union 2002b).

Finally, governments sometimes seek to protect disadvantaged consumers in markets by providing some kind of safety net arrangements. These arrangements I classify as provider of last resort (POLR) schemes. As Colton noted, these can amount to the facilitation of a residual market. This would appear to be the case with prepayment metering technology in the UK electricity market. A POLR can also mean that the state takes on or retains some of the financial cost of these customers. In this case, a POLR may provide selective assistance that guarantees universal access and affordability. In others, it may be punitive and have negative welfare outcomes.

1.6 Conclusion

Taking Colton’s observations of essential service markets, I set out to establish that redlining is a form of market segmentation. Moreover, this market segmentation has developed a high degree of sophistication with advances in information technology and its increased application is directly related to the deregulation of essential services.
Accordingly, I tested whether or not there is any evidence of emerging market segmentation in the new Victorian domestic electricity market. This involved looking for differential treatment of domestic customers according to their attractiveness to private competing retailers. The method I adopted to do this was a statewide survey of households.

I also redefine Colton’s definition of residual market and argue that there is evidence from other essential services that the problem of market abuse is not necessarily related to a lack of providers but rather to the non-discretionary nature of the service. In many markets, suppliers discriminate on the basis of actuarial assessments but, when such practices are applied to essential services, we should be asking questions about the premiums that can be extracted and the nature of the risk. For households experiencing fuel poverty, the risk premium serves to exacerbate the likelihood of default. This suggests that discriminatory practices in credit management may be warranted, but it points to the possible benefits of adopting forms of positive discrimination. Segmentation and residual markets raise questions about the efficacy of social welfare safety net arrangements to address equity concerns. But segmentation and residual markets also suggest that classical economic assumptions about market power may need revision. In turn, this suggests that the efficiency of the market in allocating resources can be questioned when it comes to certain essential services.

In this chapter I have briefly presented the central argument of the thesis: that redlining and residual markets are examples of market segmentation, and as such can be used to demonstrate that competition in an essential service such as electricity achieves neither economic efficiency nor equity. Key terms have been explained, and both the original usage of the terms ‘redlining’ and ‘residual market’ and my own new definitions have been provided. The changes that have occurred to the Victorian electricity industry were noted, providing background to the introduction of competition into the industry. Limitations to the scope of the research were also considered. In the next chapter, which focuses on methodology, the approach to the research, the primary research task and the practicalities and problems associated with undertaking the survey are discussed in detail.
Chapter 2: Methodology

2.1 Introduction

2.1.1 Research approach

In undertaking an initial review of literature concerning the liberalisation of domestic supply of electricity and the creation of markets in the UK, the US and Victoria, it quickly became evident that, while US legislators were willing to embrace markets per se, most were not willing to accept all the consequences of markets. Specifically, many states were unwilling to allow the ‘redlining’ of socially and economically disadvantaged and vulnerable domestic customers. This thesis took as its premise that redlining may occur in Victoria as a result of full retail competition. A political economy approach was used in order to understand the relationship between the various political and economic institutions and processes with redlining and market reform of domestic electricity supply:

political economists are interested in analyzing and explaining the ways in which various sorts of government affect the allocation of scarce resources in society through their laws and policies as well as the ways in which the nature of the economic system and the behavior of people acting on their economic interests affects the form of government and the kinds of laws and policies that get made (Johnson 2005: n.p.).

One starting point was a review of redlining literature. This revealed a gap between the writing of urban sociologists in the 1970s (which concerned housing and insurance) and the material being produced by contemporary consumer advocates and being acted upon by legislators. The major contributors for the latter, writing on economic discrimination in markets, market segmentation and of the problem of ‘residual’ markets, have been US advocates Colton and Coyle (Colton 1995a, 1995b, 1995c, 1996, 1997, 1999a, 1999b, 2000, Coyle 2000). If they were correct, it could be anticipated that liberalisation of essential services in countries like the UK and Australia should reveal examples of redlining/market segmentation. Outside the marketing discipline, market segmentation has not received more than a cursory examination, although writers in other disciplines have observed its impact in a number of liberalised markets. Research effort accordingly
centred on finding any literature that discussed instances of redlining/segmentation, in whatever guise. At least from the sources available to an Australian researcher, there appeared to be little academic work in the area.

The other starting point, undertaken simultaneously, was a review of literature concerning the deregulation of domestic electricity supplies. A distinction was made between literature concerning liberalisation and/or privatisation of electricity industries per se and that specifically about market reform of domestic supply. The thesis was not concerned with privatisation, but rather with markets. In the US, for example, the debate concerned deregulation rather than ownership, as a significant proportion of the industry has always been privately owned. Privatisation literature therefore was excluded. In the Australian literature there is a sharp demarcation between academic work on liberalisation (which generally does not discuss domestic supply issues in any detail), and non-academic work specifically and narrowly interested in domestic consumption. This is less the case in the US and the UK. In all three countries the subject is dominated by literature produced by governments, government agencies, regulators, think tanks and regulatory participants (industry and consumers). Another important caution regarding the literature is that most of it is pre-(full)deregulation. In most jurisdictions, the time that has elapsed between the initial reforms and full deregulation has been significant. This means many writers are making predictions or grappling with limited data. Moreover, each reform model and each starting point for reform has differed. That is, industry ownership and structure has varied at the outset of reform, as well as the underlying social welfare aims and strategies.

In political terms, the literature falls generally into one of three groups: neo-liberal proponents of free markets, proponents of social democracy, and ‘Third Way’ writers. Each to a view of civil, political and socio-economic rights. When these are specifically related to the reforms, three different constructions of social protection are identifiable. The redlining/market segmentation thesis involves not just whether segmentation occurs in deregulated essential service markets, but explores the implications for the theoretical foundations for each of these social protection regimes.
2.1.2 Primary research task

The primary research task for this thesis is to establish whether or not there is evidence to suggest the emergence of market segmentation of Victorian households since FRC in electricity commenced in January 2002. At the beginning of the research there was no up-to-date, reliable or valid data available. To overcome this, it was decided to undertake a dedicated survey of households that specifically addressed this data omission. The survey set out to identify whether there were corporate strategies involving:

- Marketing and customer policies aimed at customer segmentation, in particular, exclusionary practices;
- Systematic economic exploitation reflecting a lack of market power on the part of the customer; and/or
- Customer attitudes and experience of competitive supply.

Evidence of market segmentation could have been obtained through analysis of electricity retailers’ records. This method is employed in the US in the credit and insurance industries. Such analysis is enabled because there are requirements on providers to submit data to the relevant regulatory authority that can be accessed by the public (FFIEC 2004).10 No such powers exist in Victoria to give a private researcher access to this data. The Essential Services Commission (ESC), the state regulatory body, has general powers that would permit it to undertake a supply-side investigation analogous to that undertaken in the US, but has never used its powers for this purpose. It conducted an investigation into the effectiveness of FRC in late 200211 using data obtained from a customer survey. The ESC’s report made some findings at this time in relation to redlining. A second review undertaken in 2004 was specifically required by the state government to examine segmentation (both reports are discussed later). In both investigations, the ESC opted for a customer survey rather than the arguably more effective supply-side option.

10 There are limitations, particularly in relation to how communities can intervene (see Inner City Reporter, <http://www.innercitypress.org/cra.html>).
11 The ESC’s research coincided with my survey of that year.
Segmentation analysis requires, in all cases, knowledge of the population being segmented in order that discriminatory behaviour can be tracked. In effect, an investigator must identify on a prior basis which customers are likely to comprise which segments. I addressed this by examining customer groups who may be a credit risk or constitute poor profit targets for retailers. Those customers experiencing fuel poverty are one of the groups I regard as at risk of avoidance or exploitation. As there is strong correlation between low income and low consumption (reflecting rationing as a budget tool), profit margins for these customers can be expected to be low. If a customer fails to pay on time, the resulting cashflow loss may result in an overall negative return to the retailer. Accordingly, the fuel-poor, as low-margin customers and perceived credit risks, would in most markets be avoided. In addition I identify rural and off-peak customers, and those in public housing and private rental, as possibly at risk. This is because of a perception of public housing tenants as low-income and disadvantaged customers and hence credit risks, while private (particularly low-income) tenants are highly mobile (Duggan and Sharam 2004)\textsuperscript{12} and accordingly are perceived as potential ‘skippers’ (non-payers).

From the outset a significant barrier to segmentation was present – the Victorian government’s safety net arrangements, or more precisely, the ‘deemed’ and ‘standing offer’ tariffs. While these are in existence, each host (incumbent) retailer has an obligation to supply households in its former franchise territory, and the shedding of unwanted customers is virtually impossible. Moreover, the deemed and standing offer tariffs also entail price caps, which prevent strategic pricing aimed at shedding or acquisition. These safety net tariffs were conceived as temporary, and the original legislation had the obligation sunsetting\textsuperscript{13} on 31 December 2003. My survey therefore anticipated that retailers’ strategies would reveal in late 2002 some degree of preparation for this. I also planned to conduct a survey each year for three years. Two important developments encouraged me to change my plans. Firstly, the Victorian government extended the obligation to supply to the end of 2004. This immediately created some uncertainty as to whether or not the obligation to supply and price caps would ever be removed (in late 2004 the deemed and standing offer tariffs were further extended until the end of 2007). Certainly, households could remain inert until at least 2005. Secondly, the results of the

\textsuperscript{12} Duggan and Sharam (2004) used data from a national survey by Burke, Neske and Ralston (2004) of Commonwealth Rent Assistance recipients who were not on a waiting list for social housing.

\textsuperscript{13} ‘Sunset’ is the term used for clauses in legislation that have a predetermined date of cessation.
first survey found attitudes to be a compelling factor in explaining customer inertia. Together, it was difficult to see what would change between the first year and the next two years, hence the plan for further surveys was dropped. Both customer inertia and low switching rates were confirmed by the ESC’s research (2002, 2004a).

2.2 The survey

The survey was based on a randomised, stratified sample of 576 Victorian households. This provides a sampling error of ± 4.25% at the 95% confidence level. The findings can accordingly be generalised to the Victorian population of households with reliability (Betts, Hayward and Garnham 2001).

A pilot was undertaken beforehand. The survey was sent by email to Swinburne University staff, and given to friends and family with the view of ensuring responses were diverse. In particular, care was taken to guarantee response from those without English as a first language and those on low incomes. There were ten responses to the pilot, and many changes were made to the survey instrument.

2.3 Stratification

The stratification involved dividing households into four groups: inner Melbourne (within 10 km of the GPO); those between 10 km and the boundary of the Melbourne Statistical District; those in rural urban centres; and those in settlements with less than 1,000 persons, which includes people residing outside of towns. As postcodes were used to identify localities, there is some degree of blurring of the boundaries, which are far less absolute in the two rural categories. These categories were chosen as they correspond roughly with the different supply franchises of the electricity distribution businesses, as this is a major determinant of underlying costs of electricity. The numbers sought for each category reflected the proportion of the total population of households living in these areas, as determined by analysis of the 1996 ABS census. As shown in Figure 1, the dispersal over geographical areas was reasonably consistent with the state population.

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14 Distribution costs differ across five geographical regions or ‘postage stamp’ areas.  
15 The 1996 census was the latest available when the surveys were distributed. The 2001 census data was used once it was published. There was little difference in the distribution of population from 1996 and 2001.
The ‘rural urban centres’ and ‘rural’ categories have been combined for reporting because postcodes were used to identify the localities for the stratification but do not accurately reflect the division between the two.

Figure 1: Distribution of sample as percentage of Victorian population (n=576)


Within the stratified areas, localities were targeted because of the higher proportion of low-income households. This was to ensure sufficient representation of households that may have been subject to segmentation. The sampling frame used was an electronic version of the 2002 White Pages telephone directory. From this, localities within the four regions were selected as per the stratification and weighting noted above. Once this had been done, a skip sample16 was taken.

Surveys were individually addressed and mailed out via Australia Post. Reminder cards were sent three weeks later. A deficiency of the telephone directory is that it does not include the full address of account holders living in flats or apartments. This problem was in part later compensated for by unaddressed hand delivered surveys in new localities. An initial mail-out of 2,300 elicited an inadequate response rate of 10%. In addition to the

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16 This involves selecting respondents from a list at predetermined intervals (Betts, Hayward and Garnham 2001).
problem of incomplete addresses, the data in the telephone directory is up to 12 months old. This has a significant impact because mobility amongst Victorians is high, with around 29% moving in the three years to 2000 (ABS 2000).

Another deficiency of using the telephone directory is that households without telephones are excluded. As these are probably amongst the poorer in the community, they are of interest to the survey. However, it is not possible to identify such households.

Supplementary surveys were delivered by hand in specific localities using 2001 census data during August, September and October 2002. These were delivered to every third house in the selected streets, except for flats and apartments where each unit received a survey. In total, 5,000 surveys were delivered, with a return rate of just over 10%.

It was anticipated that households experiencing severe utility related hardship, particularly those with current debt and disconnection problems, would be unlikely to respond, as the nature of their hardship would make this a low priority. Despite the weighting, low-income households were under-represented, although the sample reflected the proportion of households who claim an electricity concession (which is linked to holding a health care card). The responses were skewed in favour of age pensioners. This explains how the sample managed to be representative of concession recipients without meeting the quota for low-income households. While the nature of the topic would have not interested some, the elderly appear to be particularly interested in this public policy issue.

2.4 Problems with the survey

The survey construction faced an inherent difficulty related to the complex terminology used by the industry, with which ordinary customers are unfamiliar. Few comprehend that they were transferred to deemed contracts at the outset of competition, or that they now have the choice of a market contract or the standing offer. Indeed, my survey and those of the ESC reveal that some customers failed to understand that the former SECV no longer exists. Conceptually, the reforms have involved very high levels of abstraction. The idea that competition does not involve duplicating poles and wires is difficult for many to grasp, particularly given that competition in telecommunications has featured duplication.
The length of the survey, with 90 questions over 10 pages, could have deterred response, although very few actually failed to complete it. In retrospect, it should have attempted to do less. Some questions and formatting could have been improved to simplify the questionnaire and its interpretation. In regard to eliciting whether or not respondents had switched, the survey attempted to capture not only whether they had done so but whether they understood key concepts and terminology. This was always going to be problematic. If the respondent was aware of and understood the concepts and terminology, they should have had little difficulty in answering these questions. However, they generally did have some problem. Answers to this set of questions were cross-checked to determine whether the response was appropriate or not.

The person who typically has responsibility for the electricity account was asked to be the respondent, because they would be able to answer most of the questions. However, the survey sought information in relation to the account holder, as this is the information which the retailer has and works with. For example, credit referencing would be in relation to the account holder, not a partner or other person who may contribute to the payment of the account. The respondent therefore was asked to relate the questions to the account holder where appropriate. This may or may not have been difficult at times, and it may not have always been adhered to. The distinction between an account holder and the household member with responsibility has a range of ramifications. One of them is that the account holder must give their explicit informed consent to switch, by either signing a contract document or providing on-tape verbal consent over the telephone.

Equally, the individual income of the account holder may bear no relation to the capacity or behaviour of the household in meeting its obligation to the retailer. Self-reporting of income is unreliable, but actual income was not as important for the survey as income source and household type. Retailers would also have difficulty in assessing household wealth, but they can far more easily collect data on employment, tenancy status and concession status. Payment method, history and consumption also reveal much about a household.

2.5 Sample characteristics

Compared with the 2001 census data (ABS 2001), the sample was highly representative of the number of respondents born in Australia (71%) and overseas (24% in sample, 23% in
One respondent (0.17% of the sample) indicated they were of Aboriginal or Torres Strait heritage, compared with 0.5 in the census. Census data revealed that 75% of households speak only English at home. The sample over-represented these at 85%.

In terms of median individual income (which was used rather than household income because retailers’ market strategies will reflect what they know about the account holder), the sample under-represented (37%) those under the median income of $300 to $399 per week (ABS 2001). There were 218 households (37.8%) in the sample who claimed government concession status for their electricity, closely reflecting the 40% of Victorian households who did so in 2003.17

As Figure 2 shows, the sample slightly under-represented families, while over-representing couples without children. Sole parent families, sole person households and group and other family households were reasonably representative.

Figure 2: Household structure: Comparing survey sample with census (n=574)


17 Total number of households in receipt of electricity concession (740,330) according to 2003-04 Victorian government budget paper no. 3, compared with total number of households in Victoria (1,838,000) according to the ABS (Australia Now, Cat. no. 4102).
2.6 Other factors influencing the survey

There were two retailer mergers in the period under study. Some respondents actively sought clarification about whether they had ‘switched’ because the company that supplied them had changed. Data was able to be cross-checked for verification where there was doubt about whether a respondent had switched or not.

Customers on the deemed and standing offer tariffs – which are effectively subject to price caps – experienced (particularly for some customers) a hefty price increase in the first quarter of 2001. Some of these were beneficiaries of a government subsidy (the Special Power Payment). It could be argued that price increases provide additional incentive to shop around. Alternatively, such increases and the existence of state subsidies may engender passivity. The survey did not seek information in this regard. Retailers have argued that the price caps are too low and this has limited the extent of competitive benefits available.

FRC in gas officially commenced on 1 October 2002, but implementation issues meant that transfer of customers in practice could not effectively take place as of that date. As ‘dual fuel’ deals – the consolidation of gas and electricity accounts with a single supplier – were anticipated as being of significant interest to consumers, electricity competition has perhaps been slower than if the two fuels had opened to competition simultaneously.

Where percentages in tables and text do not total 100, this may be due to rounding, the exclusion of ‘don’t know’ categories, multiple answers or ‘not stateds’. Throughout the report, an asterisk (*) denotes any value of less than zero.
PART 2: ELECTRICITY REFORM IN VICTORIA

In the following chapters I trace the historical development of the electricity industry in Victoria and particularly the tension between electricity as economic infrastructure and as a welfare good. The history of the SECV is the story of a modernisation project aimed at the electrification and hence industrialisation of the state. The Victorian government commenced the exploitation of the vast natural resource potential available in the La Trobe Valley in order to end dependence on fuel from New South Wales. The role of domestic consumption was not aimed at improved household welfare, although amenity was an important justification for nationalisation of the industry. Rather it was aimed at demand management intended to maximise the efficiency of the huge capital investment needed to realise the ambition of a vertically and horizontally integrated power system. Nevertheless, the welfare role of electricity was recognised early, but neither the SECV nor the Victorian government made much effort to address equity issues until the 1980s. Even though the SECV was in the broader public sector, public ownership did not mean it was or has been viewed as a part of the welfare state. It was regarded as a government trading business. Welfare entitlements relating to energy were won very late, and followed a different trajectory from that of the welfare state as it is more generally understood. Electricity supply has traditionally been dominated by industry policy and geopolitical considerations (Edwards 1969).

The contemporary struggle over electricity reform, however, owes much to the popular view that supply of domestic electricity is a ‘right’ (Zajac 1996). The following chapters demonstrate how neo-liberal reformers’ emphasis on a narrow understanding of economic efficiency translated into policy prescriptions that required skilful political manipulation regarding social entitlements to enable the reform process to proceed.

Partly because of this manipulation and partly despite it, critics managed to modify the proposed free market model in significant ways. The critics themselves, however, as a group were far from homogenous. The actual reforms therefore reflect three ideological groupings and understandings of market relations and socio-economic entitlements. In addition to the original radical free market proposal, an influential Third Way type

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18 The City of Fitzroy in inner Melbourne, for example, was still providing free firewood to age pensioners in the mid-1980s (personal communication, Robert Scates, former councillor).
movement or new consumerism emerged. The alternate grouping espoused traditional social democratic views. The influence of these ideologies on what has actually been implemented reveals how the reforms promote market segmentation, but also how elements of the reforms pose a barrier to segmentation.
Chapter 3: Electricity: Economic infrastructure or welfare good?

(W)e enjoy [rights that] are not founded on doctrine, but come about of struggle and...often arbitrary compromises between competing interests (Dean 1996: 11).

3.1 Early infrastructure development

The growth in the stature of electricity as an essential service has reflected its increasing penetration into domestic life and the decline of alternative means of heating, cooking and lighting. That is, the greater the monopoly of this form of energy (over materials such as wood), and the more that technology depended on electrical power, the more it assumed the role of ‘essential’ service. There is little room for argument about the improved amenity afforded by domestic electrification during the first part of the twentieth century. This process of monopolisation, however, reflected the increasingly capital-intensive nature of the industry after World War I and the need for economies of scale, which in turn dictated domestic pricing strategies.

The electricity industry in Victoria prior to the formation of the SECV in 1918 was characterised by privately owned businesses and some municipal services. Each supplier ran separate distribution systems, and there was no coordination of frequency or voltage. This meant consumers buying electrical appliances could use them in one locality but not in another. Prior to nationalisation, the electricity companies used local coal from Altona, but growing demand as a result of the manufacturing boom in Melbourne had led to importation of black coal from New South Wales. This source was both expensive and insecure, because of increasing industrial disputation in New South Wales. After World War I technological advances enabled the development of long distance high voltage transmission. Victoria could utilise its vast deposits of coal in the La Trobe Valley and end the state’s dependence on coal from New South Wales (Edwards 1969). Exploitation of this coal source called for huge capital investment. This required economies of scale, which were obtained through the restructuring and nationalisation of the industry. Over time the new SECV either took over local distributors or became the wholesale supplier to municipal retail services.
Electricity proved popular in the face of expensive gas provision which was used for lighting, heating and cooking, but the SECV still had to compete with the private gas companies. It had a natural advantage, as the quality of electrical lighting was far better than that of gas lighting. Edwards (1969: 73) argues that the improvement in the amenity of the home was crucial in gaining the political support of housewives for nationalisation of the electricity industry. At the domestic level competition between gas and electricity manifested as competition between retail appliances. Retailing of appliances was an important strategy in boosting domestic demand. The type of appliance purchased would lock a household into a particular fuel. At various times the SECV was prohibited from retailing electrical products, as independent retailers viewed it as unfair competition (Gerritson 1985: 88).

The nationalised electricity industry in Victoria was a late flowering of ‘colonial socialism’, despite taking place at a time when the private sector was increasingly hostile to government intervention in the economy. Colonial socialism, however, was characterised by governments participating directly in markets, in support of private sector interests (Butlin, Barnard and Pincus 1982). Nationalisation of the electricity industry in Victoria reflected parliament’s concern that ‘laissez-faire in electricity supply was costly, inefficient and dangerous’, as well as the belief that the ‘state’s industrial development’ must have an ‘ample supply of cheap power’ as soon as possible. The economies of scale achieved, the lowering of consumer charges and greater reliability delivered benefits to manufacturers and industrialists and enabled the rapid expansion of the network, as had been sought by rural interests (Edwards 1969: 13-21). Later, many government trading enterprises (GTEs) provided the only competition to private monopolies. It is a feature of Australian economic management that this competition has been subject to political controls that favoured the private sector regardless of the impact on consumers (Evatt Research Centre 1988).

The financial lessons of the colonial era are evident in the early planning of the SECV. The construction of large thermal generators and high voltage transmission lines to Melbourne could only be profitably realised if there were economies of scale. This required very substantial and ongoing growth in the volume of sales, and in particular consumption in those periods when it was not needed by manufacturing. The purpose was to fill in the troughs intended to enable steady output by the coal-fired stations. This maximised efficiency, as the stations take considerable time to adjust output (Edwards 1969).
obvious target. In order to attract household customers, the SECV had to offer prices that were competitive enough to entice them to switch from gas appliances, wood and oils. Its early policy was to base rates on the principle that tariffs for each class of customers should provide revenue to meet the cost of service to that class (Edwards 1969). However, as a result of initial government funding for the construction of the Morwell power station, the SECV could tolerate lower rates of return than a private project, hence lower revenues (Evatt Research Centre 1988). This in turn meant tariffs could be lower. Earlier in New South Wales, budget support had been used to reduce carriage and passenger fares on railways. This encouraged volume, improving the economies of scale. Government recouped its outlays through indirect taxation, which at the time was paid mainly by urban dwellers (Evatt Research Centre 1988). Likewise the cost of financing the early SECV ultimately fell disproportionately on the less well off, as the Victorian government at the time relied heavily on regressive consumption taxes (James 1996, Gibson 1999).

Authorities such as the SECV had a variety of non-market weapons for binding customers to them. As Butlin, Barnard and Pincus (1982: 244) noted, utilities tended to levy basic charges unrelated to volume used, make connection compulsory, regulate alternative services, and levy discriminatory or preferential charges. These strategies ‘encouraged a dependence on public supplies’. With domestic infrastructure locked into electricity, domestic prices could then be altered without threat of alternate supplies being used or a reduction in consumption. Consumption was encouraged through pricing structures that rewarded greater usage. This type of tariff is highly regressive for those with a low volume of consumption. In all, low-volume/low-income households assumed a disproportionate burden of the cost of supply.

3.2 Capacity to pay

In determining what price it could charge for domestic consumption, the SECV indirectly took account of capacity to pay. This meant pricing related to the male basic wage. By the 1920s the Australian centralised wage arbitration and conciliation industrial relations system effectively linked wages to a basket of consumer prices. This was the principle contained within the Harvester Decision of 1907. Acceptance of centrally determined wages was related to the Labor Party’s political support for customs tariffs to protect local producers, particularly manufacturing. While producers were protected from foreign
imports, they could afford to charge consumers higher prices in order to pay the higher wages demanded by the labour movement (Castles 1985). Local jobs were protected, as was local investment, although it meant a higher cost of living. Castles (1985: 92) argues that employers’ support for wage fixing derived in part from the frequency with which the lack of standardised wage rates lead to undercutting of prices and market instability.

One legacy of linking wages to the cost of living is that households without a male breadwinner\(^\text{20}\) have tended to be disadvantaged, not merely because of lower incomes but because of the higher cost of consumption.\(^\text{21}\) Also as both workers and non-workers paid the indirect taxes that funded infrastructure such as the early public power stations, the burden of such funding was regressive. There is also a legacy of the labour movement’s traditional attachment to means-tested targeted welfare. Butlin, Barnard and Pincus (1982) argue that the movement was mostly deluded in thinking welfare transfers were funded by the taxation paid by high-income earners. By the 1940s when social security was introduced, the reach of income taxes had already penetrated to low-income wage earners.

### 3.3 Pricing and equity

The fairness of pricing arrangements for electricity has never been far from public debate in Victoria. In 1926 the standard domestic supply was based on a two-part tariff comprising a monthly room charge and a per kilowatt hour (kWh) consumption charge, with a lesser rate for cooking and hot water heating, that is, an off-peak rate. During the Depression of the 1930s concerns regarding equity entered public debate. The imposition of ‘supply’ charges (the room charge) was recognised as having a disproportionate impact upon households with limited incomes.\(^\text{22}\) Edwards (1969: 121) cites a parliamentary debate in which an aggrieved member points out that ‘the two-part tariff is hard on the unemployed and those whose wages have been reduced, because they had to pay fixed room charges on which they could make no savings’. In other words, the fixed charge meant rationing

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\(^{20}\) Many male workers were also disadvantaged as a result of employment in non-unionised workplaces (Castles 1985). While Australia pioneered the invalid pension, for example, the payment rates were still well below wages.

\(^{21}\) For example, an ill or disabled member of a household may require additional heating.

\(^{22}\) Two part tariffs involve a fixed service charge part and a price per unit of electricity consumed part. The argument used at this time was that the customer could not lower costs sufficiently through rationing because the fixed charge always remained.
had little impact as a budget measure. In 1967 the room charge was abolished, and the consumption rates were set on the basis of a declining block tariff.\textsuperscript{23}

Calls were made in the early 1920s for a uniform electricity tariff across the state. A report from the SECV to the Victorian parliament in 1922 outlined the arguments put by proponents of flat rate charges that these would act ‘as a decentralising agent by drawing the industrial population from the cities’ (Legislative Council 1922: 683). Two further claims for uniform tariffs were discussed that are of interest. Proponents felt that they had contributed equally, as taxpayers, to the ‘Morwell scheme’ (the generating station) and therefore should be entitled to ‘equal’ service. The SECV responded that the ‘flat rate proposal…can be represented as a measure of an equitable and democratic character, under which all are treated alike’ (Legislative Council 1922: 683) but rejected this on the grounds that customers would ultimately fund the business, and that equality also related to the contribution to the costs of supply, not just whether a customer made an equal contribution to revenue. The cost of transporting electricity to rural areas was higher, the SECV argued, and subsidisation of rural customers would result in metropolitan customers avoiding the additional impost by substituting their electricity with another fuel, and hence the eventual bankruptcy of the Morwell scheme. Despite the failure to obtain rural subsidies, the rate of rural connections was one of the SECV’s most successful political ventures, with 24 out of every 25 farms connected within the first 34 years. Critics may have warned against ‘state socialism’, but connection rates spoke for themselves (Edwards 1969). Rural interests eventually gained their uniform tariff in 1965. The SECV was overruled.

Interestingly, when natural gas was discovered in Bass Strait in the 1960s, the Gas and Fuel Corporation (GFC) also sought economies of scale and absorbed other gas suppliers. It needed to be large enough to compete with the SECV. Whereas the SECV insisted on the primacy of economic rationality despite its unpopularity, the GFC engaged in public relations to achieve market share. Gerritsen (1985) provides a delightful \textit{realpolitik} description of its struggle to become the monopoly supplier of natural gas in Victoria.

\textsuperscript{23} Block tariffs are where different charges per kWh apply to an initial amount of consumption than to subsequent nominated amounts or ‘blocks’. A flat rate would in contrast charge the same amount per kWh regardless of the amount consumed. With block tariffs, either more or less can be charged as the volume of consumption increases. A declining block tariff results in electricity being cheaper as more is consumed. With an inclining block tariff, the electricity becomes more expensive as more is consumed.

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Under its chairmen Chadwick and Smith, the GFC adroitly created an image of public service. It garnered political support from the Country Party, the Municipal Association of Victoria, the Victorian Trades Hall Council, and from large and small consumers in Melbourne and the regions. This was achieved by the setting of uniform tariffs across the state (that is, cross-subsidies for rural consumers), maintenance of tariffs at less than rival firms, discounts for pensioners, establishment of a home service unit and energy information centres, construction of energy efficiency display homes, running courses for emergency services personnel, allowing households to pay off insulation on their gas bills, and assisting with vehicle conversion. The Melbourne and Metropolitan Boards of Works also learned that public relations and popularity with the general public were important if it was to achieve its objectives (Dingle and Rasmussen 1991).

Allegiances between these enterprises, their customers and the government shifted, depending on the circumstances, but it meant that service delivery was determined in part by political processes. Collective ownership generated a belief that the public had some entitlement in relation to the governance of these services. These businesses were also large employers and training institutions, penetrating deeply into the community. In addition, the participation of Victorians in two world wars had fostered a view common across welfare states regarding socio-economic rights (Castles 1985, Briggs 2000 [1969], Turner 2001).

Until privatisation, the electricity system functioned as a quasi-taxation system. A Public Authorities Contribution (PAC) tax was first levied in 1966, specifically to overcome the Victorian government’s inability to collect income taxes at the state level. At that time $3 in every $100 of the SECV’s revenue was paid as PAC (Edwards 1969). The SECV’s corporatisation in the early 1990s transformed the PAC into dividends and tax equivalent payments. Such charges are largely regressive forms of funding, unless pricing is explicitly linked to income. In 1983 the Energy Action Group argued:

what is not acceptable are the regressive social effects of current Victorian energy prices and energy policies...Nor is it acceptable that government charges have inflated domestic energy prices, and government instrumentalities, particularly in the area of public housing, have set up fuel poverty traps for low-income consumers (Deasey and Montero 1983: i).
3.4 Welfare

The distributive impacts of pricing structures had been of concern to specific groups such as age pensioners for decades, but in the 1970s the wider energy crisis and the realisation that poverty remained in Australia coalesced in new social movements interested in fuel poverty and energy efficiency. In the early 1980s the essentialness of electricity was linked to a broader human rights agenda. Deasey and Montero (1983: ii) declared: ‘fuel is an essential commodity for which the “user pays” currently operating [in Victoria] is totally inappropriate and a violation of the UN Declaration of Human Rights’. The Cain Labor government (1982-90) undertook significant reforms. Regressive tariff structures were abandoned in favour of progressive inclining block tariffs and no fixed charges; financial rebates (government concessions) for gas and electricity were rationalised and extended; a retrofit program undertook energy efficiency renovations and appliance replacement for low-income households; the credit management culture of the utilities was addressed by the formalisation of rights and obligations, and improved payment options; and an emergency relief grant program for one-off crisis or capital requirements (such as replacing a hot water service) was established. Energy efficiency contributed to broader SECV ‘least cost planning’ objectives that sought to delay the requirement for new generation and system augmentation. It was also recognised that disadvantaged groups were frequently marginalised politically. In the contestation over the SECV, low-income households were not necessarily heard. Accordingly, the government made funding available for advocacy.

Briggs (2000 [1969]: 20) noted a bifurcation in thinking around welfare that differentiated between the older socialised infrastructure services and the newer ‘human’ services: ‘Public health, in the administrative sphere of drains, sewers and basic “environmental” services, has been taken outside the politics of conflict…but personal health services remain controversial’. Accounts of the welfare state in Australia and the UK almost never cover utilities. Indeed, when T. H. Marshall, ‘father’ of the UK welfare state, delivered his famous lecture on Social Citizenship and Class (Marshall 1950) on why socio-economic entitlements are as important as civil and political rights, there was no mention of utilities, although housing, health, education and even legal services were discussed. Marshall may have assumed that existing socialised services such as gas (which had been extensively municipalised in the UK by the beginning of the twentieth century) were no
longer sites of social conflict because of their public status. Yet as late as the 1970s in the
UK and Victoria, fuel poverty campaigns were challenging the perception that public
ownership automatically addressed welfare needs (see for example Chesshire’s (2002)
review of UK fuel poverty literature, which dates some works to the 1960s; in Victoria see
Deasey and Montero 1983, Kiers 1983, CURA 1982). It is quite extraordinary that the
social impacts of public energy policy in welfare states could have been ignored for so
long. In contrast, the US, with extensive private ownership of electricity businesses, has a
history of attention to the social correlates of energy use.

Titmuss (2000 [1967]: 46) argued that support for the welfare state arose from the idea
that transfers could be compensatory in nature relating to ‘disservices, for social costs and
social insecurity’ that are ‘socially caused’, and that ‘they are part of the price we pay to
some people for bearing part of the costs of other people’s progress’. The difficulty in
Victoria is that the state has rarely acknowledged the ‘disservice’ that arises from
electricity production and use. This was only belatedly recognised during the Cain
government years and is now largely forgotten or ignored. Accordingly, the principle being
carried forward into the regulatory arrangements for the market is the same narrow and
anti-democratic interpretation of progress (based on growth) that characterised the SECV
prior to the reforms of the 1980s. In contrast, the UK, from which Victoria initially took its
neo-liberal reform model, subsequently rediscovered the social correlates of energy use
and has developed a Social Action Plan to eradicate fuel poverty.

3.5 Conclusion

In this chapter I have suggested that in Victoria domestic consumption of electricity
reflected the specific requirements of a vertically integrated electricity industry in its
establishment phase, which in turn was established to meet, in particular, the needs of
urban manufacturing. The SECV had to achieve economies of scale and therefore
promoted domestic consumption. This strategy in turn necessitated prices that could
compete initially with other fuels and were affordable for the average male-headed
household. As the first La Trobe valley generator was funded through government budget
outlays, customers contributed through taxation as well as through purchasing electricity.
The burden fell disproportionately upon lower-income households.
By the 1960s the SECV was a significant source of tax revenue for the state government. This exacerbated already inequitable domestic tariffs. Equity and pricing of electricity had been subject to public debate but it took until the 1980s for the welfare function of electricity to gain sufficient political attention to support reform. Until then the dis-service that arose from inequitable energy policies was largely ignored. Utilities in Victoria and the UK took their own historical trajectory to that of the welfare state, and exactly why they should have done so warrants more attention than can be given here.

Throughout its history, the production and delivery of electricity in Victoria has been orientated to the needs of the industry itself and its industrial and commercial customers. Decisions regarding supply have frequently been controversial and the SECV was subject to extensive public scrutiny and opinion. Economic rationality was often tempered by political considerations that reflected the importance of the service to all Victorians and the power such a monopoly could yield. A large degree of controversy therefore surrounded the Kennett government’s decision to privatise the industry and introduce competition. To get from a vertically integrated public monopoly to full retail competition required a long-term strategy that contained certain ideological building blocks. Political opposition meant that it was not simply a case of putting economic theory into practice. For example, on the one hand, the maximum uniform tariff (MUT) was always going to end; on the other, households were offered a rosy future based on six years of mandated price cuts (incidentally returning only what customers were paying as a result of price hikes in 1992-93). Reform blueprints named groups of customers who paid ‘unfair’ cross-subsidies whilst studiously omitting to name those who would be negatively affected by their removal (OSOE 1994: 1). In the first part of this chapter I outlined how the government addressed one crucial issue – unwinding the traditional rural cross-subsidies – by careful staging and political manoeuvring. In the next chapter I explore how another crucial issue – subsidies to poorer households – was handled. The Kennett government also largely achieved its objective of allocative efficiency as payment of subsidies was transferred from the industry to the budget sector.

The following discussion is important because the changes were highly contested at the time and the debate reflects the ideological positions that later become clearer as models of social protection. The neo-liberal proposition is that welfare of society is improved by removal of cross-subsidies that distort the efficient allocation of resources. Ideally, in this
view, subsidies should be budget funded and provided as cash lump sum transfers. This then permits consumer preferences to direct the market in the allocation of these resources (Evatt Research Centre 1988: 103). The introduction of CSOs in the Victorian electricity industry implemented the first part, but to date the budget funded transfer still supports specific consumption (electricity). This indicates that one building block was put in place. We can only speculate now on whether or not the Kennett government would have withdrawn specific concessions in favour of some kind of single cash grant or voucher system. I would suggest that the impure model now in place reflects political sensitivity to an established entitlement.

The discussion is also important because the orthodox economic argument for the removal of subsidies relies on the assumption that competition ensures the most efficient allocation of resources. I make the argument here that market segmentation limits, in a not insignificant way, the scope for competition to occur. How this happens is detailed in chapter 8. However, it is necessary to make the argument at this point (Section 4.5) because CSOs are the neo-liberal alternative to universal service provision, yet they may be a far less efficient way of addressing equity issues.
Chapter 4: The neo-liberal vision: Markets and community service obligations

4.1 Introduction

In the last chapter I showed how the needs of the electricity industry dictated policy relating to domestic usage. The monopoly nature of the industry, the essentialness of the service, and its redistributive impacts naturally and rightfully ensured that production and delivery of electricity would be a highly contested political matter. In this chapter I explore how political contestation over the distributive impacts of reform had to be addressed in order to progress the restructuring of the industry and permit the introduction of a market. Rural cross-subsidies and domestic pricing and related programs were particularly targeted for change and were accordingly the subject of community concern.

The public policy reform literature of the 1980s and 1990s, however, contains little detail in relation to domestic consumption of electricity. The nature and scope of social entitlements were debated at a more general level. While a market would replace universal service, the social welfare transfers that had been a part of the public electricity monopoly were discussed in conjunction with programs in other industries as if they were generic programs. In this way, specific needs (such as for warmth) could be addressed by a generalised policy tool – the CSO – which conceptualised under-consumption as an income issue unrelated to the specific good or market. This concession to social welfare did not convince consumer and welfare advocates.

4.2 Public policy literature

1994, Stockdale 1994, 1997). This reflects and is supported by a similar range of corporate, academic and other interests (see for example Porter 1995, Tasman Institute 1991, Hunt and Shuttleworth 1996, Thomas 1996, Mielczarski and Michalik 1998, Edwards 1995, Allington 1995, Richardson 1996). Quiggin (1996: viii) describes this as the consensus held by the policy elite of ‘leading politicians and bureaucrats, the economists who advise them, economic journalists and private sector think tanks’. Where problems are identified or emerge, they have tended to be over-looked, ignored or explained away as only temporary issues. There is, however, some notable work arising from parliamentary inquiries that provides dissenting views. Critical responses to market reform from particular regions, unions or consumer groups dissenting from neo-liberalism were seen as selfish rent seekers (see for example Officer 1993, 1996).

This public policy literature pays very little attention to domestic users of electricity, in part as a direct result of its adherence to neo-liberalism. The purpose of micro-economic market reform is to capture economic efficiencies that occur when competitive pressures are brought to bear within the industry. This guarantees cost savings and lower prices, and hence the delivery of benefits to households. There was little concern as to who the losers in competition reform may be, or why. Quiggin (1996: 44-5) attributes this to the dominance of efficiency in welfare analysis of policy and the inappropriate exclusion of equity considerations. The Industry Commission’s (1995) assessment of the benefits arising from the Hilmer Report (National Competition Policy reforms), with predicted gains of $23 billion (in 1993-94 dollars) and tens of thousands of new jobs, was generally accepted by the Commonwealth and state governments as evidence of the benefits of competition. The basis for this claim was the output of a theoretical macro-model of the Australian economy. Quiggin (1997), in particular, challenged the assessment, with the effect that the Productivity Commission subsequently revised the figures downwards. In terms of the electricity sector, important variables such as changes to tariffs (reflecting the dismantling of cross-subsidies) were excluded. This Industry Commission report nevertheless was probably the single most important evidence used by the reformers to

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24 A rare dissenting opinion was that of the Queensland government (Beattie 2001) which argued that FRC would cost more than projected benefits. 
25 For example, Victoria experienced power shortages in the summer of 1999-2000. At the beginning of 2002, high wholesale prices resulted in the deemed and standing offer tariffs rising, but customers were told that the market could result in lower prices and appropriate levels of investment in the system. When such events occur, the response has been to explain them as short-term aberrations, and that the market will deliver long-term efficiencies and reduce prices.
justifies wholesale reform of electricity in Australia. Both the Industry Commission (1996) and the Productivity Commission (2002) have reviewed the impact of reform on domestic electricity prices, but in each case methodologies were employed that avoided data which would have demonstrated less positive views, an issue that is taken up by Finn (2003). The Productivity Commission study, for example, surveyed electricity prices in capital cities. For Victoria, this gives a misleading impression of average prices as rural/ regional prices rose significantly. Further, the study included budget funded measures such as the winter energy bonus and the winter energy concession, which may alter the end price to the consumer but do not reflect performance of the industry.

The homogeneity of the governmental literature reflects a general adherence to the precepts of neo-liberalism or, as it is more commonly known in Australia, economic rationalism. Pusey (1991) maintained that this had become the ruling ideology amongst bureaucrats in Canberra. Whitwell (1998: n.p.) noted that economic rationalism has been furiously debated but is often left undefined. He cited a range of definitions: ‘dogma which says markets and money can always do everything better than governments, bureaucracies and the law’ (Pusey); ‘a profound suspicion of all forms of state intervention in economic life and an almost equally profound faith in the beneficence of unfettered, or almost unfettered, market forces’ (Manne); ‘markets usually provide more satisfying answers to questions of choice, consumer preference and so on – and in doing so, provide a more rapidly advancing level of total well-being for all concerned – than decisions by diktat’ (Stone). In Whitwell’s own definition, economic rationalism ‘draws on neoclassical economic theory…the unregulated capitalist economy is assumed to have an inherent tendency towards equilibrium: a situation in which demand and supply are in balance’. Economic rationalists such as Moore (2000: n.p) often downplay market failure, stressing the greater dis-benefit that arises from ‘governmental failure’. Nevertheless, on the spectrum of neo-liberal thought, Moore argued that most recognised some need for government intervention: ‘Economic rationalists fully agree that governments should assist those who are on low incomes and/or are disadvantaged because of some incapacity’, however, ‘they are also concerned at the many adverse effects that can and do arise from the redistributive process’.

Whitwell also cites a comment by Blandy that economic rationalism ‘is nothing but mainstream economic knowledge’. Burchell (1998) agrees, arguing that opposition to
economic rationalism over-emphasises the newness of the use of economics in public administration. Quiggin (1996: 44-5) would not disagree but sees it as diverging from traditional welfare economics by selecting efficiency over equity. Nevile (1997: 4) notes that many economic rationalists 'present their policy recommendations as no more than the logical consequences of orthodox economics', but argues that ‘the policy prescriptions of economic rationalism depend more on the values held by economic rationalists than on the theorems of economics. In any case, orthodox economics is very clear that policy recommendations must rest on both economic analysis and a set of values’.

While the hallmarks of neo-liberalism may be an emphasis on the efficiency of markets, the inefficiency of governments, individual freedom and free trade, Argy (2003: 2) warns of the need to distinguish between ‘economic liberal reform which is about better ways of doings things and is efficiency driven and hard liberal reform which is about scaling down social and environmental goods and is driven by “small government” ideology’ (author’s emphasis). Stretton and Orchard (1994: 1) argue that, for this latter group of ‘public choice’ theorists, ‘there can be no good ways to allocate public goods, manage public industries, arrive at collective social purposes, or govern democratically’. Australia’s policy elite has been influenced by the claim that there is a need for microeconomic reform and a roll-back of the state. In terms of domestic supply of electricity, both ideologies were at work.

The origins of the neo-liberal orthodoxy are to be found in the Chicago School of Economics and in the works of philosopher-economist Friedrich von Hayek and his student Milton Friedman (Kendall 2003). Cockett (1995: 2) contends in his study of right-wing think tanks that the rise of neo-liberalism was the result of an extended campaign or ‘counter-revolution’, while George (1999: 2) sees the establishment a neo-liberal orthodoxy as the result of ‘a huge international network of foundations, institutes, research centres, publications, scholars, writers and public relations hacks to develop, package and push their ideas and doctrine relentlessly’.

In Australia right-wing think tanks and the financial media, especially the Australian Financial Review, have been important in promoting market doctrines (Kelly 1992, Greenfield and Williams n.d.). Kelly (1992: 34) views the ‘revolt’ against liberalism as coming from a kind of right-wing ‘counter-establishment’ comprised of parliamentarians, academics, business people and the ‘economic community’. Quiggin (1996) traces the
influence of the Brookings Institution, an American neo-liberal think tank, on Australian micro-economic reform debates of the 1980s, and the part played by government agencies such as the Industry Commission and the Bureau of Industry Economics.

Ernst (1993) argues that the Kennett government drew heavily upon the best-selling American public choice treatise *Reinventing Government* by Osborne and Gaebler (1992) for the legitimisation of its radical program. At the time of its election, only very broad statements were available regarding the impact of market reform of electricity on households. Very little substantive analysis was undertaken then – or indeed since – about what a domestic retail energy market would mean. Nevertheless it was clear that cross-subsidies would be targeted for dismantling. These were primarily geographical subsidies favouring rural consumers and inter-class subsidies favouring households. In addition, electricity businesses were to be stripped of social programs to enable them to be put on a purely commercial footing.

Nevertheless, adherence to neo-liberalism as a public policy position within government was not total. In 1995 the Department of Health and Community Services (later the Department of Human Services) which administered the state concessions program acknowledged that corporatisation and privatisation were impacting on its ability to maintain a social safety net (Piper 1995). The department’s Concessions Unit undertook a formal review (Frameworks Consulting 1997) and commenced periodic surveys of household energy and water consumption (Reark Research 1996, Roy Morgan Research 2002). It seems clear in retrospect that the unit adopted a defensive position in anticipation that social protections would be wound back.

### 4.3 The Kennett government reforms

One of the first acts of the Kennett government in reforming the electricity and gas industries was to remove funding from Victoria’s statewide utilities advocacy organisation, the Energy Action Group.26 The Office of the Regulator-General (ORG) subsequently established a Customer Consultative Committee to:

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26 This had been funded for ten years by the Cain and Kirner Labor governments, and had been highly influential in tariff reform, establishing the Home Energy Advisory Service, regularising concessions, and developing codified rights and responsibilities of customers and the SECV.
assist customers to make their views known to the Office and to generally participate in the reforms proposals as it affects them…The Committee also provides a forum in which customer representatives can exchange information on their needs and, through the Office, make those needs known to the businesses within the industries (Davey 1995: 6).

The Energy Action Group was excluded for some years from participating in this committee. Reform entailed a new set of institutional arrangements, not just establishing a market, but also seeking to reshape politics through such mechanisms. The neo-liberal view held that there was no need for customers to act collectively in their interests when a market existed. Moran (2001) claimed that the market was more democratic, and he associated political action or ‘voice’ with vested interests:

Associations claiming to represent consumer interests rarely have the appropriate accountability or governance structure and are often dominated by and express the views of a small clique. If those groups are given preferred access, this could actually undermine consumer interests…In well-functioning markets, such as the emerging gas and electricity markets, it is retailers that represent the interests of consumers; they do so not out of benevolence but out of necessity, since the retailer failing to supply goods and services that meet consumers’ needs will lose market share and eventually be forced out of business.

A transformation of the magnitude sought by the government was always going to be difficult to achieve in a short period of time. A key obstacle was the political interest of the National Party as ‘representatives’ of rural electricity consumers. The Liberal/National Coalition almost collapsed in 1994 over the issue of rural electricity prices (Forbes 1994, Woodward 2004). The resolution was a short-term solution, ultimately not favourable to rural interests (see Section 4.4). The impact of rural interests on political processes nevertheless has remained significant in the area of energy policy. With the election of a Labor government in 1999, a taxpayer funded rural cross-subsidy (the Special Power Payment) was instituted, later becoming the Network Tariff Rebate. These have existed concurrently with the mechanism to unwind the traditional urban customer funded subsidy.
4.4 Managing the end of the maximum uniform tariff

The MUT had meant that a customer in Swan Hill (rural) paid the same price for electricity as a customer in Collingwood (inner urban). As it costs more to supply rural consumers, city consumers cross-subsidised their country cousins.

Table 1: Customer distribution across Victoria and sales (in $1993-94)

<table>
<thead>
<tr>
<th></th>
<th>No. of customers</th>
<th>Domestic sales $m</th>
<th>All other sales $m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rural customers</td>
<td>984,017</td>
<td>556</td>
<td>676</td>
</tr>
<tr>
<td>Urban customers</td>
<td>978,776</td>
<td>537</td>
<td>994</td>
</tr>
</tbody>
</table>

Source: OSOE (1994b)

This urban/rural cross-subsidy was effectively abolished by the government in 1995 when it issued the Electricity Industry Tariff Order. As it noted, charging the real cost of supply would mean significant price increases for rural customers (Minister for Energy and Minerals 1994). The cross-subsidy was valued at $100 million per year (OSOE 1994a).

The government said at the beginning of the reform process that ‘Government policy is to ensure minimal differentials in delivered energy prices between similar customers in metropolitan areas and rural and farm customers’ (Swier 1995) (my emphasis):

Uniform tariffs are incompatible with the competitive basis which is at the very heart of Government’s policy objectives...The incentives and economic signals intended to be provided by the ‘Wires’ function of the Distribution Businesses would not be meaningful if arrangements were made to equalise distribution costs outside any one Distribution Business (Minister for Energy and Minerals 1994).

The intention was to maintain retail uniform pricing arrangements for franchise customers until 2000 but unwind the network cross-subsidy over a longer period.

The government opted for ‘grid equalisation fees’ to continue the cross-subsidy. The transmission system operator, PowerNet Victoria (now SPI PowerNet), is required to over-

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27 ‘Energy’ refers to the electricity consumed, the cost of which reflects wholesale prices. ‘Energy only’ prices exclude transmission and distribution costs.
charge the urban distribution businesses (DBs) and under-charge the rural DBs. This transfers $23.95 million from city to rural consumers each year. As the fees are set in nominal terms, inflation acts to unwind the subsidy over time, and it is now very small.

In 1994 the government ‘wrote down’ the asset value of Eastern Energy (now TXU) and Powercor, the rural DBs, ascribing a lesser book value to them, and ‘wrote up’ the asset value of Citipower, United Energy and Solaris (now AGL), the urban DBs (Swier 1995). The government said the write-down was:

the equivalent to a very substantial upfront subsidy to rural and farm consumers reflecting a determination that prices should be comparable to those paid by residential urban consumers (Minister for Energy and Minerals 1994).

The impact of the asset revaluations was to alter future distribution prices, as the value of the DBs’ asset base forms a major component (building block) of the revenue allowances determined by the regulator (Stockdale 1995). With their asset base artificially reduced, the rural DBs would be constrained in their ability to raise prices to reflect costs. The urban DBs, however, are effectively permitted to over-charge. The Trade Practices Commission (1995a: 9) raised questions about the government’s handling of the cross-subsidy:

Cost reflectivity would suggest that it would be better to use some means other than price distortions to deliver support to target groups…the CPA [Competition Principles Agreement] sees a continuing role for CSOs…provided the instructions are explicit and the CSO is transparent.

This knowledge should have sent a market signal to temper the sale prices of Eastern Energy and Powercor, although it also made the urban DBs more attractive. For a government selling assets, it was a case of swings and roundabouts: what they would lose on one deal they would pick up on the other.

28 A leaked draft cabinet paper, Electricity Supply Industry Privatisation Strategy, dated 17 January 1994 also indicated concern that the rural businesses were not as attractive propositions for privatisation. The fact that one set of businesses were written up and the other written down indicates that this particular revaluation was not aimed at exploiting Commonwealth tax deductibility provisions which later became an issue (Skulley 1997). The paper does not mention this latter issue.
As regulated monopolies, the DBs are subject to an independent assessment of their revenue needs (the ‘revenue allowance’). The regulator uses the asset valuation as the basis for its determination in this regard. The purchase of new assets and asset replacement also act to mitigate this artificially determined valuation. The revenue allowance in turn represents the global amount that the DB is permitted to recover from its customers through prices. This is how the asset valuation impacts on future pricing. A lower valuation reduces the allowable revenue and consequently restricts the ability of the DBs to charge higher prices. But the impact of revaluation itself is not permanent.

It is not surprising that the Melbourne-based DBs have held their value in subsequent trade sales. The fact that the sale prices of Eastern Energy and Powercor were substantially higher than the Treasurer, Alan Stockdale, expected probably indicates that buyers may not have understood the implications of the asset revaluation, chose to ignore its message, or thought the projected earnings were reasonable despite the immediate constraints on revenue.

One could speculate on whether the Kennett government envisaged falling ‘energy only’ prices as being sufficient to take the political heat out of the first steps towards cost-reflective pricing for networks. Just as it left office in 1999, wholesale electricity prices had reached the lowest point since the reforms were introduced. While it was expected that prices would fall and rise in relation to excess and shortages of generation capacity, the reformers thought long-term energy prices would fall, and households and small business would share in the bounty of competition.

4.5 The shift to community service obligations

4.5.1 Introduction

The aim of the Kennett government in undertaking the reforms to the electricity industry were to ‘create an internationally efficient industry providing the lowest possible costs to customers; empower customers by offering choice and service; and reduce the public debt burden on Victorian taxpayers’ (OSOE 1994b: 2). The rationale was that ‘a market-based industry structure which promotes competition will create the incentives necessary to stimulate the superior outcomes needed by Victorian customers and taxpayers’ (OSOE
1994b: 6). Liberal economic theory posits the customer as an active and empowered consumer. The sovereign consumer exercising choice drives allocative efficiency (through price signals) and productive efficiency (through market disciplines) (Webber and Ernst 1996). The government also argued that ‘[p]rivate ownership has a number of benefits over public ownership including clearer goals for management, reduced opportunity for non-commercial decision making, strong capital market disciplines and improved performance incentives for staff’ (OSOE 1994b: 14, my emphasis). The neo-liberals held that conflicting management objectives, such as profit-making and social welfare or regional development, could not be balanced to achieve both effectively (Public Bodies Review Committee 1991, Allan 1994, Borthwick 1994).

Where concessions to social welfare are unavoidable, neo-liberals have argued that the market must be ‘free’, and social support must be funded directly from government budgets and means-tested. In Australia, the tool to achieve this objective has been the ‘community service obligation’ (CSO), a term which Baird (2001) sees as unique to Australia and our form of government.29

The introduction of CSOs occurred within a political context in which some neo-liberal reformers questioned the need for any kind of regulation, including a right of supply. For example, Jurewitz (2002) argued:

> The normal assumptions are that consumer protection is best achieved by active competition among suppliers and that no single supplier or group of suppliers is needed to provide safety net service at regulated prices. Is electricity different? One response is that there is no basic difference between electricity and other necessary commodities – such as food – for which there is no regulated default provider.30

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29 The UK has a similar Public Service Obligation for transport services (Bradshaw 1998: 176)
30 The closest scenario was California after deregulation. Households were able to shop around for retail supply or they could be on a default provider contract. In two of the former franchise areas, the default tariffs were not price capped (that is, they did not have a maximum price). When the wholesale market experienced highly volatile prices, the increased prices were passed through to households. The resulting price shocks caused enormous political controversy and resulted in a re-examination of the reforms. The California Public Utilities Commission makes the following statement on its website: ‘Because of flaws in the deregulation process, the…[commission] suspended direct access in September 2001. Other problems, too numerous to explain here, also occurred. Many periodicals and books have examined and analysed what went wrong with the state
An argument was made in Australia that there ‘can be no obligation to supply’ (Hunt and Shuttleworth 1996: 60). Alan Asher (1995: 4), a commissioner of the Australian Competition and Consumer Commission, said: ‘it is not clear to me that utilities will have any obligation to supply domestic customers when (and if) a franchise market completely disappears’.

Historically in Victoria, as Cornwall (1994: 8) outlines, there have been ‘few actual rights about supply of water and energy’; rather, there were ‘informal arrangements between the State government and the public authorities’ that ‘ensured access to essential services for most Victorians’. There was little in the public policy literature during the 1990s explicitly discussing whether or not there should be an obligation to supply. At this point it should be mentioned that obligation to supply does not mean a guarantee of physical supply as this has not been regarded by government as possible31 (Cornwall 1994). The obligation to supply refers to the obligation of a utility to offer access to domestic customers. An obligation to supply that intended to provide universal access would also seek to ensure that, once connected, the customer could stay connected, disregarding incapacity to pay.

In 1997 the ORG replaced the Electricity Industry Customer Charter with the Electricity Industry Supply and Sale Code. This provided that domestic customers could avoid disconnection for non-payment by accepting an instalment plan. Retailers were required to account for the customer’s capacity to pay in determining the instalments. In effect, this provision is to guarantee affordability, and although it is extremely doubtful that this was the intention (there is further discussion on this point in Section 8.3), it provided at law a formal entitlement. When this is packaged with the obligation placed on retailers later by the Bracks government to offer supply to domestic customers, the reforms inadvertently or not provided for the strongest legal entitlement to supply which Victorian households had ever had. The obligation to offer supply is explained by the ORG (2000a: 1):

deregulation efforts. We’d recommend investigating those books and magazines at your local public or school library’ (<www.energy.ca.gov/restructuring/>). See also California’s Electricity Deregulation Crisis: A National Warning (<www.aflcio.org/aboutaflio/ecouncil/ec0215b2001.cfm>), Energy Resource Centre (<www.rppi.org/electricity/>), and What Has Been the Fallout of Electricity Deregulation Fiasco in California? (<www.newsbatch.com/electric.htm>).

31 It may not be possible to ensure that sufficient generation or network capacity always exists. For example, severe weather events can damage networks.
The statutory deregulation of the Victorian electricity market alone may not be sufficient to ensure that all customers can exercise choice as to their retailer. In practice, for a variety of reasons, certain customers may find it difficult to obtain offers of supply terms from retailers. To ensure that all users have access to offers of supply, on terms that do not take advantage of this situation, the Electricity Industry Acts (Amendments) Acts 2000 provides a requirement for retailers to offer to supply and sell electricity on terms published by the licensee in the Government Gazette.

The creation of default and safety net suppliers also arose presumably as a result of the government not wanting, in the short term at least, to physically disconnect households as a means of forcing a migration onto market contracts. But this is moving too quickly into the future, as the question of obligation to supply in a market context was still years away for the Kennett government. As explored in detail in Chapter 12, the reform project in Victoria needed to overcome deeply entrenched popular views regarding expectations about entitlements. Maintaining some of the existing social protections worked to partly defuse opposition to change.

The initial steps in moving from an informal universal service to the market focused on what were regarded as uneconomic cross-subsidies and social programs. In the short term, funding for advocacy and energy efficiency retrofits was withdrawn and there was a return to inequitable tariff structures. In the wake of privatisation, the energy retailers returned to punitive credit management practices (Romeril 1998). These changes, however, only seriously disadvantaged a small proportion of customers. The effect of the unwinding of the rural cross-subsidies would only gradually be felt. Uptake of concessions, however, was and remains a significant budget outlay.\(^{32}\) The concessions remained, but they became CSOs.

In the transition period, ironically, domestic electricity customers gained stronger legal entitlement in regard to supply. This represents a quite contradictory element in the reforms, although it was unlikely that the obligation to supply would have continued under the Kennett government if they had remained in power. At the same time, other

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\(^{32}\) The provision of concessions for energy was initially paid for by the utilities but, as a part of the Cain government’s ‘Family Pledge’ commitment in the 1980s, the cost of concessions was transferred to the budget sector.
entitlements were reframed. What this reconceptualisation did not allow for, although it is implicit in some of the arguments put forward by neo-liberal reformers is that market power is likely to be exercised in relation to economically disadvantaged customers. In the next two sections I explore the development of the CSO concept and its application to the Victorian electricity industry. I introduce within the next section the argument that CSOs in essential services markets are unlikely to be successful because, within the current conceptualisation, they only address the customer’s lack of purchasing power. The essentialness of the service has ramifications for the customer’s market power and hence the CSO should also compensate for market power issues.

4.5.2 CSOs, universal service and market power

CSOs are defined as the delivery of a non-commercial service associated with a social purpose that is identified and mandated by government (Industries Assistance Commission 1989, Economic and Budget Review Committee 1991, SCNPMGTE 1994, Industry Commission 1991a, 1997, SCFIPA 1997, OSOE 1994a, 1994b, 1994c, Borthwick 1994, Allan 1994, Department of the Treasury 1998). The National Competition Council, for example, defined them as:

goods or services that governments require specific government businesses (and sometimes specific private enterprises) to provide to sections of the community and that would not be provided under commercial arrangements (Trembath 2002: 32).

The concept of CSOs has an unmistakable pedigree, and did not take very long to become an established economic concept. The Consumers Telecommunication Network argued that the term arrived in the ‘Australian telecommunications discourse’ in the mid-1980s, with the ascendancy of economic rationalism ‘as the dominant discourse of Australian economic and social policy’ (Wilson and Goggin 1993: 8). It identified the Bureau of Transport and Communication’s 1989 report, The Cost of Telecom’s Community Service Obligations, as a controversial effort to have CSOs adopted as public policy. CSOs certainly had a prominent place in the Industries Assistance Commission’s (1989) Inquiry into Government (Non-Tax) Charges, although they did not appear in Promoting Competition in Australia, despite this report being concerned that cross-subsidies by public enterprises could result in the unintended ‘misallocation of resources’ (Economic Planning...

It was argued by market reformers that existing entitlements (for example, in the electricity industry, uniform tariffs, pensioner rebates, obligation to connect and connection subsidies) needed to be defined, identified and costed, and preferably funded by direct budget outlays. This would ensure accountability, transparency and better targeting of services to those who genuinely needed them (OSOE 1994b, Allan 1994, SCFIPA 1997, SCNPMGTE 1994, Borthwick 1994, Department of the Treasury 1998, National Competition Council 1999, SSCSECNCP 2000, Industry Commission 1997, Officer 1996, SSCIST 1992). The Victorian government argued:

Government businesses have always quite properly carried out non-commercial functions on behalf of Government as owner. This resulted however in a lack of clear signals as to the cost of these programmes to the community. Hidden costs of social programmes contribute to poor accountability mechanisms and encouraged the waste of resources through poorly designed or targeted programmes. Failure to separate out the costs of social and community programmes may also have provided an excuse for Government business inefficiencies, since a poor operating return could be defended by reference to the cost of meeting a vague social responsibility (OSOE 1994c: 24).

The rationale for review and reconsideration of entitlements was to eliminate economic inefficiency (SSCIST 1992, SCNPMGTE 1994, Department of the Treasury 1998). The Industry Commission (1991b: 120) argued:

Cross-subsidies result in allocative inefficiency. Those whose consumption is taxed restrict their usage of the product, even though they may value the consumption of
additional units more than the cost of producing them. Consequently, there is a welfare loss. Conversely, those who are subsidised are encouraged to expand their use of the product beyond the point where the value they derive from the good is equal to its cost of production. Again, there is a welfare loss.

The costs of CSOs were also raised and the suggestion was made to competitively tender out such services\(^{33}\) (Industry Commission 1997, Allington 1995, Officer 1996). Another theme was that not only does the removal of non-commercial entitlements from the operation of GTEs\(^{34}\) provide a single minded focus on commercial activities, but it also removes the conflicts which ministers have in overseeing GTE performance on the one hand and the delivery of social benefits on the other (Public Bodies Review Committee 1991, Borthwick 1994, Allan 1994).

Yet beyond these apparently persuasive arguments there remain unanswered issues regarding the efficacy of CSOs in overcoming market power issues when the service in question is an essential one.

In the context of market reform, it was felt by many that defining, identifying and increasing the transparency of CSOs was merely a stage on the way to reducing and eliminating benefits (Rix 1994, Quiggin 1996, Catholic Commission for Justice, Development and Peace n.d., Romeril 1998). The axing of the Home Energy Advisory Service was considered as evidence of this (Cornwall 1993, Cornwall and Walker 1994, Siemon 1995). As an administrative lawyer, Aronson (1997: 67) held suspicions that CSOs are easily ‘postponed or avoided’, and highlighted judicial decisions in the telecommunications sector that supported this contention: ‘The court stressed that the relevant CSO was better regarded as an aspirational ideal, than a legally enforceable obligation’. The Victorian parliament’s Public Bodies Review Committee (1991) acknowledged that CSOs would be threatened by budget cuts. Sylvan (quoted in Cornwall 1993: 8) said that ‘governments administering cross-subsidies may be tempted, under economic difficulties, to simply cut… [CSOs] are less vulnerable when they are in the utility’.

\(^{33}\) In Victoria, energy concessions (CSOs) are delivered through commercially based contracts between government and private electricity retailers, on a fee for service basis. The contracts are not public.

\(^{34}\) In this era GTEs became more commonly known as ‘government business enterprises’ (GBEs).
Explicit in the conflict over the introduction of CSOs were deep philosophical concerns regarding the impact on social solidarity and social inclusiveness (Siemon 1995, Pike 1995). On the one hand, neo-liberal reformers understood reform of utilities as enabling enterprises to function in a purely commercial way. On the other hand, critics of market reform asked: ‘What is it that these providers of essential services supply, if not welfare?’ (Fitch, quoted in Webber and Ernst 1996: 139). When the Public Bodies Review Committee produced *Out on the Table*, rural MP Barry Steggall issued a minority report, questioning the rationale in defining some legislated requirements of GTEs as CSOs but not others. He rejected the idea that activities legislated by parliament and funded by budget appropriations could be unilaterally ‘demoted’ in status by the executive. As a rural representative, he understood the threat to rural cross-subsidies.

Siemon (1995) argued that there was greater efficiency in internalising the income security function of social obligations because some of the costs were not being accounted for as they were being off-set onto charities in the form of emergency relief. He supported Kiers’ (1983) contention that, far from being neutral or benign, utilities actively redistribute resources and have substantial welfare impacts. Kiers (1983: 28) had made the point much earlier regarding the seeming contradiction between providing income support but allowing utilities to have regressive pricing and customer service procedures because they ‘undermine the objectives built into the social security system’. Dufty (1995a: 9) challenged whether it is actually possible to define and separate CSOs from business practices. Some NGOs argued that cross-subsidies were the most efficient method of delivering the desired welfare or community outcome and suggested that CSOs do not identify all benefits or take account of all those who should receive them, for example, children (Public Bodies Review Committee 1991). The Council for Ageing submitted to a Senate inquiry that CSOs are not USOs, but a lesser entitlement (SCFIPA 1997). Martin (1996: 116) stated:

> the definition of what constitutes a CSO creates winners and losers. CSOs become a welfare issue with some included (pensioners) but others excluded (low-income families and individuals outside the definition). The risk is a diminution in community spirit and a diminution in the concepts of the ‘public utility’, essential services and service to the community.
Martin goes on to quote the submission by National Anglican Caring Organisations Networks to the 1995 House of Representatives Standing Committee on Banking, Finance and Public Administration’s Inquiry into Aspects of the National Competition Policy reform package:

the Steering Committee on National Performance Monitoring (1994) now defines community service obligations, not in terms of the type of activity in the community, but by the type of ‘economic concession’ it constitutes – by the type of ‘loss’ the government business sustains.

Baird (2001: 54), in seeking to develop an agreed accounting standard for CSOs, argued that private organisations could not deliver CSOs. He maintained that activities carried out by private organisations for social purposes required by government would have to be on a commercial, contractual basis, and hence ‘it is expected that they would not be described as CSOs’. Baird’s argument reminds us that CSOs were conceived firstly as providing for transparency of GBE costs and secondly (as a result of the first) as improving economic efficiency (of GBE services) through pricing signals. The usage of the term CSO for private sector delivery of services infers an obligation where one does not exist, and this is what upsets Baird. He was concerned moreover that the accountability of private organisations was less than that of the public sector. Not only did an activity have to be carried out by a public agency but, for Baird’s proposed definition, the service is required to be ‘essential to the community…it may not be viewed as being essential if the community can survive without the service’. CSO is a term that implies continuity of an entitlement or necessity when services are moved from public to private provision, when in fact the hypothecation between the service, the need and its funding is severed. I would suggest that such hypothecation in the electricity industry has been very important historically in terms of generating political support for entitlements.

It is also uncertain whether the difference between ‘community service obligation’ and ‘universal service obligation’ was understood by those who implemented competition policy, yet the difference is a substantial one. For Chisari and Estache (1999: 4). a USO

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35 Jeanette McHugh (1995), federal Minister for Consumer Affairs in the Keating government (1993-96), declared that utilities should have ‘universal’ and ‘community service obligations’, and should not discriminate against those who suffer financial, physical or geographical disadvantage. She also wanted her own consumer protection obligations (CPOs). The mechanism she proposed to use was
‘encompasses the idea of giving all community members the possibility of gaining access to product consumption by paying a sufficiently low or affordable tariff’. They make a distinction between universality based on affordability, and obligations relating to non-discriminatory access. The latter they refer to as ‘obligatory service’ which ‘occurs when a company is asked to allow access to its services to all users who wish to join the supply system at the ongoing tariff or when a user is required to consume a service’. Provision of telecommunication services to rural and remote customers in Australia is an example of the application of the obligatory service concept. The separation of the two, as Chisari and Estache admit, is commonly conflated. The concept of access is in its own right intimately connected to affordability. Colton (1998) states:

‘affordability’ includes both an ‘absolute’ (‘to have enough or the means for’) and a ‘relative’ (‘to bear the cost of without serious detriment’) component. According to the FCC [Federal Communications Commission], both the absolute and relative components must be considered in making the affordability determination…service cannot be considered to be ‘universal’ if customers who are succeeding in paying for that service nonetheless cannot pay for it ‘without serious detriment’.

Electricity CSOs could be viewed as an example of ‘vertical equity’ as they are means tested rebates. Vertical equity is where those with greater capacity to pay should pay more, in order that those with less capacity can contribute less. CSOs involve subsidisation of the user, and the compensation is for lack of income. Despite this, the market gives precedence to the idea of ‘horizontal equity’, which requires that all like customers should be treated the same. In Victoria’s market it is a principle that all customers should face their true cost of supply. USO regimes also account for vertical not really universal service, but self-regulation based on utilities fulfilling voluntary social obligations. The shift in meaning and its ramifications were sometimes identified, but distinctions were murky. For example, according to the Federal Bureau of Consumer Affairs (1995: n.p.): ‘The objective of a USO is to ensure all consumers are afforded access to essential services. USOs are conceptually analogous to CSOs with the emphasis of a USO being on providing universal access.’ There was no discussion however as to how USOs would be achieved, in what circumstances they should apply, or how and why they differ in practice from CSOs and CPOs. In the telecommunications sector, a USO was made explicit in legislation for the first time, but this referred only to geographical coverage. According to Wilson and Goggin (1993: 15), the issues of affordability and accessibility of telephony were left, to government’s social welfare departments. For the utility sector in Victoria, the shift from USO to CSO was made without ongoing debate, unlike in the telecommunications industry. Indeed, the implementation of a CSO regime in electricity stands in contrast to Europe, the US and many other jurisdictions where the debate is about how to deliver a USO in a market context.
equity but forsake the concept of horizontal equity in favour of tariff cross-subsidies. But, in electricity industries, such cross-subsidies are not between income groups per se. Cross-subsidisation has predominantly been between customer classes or regions rather than income groups. This results in a mis-match between need and capacity to pay that parallel vertical equity measures do not always remedy. This has given rise to fuel poverty campaigns, but may also explain why the USO concept is so closely associated with network services. The horizontal equity approach, it should be said, involves subsidisation of a product, and compensates (in electricity) for differences in the costs of supply. Quiggin (1996: 45) states the argument in favour of efficiency-based policies would be valid, at least in principle, if lump sum tax transfers were available; where they are not, the use of some instruments to pursue efficiency and others to pursue equity is never justified. Victorian electricity CSOs only compensate for lack of income, and then only marginally. There would be customers to whom Quiggin’s assertion applies.

The issue of what comprises equity within electricity supply is extremely important, and to that end there is a lengthy discussion in Chapter 6 detailing the complex causes of fuel poverty. Yet the arguments of neo-liberals such as Allan (1994) alert us to the fact that some customers are unattractive and may be subject to economic discrimination.

Allan (1994: 124) reiterates the income security function of the CSO concept:

The broad aim of the CSO approach is that the services provided by GTEs, and purchased by the Budget sector, should be provided under commercial contracts. Commercial contracts change CSO clients from being a charitable drain on the GTE’s earnings from other clients, to valued customers who attract additional earnings for the GTE. This change in the status of CSO clients should also improve the manner in which they are serviced and their complaints handled.

This not only ignores any potential for the CSO to be less than any previous subsidies, but states that customers with insufficient purchasing power receive different treatment in a market. They need to gain equal status (purchasing power) with attractive customers within a commercial environment before they will be treated in a non-discriminatory manner. This argument unintentionally acknowledges that it is not merely the characteristics of poor customers but the operation of the market itself that acts to
disadvantage such customers. The existence of market power is traditionally assessed according to whether or not there are a sufficient number of buyers and sellers in a market. The formation of residual markets suggests that, even when there are sufficient buyers and sellers, the providers of essential services are able to exploit their customers’ need for the product and their lack of purchasing power. The residual market theory also suggests that this exploitation is a form of widespread systemic discrimination and is not isolated to individual cases. Some form of market power is being exercised. Given this, any CSO or subsidy (the cost of ‘equalising’ such customers) needs to overcome two ‘deficits’: the customer’s lack of purchasing power, and the consequences of differential treatment by competing providers.

The Evatt Research Centre (1988) observed early on that proponents of privatisation often saw the issues of universal service, equity and social considerations only in terms of cross-subsidies, ignoring externalities and market failure. The result of this selective view was that the question competition reform advocates would raise was ‘What is the best means of providing for the subsidies?’ rather than ‘What is the best way of correcting for the failures?’ (Evatt Research Centre 1988: 56). In the past, universal service recognised monopoly as the market failure. With competition reform, that failure is addressed through the creation of markets. Or is it? Market segmentation of customers may belie this assumption. In Chapter 7 I provide a detailed discussion on market segmentation and how it gives rise to a situation analogous to simultaneous competition and monopoly. A situation such as this poses a deep theoretical problem for neo-liberal reformers. In Chapter 10 I then discuss how the monopoly side of this equation may involve market abuse that undermines the income support function that is the basis of the CSO/concession. As indicated earlier, there are two deficits in markets that CSOs need to address. One is lack of purchasing power, to which CSOs are traditionally directed. The second is the economic exploitation of customers who lack market power, and it is this that CSOs do not currently take account of. If they were to do so, it may be found that this is a more costly method than traditional universal service in addressing the problems of inequality and efficiency.
4.5.3 CSOs and the Victorian electricity industry

In Victoria, CSOs adopted for the reformed electricity industry were the winter energy concession, service to property charge (supply cap), multiple sclerosis concession, life support concession and energy relief grant scheme. These are provided through the Department of Human Services, and reflect some yet undismantled parts of the Cain Labor government legacy. The notable absence was the explicit acknowledgement of the objective of universality based on access and affordability (for example, an obligation to supply and the maintenance of uniform tariffs). Previously there had been an assumption of universal service but no legal basis for it (Cornwall and Walker 1994).

The Kennett government made it clear that CSOs would be contingent rather than absolute rights, always subject to budgetary pressures (OSOE 1994b). This is the point of departure between a neo-liberal framework and one based on citizenship rights. For the latter, budgets are adjusted through tax increases or cuts to non-rights-based parts of the budget to ensure rights are delivered. As service delivery was also to be contingent on the market, this represents not merely a reversal of policy but a profound shift. The recognition that utilities could deliver inequitable outcomes is ignored in favour of a narrow response limited to small income security measures that assume the base on which they are applied is neutral. In regard to access, there is a silence. In regard to affordability, the proponents of CSOs – by and large, neo-liberal reformers – believed that a market would result in lower prices, and hence increase affordability.

The outcome of adopting a CSO policy in preference to a USO, prior to the extension of the legislation creating the deemed and standing offers, was that in Victoria in 2004 an age pensioner would have been eligible for a 17.5% winter energy concession rebate on their electricity bill, but may not have been able to obtain supply in the first instance. Had the obligation to supply not been extended, it is possible that current corporate strategies to avoid customers36 on the basis of their low consumption, use of off-peak electricity and/or rural location may have resulted in the shedding of age pensioners and other concession recipients.

36 That is, avoid take-up of market contracts and in doing so leave these customers on the higher regulated tariffs.
4.5.4 Conclusion

The assumption that the introduction of a market automatically overcomes market failure(s) traditionally associated with certain industries does not take account of the way in which competitive pressure may engender its own market failures, as occurs when there is market segmentation. CSOs relate to one type of market failure, lack of purchasing power, but they do not necessarily compensate for the dismantling of universal service that previously addressed a different market failure, monopoly. At an ideological level they shift externality costs associated with a specific industry to the budget sector. In doing so, the issue of externalities is downplayed politically and the extent of compensation reduced. Nevertheless, CSOs implicitly recognise the likelihood of market failure arising out of some customers' lack of market power.
Chapter 5: The struggle over market reform

5.1 Introduction

In the previous chapter I provided an overview of the reform process and described the loss of entitlements and the shifting of externalities to the budget sector. In Chapter 5 I show that the struggle over market reform involved varying levels of dissent and/or accommodation by domestic user advocates. The discussion reflects very different understandings of market relations and social protection. The neo-liberal reform model that was implemented was far from pure, reflecting the impact of resistance to the proposed changes. Pre-existing social protections were reconfigured rather than transformed.

The purpose of this chapter is to introduce the alternate views to the neo-liberal approach to electricity consumption. These are the social democratic (or social citizenship) and new consumerism (or Third Way) perspectives. The chapter explains how debates over the reform process became a three cornered contest. In so doing, it not only provides context to arguments presented in Chapters 6, 7 and 8 regarding the appropriateness of the market in the delivery of electricity and the impact of shifting the externality costs, but permits us to return in Chapter 9 to critique the models of social protection inherent in each of the three contesting ideologies.

5.2 Responses to the reform agenda

Specific responses to the market reform of domestic electricity supply in Victoria took three forms. The first was largely empirically based, and had only a small ideological connection. It involved small empirical studies or internal reports that took access to affordable supply as a right, and questioned the social justice implications of increasing commodification. Chesshire (2002) describes these as ‘grey literature’. They are not important for the purposes of this thesis and will not be discussed here, but examples include VCOSS (c1995), Benvenuti and Walker (1995), Brotherhood of St Laurence (1998), Dufty (1999) and CLCV et al. (2002).

The second set of responses were based squarely on the concept of citizenship. They stand in direct opposition to the neo-liberal approach, rejecting the market as the
organising principle for the distribution of electricity as a key welfare good. The third set were broadly sympathetic to the neo-liberal attempt to empower consumers, arguing that they can gain from having choice and from the stimulation of competition. This new consumerism is distinguished from neo-liberalism proper by being grounded in a social policy rather than economic tradition, and is clearly cognisant of the historical significance of the social democratic approach.

5.2.1 Social citizenship

Most polarised from the neo-liberal model were those espousing a social citizenship or social democratic position. In this view, the people that make up a polity are citizens with civil, political and social rights (Marshall 1950). The struggle over market reform of utilities is a struggle over the distribution of resources. Distribution is determined by the extent of commodification. Social rights provide entitlements to economic resources and social participation regardless of economic position (Esping-Andersen 1990: 3). The state is a mechanism to protect citizens from the negative impacts of markets and enable the redistribution of wealth that is required to deliver such rights. Social citizenship, according to Webber and Ernst (1996), recognises substantive as well as procedural rights, ensures that access rights are guaranteed and protected, recognises collective as well as individual rights and responsibilities, and locates strategic decision making within the domain of democratic accountability and public policy.

The distinction between the neo-liberal reformers and the proponents of social citizenship can be seen in Saunders’ rebuttal of Ernst’s (1994a) study that explored the social and economic impacts of UK utility reform. Saunders (1995: 264) held that ‘it is by no means self-evident that the water and energy companies should function as extensions of the state social security system in the way that Ernst suggests’. He argued that UK customers were better off as a result of privatisation and attributed this to competition, even though FRC was still to be implemented. Saunders chose to ignore Ernst’s exploration of the differential impacts that privatisation and competition have had and could be expected to have on sub-classes of domestic customers.

In Victoria, Kliger (1998) put the market in opposition to citizenship rights and contrasted the concept of social citizenship with that of good corporate citizenship. Similarly Pike
Siemon (1995, 1997) and the Catholic Commission for Justice, Development and Peace (n.d.) saw market provision as reducing entitlements and threatening social solidarity. Lawrence (2003: 161) argued for the need for ‘electricity equity’ to be a key principle of an equitable state energy policy as vulnerable customers had to be ‘protected from excessive corporate profiteering’. Dufty (1995b) highlighted the significant changes that had already taken place and expressed concern about the impact on low-income households. Kliger (1998) and Siemon (1995, 1997) exemplify the view that private, market provision of utilities would generate inequities and are critical of the assumptions behind National Competition Policy.

These writers share a position regarding the likelihood of market failure and the inappropriateness of commodifying an essential service. The inequities they saw as inevitable in the market concerned not only harsher debt and disconnection policies, but also the ability of suppliers to take advantage of small customers’ lack of market power in a competitive environment. This would constitute a transfer of wealth from small domestic customers to business customers. Siemon cites a letter by Treasurer Stockdale which claimed the doubling of the domestic supply charge in October 1993 was partly to remove ‘intra-class subsidy’ from large users to small users. However, Siemon (1995: 46) notes:

[the] effect of shifting more of the costs of supplying electricity onto households and away from small businesses, as promised by the restructuring, is much the same as imposing a new tax on households whilst removing one from business.

The People Together Project (1995) was also concerned that prices would remain high for domestic customers as competition delivered cuts to high-profit commercial customers. Carver (1995) warned that price discrimination, or Ramsey pricing (the marking-up of prices to customers with the least elasticity of demand in favour of cuts to those with the greatest elasticity), was a real risk. She made the assumption, however, that such discrimination would only occur while domestic customers were franchised (that is, while there was no competition) and larger customers were not. This assumption was shared by Ernst (1997) who thought that FRC may diminish the risk. He nevertheless recognised that ‘not all domestic customers are equal’ and identified market segmentation and price differentials based on the form of payment within the trial phase of gas competition in England (Ernst 1997: 19). Siemon (1995) for his part envisaged price discrimination in the
market and the residualisation of poor customers, particularly if prepayment meter technology was permitted.

The experience of low-volume/low-income customers in the deregulated banking and insurance industries informed the views of the People Together Project (1995) who claimed they have been subject to higher fixed unavoidable charges (exploitation) and/or shedding strategies (exclusion). Nicholls (1995: 3) did not believe the market and welfare could be reconciled and called for universal service and affordable prices:

Low income Australians are not likely to be sought after customers in a competitive environment and are therefore not likely to be the beneficiaries of a market driven system...the protection of vulnerable Australians is a critical issue and must be addressed, not as a ‘welfare issue’ but as an integral part of the reform of public utilities.

Nicholls identified a probable market failure and rejected the idea that the social security system be used to compensate ‘losers’ in reform processes. In essence, market reform merely swaps one type of market failure for another, but it is a swap that involves redistribution of wealth.

Nicholls’ plea points to a distinction not just between social citizenship views and neo-liberal doctrine but between social citizenship and the final sub-group considered here, new consumerism, which finds an accommodation with market doctrines whilst proposing civil law protections. Before discussing this in more detail, the legacy of the social citizenship sub-group should be noted. The obligation to supply all households has formed a crucial part of the safety net put in place for FRC; most consumer rights developed prior to privatisation and competition were retained in the new Retail Code (formerly the Sale and Supply Code), which has included provisions that proscribe disconnection in cases of incapacity to pay; and the concessions framework has continued as an income security measure, rather than being used to address market failure. In all, ‘universality’ was dinted, not assailed. This is not, however, a permanent state of affairs, as the obligation to supply is still subject to the sunset provision.
While not all explicitly social democratic, a group of writings emerged after the commencement of FRC which explored the above concerns. VCOSS (2002: 1) assessed the impact of retailers’ price increases for deemed and standing offer tariffs, and concluded that the government’s use of its pricing powers under the *Electricity Industry Act 2000* ‘significantly offset predatory pricing of essential services by private electricity retail operators’. The risk of segmentation, the creation of residual markets and discriminatory POLR schemes were explored by Sharam (2002, 2003a, 2003b), Sharam and Gregory (2002) and Duggan and Sharam (2004). Langmore and Dufty (2004) also identified that the demand elasticities of domestic customers raised issues of market power. Sharam (2004) found evidence of discrimination around payment method. Bowman, Coghill and Hodge (2004) recommended the extension of the safety net arrangements, arguing that competition was not robust. Community Power, a community-based aggregation (bulk purchasing) group, also provided evidence to the ESC’s Review of the Effectiveness of Full Retail Contestability that its partner AGL had breached the anti-redlining conditions of their agreement. Community Power had inserted a ‘no exclusion’ provision in this agreement that required AGL to offer contracts to all customers participating in the scheme regardless of their demographic and credit rating:

potential CP customers will have been screened and rejected due to undesirable demographics or credit ratings etc. as per the usual AGL processes…We have been told, for example, that a potential customer that ‘lives next door or near to housing commission flats’ would be screened out as undesirable. CP has been committed to ensuring that all of our constituents are eligible for a CP offer regardless of their credit or income status. This was written into our contract with AGL but as indicated earlier we were advised post Round 1 contract offers that potential customers were screened as is standard for all potential AGL customers. Community Power recommends the ESC regulate what retailers are able to screen for, to ensure that retailers are not engaging in redlining behaviour (Community Power 2004: 7, 12).

The early social citizenship writers responded to the reforms on the basis of their understanding of markets and the peculiarities of the electricity industry, and the essentialness of electricity to domestic life. As the reforms have moved forward, their concerns are emerging as key public policy issues.
5.2.2 New consumerism

Within the libertarian view of citizenship ‘the relationship between the individual and the state’ becomes ‘explicitly contractual’: consumer sovereignty provides the mechanisms of choice and restitution (Miller 1995: 440). New consumerism refers to the emergence of a grouping within the broad consumer movement which embraced the concept of consumer sovereignty and were notable for their advocacy of procedural rights in lieu of substantive rights. The term was first used by Ernst (1994a: 155). It also now encompasses support for self-regulation or co-regulatory regimes. The new consumerist model embraces the market while claiming a legitimacy born of earlier social democratic reforms in the delivery of both private and public goods and services. The market model adopted in Victoria has many legacies from this group, such as the alternative dispute resolution scheme and the Marketing Code of Conduct. It is a model, however, that largely replaces older forms of social protection with contractual relations.

‘Old consumerism’ was ‘focused largely on issues like inflation, advertising, trading hours, food purity, packing and labelling, product safety and standards, and pricing’ (Brown and Panetta 2000: 13). The Australian Consumers Association (ACA) at the time of its foundation in 1959 typified this. Old consumerism and social citizenship advocates are informed by social movements that seek to democratise services, both government and private.

Two impulses lie behind new consumerism. The first is the effort of the broad consumer movement in Australia to promote a strong peak body that could be a participant in the corporatist style of government characterised by the Hawke Labor government of the 1980s. The second arises from the impact of neo-liberal ascendancy within government. Parts of the broad movement, such as the new consumerist group, accommodated reform and assisted in developing ‘grey’ or non-formal ‘co-regulation’ which sometimes included industry funded assistance for consumer advocacy participation in the process.

Brown and Panetta (2000: 21) state that the ACA disaffiliated from the Australian Federation of Consumer Organisations (AFCO) on the grounds that funding from industry compromised consumer advocacy:
This ‘greying’ of regulation can be seen as a privatisation of government functions. It is one of the ways in which the state has limited the scope of its intervention in markets and is part of the general phenomenon of the retreat of government. But it can also be viewed, quite positively, as a means of containing the cost of consumer complaints and disputes within industry and relieving the general taxpayer of the costs of using state institutions.

In addition, as Brown and Panetta point out, government funding was the primary source of revenue for AFCO and many other consumer organisations (the ACA being the prominent exception). The Commonwealth’s Business Regulation Review Unit opposed such funding, and the Institute of Public Affairs still actively does so (Moran 2001: 2).

Neo-liberal purists advocate that competition is the best form of consumer protection. Moran (2002: 31-2) for example argues that the retailer's interests and the consumer's interest are the one and the same:

Under competitive circumstances, the retailer is the \textit{de facto} agent of the consumer. That role is assumed of necessity – if abandoned or neglected a rival will step in. The retailer’s activities, to ensure its on-going success and even its existence, must extend far beyond passively breaking down bulk and ensuring products are delivered at convenient locations. It must extend to assisting in discovering what the consumer wants...the retailer is \textit{compelled} to be the agent of the consumer, as long as the consumer can move to an alternative agent if the retailer provides unsatisfactory service.

While the new consumerist group lends support to the market model, their concept of the market diverges from that of the neo-liberals. This in part arises from a historical recognition that markets do not always serve customers as well as commentators such as Moran would like us to believe. Secondly and related to the above, if there were no legal protections for consumers, then there would be no complaint or formal consultative mechanisms that have become intrinsic to the survival, both in terms of finances and legitimacy, to much of the contemporary consumer sector.
New regulatory forms of consumer protection reflect the new environment. The neo-liberal reformers had compromised, but so had much of the consumer movement, which had always been filled with ideological tension reflecting the attempt to merge consumer campaigns with social justice oriented reform (Brown and Panetta 2000). As Yeatman (1998: 229) argued, the democratic expectations underpinning new social movements such as feminism and environmentalism contributed to the dis-establishment of older ‘paternal principles of protection’. This, she suggested, would inevitably lead to a consideration of the conditions under which choices are made. New consumer orientated civil rights based on choice increasingly replaced old paternalistic social rights based on status. Yeatman (2002: 63) argued that choice could be facilitated by adopting a service user/provider relationship model that embraced the ‘individualised personhood’ which is central to the liberal use of contract.

Yeatman has been criticised by Ramia (2002) for being a supporter of a shift to market-based contractualism that is devoid of social protections. Irrespective of the merits of Ramia’s argument, this debate is useful because the democratic expectations of individual choice and treatment of which Yeatman speaks ended up finding their way into co-regulatory regimes via new consumerism. The problem which, Yeatman (1997: 40) identified is that choice is conflated with contract: ‘Contract can establish the conditions of entry and exit with regard to a relationship, but it cannot regulate the internal workings of that relationship’. Consent is contingent. The exercise of choice:

- can be argued to be operating when the parties to a relationship are adequately informed about their relationship, and their respective entitlements within it, and they have the right to negotiate the substance, process and direction of this relationship. This right of negotiation involves the right to discussion, debate and contestation in respect of this relationship. Negotiation entails the additional principles of explicitness and accountability (Yeatman 1998: 231).

Choice and consent are different. The latter requires democratic participation.

Sturdy (2001) argued that consumer sovereignty as it is promoted by neo-liberals simply serves to obscure producer power. Neo-liberal reform in Australia has resulted in new or transformed forms of governance in regard to domestic electricity provision whose defining
characteristics are the primacy of the market and the weakening of political debate and
democratic participation. As Marginson (1997: 78-9) has suggested, ‘The New Left rubrics
of freedom and participation survived but were transformed’ in the displacement of the
New Left in the 1970s by the New Right in the 1980s. Complaints mechanisms such as
industry dispute resolution schemes are accordingly an example of a new set of ‘rights’
which Marginson describes as containing a ‘curious mixture of continuities and
discontinuities’ between left and right politics.

Most of the new consumerist writers argued for USOs on the basis that electricity is
essential to survival, but they put considerable emphasis on procedural rights and the
maintenance of CSOs (Nelthorpe 1995, Cornwall 1993, 1994, Cornwall and Walker 1994,
Morley 1994, Walker 1996). Some such as Johnston (1995b, 1995c) tended to argue that
a commercial focus in the management of essential services would be likely to reduce the
welfare of disadvantaged households, but it was the fear of the removal of existing social
regulation rather than the operation of markets or competition that concerned him (the
connection between the two was not articulated). The response therefore was to propose
the recognition of consumer rights as an overlay on the new commercial environment.

Romeril (1998: vi), for example, argued that unrestrained emphasis on the market is
detrimental to low-income customers and that this loss of capacity to participate as a
citizen in turn has an impact on the ‘functioning of democracy’. However, she fell back to
calling on the Victorian government ‘to establish community service obligations for the
corporatised and privatised utilities in order to ensure that no household is disconnected
through inability to pay’. Benvenuti and Walker (1995) called for a regulator with the role of
ensuring universal access to supply. These arguments tend to sidestep the apparent
contradiction between market provision and universal service provision or blur the
distinction between market and non-market forms of accountability. Facing criticism from
Ernst (1994a), Carver (1995) acknowledged the shift from a rights-based model of
consumer benefit to the economic concept of consumer sovereignty. As Johnston (1995b)
noted, these are two different concepts of empowerment: the former emphasises collective
action for government intervention into markets, the latter focuses on empowerment
through individual choice. For Ernst, the development of elaborate consumer rights based
on contractual procedures failed to deliver positive rights that would address the
‘fundamental problem of fuel or water poverty’ (Webber and Ernst 1996: 138). The contract
model that underpins the concept of consumer sovereignty is, it has been argued, inherently flawed in relation to essential services (Aronson 1997). Siemon (1997: 6) contended that the new contractualist ‘minimum standards’ were intended to achieve ‘marketing objectives’ rather than better uniform treatment and cheaper prices for all. He noted with irony that the minimum consumer protection standards developed for FRC were based on rights gained by collective action a decade earlier. Johnston (1995a: 42) did concede to Ernst that affordability was the issue: ‘access to supply is linked to affordability, rather than a denial of a “right” or reluctance by providers to extend market penetration’. Ernst (1999: 96) later stated:

To market advocates, accountability is refracted through individual interactions with the service system – hence the emphasis on accountability mechanisms such as individual service guarantees and consumer surveys. For opponents of privatisation and market testing, accountability is refracted through the idea of collective responsibility for collectively provided services, and the machinery of democratic politics is seen as central to the achievement of this.

Brown and Panetta (2000: 23) argue that the rise of co-regulation in Australia is an unconscious heralding of Third Way politics. They provide what could be described as a definition of new consumerism:

What the last decade has seen is a blurring of the boundaries between consumer advocates and business men and women. Indeed, there seems to be an increasing flow of people from the [consumer] movement into business, particularly into customer relations areas. While there has not been a big return flow, a growing number of men and women in business seem to be becoming members, in a broad sense, of the consumer movement. The consumer is no longer a thing outside, or other than business; it is an association of people in many walks of life subscribing to the idea that markets can be made to work for people.

Turner (2001: 194) observed that the Blair government’s Third Way strategy sought to help ‘people participate successfully in the market’. Dean (1996: 18-21) argued that the civil rights envisaged by its Citizen’s Charter referred to ‘the kind of rights “customers” enjoy in the marketplace’ and these were ‘at the expense of both political rights and social rights’.
New consumerism represents a break with the more social democratic elements of the broader consumer movement because of an unwillingness to seriously challenge the distributional impacts of markets and acknowledge the limitations of civil rights where economic resources are unavailable or obligations to supply do not exist. Attempts to include new consumerism as part of the global Third Way may be reasonable, but writers such as Giddens (1998, 2001) offer little guidance in relation to equality measures ‘which deal directly with the unfavourable outcomes of competition policy’ (Lowy 2002).

5.3 Conclusion

The original emphasis of market reform changed over time, suggesting the influence of other political actors. Victoria’s domestic electricity market is a co-regulatory regime rather than a free market. This reflects the impact of the new consumerist group of domestic end-user advocates. The social citizenship group certainly had influence to the extent that the protections of the preceding era have not yet been entirely lost. But universal service is not the current policy objective, and current efforts are directed to a move towards a targeted welfare model. The social citizenship group warned that market segmentation could be anticipated. If this were to occur, it would not only have the potential for market failure (as Siemon suggested) but would undermine both the neo-liberal and new consumerist understanding of the market and require a revision of what should constitute social protection. Part 3 explores the applicability of the market to an essential service like electricity.
PART 3: TRADITIONAL AND NON-TRADITIONAL ARGUMENTS CONCERNING ELECTRICITY AS A MARKET

In Part 2 I showed that the electricity industry in Victoria developed within a very specific context in which supply was highly politicised. In Part 3 I take a closer look at markets, and whether or not the fears of critics may be realised. In Chapter 6 I present traditional arguments as to why electricity markets are likely to fail. I give emphasis to the demand characteristics of low-income and vulnerable households because this group has been the subject of much debate concerning the impact of the market and, if segmentation were to occur, it is this group that could be expected to be subject to segmentation strategies. In Chapter 7 I present a non-traditional argument that a market for domestic electricity is likely to result in market failure because of new developments in information technology and marketing giving rise to segmentation and hence market failure. How concern about segmentation and social protection has translated into electricity reform models forms the subject of Chapter 8. The lessons of electricity industry reform and segmentation in other industries are distilled into three models of social protection critiqued in Chapter 9.
Chapter 6: The significance and peculiarities of electricity as a consumer good

6.1 Supply-side characteristics

Traditionally electricity was supplied by vertically integrated monopolies that generated the power, transported it (transmission and distribution), and carried out retail functions. This model of supply exhibits both economies of scope and economies of scale. Disaggregation assumes that the benefits arising from competition will outweigh both of these. Quiggin (1996: 63) states that the electricity industry displays natural monopoly features in that excludability is not a major problem and scale economies are not so extensive as to result in pure non-rivalry. Both positive and negative externalities are major features of electricity supply. Greenhouse gas emissions and localised pollution are examples of negative externalities. The macro-economic effects of a dynamic electricity industry are regarded as positive externalities, as are social benefits (such as health improvements) (Ernst 1994: 49, Johnson and Rix 1991: 31).

Electricity has some quite specific characteristics. It cannot be stored. Demand must be supplied instantaneously. It has therefore the shortest possible time constant between production and use: zero (Casazza 2001). It is an industry that is typified by long lead times in bringing production on line. That is, it has the longest time constant between production and delivery capacity: years (Casazza 2001). The product itself is an undifferentiated commodity – there can be different producers but all produce identical electrons: only price can alter (Coyle 2000, Casazza 2001). The producers can differentiate themselves in marketing terms, however, all electricity is sold through a common pool and the output of the producers is only hypothecated in cases such as ‘green power’.

Colton (1995d) and Taggart (1995) suggest that a characteristic justifying public intervention in the electricity industry is ‘eminent domain’. This refers to cases where private property rights can be overridden by a private interest. In the case of electricity it refers to the extensive organisation of natural resources and infrastructure required by utilities. Utilities need to plan into the future – for the extraction of coal, for provision for easements for transmission and distribution, and river diversion, for example (Edwards...
1969: 256). In the US eminent domain is one of the reasons for support of public regulation of private utilities.

The electricity industry has huge sunk costs and investment is ‘lumpy’. Marginal cost pricing fails to recover all the costs, but pricing based on average costs is not regarded by standard economic theory as efficient. Generators in the national electricity market now sell through a spot market, but predicted problems with collusive market behaviour appear to have been justified (Finn 2003). The monopoly distribution and transmission networks are regulated. ‘Rate of return’ regulation was rejected by reformers in favour of ‘incentive regulation’ (or ‘CPI – X’ regulation) but, as Quiggin (1996: 195) argues, there are questions concerning its long-term efficacy too. The price that households see now is comprised of these elements plus the retailer’s margin. Despite the introduction of a market in generation and retailing, domestic customers cannot be said to receive a price signal in its proper sense. They obtain supply on the basis of credit and accordingly pay generally three months after use, and on the basis of their accumulated consumption. The price signal therefore is as blunt as it possibly can be. In the absence of real time pricing signals, retailers treat their domestic consumption load as a form of pooled risk. It needs to be remembered that one of the outcomes of disaggregation is that retailers have generators and networks as creditors. If a customer defaults, the retailer assumes all the losses, whereas previously the costs would have been shared proportionally across the industry. Credit management accordingly takes on increasing importance.

6.2 Demand-side characteristics

Many commentators see a role for public intervention in utilities as arising from the characteristics of the demand side of the market, particularly those of domestic customers. Ernst argues that electricity is a ‘merit good’ as it conforms with Musgrave’s definition of being a good ‘the provision of which, society (as distinct from the preferences of the individual consumer) wishes to encourage or, in the case of demerit goods, to deter’ (quoted in Ernst 1994: 39). Electricity in developed nations is regarded as an ‘essential’ service (Zajac 1996).

Arising out of the ‘essentialness’ argument, Ernst suggests that the current form of delivery of energy means electricity is non-substitutable. Households are demand inelastic and are
locked into ‘particular patterns and levels of demand’ (Ernst 1994a: 42). Households face a considerable disparity in bargaining power (Colton 1995a). Information asymmetry and high transaction costs are ‘formidable barriers to the realization of consumer sovereignty’ (Ernst 1994a: 39).

Customer inertia is also an issue. Knights, Sturdy and Morgan (1994) suggest that some services are characterised by customer inertia. This makes these industries supply-side focused and they assume, perhaps appropriately, a product led approach to their businesses rather than a marketing approach.

The absolute and relative level of prices determines whether people have access to electricity, and can also influence the extent to which they have sufficient income left after paying for electricity to afford other necessities, such as housing and food. It is because of this significance that social policy analysts have coined the term ‘fuel poverty’. In the following part of this chapter I focus on the significance of electricity as a consumer good, paying particular attention to fuel poverty as a pressing policy issue. By so doing, I try to demonstrate why a privatised and marketised electricity industry will of necessity be a problematic issue for social policy.

6.3 Fuel poverty

the scope for consumer choice which market systems provide is meaningless in a situation where the consumers concerned do not have the material resources necessary to exercise it. Put another way, the advantage of the market operates only for those who have sufficient money to express their aspirations in the form of an effective demand for goods and services on offer (Saunders 1993: 63).

Households who experience fuel poverty have the characteristics and behaviours that in other markets would see them excluded or served on a differential basis. In the finance sector, for example, credit worthiness determines both access to credit and its cost. The response of the suppliers of goods and services to less credit worthy customers is to risk manage. The purpose of a lengthy elucidation of the demand-side characteristics of low-income and vulnerable electricity customers is twofold. Firstly, it demonstrates that risk(s) can be perceived differently and managed differently. Secondly, it highlights the likelihood
of a demand-side market failure in which these customers are excluded or subjected to market abuse.

Fuel poverty arises from a combination of inadequate income and/or poor thermal efficiency of housing and/or inefficient appliances and/or needs (lifecycle stage), and tariff structures (Kiers 1983, Backman et al. 1987, Day Rate Working Party 1991, Deasey and Montero 1983, Kymantis 1986, Brotherhood of St Laurence c1996, Mills 1988, Kliger 1998, Reark Research 1996, Neilson c2001, DITR 1985). Deasey and Montero (1983: 5) state that ‘fuel poverty, or fuel hardship, is a term originating in the UK to cover the problems which arise from people’s inability to meet their basic needs for energy’. These problems are primarily under-consumption, disconnection from supply, prioritisation of utility payments over other essentials such as food, and accumulation of debt:

For some people, staying connected to utilities means that they have had to do many things to prevent disconnection. They may have had to go without necesseties, ask for a deferment of payment or obtain material aid. As a consequence, disconnection rates alone are not always an accurate indication of fuel poverty (Neilson c2001: preface).

Richardson and Travers (2002) refer to the UK definition of fuel poverty as needing to spend more than 10% of household income on fuel ‘in order to keep the house comfortably warm’. They stress this definition is based on ‘need’ rather than what is actually spent. Such fuel poverty indices have rarely been used in Australia, with Backman et al. (1987) being an exception.

6.3.1 Income security

The fundamental mismatch between income and expenditure means that even very small changes in circumstances or charges can precipitate a minor financial crisis capable of cascading into a major crisis (Benvenuti and Walker 1995, Romeril 1998, Nielson c2001). Traditionally, electricity customers in Victoria are provided with three months credit, as metered consumption forms the basis of customer charges. Thus, by definition, all customers accrue a debt. For some of the fuel-poor, payment cannot necessarily be made when due. The threat of disconnection is ever present as the ultimate sanction but, in this
case, its purpose given the inability to pay is punitive (Mills 1986). There are typically two groups of fuel-poor who struggle with debt: those who have an outright incapacity to pay, and those who have an inability to pay within the specified period (Dufty 2003). Customers who experience fuel poverty require flexible payment arrangements in order to juggle competing demands for their scarce financial resources, and in some cases recourse to debt forgiveness if disconnection is to be avoided (Kliger 1998). The provision of credit therefore is instrumental in maintaining supply to the fuel-poor. On the other hand, policies such as the imposition of security deposits are counter-productive to the maintenance of supply (Benvenuti and Walker 1995, Kiers 1983).

The recurrent nature of energy bills adds to this precipitous state (Backman et al. 1987, Kymantis 1986). Reark Research (1996: 6) concluded that the non-age concession groups of households faced the ‘most impediments to comfort, in terms of housing stock and affordability of bills’. They linked this to housing tenure, lack of energy efficiency, health problems, ‘perceived difficulty in paying their bills’ and less awareness of concessions.

Low-income households spend a higher proportion of their income on essential items such as energy than do wealthier households (Kiers 1983, Deasey and Montero 1983, Siemon 1995, Ernst 1994a, Lawrence 2002a). The Victorian Utility Consumption Survey conducted by Reark Research (1996) for the Department of Human Services found that the estimated average income of age pensioner households in their survey was $14,728, and these households spent an average of $504 p.a. on electricity. Non-age concession average income was $20,026 and average electricity expenditure was $549 p.a. The average income of non-concession households was $52,303 and electricity expenditure was $665 p.a. This represents 3.4%, 2.7% and 1.3% of expenditure of each household category. These figures do not absolutely accurately reflect the degree of fuel poverty as the non-age concessions group would include families, and the age pensioner group includes around 70% single person households. The Victorian Utility Consumption Survey conducted by Roy Morgan Research (2002) found that the average non-concession household in their survey spent 32% more than an age or service pensioner household ($765 p.a. compared with $576 p.a.).

The income security policies of government – from Commonwealth payments for pensions and private rental housing assistance through to provision of public housing or state-based
utility concession programs – are undermined by the absence of government standards for housing and appliances, regressive pricing structures, and debt and disconnection policies (Kiers 1983, Siemon 1995). Kiers (1983: 28) noted how income security measures and utility services are handled as different policy areas without a relationship; until income security policies considered ‘the ways in which utility financing and management policies fit into the present and future context of income security in the community’ they would be ‘inadequate or misdirected’. There is wide agreement that utility practices must change substantially if low-income households are to be guaranteed affordable supply (Kiers 1983, Kymantis 1986, Siemon 1995, Kliger 1998, Romeril 1998, Neilson c2001).

For households which take both gas and electricity supply, there is a relationship between the two fuels. Financial counsellors report that, in generalised terms, customers prioritise electricity over gas, although this will depend on the season as gas is commonly used for winter heating (Sharam 2004). The result is that the use of disconnection and reconnection in the same name as an indicator of hardship should view gas and electricity together, and take account of policies in regard to one fuel for its impact on the other. For example, gas disconnections in Victoria rose sharply in the first quarter of 2001. This coincided with an increase (sometimes considerable) in electricity prices.

6.3.2 Thermal efficiency of housing and appliance standards

Poor energy efficiency of housing stock and poor efficiency of appliances such as space and hot water heating have been identified as major contributors to the high energy costs borne by some households (Kiers 1983, Backman et al. 1987, Mills 1988, SSCIST 1992, Siemon 1995, Kliger 1998). Such housing locks users into unnecessary consumption and expenditure on energy bills, adding to income insecurity. Tenants in particular have little ability to overcome the problem of ‘split incentive’ in which landlords avoid capital expenses by installing cheap appliances with high running costs (Mills 1988, Deasey and Montero 1983, Backman et al. 1987, Day Rate Working Party 1991). The Industry Commission (1996) recognised that low-income households tend to own older and less efficient end-use appliances and have less ability to change technology, and acknowledged that pricing has a differential impact on different income groups. The benefit of remedial work to fix these problems (retrofitting) was recognised (DITR 1985), and
formed the rationale for the Victorian government’s establishment of the Home Energy Advisory Service (HEAS) in 1983.37

6.3.3 Lifecycle and energy needs

Fuel poverty also depends on household size and lifecycle stage. Some households have fixed or unavoidably high consumption patterns (Deasey and Montero 1983, CURA 1982). Families with children (especially sole parent families), householders with an illness or disability, and households with persons at home during the day such as the aged and unemployed are vulnerable because of their fixed limited incomes and/or the need to consume (heating in particular) during the day in addition to at night (Kiers 1983, Backman et al. 1987, Deasey and Montero 1983, Mills 1988). Health status specifically contributes to energy requirements and fuel poverty (Backman et al. 1987, Deasey and Montero 1983). Reark Research (1996) acknowledged the implications of energy usage for health and comfort, and Waters (2001) directly linked housing conditions with health inequities.

6.3.4 Tariff structures and prices

Electricity pricing structures have significant distributional or welfare impacts (Feldstein 1972, CURA 1982, Deasey and Montero 1983, Kiers 1983, Backman et al. 1987, Dufty 1999, McColl-Kennedy and Dann 1989, Siemon 1995). Upfront charges such as those for supply or service to property lift the average price per kWh for those with low volumes of consumption, whilst working to lower the average for high-volume users. Consumption can be rewarded through per unit prices that decline as consumption increases. High fixed charges impede the use of rationing as a budget measure. Kiers (1983: 4) argued that ‘[t]he impact of any tariff structure is dependent upon the social correlates of energy consumption’. While advocates such as Kiers argued for minimising or removing upfront charges, there was also awareness that pricing signals that discouraged consumption penalised large families and others with high consumption needs. Kiers proposed that additional income support would be appropriate in these cases. CURA (1982: 29) proposed ‘lifeline tariffs’ which were:

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37 The HEAS was abolished by the Kennett government in 1993.
designed to avoid the social problems generated by using pricing mechanisms to promote energy conservation, which in creating real economic incentives to conserve also penalise low-income groups whose consumption patterns may be relatively fixed.

Other mechanisms such as the federally funded family tax benefits can be used to compensate families.

Dufty (1999) also examined the impact of tariff and non-tariff charges (‘excluded charges’) such as connection and reconnection fees, concluding that these disproportionately impact on tenants and increase the overall cost and debt spiral for low-income households.

The fuel-poor are not homogenous. While rationing is an inevitable response to inability to pay, customers prioritise their needs in different ways. Rationing to below what are ordinarily considered essential levels of energy usage is common across the fuel-poor (Kiers 1983, Backman et al. 1987, Siemon 1995, Kliger 1998, Neilson c2001, Mills 1988), but many also deny themselves other essential items such as food in order to pay electricity bills and maintain supply (Mills 1988, Kliger 1998, Neilson c2001, Duggan and Sharam 2004). The elderly in particular regard disconnection as unfair and humiliating, and are more likely to go without food or other essentials to avoid it (Backman et al. 1987, Lawrence 2002b). Backman et al. (1987) found that families were more likely to seek emergency relief (cash or vouchers from charity or government funded agencies) rather than deny their children other essentials. In Victoria in the 1980s, the Cain Labor government’s Social Justice Strategy was central in enabling an effective ‘no disconnection’ (for inability to pay) policy (Ernst 1994b).38

Trends in electricity prices have become a topic of considerable controversy in recent years, with heated debates over the degree to which privatisation has been accompanied by price falls. The Industry Commission (1996) found that domestic electricity prices in Victoria decreased by 6% in real terms between 1986-87 and 1990 but increased by 18% between 1990 and 1994. Table 2 shows that on average (GD/GR tariff) domestic consumers of electricity in Victoria experienced a 3% real increase in the cost of their

38 Also personal communication, Marie Stivala-Andrews, financial counsellor and former HEAS staff member.
annual consumption between 1991 and 2003. For domestic customers who also had off-peak electric hot water heating (Y6/T6) (Table 3), the average increase was 8.2%. Low-volume users, who correlate strongly with low-income households, fared badly. For a low-volume TXU customer with off-peak hot water, the increase was 24%. High-volume Citipower customers were the only off-peak hot water customers to obtain savings (6.1%), although this only represents savings of about 0.5% per year. For those without off-peak hot water, the biggest savings also went to high-volume Citipower customers (5.5%). The increasing number of low-income households locating to the outer fringes of Melbourne where they are subject to rural prices means that the ‘fuel poor’ have been doubly disadvantaged in price terms.

6.3.5 Elasticity of demand

Finally, some writers on domestic energy consumption argue that demand for electricity is highly inelastic, that is, customers will not reduce consumption when presented with higher prices (Field, Lowe and Nelthorpe n.d., Walker 1996). This appears to hold true for middle- and higher-income households, but the observation in relation to fuel poverty is that low-income customers are very price sensitive (Langmore and Dufty 2004). Rationing moreover suggests they are price responsive (Siemon 1995, also see p. 109). A HEAS study, for example, noted that energy efficiency savings were split between increased take-up of heating and budget gains (DITR 1985).

6.3.6 Discussion

The purpose of such lengthy discussion about fuel poverty is to demonstrate the complexity of issues it involves and some of the pitfalls in attempting to find or establish indices, indicators or benchmarks (Allen Consulting Group 2003). Richardson and Travers (2002), for example, make many legitimate points about the difficulties of identifying and measuring fuel poverty and its relationship to more generalised poverty measures. Nevertheless, their claim that fuel poverty is a new concept in Australia was clearly formed on the basis of a limited literature review. Probably the best observation they make is that lower quintile households in Australia spend considerably more per week on fuel than allowed for in the budget standards approach of Saunders (1998), and they conclude from this that the ‘issue is thus not so much fuel poverty as fuel-driven poverty’ (Richardson and
Travers 2002: 28, authors’ emphasis). While they were suggesting that households do not necessarily under-spend on energy (which is probably not a reasonable conclusion), the priority which households assign to energy use does have ramifications for other essential expenditure. Ultimately they viewed fuel poverty as not having any specific characteristics that really differentiated it from poverty more generally:

If the poor people whose plight attracts compassion are taken to possess an adequate capacity to manage their own lives, then the most direct and respectful way in which to reduce their avoidable suffering is to increase their incomes (Richardson and Travers 2002: 10).

Contrary to the idea that fuel poverty reflects a more generalised poverty, a better understanding of a household’s energy consumption could act to improve data collection and analysis that seeks to define and measure its financial stress. The ABS collected for the first time in the 1998-99 Household Expenditure Survey data intended to provide indicators of financial stress. Bray (2001) grouped these into three categories:

- **Missing out**: being unable to have family or friends over for a meal, nights out, hobbies, holidays away from home, or having to buy second-hand clothing, due to a shortage of money;
- **Cashflow problems**: being unable to pay bills on time or needing to borrow money from friends or family;
- **Hardship**: being unable to afford heating and meals, having to pawn or sell possessions, or needing to obtain assistance from community organisations.

These three measures are translatable into the above definition of fuel poverty. However, the empirical research cited above also highlights deficiencies. A key measure of hardship – inability to afford heating – fails to take into account the provision of credit by utilities. Credit permits consumption even where hardship exists, but it also means the accumulation of arrears. This can explain the high incidence of ‘inability to pay bills on time’ (Bray 2001: ix). This measure also is problematic because many respondents normally ration their consumption to enable affordability but may not recognise the questions as asking about rationing. Inability to pay on time may be a cashflow situation or

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39 He excluded ‘capacity to raise emergency money ($2,000)’ and ‘living standard worse than two years ago’ as these were of a different conceptual nature.
may indicate inability to pay at all. The experience of community-based financial counsellors is that households prioritise electricity payments and, if they are disconnected, all stops are pulled out to get supply back on (Sharam 2004). This may mean in Victoria that intervention by a financial counsellor, for example, can persuade the utility to reconnect despite outstanding debts and ongoing accumulation of arrears, or it may mean accessing a payday lender. That is, for an income constrained household, electricity as a non-discretionary but periodic purchase is likely to cause cashflow and debt problems which in turn will impact upon its financial viability. This raises an issue as to why the ABS asked whether the household ‘spends more money than it gets’ per week without seeking to understand whether the deficit was addressed through access to savings or use of credit. There is a danger that the indebtedness of vulnerable households masks both cashflow problems and hardship. The obvious implication is whether or not they can service the debt, as highlighted by Burke and Ralston (2003).

The relationship between utilities and household financial stress is explored by Duggan and Sharam (2004) who argue that energy consumption and housing tenure are intimately linked, but that the full privatisation and commercialisation of utilities in Victoria means that energy providers are seeking to have customers prioritise utility payments over other essential household expenditure and minimise arrears and bad debts to a greater extent than in the past. This is one of a number of factors that do not augur well for indebted low-income households. The outcome, they say, will be an increase in the incidence and intensity of ‘hardship’.

To a great extent, fuel poverty arises from exclusion or disadvantage experienced in other markets such as housing and labour markets. The contribution of lack of access to two other essential services – affordable credit and telephone – also has a direct impact on disadvantaged customers maintaining their utility connection (Kymantis 1986).

6.4 Conclusion

Low-income and vulnerable electricity customers exhibit particular characteristics that put them at a disadvantage in a market. The propensity for the accumulation of arrears, the need for flexible payment arrangements and low consumption mark them out as potentially unattractive. On the other hand, many of these customers demonstrate a willingness to
ration consumption and the capacity to budget effectively. Poor payment records can to a large extent be attributed to cashflow crises. Credit management practices that reflect the needs of these customers have been demonstrated as minimising arrears and non-payment. However, it is more typical of utilities to prioritise their own cashflow position, although this often compromises the customer’s capability to pay.

These customers in a market may be subject to corporate strategies aimed at shedding them as customers, or alternatively increasing the rate of return obtained from them in order to adjust for the increased risk. This later scenario would require discriminatory terms and conditions of supply. Exclusion from the market or market abuse would constitute a demand-side market failure.
Chapter 7: Critiques of the market: Commodification, market segmentation, redlining, residual markets and provider of last resort

7.1 Introduction

In the previous chapters I have discussed the contestation over the reforms to the electricity industry with attention to: the nature of supply and demand in this unusual industry; the historical development of the industry and how this has related to domestic demand; the idea, whilst not in law, that electricity is essential and a right; and how neo-liberal reform has sought to change this conception. Despite being sold commercially and despite the owners of the industry (government) requiring and making profits, electricity in Victoria has never been fully commodified. That is, sale of domestic electricity has not been voluntary on the part of the suppliers, domestic consumption has been regarded as non-discretionary (essential), and prices have not been set through a market. Even today, retail domestic prices do not (yet) reflect a free market. In the following chapter I will discuss what is meant by full commodification, so that the distinction between a pure market and non-market provision (or limited market) can be appreciated. Secondly, an understanding of commodification as the basis for markets segues to market segmentation: for segmentation to occur, there must be full commodification. I describe market segmentation and provide some history and some examples. I give attention to two specific segments: the residual market and those customers who are redlined or excluded. Segmentation is then placed in the context of a broader understanding of consumer disadvantage, followed by discussion of some theoretical issues that arise for economics and policy making. Chapter 7 shows that segmentation is occurring in many essential service industries, although largely unrecognised as such.

7.2 Commodification

In this chapter I will demonstrate that market segmentation is not peculiar to electricity but is a reflection of the commodification process that occurs as a consequence of market relations. Polanyi (1945) identified the commodification of labour, land and money as the change that enabled, historically, the development of the market economy. In his view, this specific form of commodification constituted a rationality that required the development of social protections or interventions in the market to counter its destructive tendencies.
Marshall (1950: 18) said that the growth of social citizenship, as he termed protections against the market:

...coincides with the rise of capitalism, which is a system, not of equality, but of inequality. Here is something that needs explaining. How is it that these two opposing principles could grow and flourish side by side in the same soil?...The question is a pertinent one, for it is clear that, in the twentieth century, citizenship and the capitalist class system have been at war.

Later in this chapter I will return to how the difficulties in combining the ‘principles of social equality and the price system’ (or commodification) have translated into utility policies (Marshall 1950: 31). For now, I explore commodification as a process.

Market segmentation and economic discrimination are the logical outcomes of commodification. Polanyi (1945: 72) argued that the emergent market economy of the industrial revolution required labour, land and money to be decoupled from the facts of their concrete existence and commodified to permit the organisation of production through the price mechanism of the market. Despite the fact that they could be bought and sold on the market, none are produced for sale, and their description as commodities was ‘entirely fictitious’. This ‘commodity fiction’, for example, ignored ‘labour’ as people in need of shelter, sustenance and social meaning. Polanyi makes the point that people starved in many famines, not necessarily because there was no food, but because prices rose beyond capacity to pay. In terms of land, he meant the integrity of the natural environment as well as food production. The effect of the commodification was to sever the connection between these commodities and their use value, cost and sustainability. Put another way, the buying and selling of these particular things in a market economy refuted their status as essential because the purpose of the market was not the survival of the community or the individuals that comprised it. Esping-Andersen (1990: 3) has argued:

...the outstanding criterion for social rights must be the degree to which they permit people to make their living standards independent of pure market forces. It is in this sense that social rights diminish citizens’ status as ‘commodities’.
It has been argued that commodification atomises and alienates the objects of exchange. In a market economy, trade in commodities involves profit seeking, frequently based on speculating against movements in prices. The best known contemporary example is foreign exchange in which the vast majority of currency trades are speculative. A run on a national currency can rapidly destabilise an economy.\textsuperscript{40} Polanyi was very particular about the commodification of money because script functions as a symbol of value (exchange). Commodification acts to sever the symbolic link.

Markets in commodities constantly test willingness to pay. The upwards movement of prices is checked by rivalry on the part of competing suppliers. Competition for market share then leads to mergers and consolidation. The result can be oligopoly and sometimes monopoly. Segmentation of the customer base allows the firm to understand which customers provide the greatest profits, and potentially those on whom the firm is incurring losses. Profitability per customer will improve if loss-making customers are shed or a way is found to charge them more. For the existing profitable customers, the strategy is usually how to sell them more. The need to improve profitability and grow market share will increase attention to each customer’s demand and their elasticity of demand, that is, to the profitability of each individual customer.

\textbf{7.3 Segmentation}

Few marketers view each and every consumer as a potential customer. Marketers recognise that their brand, product, or service is not equally valued by all consumers. Instead, they take one of two routes. They either present their brand to a selected group of consumers in the same way, or they market the brand differently to different groups of consumers. The selected group of consumers to whom a firm present its brand is called a market segment. By selecting some but not all consumers as potential customers, a firm focuses on a segment of the market and uses \textit{market segmentation} (Alwitt and Donley 1996: 14, authors’ emphasis).

\textsuperscript{40} George Soros made an estimated billion dollars by speculating against the UK pound in 1992, resulting in the UK floating its currency (<http://news.bbc.co.uk/1/hi/events/the_launch_of_emu/euro_latest/231493.stm>).
Information technology companies are actively promoting segmentation strategies in the electricity industry (Peace 2003, Grey 2002). Segmentation is highly suited to industries that are low margin, high-volume and lend themselves to automation (Coyle 2000). Information technology not only permits collection and storage of data necessary to determine individual profitability, but also adds a great deal of sophistication to the process of assignment into segments – and its policing. The ability of corporations to extensively data-mine individuals means they no longer have to base their risk assessment on crude indicators such as race or gender. The commodity, whether it be a bank account, insurance or electricity supply, under the pressure for profit growth will involve in the delivery to its purchaser a concomitant invasion of personal privacy. This is not merely a matter of the civil right of privacy, but a demonstration of the way in which the act of exchange becomes increasing subject to the will of suppliers (Leyshon and Thrift 1999, Ericson, Barry and Doyle 2000).

An example of this diminished lack of balance between buyer and seller is where firms practise ‘perfect price discrimination’, premised on developing profiles of actual customers that provide a basis for predicting their behaviour (the ultimate segmentation). The seller knows in advance how much the buyer is willing to pay and can mark up the price accordingly. In theory, each customer can be charged a different price. Recent experience with internet selling has, however, shown consumers to be alert to and avoiding systematic attempts at price discrimination. A variation is the application of risk-based pricing. While perfect price discrimination is in some ways covert, risk-based pricing is explicitly actuarial. It involves discrimination aimed at extracting premiums from less attractive customers. It is argued that these prices reflect the cost of supply and the risk associated with specific customers. POLR schemes often involve risk-based pricing.

In order to segment and/or price-discriminate, sellers manipulate the conditions of entry and exit to markets to corral buyers into particular ‘choices’. Hence segmentation takes away some of the freedom out of choice. In cases of product differentiation such as book marketing and computer software, segmentation may extract greater returns from gullible or status conscious customers, but in services such as credit, electricity and even health, lack of discretion to purchase and/or purchasing power may open the way for selective exploitation. Markets in which segmentation is practiced assign customers status, which then determines the type of offers (if any) they will receive. This affects their capacity for
self-determination. It may be argued that strengthening privacy laws would prevent economic discrimination, but this ignores the incentives which firms have, as well as the likelihood of voluntary data disclosure by customers. Information is only one aspect of market power. Perri 6 (2001: 7) argues that:

> the rise of an economy fuelled by detailed personal profiles creates the risk that, if those profiles are handled and interpreted rigidly, many people could be excluded from basic services and opportunities essential to achieving a decent standard of living.

The establishment of buying cooperatives in the late nineteenth and early twentieth centuries was prompted by lack of market power and/or access to markets (Saunders 1993, Purvis 2003). Purvis (2003: 69) states that these cooperatives ‘sought to distance acquisition of the necessities of life from the sphere of competitive capitalism’; however, the attempt at de-commodification was met with opposition from capitalists who, with varying success, sought legislation to curb the cooperative movement’s ability to offer an alternative to the market proper. Esping-Andersen (1990) argued that workers’ cooperatives restricted benefits to higher wage earners, further alienating those who were excluded (the unemployed and poorly paid). This was recognised as a problem impeding working class social solidarity. These early consumer aggregation efforts represent early market segmentation. They also demonstrate the benefits of pooling resources and risks, as well as the distributional implications of de-pooling.

### 7.4 Segmentation: How it works

Market segmentation was identified in the US in the 1930s, although it is generally considered to be a post-World War II phenomenon (Church 1999), and became a regular topic in marketing textbooks from the 1970s onwards. The early periods tend to address demographics, psychometrics and lifestyle. Contemporary texts address companies wanting to attract and retain the most valuable customers, to increase the ‘share of wallet’ they receive from these customers, and to rid themselves of customers who are unprofitable (Fair Isaac 2003). New information technologies which allow for data mining and warehousing have spawned an industry extolling the virtues of identifying the small percentage of consumers who are responsible for the vast majority of spending, and
promoting the capacity and desirability of separating them from those customers who are to be avoided (Hallberg 1995, Berry and Linoff 1997, Clancy and Shulman 1991, McDonald and Dunbar 1995, Stewart 1996).

Segmentation has been subject to very limited examination outside of marketing, although redlining in the US came to the attention of urban sociology in the 1970s. This is not difficult to explain. The conditions for widespread market segmentation across a broad range of sectors – and especially essential service sectors – did not exist in the US, UK or Australia until recently. Apart from industries being state owned or regulated, much of the twentieth century was characterised by monopoly capitalism. Market segmentation, moreover, is a feature of mature mass markets. As Knights, Sturdy and Morgan (1994: 46) argued, regulatory changes to stimulate competition, and changes to the socio-economic profile of the population, were two crucial elements promoting market segmentation of deregulated UK financial markets. They observed that 'market saturation of certain core products' arising out of increased personal incomes in the 1980s initially encouraged segmentation, and this was followed by economic recession and the housing crisis that ‘focused managerial attention more acutely towards costs and profitability as well as new markets’. The decline in household wealth resulted in efforts to ‘select out’ low-profit customers. Ericson, Barry and Doyle (2000: 534) also noted the insurance industry's 'increasingly pronounced' tendency towards segmentation in the neo-liberal era.

Coyle (2000: 90) argued that sophisticated techniques for market segmentation now exist:

The enormous leap recently in computer power, and in data storage and retrieval, means that the complex history of each customer is stored somewhere that will be available to the marketers. A whole industry, called 'data mining,' has sprung up to extract meaning from the information mountain within which our (non)secrets and financial capability lie. The astonishing data-manipulation capabilities already in use – and constantly expanding – ensure that sorting through the data to segment the market into ever tinier slices is the way of the future.

Data mining enables the use of statistical evaluations such as 'credit scoring'. This is the assignment of a value on a person, using not just factual data such as unpaid debts or employment status, but also a risk evaluation based on generic information such as the
locality in which they live. In essence, credit scoring makes up values that are missing in individual profiles compiled through data mining. It is a risk assessment process that is suited to redlining and its opposite, cherry-picking, that is, positive discrimination in favour of affluent (attractive) customers.

The ability to data-mine, credit-score and market-segment works to preclude some of the traditional anti-redlining remedies: 'Electronic redlining will not exclude customers, as the traditional form of redlining did, but rather will avoid including unwanted customers' (Coyle 2000: 102). In the past, providers denied service when it was requested. With new forms of redlining, they simply do not promote their product to people they do not want. Ironically, the same technology can be employed to track redlining, which is what Ralph Nader's Essential Information's Geographic Information Systems project sets out to do. The GIS 'allow[s] traditional database queries to include the ability to analyze data based on locality'. Essential Information (n.d.) uses the GIS 'as a tool for advocacy purposes...to analyze a variety of databases highlighting patterns of discrimination'.

A central issue raised by segmentation is market power. Marginson (1997: 202) observed that liberal theory seems to imagine there is a single 'borderless contestable market'. The concept of 'sub-market' used in trade practices law fails to adequately explain the relationship between their different 'bits'. Edwards (2003: 4) argues that the term 'sub-markets' has been used to suspend the delineation of a 'relevant market at too high a level by referring to smaller loci of significant pricing discretion as sub-markets rather than recognising them as relevant markets in themselves'. Beaton-Wells, Beaton and Beaton-Wells (1997: 38) define market segmentation as:

> a strategy used by suppliers to identify those segments within a market in which they might seek to establish a competitive advantage over their rivals, and thus enhance market share and profitability.

Similarly to Essential Information's approach, Beaton-Wells, Beaton and Beaton-Wells (1997: 41) argue that investigation of market power issues under Part IV of the Trade Practices Act (that is, in anti-competitive conduct cases) would be enhanced if market segmentation as an analytical tool replaced the disputed concept of 'sub-market'. This would work to resolve the judicial 'confusion over the distinction between sub-markets and
market dimensions’. Beaton-Wells, Beaton and Beaton-Wells (1997: 38) also argue that the ‘adoption of a market segmentation method...would facilitate a more theoretically robust, systematically applied and commercially insightful resolution of the issues raised’ in competition cases involving potential abuse of market power. Market power may be exercised but, because market segmentation is systematic, it can also by definition be tracked using statistical analysis.

Leyshon and Thrift (1999: 440) argue that information technology and credit scoring as it is now applied in the UK retail banking sector permit sellers the ‘knowledge competency…to overcome the information asymmetries that lenders confront in their dealings with potential customers’:

Traditionally, there are two ways in which lending institutions have sought to circumvent the problem of information asymmetries. The first has been to accept that these problems are intractable, and opt for a method of 'pooling equilibrium', setting an interest rate that ensures excess demand for debt, and then choosing borrowers at random from all the applicants. However, this passive method of selecting borrowers can be safely abandoned if lenders are able to identify significant characteristics displayed by potential borrowers that might indicate whether or not they will be 'capable' or 'incapable'. Therefore, in order to overcome information asymmetry, retail banks have attempted to collect information about customers in order to be able to be knowledgeable about what sorts of people are 'good' and 'bad' customers…

[C]redit-scoring systems, in becoming the obligatory point of entry to the retail financial system, have set new conventions for deciding who is a ‘good’ and who is a ‘bad’ consumer, producing new patterns of inclusion and exclusion. Credit-scoring systems and an intensification of competition within the industry may well have brought about an absolute increase in levels of financial inclusion, but they have also brought about increases in relative levels of financial exclusion; that is, financial exclusion is now a problem which overwhelmingly afflicts the poorest and most disadvantaged sections of society. Such marginal groups constitute a large and growing proportion of those excluded from financial services, so that if an individual lacks access to a basic financial product such as a current account then
they are in all likelihood living in poverty and suffering from wider problems of social deprivation. It is clear that many people, because they are poor, have an irregular employment history, have encountered problems with debt in the past or have had no previous contact with the financial system are effectively ‘invisible’ to financial institutions (Leyshon and Thrift 1999: 440, 448, authors’ emphasis).

Leyshon and Thrift identified the use of telecommunications systems and information technology in the attraction/avoidance of customers. Incoming telephone calls were screened in relation to area codes. Customers from ‘bad’ localities simply did not get through. ‘Good’ customers received faster connection to an operator and their loyalty was rewarded. Competition and new technology had also removed the emphasis on a network of branch offices. This allowed easier entrance into the market for new competitors and increased cherry-picking. This in turn meant existing financial service providers came under pressure to further limit their exposure to possible bad loans (as the margins in the pool across which risk was spread dropped): more potential customers were denied access to services. In Australia, attractive banking and telecommunications customers have become known as HVCs (high-value customers), and unattractive ones as transactors, value dilutors, barrens or BOZOS (brings only zero outcomes). BOZOS are frequently discussed in terms of requiring ‘terminating’ (Cornell 2003). This surveillance is used in the insurance industry, Ericson, Barry and Doyle argue (2000: 534), to ‘panoptically sort individuals into pools of standard, sub-standard, and uninsurable risks’.

Stepanek (2000) and Bowers (2001) explore the emergence of ‘web-lining’ — the use of the internet to segment markets — and the potential for abuse. Even food retailing has been scrutinised (Bell and Burlin 1993). In Australia the telecommunications and banking industries are increasingly subject to reporting on their customer acquisition and shedding strategies and the language that has developed as a result (Nicholas 2003, Cornell 2003, Lampe 2001, Barker 2001). McDonnell and Westbury (2001) argue that deregulation of banking in Australia has led to discrimination against low-income customers predicated on the combination of producer power and the essentialness of the service. The Parliamentary Joint Standing Committee on Corporations and Securities (2001: 9) noted that ‘fees do not apply equitably, with high-value customers given exemptions while high transaction and low balance customers pay disproportionately more for what is fundamentally an essential service’. Marginson (1997) identified segmentation in emerging
education ‘markets’ in Australia and elsewhere, and the formation of a residual market comprised of government schools lacking the resources to compete. He argued that segmentation in education works to exacerbate socio-economic disadvantage. His view is supported by a review of literature of nine UK public service fields. Perri 6 (2003: 252) examined the experience of individual choice in these services. In terms of distributional outcome he identified a situation in which:

*the market separates into a ‘sink’ sub-sector of under-performing suppliers located in disadvantaged areas unable to attract good staff and for which there are falling levels of consumer demand and no competition between consumers for access, and an ‘elite’ sub-sector of high performing suppliers located in wealthy, leafy areas able to attract good staff, with high levels of application, where there is congestion, and where in effect the suppliers choose the consumers (my emphasis).*

Perri 6 (2003: 259) described the separation of sub-sectors as ‘polarisation’, and noted that research in the education sector appeared to reveal that ‘polarisation limits competition, unless regulation limits its effects’.

### 7.5 Residual markets

Segmentation results in identifiable segments, one of which is the ‘residual market’. Colton (1995d: n.p.) defines this as one ‘for which little or no effective competition exists… Consumers take what is available’. Rosen, Sverrisson and Stutz (2000: 56-7) state:

> When price discrimination is not based on the willingness to pay but, rather, on the consumers’ inability to negotiate the terms of the sales contract, or some other manifestations of market power that turns a particular customer class into *price takers*, particularly for a necessity of life, then it is clear that price discrimination has taken a negative turn. It is also clear that such price discrimination is likely to hurt small customers, while large customers are likely to benefit (authors’ emphasis).

Stutz, quoted in Colton (1999a: 36), warns that small customers face the risk of ‘cost shifting and lack of market power [that] will result in small captive customer rates
increasing’. The view that ‘low-income customers, in a competitive market, will be the least desired customer segment’ is shared by Binz, Feiler and McFadden (1997: 16).

The credit industry is a segmented market, and payday lending represents the residual segment. Segmentation in the industry is premised on risk-based pricing (RBP), with increased risk being addressed through higher prices. Even in cases of default, these higher risk premiums can ensure profitability (Temkin et al.). RBP of loans using credit scoring:

establishes the interest rate for an individual applicant rather than placing the applicant in a pool where the risk is shared…fair [Fair Access to Insurance Requirements] housing advocates fear that RBP may result in higher interest rates for people of color and female-headed households (Smith 2000).

Social status can be the trigger for assignment into the residual market but, as Colton argues (see below), care needs to be exercised in assuming that social status causes economic discrimination, rather than discrimination reflecting market power. In Australia, Stagoll and Lynch (2002) argue that the homeless are discriminated against on the basis of their social status. They conclude, however, that ‘[t]he chronic shortage of affordable, appropriate housing, together with the obvious fact that homeless persons need housing, creates a situation that is often exploited by landlords and proprietors’ (Stagoll and Lynch 2002: 12), arguably supporting a view that rational economic discrimination is being practised, not social discrimination.

Ericson, Barry and Doyle (2000: 535) argue that:

segmentation is simultaneously a process of marketing and one of risk assessment or underwriting, because preferred risks are doubly desirable as insurance clients: they are seen to be both affluent consumers, on the one hand, and less risky in terms of claims, on the other. However, insurers also profit by pooling substandard risks, as insureds in the resulting pool, with little market choice, are compelled to purchase under the most substandard of arrangements.
Ericson, Barry and Doyle (2000: 536) go on to describe compulsory private sector vehicle insurance in Canada as ‘de-selecting’ the poor into a market sub-segment where they are ruthlessly exploited, not just through higher premiums, but through credit provision to pay for these higher premiums, direct debit schemes and unfair termination penalties:

One of the ironies of insurance is that, while it is supposed to pool risks, in practice it tends to unpool them, breaking down the larger pool of potential insured in search of smaller, less risky pools, which are more advantageous for some, while excluding other. Premiums within these smaller pools can be kept lower and claims service can be higher, but only for those fortunate enough to be included. As they observed, insurance is the basis of the welfare state as all risks (such as poverty in old age) are pooled. De-universalisation or marketisation amounts to segmentation.

Alwitt and Donley (1996) question whether market segmentation is ethical. They conclude that it is frequently not, given the propensity for exploitation of vulnerable segments, but that it can also be an ethical means by which the balance of exchange is altered to support the needs of poor consumers. That is, segmentation identifies vulnerable customers, and some form of positive discrimination could protect them.

7.6 Redlining

Another group identifiable through segmentation is those customers who in market terms are regarded as unprofitable. Suppliers may seek to exclude or avoid them through redlining. With a history of redlining, particularly in the insurance and mortgage lending sectors, many US models for electricity competition at the household level have attempted to address the potential for negative economic price/service discrimination by adopting specific anti-redlining legislation. Colton and Coyle have been major contributors to the literature on economic discrimination in electricity markets and markets more generally, market segmentation and the problem of residual markets (Colton 1995a, 1995b, 1995c, 1996, 1997, 1999a, 1999b, 2000, Coyle 2000, see also Shames 1997, Rosen, Sverrisson and Stutz 2000). Colton (1995b: 1) defines redlining as a ‘process of geographic discrimination, where a company either refuses to serve, or to serve on equal terms, an area that is demarcated by racial or socio-economic characteristics’. This meaning relates
to location so that, while there may be heavy correlation between locality and low-income and/or minority status, it is the geographic basis that is relevant.

Colton also defines a second type of action frequently referred to (erroneously, he claims) as redlining: discrimination on the basis of a designated socially sensitive factor such as gender, race or socio-economic status. Colton argues that the distinction is important in determining the appropriate policy response. Equal opportunity laws, for example, address discrimination against minorities – against ‘socially sensitive’ factors. These laws are aimed at preventing certain actions. However, addressing lack of mortgage lending in a low-income minority neighbourhood would require the use of remedies intended to promote specific actions by an industry, such as community reinvestment schemes. The distinction is also important because some discrimination is economically rational, although it may not be socially desirable. Application of policies without this recognition could result in the failure of the policy or exacerbate the discrimination. In stating that some discrimination is economically rational, what is meant is that the seller does not discriminate against a customer on the basis of their skin colour (for example) but, in the case of insurance, on the basis of the propensity for theft in their neighbourhood. The 1968 Governor’s Commission on the Los Angeles riots concluded that it was the prevalence of poverty among minorities that accounted for consumer discrimination rather than racism, although the riots were regarded as race riots. This in part arose from the observation of discriminatory practices within minority groups (Sturdivant and Wilhelm 1973). While geographical redlining in the US is regarded as racist, the correlation between minority status and low income suggests that race becomes a crude way of demarcating populations whose economic status warrants they be avoided by sellers.

7.7 Towards a broader understanding of consumer disadvantage

Redlining involves not just a refusal to serve, but a refusal to provide the same level of service. Colton (1995b) cites research by Zidek comparing banking services available to poor black neighbourhoods and those available to nearby wealthier white neighbourhoods which had three times the services, and their branches had more tellers and loan officers. In the UK the National Consumer Council (2000) developed a framework for examining ‘consumer disadvantage’ after the findings of two earlier studies on why the poor pay more (National Consumer Council 1977, Scottish Consumer Council 1994). They describe
‘consumer disadvantage’ as a persistent shortfall in ‘consumer benefits’ and identify the causes as lack of purchasing power, exploitation, discrimination, social exclusion, other people’s transactions, and provision deficit.

Their analysis of how ‘vulnerability factors’ combine with ‘supply features’ (the characteristics of a particular market) to cause consumer disadvantage is very close to that of Andreasen (1993). Alwitt and Donley (1996) answer the question of why the poor pay more under six headings: unable to take advantage of quantity discounts (low income), mix of commodities they buy in the market, characteristics of marketers in the neighbourhood, lower quality offered for price, differential credit arrangement, and non-monetary costs such as the need to travel to obtain service. The University of Newcastle upon Tyne (2000) found after examining privatisation and restructuring that, for disadvantaged neighbourhoods:

there was evidence of [now private] service providers either physically withdrawing from an area or distancing themselves from customers there…While disconnection from services was uncommon, use of services, particularly energy, was very restricted. Households often experienced difficulties with a range of services at the same time, compounding financial problems. Generally, the poorer the access to a service, the more it cost. The higher costs of using pre-payment meters…exacerbated the difficulties of managing on a low income.

The study concluded: ‘Privatisation and restructuring have left less affluent neighbourhoods and social groups with only limited access to services which could be considered essential for full participation in contemporary society’. Knights, Sturdy and Morgan (1994) found that financial deregulation in the UK had resulted in the withdrawal of many low-margin products, which they believed was intended to limit consumer choice to more expensive and profitable services. Moreover, industry executives understood that competition for the most profitable customers had led to discounted premiums for such customers at the expense – in the form of higher premiums – of lower-income households. This effectively denied some customers access to the market.

Andreasen (1993) examined the renewed interest in the concept of consumer disadvantage in the wake of liberalisation. Like the National Consumer Council he posits
that disadvantage arises from the intersection of the characteristics of consumers and of the markets in which they shop. He places greater emphasis, however, on the ‘rapacious behaviour of sellers’. Accordingly, Andreasen is critical of the 1970s and 1980s consumer rights model that advocates more and better information disclosure and the development of complaint handling schemes because these fail to address the fact that low-income customers are constrained in their choices. While he argues that regulatory regimes should be skewed to the benefit of disadvantaged consumers (who are not responsible for their characteristics) and that the advantaged have a moral onus or ‘special obligation’ to worry about the problems of the disadvantaged, he suggests on a practical level that consumer disadvantage can be addressed by making customers more equal through increasing their participation in the labour market. This ethical concern is also addressed by Alwitt and Donley (1996: 19-20) who recognise that market exchanges between marketers and poor customers frequently involve a lack of trust, are based on a presumption by the marketer that the customer ‘does not have sufficient resources to pay for goods and services’, and on the part of the customer that they will not or do not get a fair deal. They also note that there is often a lack of commitment by marketers to maintain a long-term relationship, ‘as though they are unaware that most poor people are only temporarily in poverty’.

The identification by the National Consumer Council of ‘supply features’ and ‘vulnerability factors’ is important because the various understandings of market relations and models of social protection may or may not reflect or take account of both. The neo-liberal market model, for example, rejects amelioration of consumer disadvantage through changes to the supply features of an industry (such as permitting cross-subsidies). On the other hand, there has been considerable interest in ‘social exclusion’ that tends to focus on the vulnerabilities arising from customers’ social characteristics (Social Exclusion Unit 2004a, Howarth et al. 1998, Gordon et al. 2000, Palmer et al. 2003, Consumer Affairs Victoria 2004, Connolly and Hajaj 2001, Conaty and Bendle 2002, Stagoll and Lynch 2002). The Social Exclusion Unit in the UK, for example, describes disadvantaged persons in terms such as ‘people who have poor basic skills, who have disabilities and long-term health problems or who are from certain ethnic minority groups. Social exclusion happens when people or places suffer from a series of problems such as unemployment, poor skills, low incomes, poor housing, high crime, poor health and family breakdown’ (Social Exclusion Unit 2004b: n.p).
7.7.1 Supply-side dominance of competition policy

Kolsen (1997: 263-4) suggested at the time when the National Competition Policy Act (1995) was being debated in Australia that economic efficiency as the objective of competition reform should really be concerned with the balance of market power between buyers and sellers. He was critical of the Hilmer Report’s assumption that more competition is always better than less, regardless of:

unequal market power and income distribution. Some markets are characterised by monopoly or oligopoly or monopsony or oligopsony on one side and a high level of competition on the other. Many rural product markets have a small number of buyers and a large number of sellers. While numbers alone are not sufficient to establish market structure, or the distribution of income in a market, recognition of a marked imbalance resulted, in the past, in measures to strengthen the bargaining power of the more numerous, weaker, group...Monopsony power and monopoly power will tend to counteract each other. In other words, the monopsony power of buyers will reduce the effective monopoly power of sellers, and vice versa.

He proposed that efficiency could be improved by addressing the issues of the demand side rather than seeking to introduce competition amongst suppliers:

Increasing the extent of competition in that part of the market which is already weaker than the other does not ensure that greater economic efficiency is achieved. Perhaps more important, it also will tend to change the distribution of income in favour of those with greater market power (Kolsen 1997: 253).

Theoretically, the introduction of multiple suppliers has permitted greater choice. But, using Kolsen’s argument, market reform has diminished the market power of domestic electricity customers in Victoria rather than made them sovereign consumers. Prior to competition reform, households were represented collectively (by the state government) and, as aggregated demand, had greater bargaining power with the monopolist SECV than any individual household does today with any retailer. There is an implicit acknowledgement of this in the legislative requirement for the host retailer to offer supply on request. Some groups of domestic customers today (off-peak and rural users, who make up 50% of the domestic customer base) have already lost power in the exchange relationship. At the
present time they are price takers. In the past, monopsony power countervailed against monopoly power. Today there is oligopoly (new entrant retailers comprise only 3% of the domestic and small business market, leaving three retailers who serve 97% of the market (ESC 2004a)) and customer inertia. The market structure under ‘competition’ may be less economically efficient than it was under the previous monopoly arrangement.

7.7.2 Consumer rejection of choice

Markets can be created; institutions can be fashioned to shape the nature of the market; consumers can be educated and trained; and ideology can be wielded to deny alternatives. But markets only really work if embraced by consumers. What makes individuals comfortable with a specific model of exchange? The answer to that is it is contingent. Some industries and some items of consumption, it would seem, have certain characteristics that lead consumers to resist competition, to turn away from the market and the possibility of exercising choice. In these cases it is not politics that is the challenge for neo-liberal reformers but customer inertia:

The apparent preference for convenience and confidence is typically understood as a product of consumer ignorance resulting from the complexity and non-comparability of financial services. However, an alternative account is that it reflects not so much consumer preference, but a lack of interest in, or even an indifference towards, financial services – an attitude which is reinforced by the complexity of products in this field. Even in terms of service provision or delivery there remains considerable ‘inertia’ – consumers do not tend to ‘vote with their feet’ (Knights, Sturdy and Morgan 1994: 50).

Knights, Sturdy and Morgan are alert to the orthodox explanation given for lack of consumer responsiveness: the need for further consumer education. In Victoria the ESC did not feel the need to look any further than consumer ignorance to explain lack of consumer participation in the market. This probably should not have been the case, given that switching rates have been low internationally. The ESC managed to studiously avoid investigating, for example, why only half the switchers they surveyed could name more than one retailer (when as switchers they should have been able to name two). Moreover, 50% of switchers did not know they had actually done so, which should also have
instigated further research (ESC 2004a). Despite being alerted to the impact that moving
dwelling has on putative switching rates, the ESC would appear to prefer to conflate
unintentional switching with intentional switching as if there was nothing problematic about
doing so. If we were to take the above quote by Knights, Sturdy and Morgan, the words
‘financial services’ could be swapped for ‘electricity’ and it would describe the experience
of FRC in electricity in Victoria. Knights, Sturdy and Morgan (1994) suggest, as this
research does, that because of customer inertia some industries will be characterised by
producer power even in situations where there are numerous suppliers.

It may be the case that in years to come consumers will engage in the market. This may
simply be a result of having no experience of any alternative form of delivery. At the
moment, however, we have markets being imposed despite popular resistance to such
change (see Chapter 12). The ‘choice’ that was sought (politically) was to not have choice
(between competing private firms). In the words of an age pensioner when door-knocked
by an electricity retailer: ‘I don’t want choice – I want service’. 41 For economists, customer
inertia may need theoretical investigation. The possibility that consumers may not want to
have choice is not considered by economics. Customer inertia would normally be regarded
as an example of market failure, which it is. Economists may need to be more specific in
nominating the cause of market failure, and add ‘consumer indifference’ or consumer
preference for alternatives to the possibilities that may present in a real life situation.

7.7.3 Macro-economic consequences of segmentation

Froud, Johal and Williams (2002: 62-3) have identified macro-dynamics associated with
market segmentation. They do not identify segmentation per se but a ‘cheap goods/jobs
nexus’ that produces disadvantage or a ‘micro experience of inequality’. They identify two
drivers interacting so that ‘inequality reinforces inequality’. The first is a bifurcated (that is,
segmented) labour market/goods market that is the ‘primary direct cause of inequality’.
The second is the need for households to privately provision for old age. The latter, given
the mooted end of universal provision of old age pensions, drives economic restructuring.

Economic restructuring aimed at increasing profits renders much employment precarious
in the never-ending search for lower wages. The bifurcated labour market produces

41 Personal communication, Angela Savage, policy analyst, Victorian Council of Social Service.
inequality that interacts with consumption. In my terms they have identified a residual market. They make the observation that the ‘resources and choices of the non-poor have so much weight in a market economy where incomes are unequally distributed’ that poverty analysis needs to look beyond the characteristics of those who are poor to the behaviour of the upper income quintiles (Froud, Johal and Williams 2002: 64). An example in Australia would be investment in rental properties and the contribution this has made to both the inflation of housing prices and rental costs. This private investment has worked to make home ownership unaffordable for lower-income groups, but it has also meant these households are in tenancies that require rates of return that more than cover the cost of the inflated housing price.

Froud, Johal and Williams’ argument is that the current drive for economic growth, which is at the expense of social protections, has engendered such significant inequality that we are entering a period of economic and social instability. The conclusion that could be drawn is that pressure for increased profits will push more customers into the residual market, and more out of the market altogether. Society will become more economically polarised, and demand will ultimately collapse because too few customers can support production and because these customers will face higher prices, given the decline in subsidies from the residual market segment.

7.8 Conclusion

In this chapter I have shown that segmentation in essential services appears to occur where there is a lack of regulation to protect disadvantaged and vulnerable customers, or put another way, where people as customers are denied the opportunity to avoid full commodification. It is not that information technology may become an ‘engine of exclusion’ as Perri 6 (2001: 42) fears. Rather it is that technology has combined with competitive pressure. In Perri 6’s words, ‘competition policy’ construed as economic liberalisation has created opportunity in more sectors of the economy for exclusion to occur. Segmentation and exclusion existed prior to the rise of sophisticated information technology.

In the following chapter I turn to the experience of electricity industry reform in the US, the UK and Victoria. In Chapter 8 I demonstrate that concern regarding segmentation has been a crucial issue in the US. In the UK the household sector was extensively segmented.
prior to competition, highlighting the role of public policy in promoting segmentation and residual markets. In Victoria public policy appears to support contradictory objectives: the safety net encourages segmentation and is discriminatory, but government has extended price caps and the universal obligation to supply. The Retail Code that sets out the terms and conditions of supply has shifted over time from ensuring the customer has the flexibility to pay to a focus on protecting the retailer’s cashflow, but also prevents disconnection for incapacity to pay. This confusion reflects the continuing struggle over reform. I provide a detailed discussion on prepayment metering technology as this has enabled segmentation in the UK and is a method of subverting social protections.
Chapter 8: Electricity deregulation and liberalisation

In this chapter I take the observations made of segmentation in other essential services markets and reflect upon market reform of the electricity industry in the US, the UK and Victoria. In each case it can be demonstrated that the impact of potential or actual market segmentation is a matter of public policy debate. Of particular interest is the role of government mandated safety nets or POLR in aiding or preventing the formation of a residual market.

8.1 Electricity deregulation: The US experience

Not every electricity customer is equally profitable to serve. Not every area costs the same to serve. In a deregulated industry, electricity service sellers that operate solely on a for-profit basis may be allowed to choose freely whom they will serve and the rate they will charge each customer. If they do, they can be expected to segregate customers by geographic area, past credit records and income level, and sell to the most attractive customers. If they do, what quality at what price can people in high-cost, difficult to serve, areas expect? How will people with lower incomes be assured they can afford electric service? Unless these questions are equitably resolved, deregulation will not benefit the whole nation (Alliance to Protect Electricity Consumers 1998).

Literature on the experience of domestic customers in fully competitive electricity markets is limited, due to their recent opening to such customers. In the US, less than half the states embraced deregulation. Most which did so inserted specific anti-redlining provisions into their legislative frameworks, and continued both the right of supply at a fair and reasonable price, and lifeline tariffs that are in some cases as much as 50% discounts on the standard tariffs for low-income customers (NEAAP 2002). These provisions specifically act to mitigate market impacts, and hence the US experience must be treated with a good deal of caution. Nevertheless, in working through deregulation where it occurred, the experience and the debates provide useful insights.
The New Jersey Board of Public Utility Control (n.d.), for example, explicitly provided for anti-economic discrimination measures in its Interim Retail Choice Consumer Protection Standards for electricity competition. It defined redlining as

a procedure which involves unreasonable discrimination based upon race, color, national origin, age, gender, religion, source of income, receipt of public benefits, family status, sexual preference, or geographical location.

Colton (1999a) prepared a similar definition for the Colorado legislature which also included credit status and disability, both strong indicators of level of income. However, as Coyle (2000) noted, governments may recognise economic redlining as a problem, but they are failing to understand the distinction between active exclusion and omission.

Many states in the US decided that the legal obligation to supply could be satisfied by having a safety net tariff or POLR (also called standard offers, default, basic generation service – approximates of Victoria’s standing offer) (Tschamler 2000). Ohio and Pennsylvania decided their POLR rates would be the same as their ‘standard rates’ – the price cap offered by the incumbent. Most states had the utilities bid in the first instance to become the incumbent supplier of the standard service to their local domestic market. Non-incumbents compete against this ‘standard service’ tariff. Low-income customers in most states are recipients of rate discounts. For example:

Low-income Pennsylvanians also enjoy some of the biggest power discounts in the country…people below the poverty level in Philadelphia pay just 50 percent of their power bill for their first 500 kilowatt hours, said Philip Bertocci, a supervising attorney at Community Legal Services in Philadelphia. The subsidy costs the Philadelphia utility and its customers $ 50 million a year, he said. Those discounts don't disappear under deregulation, even if low-income customers switch to a new retail electric provider (Oldham 2001).

Texas, in contrast, implemented a POLR scheme for customers who pay their bills late or those whose retailer exits the market that was 50% more expensive than the standard rate and 60% more expensive than the low-income rate (Oldham 2001):
DALLAS KEEPS POWER ON – Dallas ACORN [Association of Community Organizations for Reform Now] is keeping the pressure on the local electricity provider, TXU, to fend off the most damaging elements of the Texas deregulation plan and keep the power on for low-income residents. On April 27, ACORN members visited the home of a top TXU official, along with television cameras, to present him with a ‘Screwed’ award (a giant screw). TXU had recently announced that anyone who falls two months behind on their electricity bills will immediately be dropped from their standard service and handed over to the Provider of Last Resort (POLR). This means that many low-income residents who struggle to meet the rising cost of their bills will be quickly transferred to another company, which will require large deposits and charge them much higher rates (ACORN 2002).

After protests, the POLR rate was lowered to 20% above standard rates. Randy Corbin, assistant director for analytical services at the Ohio Consumers' Counsel, argued that a ‘vicious cycle’ is created when the POLR is priced higher than standard service offers because those having the greatest difficulty in keeping up with payments are those most likely to find their way into the POLR where their disadvantage becomes exacerbated by the higher costs (Oldham 2001). Alexander (2001b: n.p.) argued:

> low-income customers are clearly more at risk in a system that adopts the Texas POLR model because this approach focuses on those that drop out of the competitive market and does not link this smaller group to the larger pool of residential customers who do not shop around for electricity in the competitive market.

Oppenheim (2001) argued that the relationship between standard offers and POLR replicates disadvantage and marginalisation. Customers in Massachusetts lose the protection of their standard offer, a fully regulated fixed rate, when they move to a dwelling in a different utility service area. They are supposed to choose a competitive supplier, otherwise they are assigned the default (POLR) tariff (the price of which has trebled since deregulation). Because of low levels of home ownership, low-income households tend to move more frequently than those on higher incomes, and are further disadvantaged because the POLR is frequently the only offer they can access. They in effect cross-subsidise better-off households who can stay on the standard offer because they have
greater housing stability. The National Energy Affordability and Accessibility Project reported in May 2002 that Massachusetts utility NSTAR was refunding $1.45 million to customers (after a class action had been initiated) because it had ‘erroneously’ moved 24,000 households to the more expensive default service. The utility said that its computer had failed to distinguish between customers relocating inside its service territory and those who were new (NEAAP 2002). Whilst this may be construed as a cynical attempt to raise revenues, it demonstrates how poverty issues intersect and, specifically, how default or POLR schemes can institutionalise discrimination against disadvantaged groups.

The State of New York Public Services Commission (2001: 52-65), in grappling with the notion, concluded that with sufficiently robust competition a POLR would not be needed. Despite this, it acknowledged that, unless the law imposes an obligation to serve all customers, some would not be served. It argued further that ‘the greater concern is the price a poor customer would have to pay to receive service from the market’. The commission regarded rational economic discrimination (providing price signals for load management) as allowable, but discrimination based on the customer’s income ‘should not be permitted for the supply of these essential services’. This was basically saying that a vulnerable customer’s lack of economic power should not be exploited. The commission also discussed the problem of creating a POLR to supply vulnerable customers as this depooling of risk spreads the cost of supply over a smaller customer base, effectively lifting the cost of supply to each customer in the scheme.

Alexander (2001b) reported on official efforts to jump-start competition in Massachusetts by providing competing suppliers with a list of information about customers who have not switched. Not surprisingly, utilities supported such moves, although they declined an interest in obtaining customers’ credit histories, arguing instead that those with arrears of 30 days or more should simply be left off the list. The state regulator rightly refused to permit release of this information. Utilities also sought the removal of barriers to the taking of electronic signatures (internet-based enrolment). In internet-based selling, the customer base is already segmented, as the poorest sections of the community have less access to quality telecommunications infrastructure, personal computers and the education necessary to use them, a phenomenon described as the digital divide (Cooper 2000, Cooper and Kimmelman 1999, Kahl 1997, National Telecommunications and Information Administration 1999).
Colton (1995c: 1) also pointed to the rush to disconnect when California deregulated its electricity industry.

Southern California Edison has already cited competition as the primary reason to change its collection practices. In that case Southern California Edison chose to treble its service disconnection (up to one million customers in 1995 alone), citing competition as the main reason it was calling in debt.

Either lack of competition or customer inertia provides incumbent firms with market power. An effective monopoly allows prices for captive customers to be subject to undue increases. Stutz, quoted in Colton (1999a: 36), makes the comment that many existing programs do not afford adequate consumer protection in a competitive environment and 'would need to be strengthened and expanded'. Fear of cost shifting, price discrimination and market failure were central to a Consumers Union/Consumer Federation of America (1988) report on electric utility restructuring. The Consumers Union (2002a: 3) later reported electricity providers offering two service fee brackets, one for customers with 'good' credit histories, and the other for those with 'poor' histories: 'never before has the price of electricity been based on a consumer’s credit history'. It also found offers that required electronic billing and payment or else surcharges applied, discriminating against customers who needed traditional paper-based payment methods.

Alexander (2001a: 5) argued that residual markets for low-income electricity customers should be avoided because, with no cross-subsidisation from other customers, the POLR price will 'be higher than that available in the competitive market' (author’s emphasis). Alexander developed a model consumer code for competition that has been utilised by a number of US states. She observed that the adoption of POLR tariffs has been the result of two conflicting policy objectives and identified that:

If you believe that the prime imperative that must govern the decisions surrounding the implementation of retail competition is the need to create a competitive market as soon as possible, Default Service is a tool that should be wielded to achieve that end.

If you believe that the competitive market is unlikely to develop in the near future or when developed, is likely to result in higher prices or less stable prices for
residential customers, Default Service is viewed as a tool to maintain important consumer protections and maintain the longstanding acceptance of the universal service aspects of basic electricity service for residential and low-income customers.

Disregarding the imperatives behind the default service, she noted that, as the vast majority of domestic consumers have opted not to enter into the market:

the Default Service decisions have [therefore] been the primary factor in determining the price and identity of the provider of basic electric service for the overwhelming number of customers in states that have implemented retail electric competition (Alexander 2001a: 3).

Paul Fenn (2000), representing Local Power – a consortium of Californian consumer representatives – in his testimony before the Joint Hearing Senate Energy, Utilities and Communications and Assembly Utilities and Commerce said the default supplier arrangements for California’s deregulation and customer inertia meant these suppliers had a monopoly over the customers:

Under AB1890, these companies are designated as ‘default suppliers’ of Californians who do not find their own power suppliers. As I mentioned before, 95% of Californians have not found a supplier. By allowing these deregulated former power suppliers to hedge the state pool or California Power Exchange (PX) and offer hedged ‘service packages’ to their former power supply customers, they are in effect being unofficially reinstated as default aggregators, which in effect amounts to re-monopolisation.

The Power Exchange is not – as some revisionists have recently argued – the competitive market that Californians were promised for their $30 billion in 1996. It was created as a backup system for the unprofitable consumers (hence the term ‘default service’), much as many states have created property insurance redlining pools for poor people in ‘high risk neighborhoods’ who often cannot find an insurer who will offer them coverage. The fact that this redlining pool includes 95% of Californians does not make it a market.
The concerns of these advocates need to be contrasted with the radical free market position in which the notion of electricity being a ‘right’ is strenuously refuted. Rochlin (2002: 33), for example, argued: ‘When prices rise, consumers, not third parties, [should]…decide when to voluntarily forego the use of electricity’.

8.2 Electricity deregulation: The UK experience

Even in the UK, which has had switching rates in the order of 30%, customer inertia and strategic pricing have raised doubts about the success of competition (Brigham and Waterson 2003, Giulietti, Waddams Price and Waterson 2000). Long before competition commenced, segmentation of the domestic electricity market had been achieved through differentiating prices according to payment method. The options are direct debit, traditional credit and prepayment metering (PPM). Competition is weakest (and prices highest) in the PPM segment, while the largest savings are accruing to customers who use direct debit (Ofgem 2004). PPM is associated with low-income households and private rental, raising concern that competition is in effect taxation of the poor (Boardman and Fawcett 2002). National Energy Action (2000) also expressed concern about the lifting of price controls, as ‘from the perspective of prepayment customers it will be difficult to view such developments as non-discriminatory’. The Public Utilities Access Forum (1999: 2) said:

If disadvantaged consumers are seen as too costly, suppliers may either seek not to provide them with services, or charge them at higher price than the average consumer (‘social dumping’). Suppliers may seek to concentrate their supply of service to better-off consumers (‘cherry-picking’), and avoid supplying low-income consumers by offering unattractive prices to them. Both ‘social dumping’ and ‘cherry-picking’ could broaden the gap between the advantaged and the disadvantaged.

A three year longitudinal survey of the experience of low-income households in the competitive UK energy market, commissioned by the National Right to Fuel Campaign and the Centre for Sustainable Energy, found that many people had been lifted out of ‘marginal fuel poverty’ as a direct result of lower prices (acknowledging that gas input prices had declined substantially over the period), but that the number in severe fuel poverty had increased:
New suppliers were continuing to ‘cherry-pick’ the more affluent consumer. Most companies were competing on price for certain consumer groups, primarily Direct Debit payers, rather than ‘added value’ services. Special services to vulnerable groups, such as disabled and pensioner households, were not improving (Baker 2001: 8).

The study referred to this disparity as ‘uneven development’, which is characteristic of economic discrimination or segmentation:

they [fuel suppliers and Ofgem] argue that Direct Debit consumers are much cheaper to service than prepayment meter and frequent cash payment customers. Competition, encouraged by regulatory action, leads to cost reflective pricing and the elimination of cross-subsidies. This means that previously ‘hidden cross-subsidies’ of certain payment options are revealed. Suppliers seek to gain competitive advantage by attracting consumers who pay by more cost-effective payment options. However, these trends exacerbate existing inequities between affluent and low-income households since prepayment meter and frequent cash options are more commonly used by low-income households (Baker 2001: 14).

Misleading and deceptive marketing has also contributed to low-income customers not obtaining discounts by switching. Brigham and Waterson (2003) found retailers did not intend to market door-to-door to poor neighbourhoods, but their door-knockers working on commission shied away from their assigned targets – wealthy suburbs. The National Association of Citizens Advice Bureaux said:

evidence of service failures experienced by customers who are on the lowest incomes, or benefits, and who are arguably the most vulnerable is so widespread we believe it threatens the present Government’s strategy for tackling fuel poverty experienced by the most vulnerable households...The force of competition alone is clearly not eliminating poor service for customers who are CAB clients. Indeed the competitive pressures on companies seem to produce the conditions in which vulnerable consumers who lack resources and skills are taken advantage of (Monroe and Marks 2002).
Though a great deal of research shows deregulation to be of overall benefit to consumers in the UK, the evidence suggests that this has not been evenly distributed (Boardman and Fawcett 2002, Baker 2001).

### 8.3 Electricity deregulation in Victoria

In the following section I argue that the Victorian government’s safety net provisions constitute a POLR that discriminates against the customers it presumably is meant to protect. In addition I detail how commercial pressures have been brought to bear on the consumer protection framework over time. These changes do not particularly affect wealthier customers, but they reduce the flexibility required by low-income customers to make payment. The options available to retailers under the Retail Code have the effect of specifically enabling discrimination against low-income, disadvantaged customers. It demonstrates how the pressure to commodify acts to segment the customer base. These measures allow the retailers to reorder household expenditure or, as Drakeford (1997) suggests (in regard to PPM), permit retailers as creditors to ‘leapfrog’ over others. The changes to the Retail Code that occurred in preparation for FRC are the type of retailer ‘benefit’ sought through the introduction of PPM, except that this is less clumsy and hides the ‘problem’ of disadvantage and disconnection. I return to PPM as the looming residual market later in the chapter. Before that, I explore some governance arrangements and show that these also aid segmentation whilst distancing customers politically from decision making that affects them.

#### 8.3.1 Background

The reform model envisaged a three year period in which customers would migrate onto market-based contracts from their deemed tariffs, which were temporary contracts onto which all former franchise customers were transferred when the market opened in January 2002. Once a customer switches or moves residence, the deemed contract is void. A standing offer tariff was also created at this time, constituting a temporary safety net that ensured all domestic customers had access to supply from at least one retailer (their former host retailer) on regulated terms and conditions. Both the deemed and standing offer tariffs were subject to a sunset provision in the legislation. While the standing offer exists, it can be considered as a POLR. The government did not provide any advice on
why it had included a sunset provision and how it would reach any future decisions in regard to social protections. It sought advice from the ESC in 2004 on the potential for winding back the safety net provisions afforded by the existence of the deemed and standing offer tariffs after 2005 (ESC 2004a). The terms of reference for this ministerial investigation excluded any consideration of simply extending them into the future. This indicated a potential policy direction favouring some type of targeted assistance rather than universal service provision. The deemed and standing offer provisions have subsequently been extended in time. The coverage of the safety net remained universal.

8.3.2 The standing offer as POLR

Government reserved the right to set prices for deemed and standing offer tariffs which are deliberately higher than those available in the market. This premium is known as the headroom, and its purpose is to facilitate the entry of new retailers and to encourage competition amongst existing retailers in order to instigate downward pressure on prices. Given the standing offer tariff was intended to support customers that are unattractive in the market, the higher tariff rate means this POLR scheme can be regarded as discriminatory. As ‘attractive’ customers migrate to market-based contracts, the loss of universal service will place upward price pressure on those in the POLR (Alexander 2001a, 2001b). However, until some change in the nature and coverage of the safety net occurs, it would appear that customer inertia (see Chapter 12) is impeding the migration of more attractive customers. The implication is that the market is not likely to segment without the active intervention of government. The ESC (2004a) suggestion that high-volume customers lose coverage of the Retail Code would facilitate a two-tiered system that would constitute such an act of intervention.

8.3.3 Commodification and the reordering of household expenditure

Utilities have always been concerned about protecting their revenue and cashflow against late payment and default. Competition has served to heighten this concern. Market segmentation can assist in addressing the problem by identifying customers for shedding or by ensuring problem payers are offered only products that will guarantee returns for the retailer. Retailers remain, at present, constrained in the use of such a strategy by the existence of the deemed and standing offer tariffs and by customer inertia. Nevertheless,
the shift to the market is reflected in the Retail Code, which has been altered considerably since the early 1990s to permit a more expressly ‘commercial’ approach (ORG 2000b). The following section shows how the shift to the market already leans towards differential treatment of customers and segmentation.

The *Electricity Industry Act 2000* made the ESC responsible for establishing the minimum standards of consumer protection for FRC and prescribing the terms and conditions of supply for the deemed and standing offer tariffs. The ESC is an independent energy regulator charged with a number of obligations, the primary one being to ‘protect the long-term interests of Victorian consumers with regard to price, quality and reliability of essential services’ and at a secondary level ‘to ensure that users and consumers (including low-income or vulnerable customers) benefit from the gains from competition and efficiency’ (*Essential Services Commission Act 2001*). The regulator prepared a position paper, *Minimum Standards Framework for FRC*, detailing its formulation of the role of consumer protection in the competitive market (ORG 2000b). It also revised the Electricity and Gas Retail Codes, the legally binding instruments which detail the rights and responsibilities of both customers and retailers once competition commenced. The Retail Code was based on the Sale and Supply Code in use under the SECV (Siemon 1995).

The shift in the regulation of domestic supply from monopoly to competitive supply has effected a reordering of household expenditure. Just how this occurs is described below, but the results have been evident for some time. Benvenuti and Walker (1995) examined an apparent trend towards harsher credit and debt recovery practices by the corporatised retailers.42 Romeril (1998) later attributed the significant jump in household disconnections during the corporatisation period to the retailers’ increased commercial focus. Kliger (1998) studied the credit management and debt recovery practices of the privatised retailers, finding harsher practices and regular non-compliance with the Retail Code. A similar study also undertaken for a financial counselling peak body subsequent to FRC had similar findings (Sharam 2004). Two themes emerge. The first is that the regulation of credit management and debt recovery has shifted focus from the needs of vulnerable customers to providing retailers with greater flexibility. The second is that, even where protections

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42 The Victorian government disaggregated the SECV and corporatised the new businesses (that is, set them up under corporation law rather than as statutory businesses), which were later sold to the private sector.
exist that favour disadvantaged households; retailers have frequently ignored them, and the regulator in turn has ignored such non-compliance. The state, rather than the market, has been instrumental in permitting private energy retailers to leapfrog over other creditors. This reordering provides a foundation for later market segmentation.

8.3.4 Regulating for risk

Under the Retail Code and its subsidiary guidelines, there are a number of measures to mitigate retailer losses accruing from non-payment or late payment. The key methods of containing financial risks are the application of risk premiums, the seeking of compensation, and a general strategy to increase the price paid by problem payers. I call these ‘recovery’ and ‘pre-covery’ mechanisms.

Risk premiums increase the price paid by vulnerable customers, but this heightens the probability of arrears and default on payment. If a service is non-discretionary but chronically or periodically unaffordable, the consequences are obvious. On face value, this strategy may lift profits, but increased default and late payment might offset the gains. In practice it depends on the size of the risk premium and who assumes the cost.

8.3.4.1 Security deposits

A customer at the point of connection or reconnection may be asked to provide a refundable advance (a security deposit or bond). If they are experiencing chronic fuel poverty, this merely increases their financial stress. The bond may protect the retailer from potential losses, but it adds to the likelihood that the customer will default. Refundable advances are like maximum tariffs and high standing charges in that they act as pre-covery mechanisms for the retailer, being a form of insurance against potential default.

8.3.4.2 Reconnection fees and late payment fees

High reconnection fees and late payment fees (if they were ever permitted) act in the same way as security deposits except that these are recovery forms of compensation.
8.3.4.3 Collection cycles

The collection cycle is the timing of bills, reminder notices and disconnection warnings. Its length will reduce or increase the customer’s flexibility in making payment (McLeod 2001). If it is longer, it is a cashflow loss for the retailer. The Energy Industry Ombudsman (Victoria) in a confidential submission to the ORG (obtained under Freedom of Information) said shortening the gas collection cycle would be ‘likely to have a major impact on increasing disconnection’ (McLeod 2001) because many customers would not be able to overcome their own cashflow problem. Where the customer manages to do so, the shortened cycle effects a reordering of their expenditure, placing the utility over other essentials. The established practice for many years had been to allow for two pension or benefit payments (four weeks) between the date of issue and the due date. Shortened collection cycles have been permitted since the privatisation of the industry, and the standard cycle has been reduced by two days. Simply failing to pay by the due date (rather than on the disconnection notice) can result in the customer being shifted to a collection cycle in which reminder notices are no longer issued, but disconnection warnings are issued immediately if there is non-payment by the due date.

Customers who have had arrears are also frequently placed on a monthly rather than quarterly cycle. If they default, the disconnection will be, by definition, for a far smaller amount. The size of the debt is relatively unimportant as the issue for the customer is cashflow.

8.3.4.4 Debt recovery

The Retail Code provides retailers with the legal right to payment in full and hence to debt recovery. However, a customer assessed as experiencing incapacity to pay has the right to an ‘affordable’ instalment plan and can therefore avoid disconnection for arrears. Retailers routinely contravene this legal requirement, and customers disputing decisions involving incapacity to pay have not necessarily been able to enforce their rights by recourse to the Energy and Water Ombudsman Victoria (EWOV) (Sharam 2004). The ESC has failed to enforce this provision (Sharam 2004, VCOSS 2004b, Royall 2004).
8.3.4.5 Credit checks

Generalised credit checks are not permitted under the Credit Management Guideline that forms a subsidiary instrument to the Retail Code. Retailers are able to check for debts relating to gas, electricity or water only. A recent development is the emergence of firms that work with real estate agents offering a ‘one-stop shop’ service to connect tenants to all their utilities, including telecommunications (VCOSS 2004b). The emergence of ‘moving agents’ as they are known has led to concerns regarding misleading or deceptive practices on the part of the agents and retailers involved. Accordingly the ESC, the EWOV and Consumer Affairs Victoria are examining the issue (ESC 2004a).

Such a service has a significant advantage for energy utilities as potential tenants supply considerable amounts of personal information to landlords and estate agents in order to secure a tenancy. A successful tenant is assessed as a worthy credit risk. In this way, utilities can avoid undertaking their own credit assessments and also avoid some of the restrictions of the Credit Management Guideline issued by the ESC. The effect is market segmentation of customers in private rental housing.

8.3.4.6 Higher prices

As a safety net tariff, the standing offer was likely to service those customers considered credit risks or regarded as low- or no-margin. For the most vulnerable low-income customers, access to supply is premised on the payment of a premium, that is, the headroom. But domestic tariffs have already increased significantly for many customers, and regressive changes to tariff structures mean lower-volume customers assume the bulk of such increases. Tables 2 and 3 demonstrate the impact of the increased fixed charges on low-consumption households between 1991 and 2003. Low-income households spend proportionally more of their income on their energy needs than higher-income

43 I would argue, nevertheless, that if a household had utility related debts it would be likely that they would have other debts, so prohibition on access to wider data is probably ineffective.
44 Tariff structures changed significantly under the Kennett government reforms. Firstly, the tariff rate was raised by 10% in late 1992. In 1993 the fixed charge, which had been reintroduced during the early corporatisation phase of the SECV, was doubled from $17 to $33 per quarter. While the government and indeed the ESC claim that domestic prices fell as a result of the reforms, those claims only consider the period after 1995 from which time legislated cuts took effect.
45 Gas, electricity, LPG, wood and other fuels used for domestic purposes (heating, cooking, lighting, hot water heating, refrigeration).
households (Kiers 1983, Deasey and Montero 1983, Siemon 1995, Ernst 1994a, Lawrence 2002a, Roy Morgan Research 2002). My survey found that 42% of Victorian households engaged in rationing as a budget measure. Table 2 shows that low-consumption households across all retailers experienced price increases in this period. These correlate heavily with low-income households. Other than Citipower customers with a medium level of consumption, the only customers to receive price cuts were the high-volume users. Vulnerable households not only pay a higher tariff rate, but the fixed charges guarantee the retailer a minimum level of payment that is significantly more than in the early 1990s.

Table 2: Percentage change in end-cost electricity, general domestic customers, 1991-2003, including GST (GD/GR tariff SECV and deemed/standing offer tariffs)

<table>
<thead>
<tr>
<th>Retailer</th>
<th>Low</th>
<th>Medium (0.32)</th>
<th>High (5.5)</th>
<th>Average 0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citipower</td>
<td>6</td>
<td>5</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>TXU</td>
<td>11.3</td>
<td>5</td>
<td>2.8</td>
<td>5</td>
</tr>
<tr>
<td>Origin</td>
<td>13.8</td>
<td>8</td>
<td>5</td>
<td>9</td>
</tr>
<tr>
<td>Pulse</td>
<td>6.7</td>
<td>0</td>
<td>3.3</td>
<td>1</td>
</tr>
<tr>
<td>AGL</td>
<td>6.7</td>
<td>1</td>
<td>2.6</td>
<td>2</td>
</tr>
<tr>
<td>Average</td>
<td>8.9</td>
<td>3</td>
<td>1.8</td>
<td>3</td>
</tr>
</tbody>
</table>

Note: Low volume = 2,500 kWh p.a.; medium = 4,000 kWh p.a.; high = 6,000 kWh p.a. Two-block inclining tariff, with differential between first 1,020 consumption per quarter and balance per quarter. An assumption is made regarding how much annual consumption is charged at the higher rate, given the lack of actual consumption data. This assumption is that consumption is uniform over each quarter.

Tables 2 and 3 show the impact of the tariff structure changes. The lower the annual consumption, the larger the price increase. The difference between customers with off-peak (Table 3) and those without (Table 2) is quite considerable. The price change for off-peak users has been dramatic. There are approximately 500,000 off-peak domestic customers in Victoria. The government and the ESC have not responded to calls from domestic consumer and welfare groups to introduce ‘pricing principles’ to ensure equitable tariff structures (VCOSS 2003).
Table 3: Percentage change in end-cost of electricity consumption to general domestic customer also taking supply under Y6/T6 off-peak hot water, 1991-2003, including GST (GD/GR tariff SECV and deemed/standing offer tariffs)

<table>
<thead>
<tr>
<th>Retailer</th>
<th>Low</th>
<th>Medium</th>
<th>High</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
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<td>7.3</td>
<td>1.3</td>
<td>(6.1)</td>
<td>0.8</td>
</tr>
<tr>
<td>TXU</td>
<td>24</td>
<td>15</td>
<td>3.9</td>
<td>14</td>
</tr>
<tr>
<td>Origin</td>
<td>18</td>
<td>12</td>
<td>7.8</td>
<td>11.2</td>
</tr>
<tr>
<td>Pulse</td>
<td>15</td>
<td>7</td>
<td>1.7</td>
<td>8</td>
</tr>
<tr>
<td>AGL</td>
<td>11</td>
<td>4.7</td>
<td>0.4</td>
<td>5</td>
</tr>
<tr>
<td>Average</td>
<td>15.2</td>
<td>3</td>
<td>1.5</td>
<td>8.2</td>
</tr>
</tbody>
</table>

Note: Low volume = 2,500 kWh p.a.; medium = 4,000 kWh p.a.; high = 6,000 kWh p.a. Two-block inclining tariff, with differential between first 1,020 consumption per quarter and balance per quarter. An assumption is made regarding how much annual consumption is charged at the higher rate, given the lack of actual consumption data. This assumption is that consumption is uniform over each quarter.

While there is evidence to support the contention that retailers may seek to avoid low-profit customers (Community Power 2004, Sharam 2004), the government’s safety net arrangements currently make it difficult for retailers to shed customers. Alternatively they can retain these customers but increase prices further. While there is customer inertia, my survey found that the single largest group of switchers were low-income customers. Due to inadequate response to questions relating to price offers, I was unable to determine whether they received benefits as a result of switching. However, analysis of Origin Energy’s ‘Inside 50’ offer suggests that customers can be misled into accepting market offers that result in them paying more rather than less. Only 8% of switchers in the survey actually compared tariffs. While inducements are necessary to encourage switching, retailers are not necessarily offering much: Citipower, for example, was offering tickets to cinemas and the aquarium.

In summary, retailers have secured a minimum rate of return on each customer and have increased the returns available from low-volume households. Higher-volume, wealthier households obtain discounts, while lower-volume, low-income households face higher prices.

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46 This offer was first made during the 2004 football season, and involved Origin providing a $50 contribution to the membership of a football club. However, the customer offer I analysed would have seen the customer worse off by $5 p.a., and more so if consumption was greater than the previous year.
8.3.5 Governance

Reform has been accompanied by the introduction of independent regulators, codes of conduct, charters and alternative dispute resolution. These are not forums for dialogue about the governance of the market, but constitutive elements of ‘government at a distance’ (Hodgson 2001). Self-regulation and co-regulatory regimes are examples of what Michel Foucault may have regarded as ‘technologies of power’ (Gordon 1991, Pizzorno 1992) which ‘determine the conduct of individuals and submit them to certain ends or domination, an objectivising of the subject’ (Martin et al. 1988: 18).

Individuals are by definition atomised in markets. Ryan (2001: 105) argues that the point of constructing the ‘citizen as consumer’ is to isolate service delivery from policy making and protect governments from the ‘political demands of society’. This is why the formal and conspicuous self-regulation regimes of governmental oversight of privatised and deregulated markets are ‘no less powerful for being detached from government-as-state’ (Marginson 1997: 82):

by transferring certain activities from politics to economic management, market reform narrowed the scope of public policy and reduced political pressures on government [which can] steer output, methods of production and pricing from a distance, while evading responsibility for the effects on users and employees (Marginson 1997: 85).

Corporate self-regulation places a requirement on private firms to comply with performance reporting\(^{47}\) in order to demonstrate publicly that actual, enforceable regulation is not required – that is, to establish that competition works to protect and benefit consumers (Knights, Sturdy and Morgan 1994). Industry generally resists the obligations of self-reporting but Hodgson (2001) explains that such impositions have considerable benefits for these firms. Customer information systems (CIS) are:

instrumental in the complementary objectification of the consumer, building on new technologies of marketing and operationalising the ‘segmentation’ of the consumer

\(^{47}\) The ESC publishes data collected from the retailers regarding their performance against specific indicators such as disconnection. It has not attempted to date to triangulate such research against reported customer experience.
population...Through the CIS, each individual client is quantified on a number of axes which forms the basis for internal marketing (Hodgson 2001: 126).

Performance reporting as a technology is intended to provide public accountability, but it can inadvertently assist the formation of a residual market. Along with competition reform and the changed socio-economic profile of the population, Knights, Sturdy and Morgan (1994: 48) argue that increasing competition in some markets further promotes a market-led approach rather than a sales push/product-led approach. Despite this approach supporting consumer sovereignty in an ideological sense, they suggest that considerations:

of cost and profitability limit the possible diversity of products and services offered to the consumer. This is underplayed if not neglected in the marketing literature at a time when, owing to intensified competition, the tension surrounding the potential conflict between profit and responding to consumer ‘needs’ has heightened.

They highlight the ‘tension with the marketing concept between responding to “needs” and achieving profitability’. Competitive pressures reinforce ‘managerial concerns with costs and profitability. Here, high-cost/low-profit consumer segments and hence their “needs”, are selected out through pricing and targeting’ (Knights, Sturdy and Morgan 1994: 43). The result in a competitive market is denial of service and/or less choice for some rather than a response to ‘need’.

8.3.6 The regulator, competition and social protection

As competition for domestic customers has rolled out since 2002, the question of social protection has again come to the fore. State governments have appeared to become less important in policy making; instead, regulators have seemingly become more important. We have, for example, the South Australian Independent Industry Regulator rather than government commissioning research into fuel poverty (Richardson and Travers 2002). In Victoria, it was the ORG that undertook the preparatory research for FRC which revealed household resistance to reform. Survey respondents reported concerns about competition, especially about costs, reliability, customer service, privatisation, lack of information and foreign ownership (Millward Brown 2001a, 2001b, 2001c). In reporting on the findings of
the first review of the effectiveness of FRC, the ESC largely ignored the responses of earlier research (Wallis Consulting 2002) that indicated a possible attitudinal impact on the take-up of market contracts. To that end, it made an assumption that customer inertia relates to market maturity rather than customers’ views of the market (see Chapter 12).

The ESC (2002: 47-8) did find evidence of market segmentation:

retailers...targeted small and medium enterprises and larger residential market sectors...retailers often targeted customers in particular suburbs (mainly affluent) or with large houses...one customer segment that most retailers appeared deliberately not to target were off-peak customers.

It also noted that concession card holders, those receiving Special Power Payment and country customers with CSO exposure were being avoided. However, the ESC concluded that segmentation was on the basis of ‘supply costs’ rather than ‘income levels’, and that there was no evidence of discrimination against low-income customers. This was argued on the basis of submissions made by retailers that low consumption is usually equated with two income households, and higher consumption with pensioners and large families. The findings also referred to the results of ‘mystery shopper’ research in which they used actual customer identities to obtain real offers. As a generalisation, the claim that low consumption is associated with DINKs (‘double income, no kids’) and is not associated with low-income households is untrue. On the contrary, it is well understood that low-income households consume less energy than higher-income households (see Chapter 6). The ESC’s Customer Consultative Committee questioned the methodology for the mystery shopper exercise, and the ESC admitted that none of the 20 households chosen were problem payers with any history of arrears or disconnection. In effect, those most likely to be discriminated against were excluded from the research. The second review of FRC (ESC 2004a) required ESC to specifically examine the issue of market segmentation. This review found that segmentation strategies were oriented towards the acquisition and retention of attractive customers. Accordingly, retailers were avoiding off-peak and rural households. Differences in behaviour and attitudes amongst retailers regarding the avoidance of low-consumption customers, customers who posed a credit risk or had concession status were found:
All retailers regarded poor credit risk customers as unattractive due to the probability of bad debts and the debt management response processes required under the Retail Code. Customer targeting on the basis of credit risk is usually confined to avoiding areas for door-to-door sales – but retailers suggested this may affect only around 10 per cent of customers…Lower consumption tends to be associated with low income and potential credit risk, as would be intuitively expected of customers with severely constrained budgets (ESC 2004c: 62).

Despite these statements, the ESC depicted segmentation as a positive competitive outcome. It failed to mention the impact of the continuing existence of the obligation to supply and price caps as the barrier to shedding strategies. Studiously avoiding any suggestion that segmentation may have possible undesirable economic or social consequences, the ESC (2004c: 64) still stated:

some customers will be relatively unattractive to all service providers due to their credit worthiness or particular circumstances imposing a very high risk of non-payment for retailers, and must be supported by general measures.

The ESC viewed segmentation as related only to the cost of supply and would not entertain the possibility that it may also reflect market power. Finally, it recommended that the safety net (the obligation to supply and price caps) be rolled back and more competitive households (higher-volume consumers) be exempted from consumer protections other than general fair trading provisions. This represents the final assault on the principle of universality. Government rejected this recommendation, although the terms of reference for the investigation did specifically state that a roll-back of regulation was the objective. No allowance was made for continuing the status quo.

8.4 Conclusion

In Victoria segmentation has been limited by the existence of an obligation to supply and the imposition of price caps on the deemed and standing offer tariffs. Nevertheless, consumer protection provisions have been substantially revised in order to facilitate the development of the market, and this encourages segmentation. The new Retail Code and the lack of regulation regarding tariff structures has permitted growing differential treatment
of customers based on market assessment of credit worthiness and profitability. As retailers are not yet able to shed undesirable (in market terms) customers, this treatment manifests as a series of (mainly) financial penalties. As these customers are unable to avoid the penalties, they are potentially more profitable than average customers.
Chapter 9: Prepayment meters: The electricity residual market

9.1 Introduction

PPM technology where it has been introduced in the electricity industry has been a key tool enabling segmentation. In the UK PPMs have enabled the development of a clearly defined residual market. Although PPMs are not vital to segmentation because other methods can be used to effect similar policy, as Section 8.3.4 on Victoria's Retail Code demonstrated, this technology is very effective and has additional benefits for retailers. In each jurisdiction under consideration, PPMs have required regulatory or government approval. Accordingly, the PPM customer class, as the residual market, is one which government has had an active role in creating. The extent to which markets segment is highly dependent on public policy settings.

9.2 Prepayment meters in the UK

The most marginal low-income and vulnerable households in the UK were moved onto PPMs well before competition commenced (Ernst 1994a). Ofgem, the gas and electricity industries regulator, found that only around 10% of PPM customers would change back to traditional credit payment arrangements, despite knowing that they could achieve price cuts (MORI 2001). Ofgem believed this indicated ‘satisfaction’ and should be read as consumer preference, but did not test this. Customers who have experienced disconnection and who know that they are likely to have difficulties in paying for their electricity or gas know that they will need to pay reconnection fees, spend time negotiating with the utility over payments of arrears, and be unsure of when disconnection will occur. In addition, there is the public embarrassment of disconnection (Neilson c2001). These customers know that the cheaper price of paying by credit is illusory, because payments may not be maintained. The fact that PPM customers in the UK are participating in a market (although not to the same extent as credit or direct debit customers) to the extent that it is available for them to do so (as transfers can be blocked because of arrears).

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48 National Energy Action (2000) said in reaction to changes to permit PPM customers with debt to transfer: ‘this protocol will allow at least some consumers in debt to take advantage of lower prices available from alternative suppliers. We regret that it has taken more than three years to devise a workable solution and have some difficulty in understanding suppliers’ reluctance to countenance the simple solution of abolition of debt blocking, particularly for prepayment customers where
shows that they are price sensitive. Customers who pay by direct debit are offered the lion’s share of price discounts. The National Office of Audit (2001) reported that, in one region, PPMs were 20% more expensive than direct debit, while SRC International (1998) reported the gap to be 30%. As the poor in the UK tend not to have bank accounts, energy retailers can use direct debit as a screening process to ensure they are not attracting the wrong sort of customer, much as loyalty schemes can be used (Drakeford 1997). PPMs are, in effect, a pernicious POLR. Drakeford argues that the spread of PPM in the UK did not:

lie in more advantageous treatment of struggling customers. Rather it shifted the burden of disconnection from the public to the private sphere. In social policy terms, it represented a parallel to economic privatisation.

The idea that provision of bank accounts would remove this barrier, as suggested by Conaty and Bendle (2002), fails to recognise the existence of discrimination and residual markets in the banking sector, and more obviously the financial penalties imposed by banks for dishonoured direct debit requests. Moreover, suggestions such as that by the Department of Trade and Industry (1998) that PPM customers be subsidised through cross-subsidies from other customers appear ludicrous. Why not subsidise them as traditional credit customers?

Most customers stay where they have always been, with the traditional credit system, paying something in between the two other price extremes. There is also a ‘Fuel Direct’ scheme that is like Centrepay in Australia. Such schemes guarantee payment to providers such as utilities, removing the householder’s capacity to juggle expenses. That is, the utility gets paid even though there may be no food in the house for a week.

collection of arrears is in any event assured via calibration of the meter.’ National Energy Action speculated that the reason has to do with the period of time required to repay arrears using a PPM. A new retailer can buy the debt, but the customer will only be profitable if it can be collected within a specific timeframe. However, PPM customers actually have to be consuming if arrears repayment is to occur. Self-disconnection effectively suspends the debt collection process and is more likely if the customer is paying higher prices and making debt repayments.

49 A scheme in which Centrelink clients have deductions transferred directly to a nominated creditor, such as a utility or housing provider.
9.3 Prepayment meters in Australia

The UK experience demonstrates how efficiently PPMs can effect the segmentation of customers, using the payment method as the basis. The widespread uptake of PPMs\(^{50}\) in the UK also led to a dramatic reduction in disconnections, to 1\% (Ernst 1994a). But PPMs do not solve the problem of disconnections. They can simply hide them in that those who use this form of payment simply ‘choose’ not to connect whenever they do not have the cash to pay for their electricity in advance. PPMs enable a perfect residual market. Rather than mitigating fuel poverty, they exacerbate it.

The Victorian government is under considerable pressure from the industry to further deregulate domestic supply, as the following submissions to the Special Investigation: Review of Effectiveness of Retail Competition in Gas and Electricity (ESC 2004a) indicate:

[T]he cost of compliance in energy, regardless of jurisdiction, is high because the sector is too heavily regulated…The regulated safety net arrangements could be reduced in scope or eliminated where a significant part of the market is on negotiated contracts (Energy Australia 2004: 4-12).

It is our view that competition in the market has now developed to such an extent that the current safety net framework, covering price and minimum standards regulation for all domestic and small business customers, is no longer warranted, and that any strategy to further competition must include winding back regulatory impediments (Origin Energy 2004: 1).

Competition in the energy market in Victoria has continued to develop over the last two years and has reached a level of maturity where it is appropriate that the regulatory arrangements established at the commencement of full retail competition be relaxed (AGL 2004: 1).

Increasing focus on the margins available from individual customers – disregarding the barriers to segmentation – results in greater attention to cashflow and credit management.

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\(^{50}\) In the UK, traditional credit customers with arrears are given a choice of disconnection from supply or the installation of a PPM (Ernst 1994a). In effect, there was a forced migration onto PPM.
Howat (2001) noted that the pressure for PPM in the US coincides with rising prices in the market and deceasing affordability of basic energy requirements. As the above statements indicate, the debate about regulation has centred on the possibility of some form of targeted assistance, so as to enable further development of the market, that is, removal of the obligation to supply from some customers and the demise of universality. If the breach of universality is permitted, it is only a small step to see the compulsory provision of a meter rather than electricity supply itself as constituting the obligation to supply for those still regarded as protected. In this way PPM can become the POLR. In some respects it is merely an extension of processes that already permit the reordering of household expenditure.

The use of credit enables customers without means of payment to retain supply, and provides scope for the juggling of finances that is increasingly part and parcel of the financial life of low-income households. The Electricity Industry Ombudsman Victoria (2000: 8) captured how flexible payment plans can assist financially vulnerable customers, and how the wrong emphasis in credit management can precipitate default:

The companies state they are reticent to establish plans which result in debt accumulation, however, simply extending the repayments of arrears and leaving current consumption payments in place can frequently reduce the impact of debt arrears so that the customer can get over a particular financial crisis.

If on the other hand, customers accept payment arrangements they know they cannot afford, they cannot keep to them and are then disconnected. Company records of customer payment histories often show a string of broken payment plans and disconnection. These in turn further damage the ability of the customer to negotiate an arrangement in the future.

In contrast, PPMs simply deny supply when the customer cannot pay. Their ‘emergency credit’ feature permits strictly limited indebtedness, and these arrears must be repaid before supply can be restored:

Disconnecting after the meter has run up a significant deficit such as $25 in our view is not a good idea. Firstly it promotes the concept of customers living in debt
which is contrary to a pay-as-you-go system. Secondly after disconnecting customers must pay more than the money owed to put the meters account back into positive credit before they can restore their supply, something that might not be possible for some customers who might have opted for prepayment because of their financial situation (Nilsen Technologies 2003).

The disadvantage of traditional credit-based provision is the stigma and disempowerment that is associated with disconnection of supply. Disconnection as the ultimate sanction for non-payment has been intentionally punitive. In the case of PPM, self-disconnection privatises the act of disconnection, hiding a social problem but also permitting the customer to avoid embarrassment and public humiliation. Like traditional poor relief, disconnection as stigma is used as a disciplinary device. The traditional credit relationship, however, provides some flexibility so that households are not put in a position of having to choose between essential goods. PPM, create a ‘Sophie’s choice’ situation in which families are forced to select, for example, between energy needs such as heating, lighting and cooking on the one hand over food or vital medicines on the other. The efficacy of PPM from the retailer’s perspective is that as payment devices they enable them to bypass state consumer protections and undermine universal service (Howat 2001). This includes the ability, Drakeford (1997: 122) argues, to circumvent existing legal means of dealing with debt recovery. Moreover PPMs ‘allow companies to leapfrog over other creditors’ and permit the companies to ‘escape the opprobrium which disconnection brings’. As Colton (1998b: 19) argues:

perhaps the most readily evident alternative for credit and collection purposes is the installation of cost-effective utility financed demand-side management measures.

He argues, as does Leonard (2002), that such measures are effective in improving credit management and payment collection and in achieving budgeting and energy consciousness amongst customers. Leonard (2002: 5), the CEO of a major US utility, described the traditional utility approach to disadvantaged customers as the waging of a ‘war’.
Two industry submissions to the review of the Electricity and Gas Retail Codes which ran concurrently with the review of the effectiveness of competition (Aurora 2004, Ezikey 2003) advocated the introduction of PPM. The ESC responded by scheduling a specific investigation for mid-2004 (ESC 2004b).\(^{51}\) Aurora and its subsidiary Ezikey are owned by the Tasmanian government and share the meagre 3% of the market not held by the incumbents. Aurora has already rolled out around 24,000 units. The New South Wales Department of Energy has approved the introduction of PPMs (the retailers who made submissions to that consultation were also in favour\(^{52}\) and trials are planned in that state. AGL has conducted trials in South Australia, it can be reasonably assumed that there is pressure on the ESC to facilitate its introduction in Victoria\(^{53}\), even though no formal application has been made by any retailer to introduce them. Victorian retail licensees have been looking at introducing PPM for some time.

As retailers operate within a national environment, and in the context of the attempt to create a truly national electricity market, the pressure is on Victoria to align itself with the other states. PPMs are promoted as providing ‘choice’ to consumers. Some retailers suggest that there is latent demand for PPM, inferring that their introduction is in essence customer driven, but there is no evidence that this is the case. Policy decisions to permit PPMs have largely occurred in the absence of discussion about fuel poverty and strategies to address it. The idea of ‘choice’ is very attractive to neo-liberal governments but the question that should be asked is: when have the poor ever had choice? As the Australian Consumers Association (2003) is at pains to point out, the difference between ‘choice’ and coercion for low-income customers is a fine line. It argues that even if contracts with small consumers could be individually negotiated in any meaningful sense:

\[
\text{there is a significant power asymmetry between large corporations and small consumers. The end result is that consumers are always at risk of contracts skewed against their interest. This is a consistent finding of the consumer movement in investigating mass-market contracts.}
\]

\(^{51}\) The ESC subsequently abandoned this investigation, as the government indicated it would hold its own inquiry.


\(^{53}\) The Minimum Consumer Protections developed by the ESC permit the introduction of PPM but there is a requirement that each PPM be individually authorised by the ESC. This poses a considerable barrier to their wide-scale introduction.
For example, in Tasmania, Aurora provides customers moving into a dwelling with a pre-existing PPM considerable inducement to keep the PPM, as they pay only half the regular connection fee.\textsuperscript{54} This strategy will ensure the rapid spread of PPM into low-income private rental. For many low-income households, immediate needs tend to take priority over future expenditures. In an advertisement in the \textit{Hobart Mercury} (20 Nov. 2003), Aurora encouraged customers attending a demonstration at a shopping centre to sign up to a PMM on the spot to gain the chance of winning $55 worth of ‘free power’. Low-income households could well be subject to similar strategies in Victoria.

PPMs have a number of advantages for utilities. They hide the level of disconnection, permit the utility to bypass existing disconnection procedures, provide a cheap method of debt recovery, permit a formally segmented market, reduce operating costs, and improve cashflow. It is, however, questionable whether PPMs are cost-effective, except to the extent that costs can be imposed upon the customer. In the longer term, PPM undermines solvent demand, and volume of sales must drop.

Promotion of PPM involves the propagation of a number of myths. The most common is that PPMs are ‘pay as you go’. This more appropriately describes coin operated meters. PPMs are exactly that: ‘prepayment’ involving outlays in advance of usage (where the customer foregoes the interest, which is traditionally collected by the retailer – who can invest it at higher rates than a low-income customer without savings). The use of tokens or smart card technology involves considerably greater transaction and time costs for the customer than cash.

PPMs are claimed to provide a flexible payment option that assists households to budget. If the issue is incapacity to pay, either acute or chronic, PPM can do nothing and, as it is usually a more expensive payment option, will exacerbate budget problems. There are in Victoria non-penalising alternatives such as Easyway (payment by instalments) and bill smoothing (payment by predetermined instalments).

Proponents also claim customers can track their usage of electricity and hence maintain better control over their consumption. Given that a large proportion of the Victorian household sector ration their electricity usage, it can be assumed that these customers

\textsuperscript{54} Reversion to a standard meter attracts a fee equal to the standard connection fee (KPMG 2004).
already have the skills and tools to control their consumption. My research found respondents to be aware of their consumption, as 74% always looked at the graph printed on their bill that compares the current period with the previous four quarters, and 20% sometimes did. This suggests that customers are aware of their consumption in general terms and effectively benchmark themselves against their previous consumption. Colton (1998b) warns that, in regard to low-income/low-consumption households, most consumption is non-discretionary in nature. This non-discretionary usage relates to space heating, hot water heating and refrigeration. These appliances and/or forms of consumption do not easily lend themselves to reductions without a corresponding impact upon household welfare. To the extent to which households can reduce their non-discretionary consumption, low-income households frequently do so already. PPMs offer nothing particularly distinctive in regard to customer awareness of consumption, other than the need to be conscious of it in order to avoid running out of credit and being disconnected.

Another claim is that PPMs can provide time of use (TOU) pricing signals. But as international metering company Actaris (2003) states:

> the introduction of TOU PrePayment meters around the world, including Australia, has shown that, on average, consumers do NOT adjust their consumption pattern when paying a TOU tariff, unless the difference in price is really restrictive.

The TOU debate needs to be separated from PPM: they are different issues. However, emphasis for policy making needs to be given to the twin issues of ability to gain savings from usage changes and the relative value of the rewards of doing so. These two hurdles largely determine responsiveness to pricing signals. PPMs as an energy management tool also presuppose that the householder has control of the thermal efficiency of their housing and their appliance quality – which tenants in particular generally do not, and many low-income home owners such as age pensioners have difficulty with. PPM proponents are particularly active in the national electricity market because of the potential for a mandated roll-out of interval metering (IM) technology. Were IM universally rolled out with real-time interactive communications, demand responsiveness could be far more sophisticated and beneficial to low-income households, especially those without refrigerative air-conditioning, than PPM (Pareto Associates 2003).
There are a number of other issues that make PPMs problematic. Theft poses a physical security problem as the smart card (two way) technology involves externally located meters, which are very common in Victoria. The virtual technologies (one way) involve keypad systems that in many circumstances require considerable installation costs, as these units need to be internally located but connected to the actual meter which is usually externally located.

The Victorian government provides a range of concessions such as a winter energy concession, utility relief grants (URGs), multiple sclerosis concession, service to property charge concession, and life support machines concession. With the exception of the URG, these are delivered in relation to actual consumption within a specified period of time to which a percentage-based deduction is applied. The URG is designed to give financial assistance to households that through unforeseen circumstances find themselves temporarily unable to meet gas or electricity bills. Assistance is rendered where a debt is outstanding. The account enables the government to determine the nature of the problem and the extent of assistance required.

PPM can also be calibrated to recover debts accrued when the customer used traditional credit. In the UK some customers have 30% of payment going to arrears. In Tasmania debt recovery via PPMs is based on an effective percentage surcharge (KPMG 2004). This means that debt repayments are higher in winter when there is more demand for energy and household budgets are already stretched. Accordingly customers repay their debts when they can least afford do so. PPMs reorder household expenditure to prioritise debt repayment over current consumption. Debt recovery via PPMs means rationing is more likely, but ironically it slows down the rate of repayment.

The Energy and Water Ombudsmen in Victoria (EWOV) and in New South Wales have been actively promoting the potential for PPM (McLeod 2003, Needham 2002). This is occurring in the context (at least in Victoria) of a wider debate regarding incapacity to pay (hardship). Since privatisation and deregulation of the energy industry, retailers have been required by a condition of their licence to participate in a formal complaint scheme acceptable to the jurisdictional regulator. In some states this has resulted in the establishment of industry-based alternative dispute resolution schemes. The term ‘ombudsman’ is used, although they are not a statutory office as understood in the past.
The EWOV, for example, is a company limited by guarantee whose members are utilities which pay a levy to operate the scheme. It is managed by a board in which the chairperson, appointed by the members, holds the deciding vote. Consumer directors, in numbers equal to that of industry directors, are appointed by the ESC. The EWOV is partially funded on the basis of the number of complaints incurred in relation to each member.

One of the EWOV’s roles is to notify the ESC of systemic issues appearing in their complaints casework. While it has been active in relation to hardship, having held a special conference on ‘Staying Connected’ in 2001, it only publicly cited hardship as a systemic issue it reported to the ESC in 2003 (EWOV 2003). Financial counsellors’ experience suggests that significant numbers of payment-troubled clients have been unable to enforce their rights under the ‘incapacity to pay’ provisions of the Retail Code (the hardship provision) through the making of complaints to the EWOV (Sharam 2004). Moreover, the ESC had failed to enforce the code, despite the matter being brought to their attention. Most enquiries made at the EWOV relate to incapacity to pay. To date it has only made one binding decision on the issue. It may be the case that this reinforces the preference which utilities have for PPM technologies, but it is more likely that any roll-back of the safety net legislation will result in increased competitive pressure on the retailers to shed under-performing customers or alternatively attempts to increase revenue from these customers. Should this occur, the number of complaints regarding hardship being made to the EWOV should increase. Given that PPMs reduce the interaction between customer and utility, the number of complaints against utilities may also be expected to drop, and hence the cost of the scheme to the industry would reduce.

9.4 Conclusion

In Chapter 9 I used the example of prepayment meters to show where deregulation of domestic electricity supply has resulted in segmentation or indicates the potential for a residual market. PPMs have the dual ability to exclude poor customers when they are poor (that is, the loss making transactions can be distinguished from the profit enhancing transactions) and to increase the value taken from the customer. In this sense PPMs both exclude and residualise. While these ends may be achieved by other means (as indicated in Chapter 8), PPMs are the most efficient tool. For governments that want to remove
themselves not only from direct service provision but from a role of formal guarantor of service provision, PPMs permit the offer of a right to a meter in place of the right to access.

The links being made, particularly by US commentators, between earlier segmentation in industries such as insurance and mortgage lending and deregulated electricity make it possible to identify underlying assumptions about social protections. In the following chapter I draw out three main models of social protection that are either explicitly or implicitly argued by protagonists in the reform processes in the US, UK and Victoria. These are what I call the 'civil rights' model, the ‘universal service’ model, and the ‘market’ model. As indicated by the debates outlined in Chapter 5, these are not necessarily absolutely distinct from each other.
Chapter 10: Three models of social protection

10.1 Introduction

In Chapter 8 I explored market segmentation, demonstrating that it is not peculiar to electricity but is a reflection of the commodification process that occurs as a consequence of market relations. I have shown that unregulated markets in essential or non-discretionary services often result in the formation of a residual market (or market of last resort) segment in which customers are subject to market abuse. The US and UK provide examples of how governments can inadvertently assist in the facilitation of such residual markets. But governments can also deliberately segment the market and assume responsibility for the least attractive customers through POLR schemes. Sometimes these genuinely provide affordable services, sometimes they are punitive. In both cases, governmental action is discriminatory.

In the past, the understanding of utilities as monopolies informed social regulation as well as economic regulation of the electricity industry. Until recent competition reforms, monopoly provision meant domestic customers were protected by some form of universal service obligation on the utility, whether the form of regulation was statutory as in Victoria or the UK, or public utility law as in the US. Deregulation specifically aimed to introduce competition into the industry, and accordingly social protection has also been targeted for change so that it reflects market provision rather than monopoly supply. In this context, two models of social protection, that of ‘universal service’ and the ‘market’, stand in opposition to each other. The change from universal service to market aligned protections in Victoria was discussed in Chapter 4. The third model I call the ‘civil rights’ model. It is taken from the experience of redlining in the US, that is, the experience of market-based provision of other essential services. From redlining in the US (and its emergence in the UK since various industries have been deregulated) it is possible to recognise new and old versions of this model: the latter in response to market failure, and the former, ironically, in response to market reform. New consumerism has more in common with the old civil rights model than the new.
10.2 The civil rights model

Many US states introduced anti-redlining provisions in the 1970s for insurance and mortgage lending which prohibited discrimination on the basis of a range of social characteristics. In addition, the federal government introduced the Community Reinvestment Act (CRA) in response to the inner city race riots of the 1960s. The CRA mandated, for example, that private banks open or maintain branches in redlined areas and that a prerequisite proportion of minority customers were served. But redlining was not seen as an example of market segmentation, and only some saw underlying economic discrimination. This is why Marcuse (1979: 549) was able to show that some anti-redlining solutions perpetuated disadvantage:

Reinvestment strategies...as they are generally discussed assume the appropriateness of normal economic criteria for real estate investment, and seek, through governmental aid, cooperative and coordinated public and private efforts, education and training, and planning and legislation to create conditions by which such private economic criteria can be met for investments.

There was a failure to recognise that even in so-called competitive markets, some sub-groups of customers, because of the structure of the industry and the needs of the market, would remain unattractive. Poor diagnosis led US policy makers in the 1970s to establish selective (segmented) assistance, such as the Fair Access to Insurance Requirements (FAIR) laws that resulted in the creation of a POLR. In effect, an involuntary market was established, comprising that segment of the market that had been excluded from the voluntary market. The laws guaranteed service but, like residual markets, this POLR was more expensive. It was a policy that ended exclusion in favour of exploitation.

Marcuse (1979) pointed out that the prohibition of non-economic discrimination for insurance and mortgage lending in the private housing market was unlikely to prevent discriminatory practices such as racism, due to providers’ capacity to discriminate on rational economic grounds. Contemporary community campaigns in the US against redlining have revealed a trend in unsuccessful prosecution exactly because providers have been able to establish that they are utilising ‘colour-blind’ statistically-based assessments that rely on ‘legitimate’ economic discrimination. The correlation, for
example, between race and economic position is in effect reversed. Whereas once a zip code would be used as a denominator of a black neighbourhood to be avoided, now credit scoring of the individual customer incidentally results in disproportionate numbers of black customers in specific geographical areas being refused service or charged more. The problem in addressing redlining is that it has been viewed as illogical or a specific market dis-function whereas, where it can be disassociated from race and other social characteristics, it is logical and can pertain to a more general phenomenon.

Anti-redlining strategies have traditionally assumed the primacy of the market as an allocative mechanism. The state then intervenes to grant members of minorities special protection that in effect compels firms in each prescribed market to serve them. The protection is provided through civil law prohibiting discrimination and is similar to Victoria’s Equal Opportunity statute. This addresses refusal to serve but, as Coyle (2000) points out, omission is as serious, and this is what the CRA is intended to remedy. Commodification is endorsed but, where the process results in the selecting out of losses and/or risks using social correlates, it is disapproved of. Where the selection process uses economic data, such discrimination is regarded as legitimate. The anti-redlining laws accordingly fail to address the correlation between minority status and economic status.

Marshall (1950) noted that civil rights, which had traditionally been associated with individuals, were being transformed in the UK into legal instruments that could also take account of communities of interest. There was a plaintive air about his observation, because equal opportunity and anti-discrimination law paradoxically addresses exclusion from the mainstream by identifying communities of interest and differentiating them. Marshall argued that exclusion should be addressed through the sharing of a common heritage in the form of socio-economic entitlements that would be universally available. Direct state intervention in the delivery of services, particularly ‘universal service’ provision, was used to overcome the problem of exclusion from markets.

The withdrawal of financial services from disadvantaged areas in the UK since the deregulation of the financial services sector has recently been described as redlining (Drakeford and Sachdev 2001). The UK Office of Fair Trading moved to prohibit redlining ‘because of its capacity to act as a cover for discrimination on the basis of race’ (Drakeford and Sachdev 2001: 216). Yet again the distinction between social and economic
characteristics and between irrational and rational discrimination was not explored. Knights, Sturdy and Morgan (1994) cite UK Equal Opportunity Commission opinion approving of credit scoring specifically because it avoided using social characteristics such as race. Discrimination based on economic standing was ignored. As discussed earlier, the UK electricity reforms have resulted in rapid segmentation, service withdrawal and the formation of a residual market.

However, the US experience of electricity deregulation is different. Debates over POLR schemes have centred on the recognition that markets have a propensity to fail to serve some segments of the community and that they can be discriminatory. The anti-redlining provisions in electricity industry restructuring legislation therefore are illuminating and paradoxical. While equal opportunity and anti-discrimination law traditionally focuses on opportunity, with discrimination only acknowledged 'when it does not question in a fundamental way the structure of inequality' (Procacci 2001: 65), the anti-redlining laws go some way towards closing the distinction. These comprise prohibitions on discrimination that are typical of equal opportunity laws, but also discrimination on the basis of source of income, social security status, zip code and low income. These are in effect anti-economic-discrimination measures. There is an implicit understanding that markets act on economic inequality. In the US the regulation of monopoly utilities traditionally required universal supply to households at fair and reasonable prices, recognising that market power could be exercised to the detriment of some or all customers. Taggart (1995) argued that this regulation was infused with ancient common law anti-discrimination principles that addressed economic discrimination, not social discrimination. It was not simply that some enterprises were monopolies, but that they were ‘businesses affected with a public interest’. Anti-redlining provisions that include prohibitions on economic discrimination in part reflect this legacy. Market reform of electricity utilities may replace monopoly with competition, but competition cannot ever eliminate the public interest involved in the production and delivery of electricity. The effect of electricity industry anti-redlining laws is an attempt to achieve universal service by other means. The problem is the same, regardless of whether this essential service is a monopoly or purportedly a market: the lack of market power of the customer. As the State of New York Public Services Commission (2001) pointed out, a general legal obligation to supply removes the need to identify individually all the forms of discrimination that may be envisaged.
The civil rights model has its origins in liberal conceptions of freedom, and especially the ability to contract in the market. It has, however, in the context of utility reform in the US, attempted to incorporate positive rights in the form of socio-economic entitlements associated with earlier universal service provision. This is in part an acknowledgement that the liberal conception of rights fails to account for differences in market power, and hence fails in its own terms. Marshall (1950: 22) did not believe that the law could be used to eliminate ‘class prejudice’, which would require what we now call ‘cultural change’ on the part of those holding the prejudice. However, he advocated universal entitlement to some economic resources that could mitigate ‘the automatic effects of the unequal distribution of wealth, working through the price system’ (that is, ‘commodification’) (Marshall 1950: 22). The experience of redlining in the US and subsequent struggles over utility deregulation point to the need for civil rights (such as equal opportunity statutes) and social rights (such as specific economic entitlements) to be combined to ensure the success of both. This is what universal service provision in effect does.

10.3 The universal service model

The second model, universal service, was briefly discussed in Chapter 4. It requires a mix of prohibition and compulsion. Firstly, customers must be served regardless of their location. Secondly, service must not be denied on the basis of social characteristics such as race or gender. And lastly, access to the service must be linked to capacity to pay. These represent a mix of positive (substantive) and negative rights. In the electricity industry in Victoria and in many states of the US, additional selective assistance has formed a component of universal service. Concessions or rebates have traditionally been aimed at improving the access of low-income households to essential energy supplies. Put another way, concessions alleviated some of the pressures on low-income households to ration. They compensated for the disadvantage of low income, not for the characteristics of the industry. That was taken care of through the way the industry was structured, namely, through internal cross-subsidies and universal service provisions. In the US, industry accepted this as a condition of monopoly service (Yarrow 1996), and in Victoria, public ownership meant the distinction was largely irrelevant.

Market provision and universal service appear at first glance to be antithetical but this depends, according to market reformers, on whether or not governments accept the costs
associated with delivering universal access. Competition advocates such as Yarrow (1996) argued that transfers should be paid out of government budgets rather than be internally funded by utilities as this is more efficient administratively and removes the economic 'distortions' caused by cross-subsidies. Speaking of telecommunications, he says:

Relief of poverty and public provision for special needs are much better handled by the Department of Social Security (DSS), which can look at the position of the relevant individuals and groups in their entirety, and not just at their positions as buyers in the market (Yarrow 1996, my emphasis).

To appreciate why markets and universal service may in fact be antithetical, we must turn to the third and last model under discussion: the market model.

10.4 The market model

Samuel 200355). The Kennett government for its part appears to have avoided any explicit statement that there would be any possible losers in the reforms. For example, Treasurer Stockdale (1994: 10) referred to the need for tariff reform and the existence of subsidies but only mentions the groups that would benefit, rather than those that would have to relinquish their subsidies.

In this view, an ideal market would require no intervention by government. However, as discussed in Chapter 5, even neo-liberal governments make compromises. The compromise, however, is generally made not at the micro-economic level but at the macro-economic level. Each individual market should be as close to the ideal as possible. If consumers require economic subsidies, these should be funded directly by government. This permits them to be targeted to only those assessed as having a recognised need. This eliminates the ‘free-rider’ problem in addition to allowing the more efficient market allocation of resources. Saunders (1993: 64) argued that economic growth has made the need for universal services redundant:

> what was effectively a society-wide problem in the nineteenth century is today a specific and targetable one. When the mass of the population could not afford to live decently, mass solutions were required and this necessitated the mobilisation of the state as universal provider. When, on the other hand, it is a marginalised stratum which cannot achieve access to the market, other possibilities present themselves.

One such possibility is the provision of selective or targeted assistance. This is not specific to the market model as it can also comprise a component of universal service. The distinction is that, under universal service, the assistance is in addition to benefits accruing out of the industry’s structure, such as where a provider is required to redirect resources in particular ways (for example, selling electricity below cost in rural areas). Esping-Andersen (2000: 159) puts the traditional social democratic counter-argument to selective assistance:

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55 Samuel’s statements are discussed in Section 12.7
The poor relief tradition and its contemporary means-tested social-assistance offshoot was conspicuously designed for the purposes of stratification. By punishing and stigmatising recipients, it promotes social dualism.

The market model assumes that economic growth and improved economic performance will lower prices, bringing benefits to all. The model for reform is the perfect market – an ideal type. No account is taken of circumstances in which the market may not be perfect. Accordingly, market power issues have been very inadequately explored:

In their zealous pursuit of market-based alternatives to public provision, contemporary governments often overlook the obvious fact that the underlying dynamic of the market is driven by contest and inequality. Therefore, to rely on the market (or quasi-market) forces alone for the production and delivery of essential and community services, is to expose the most vulnerable sections of the population to the chill winds of service access, based simply on market power (Webber and Ernst 1996: 120, my emphasis).

Households in a market are likely to be subject to segmentation. This would mean that there would be issues of market power. Some customers will not be attractive to retailers unless more revenue can be earned from them. Selective assistance, in the form of cash rebate, for example, can provide a recipient with additional purchasing power in the market, and this can make them somewhat more attractive to suppliers. If recipients are assigned into a residual market, however, the question is whether or not the rebate compensates for the increased costs they face. The oversight made by reformers such as Yarrow (1996) who advocate markets and interpret social responsibility not as a matter of market design but of government funding is that each individual is a buyer in the market. Traditionally, government provision of selective assistance has been determined in relation to the recipient’s income (the means test). Income tests assess only income, not position in the market. Markets are supposed to reflect costs, but they also reflect market power. Segmentation means that assistance should also take account of market position because it has a material bearing on the costs faced by the recipient. In contrast, under universal service regimes, the end-cost of the service to each customer is the same for each member of that tariff class.
Selective assistance may work if there were not sharp economic differences between customers. In egalitarian societies, market segmentation would be redundant. In Australia, the US and the UK, however, there is considerable inequality of wealth. Any transfers would need to be substantial to prevent the market acting on inequality, segmenting and forming a residual market. A review by Perri 6 (2003: 253) of the literature concerning public services in the UK noted that, in regard to schools, choice had resulted in market segmentation, with:

the possibility that the financial size of the 'voucher' compensation for disadvantage may be inadequate to create a sufficient incentive for good schools to compete for these children, and to attract the best teachers to work with them.

The schools 'market' was acting on inequality, which selective assistance was not overcoming specifically because it did not take full account of segmentation. Leyshon and Thrift (1999) also observed in their study of financial deregulation in the UK that the market functioned to increase the relative level of disadvantage.

Welfare transfers moreover are regarded by neo-liberals as removing the economic incentive to work (Crouch 2001). Transfer payments that compensated for the disadvantages of market segmentation would potentially need to be larger than traditional income supplements provided through universal service. Potentially, payments may be needed for a larger group. This arises because with universal service the objective was merely to cross-subsidise whereas, in a segmented market, market power provides an opportunity to extract economic rents. Proponents of markets would argue of course that excessive profiteering would attract new entrants who would then compete and bring prices down, but this is exactly what the history of redlining in the US and more recent experience of financial deregulation establishes as not occurring. It is not only difficult to imagine that governments would increase funding to compensate individuals in residual markets; if they were to do so they would, in effect, be rewarding the retailers profiting from market abuse.

In regard to electricity in Victoria, government has retained its long-standing means-tested direct budget support to low-income or otherwise disadvantaged customers in the shift from universal service to market provision. A range of internal cross-subsidies are being
unwound, although this policy was modified with the election of the Bracks Labor government in 1999 which countered the impact of the reduction of rural cross-subsidies by introducing a budget funded rebate. Since these rural rebates were introduced, they too have been scaled back, which highlights the contingent nature of such funding.

10.5 Conclusion

A number of problems have been identified with the application of market relations to the delivery of essential services. The most obvious point is that consumer sovereignty relies on purchasing power and, in relation to many essential services, many customers simply do not have such power in a market. The market model of social protection may involve some acknowledgement of inadequate incomes but it does not recognise issues of market power. There are further problems with the model. Firstly, neo-liberal reformers have failed to account for the likelihood of market segmentation, which results in simultaneous competition and monopoly. Monopoly is regarded in economic theory as being inefficient, yet market segmentation presents the prospect of the competitive segment – that servicing attractive customers – actually being subsidised by the monopoly segment. In both scenarios there is market failure. Secondly, the economic objective of growth may not be satisfied where there is segmentation because of the likelihood of rent seeking. The provision of selective assistance as income support may well not offset the disadvantage of being in a residual market. In addition, as Froud, Johal and Williams (2002) argue, the jobs/goods nexus or segmentation may unleash a macro-economic dynamic instability that has the potential for considerable economic and social disruption. For these reasons, the civil rights model to which new consumerism in Victoria and the Third Way can be linked also fails to protect vulnerable customers. Civil rights in the absence of socio-economic entitlements cannot prevent the exploitation of customers who experience inequality. The lesson from the deregulation of electricity industries is that industry structure matters greatly in providing social rights.
PART 4: THE EXPERIENCE OF FULL RETAIL COMPETITION IN VICTORIA

Chapter 11: Empirical research: Segmentation?

11.1 Introduction

In the previous chapters I have explored how it could be expected that deregulation of an essential service such as electricity may result in the market segmentation of customers. In this chapter I report on the findings of a survey designed and undertaken specifically to ascertain whether or not there is any evidence of segmentation of domestic customers in the Victorian electricity industry. The purpose was to track the possible emergence of customer segmentation, exclusion and/or exploitation in the new electricity market.

Consumers of goods and services are not homogenous and can represent varying profitability (Hallberg 1995, Berry and Linoff 1997, Clancy and Shulman 1991, McDonald and Dunbar 1995, Stewart 1996). Electricity customers also vary in their profitability and this will influence their attractiveness to competing retailers. In a low-margin, high-turnover business such as electricity retailing, considerable attention is given to customer acquisition costs and payback periods (Grey 2002). Profitable and unprofitable customer segments and individual customer profitability can be identified using technology software (Peace 2003). Those who are identified as unprofitable or low-profit may experience avoidance and/or shedding strategies, as is increasingly the case with telecommunications and banking customers (Cornell 2003, Nicholas 2003).

The existence of sub-prime or non-prime markets in lending also provides an example of how markets address risk by effectively making the customer insure the provider against possible default through higher prices (Temkin et al. 2002). The capacity of unattractive customers to participate in the electricity market therefore may depend largely on statutory provisions. In either case of exclusion or exploitation, customers will be assigned to a specific position (or sub-market) within the market. Of interest in this research was whether or not there is any evidence to suggest corporate strategies of:

- Marketing and customer policies aimed at customer segmentation, in particular, exclusionary practices; and/or
- Systematic exploitation.
11.2 Background

As has been established, fuel poverty arises as a result of an intersection of inadequate and/or irregular income, poor thermal efficiency of housing, inefficient appliances, needs (lifecycle stage) and tariff structures (Kiers 1983, Backman et al. 1987, Crossley et al. n.d., Day Rate Working Party 1991, Deasey and Montero 1983, Kymantis 1986, Mills 1988, Kliger 1998 Neilson c2001, DITR 1985). The ‘fuel-poor’ exhibit particular characteristics that mean a ‘one size fits all’ approach to utilities service delivery will result in disadvantage. To a great extent, fuel poverty arises from exclusion or disadvantage experienced in other markets, such as housing and labour markets and to a lesser extent credit and telephony. This imposes a basic lack of control in regard to utility services. The fuel-poor are more likely to be ‘problem payers’ or to require additional support from call centres and linkage to government programs, or they may simply be low-consumption and hence of low value.

The disaggregation of the electricity industry has resulted in the retail companies assuming all the risk of customer arrears and default on payment, whereas previously these costs would have been shared across the industry. This places additional pressure on retailers to prevent arrears, as the ‘upstream’ parts of the industry now function as their creditors. If a domestic customer defaults, the retailer remains liable for network and energy charges incurred on their behalf.

In Victoria, the removal of some cross-subsidies (both in terms of networks and energy supplied) has resulted in ‘tariff rebalancing’. To date, the two groups that have borne the brunt of increases are the customers of the ‘rural’ DBs (TXU and Powercor), although these also take in parts of outer Melbourne, and off-peak users. For domestic customers, the increased cost of off-peak electric hot water heating has been pronounced. However, as price caps still apply to deemed and standing offer tariffs, the capacity to make off-peak tariffs cost-reflective has been limited. For example, the government has permitted price rises, but within a specified average across all applicable tariffs.

Retailers have considerable incentive to shed some customers or significantly raise prices for some segments but, for the moment, legislative hurdles largely prevent this. In terms of
acquiring customers, some classes are not attractive while the price caps are in place, and others may never be cost-effective unless purchased through trade sales.

11.3 **Survey results**

11.3.1 **The experience of rural/regional households**

28% of Victorian households are located in rural and regional areas (Table 6). The sample very slightly over-represents this grouping at 31%. Inner Melbourne was very slightly over-represented (16% instead of 15%), and outer Melbourne was slightly under-represented with a 52% share of the sample when the population share is 57%.

It would be anticipated that the rural/regional share of contacts, offers and switchers would be in proportion to their share of the state population (of households). Respondents were asked how many retailers had made contact with them, and conversely how many retailers they had contacted. 50% of inner Melbourne households, 57% of outer Melbourne households and 19% of rural/regional households recall retailer initiated contacts, and 15%, 10% and 1% respectively had made the contact themselves. In regard to actual offers perceived to have been made, outer Melbourne’s share is consistent with its share of the state’s household population. Inner Melbourne respondents appear twice as likely to be made an offer than their share of household population would suggest. Conversely, only one in four rural/regional households indicated they had received an offer.

<table>
<thead>
<tr>
<th>Locality</th>
<th>Retail initiated contacts</th>
<th>Customer initiated contacts</th>
<th>Offers made</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inner Melbourne</td>
<td>50</td>
<td>15</td>
<td>33</td>
</tr>
<tr>
<td>Outer Melbourne</td>
<td>57</td>
<td>10</td>
<td>55</td>
</tr>
<tr>
<td>Rural/Regional</td>
<td>19</td>
<td>1</td>
<td>7</td>
</tr>
</tbody>
</table>

These differences may be explained by differences in attitudes. Asked how important price was as a factor in shopping around, there was little difference between the localities with 61%, 67% and 62% of inner Melbourne, outer Melbourne and rural/regional indicating that it was ‘very important’. Likewise there was only a small deviation in those who thought price was ‘unimportant’. In relation to the importance of reliability of supply, inner
Melbourne and rural/regional were a little less likely than outer Melbourne to regard it as ‘very important’ (61%, 62% and 67% respectively). Customer service also showed a consistency across localities with 37%, 44% and 41% of inner Melbourne, outer Melbourne and rural/regional households respectively seeing it as ‘very important’.

Table 5 shows that households in both inner and outer Melbourne were twice as likely to believe prices would increase rather than decrease. Regional/rural households were six times more likely to believe this. Inner and outer Melbourne were twice as likely to say that customer service would improve rather than worsen. Rural/regional customers went against this belief with almost twice as many stating it was likely to worsen.

<table>
<thead>
<tr>
<th>Locality</th>
<th>Price</th>
<th>Customer Service</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Lower</td>
<td>Higher</td>
<td>Better</td>
</tr>
<tr>
<td>Inner Melbourne</td>
<td>2.1</td>
<td>4.2</td>
<td>4.2</td>
</tr>
<tr>
<td>Outer Melbourne</td>
<td>5.7</td>
<td>13.0</td>
<td>12.0</td>
</tr>
<tr>
<td>Rural/Regional</td>
<td>1.8</td>
<td>11.7</td>
<td>4.2</td>
</tr>
</tbody>
</table>

Note: ‘Same’ and ‘don’t know’ answers not shown.

These results indicate considerably greater pessimism in rural/regional areas regarding the impact of the market on prices, service and reliability. Only in regard to customer service was any group of the belief that it would improve rather than deteriorate.

11.3.2 Switching

Attitudes to competition, particularly poor expectations about price reductions and customer service, would appear to be very significant factors in explaining why customers have not switched. However, attitudes do not explain why customers did switch, as the 10% of respondents who felt positively about lower prices in the market, for example, were under-represented amongst those who had switched. Of the 59 households who thought they would be better off, only 16 switched. Only 23 of the 117 who thought customer service would be better with competition exercised choice. Attitudes themselves were not especially differentiated by income.
11.3.2.1 Regional differences

There was a marked regional difference in the uptake of market contracts (Table 6). Inner Melbourne, while being under-represented in the sample (16% instead of 25%), had a 25% share of switchers. Outer Melbourne was under-represented in the sample (52% instead of 57%) but took the lion’s share of market contracts (63%). The rural/regional areas’ share of the sample was 31%, but their share of contracts was only 12%. Only one rural customer (out of the seven) took up a contract with a retailer other than their existing supplier, seeking better reliability of supply. Two had moved house, three took their incumbent’s market offer without shopping around. One believed the advertising pitch that discounts would disappear if they did not sign up quickly.

Table 6: Locality and switching rates compared to share of Victorian population (n=576)

<table>
<thead>
<tr>
<th>Locality</th>
<th>% Victorian population</th>
<th>% share of sample</th>
<th>% share of switchers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inner Melbourne</td>
<td>15</td>
<td>16</td>
<td>25</td>
</tr>
<tr>
<td>Outer Melbourne</td>
<td>57</td>
<td>52</td>
<td>63</td>
</tr>
<tr>
<td>Rural urban centres</td>
<td>19</td>
<td>13</td>
<td>5</td>
</tr>
<tr>
<td>Rural – remaining</td>
<td>9</td>
<td>18</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100</strong></td>
<td><strong>100</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Note: ‘Don’t know’ answers not shown.

Households with electric off-peak hot water heating comprised 26.7% of the sample, but only 5.8% of switchers. Of these 153 households with electric off-peak, 100 were in rural/regional areas. Of those customers who sought a market contract and were refused, off-peak hot water users feature in six out of the 12 cases. While the small numbers involved here do not permit any generalisation, the ESC recognised that retailers were avoiding these customers. The propensity of rural/regional households to have electric off-peak hot water heating appears to result in them being designated as less attractive customers.

Respondents were asked if they had considered switching but had not done so. Those who had considered changing represented 48% of total respondents. Table 7 reveals that rural/regional households are only a little less likely to have considered switching but, if
they had done so, they were far more likely to have taken the next step (twice as likely as outer Melbourne and three times as likely as inner Melbourne). It appears that rural/regional customers tolerate higher search costs than metropolitan households. The major impediment for them in switching appears to have been the lack of offers made.

Table 7: Reasons for considering changing but not doing so (%)

<table>
<thead>
<tr>
<th>Reason</th>
<th>Inner n=71</th>
<th>Outer n=237</th>
<th>Rural/regional n=157</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have not considered</td>
<td>40</td>
<td>36.2</td>
<td>46</td>
</tr>
<tr>
<td>Have not taken next step</td>
<td>16.9</td>
<td>13.5</td>
<td>5.7</td>
</tr>
<tr>
<td>Insufficient information</td>
<td>7</td>
<td>8.4</td>
<td>5</td>
</tr>
<tr>
<td>Unable to compare</td>
<td>9.8</td>
<td>9.2</td>
<td>4.4</td>
</tr>
<tr>
<td>Too much hassle</td>
<td>15.4</td>
<td>12.2</td>
<td>5.7</td>
</tr>
<tr>
<td>Not worth changing</td>
<td>1.4</td>
<td>8</td>
<td>3.8</td>
</tr>
<tr>
<td>No offer made</td>
<td>5.6</td>
<td>10.9</td>
<td>28.6</td>
</tr>
</tbody>
</table>

Note: ‘Other’ answers not shown.

Respondents were also asked why they had not considered switching. Rural/regional households represented 41% of this group (n=240). The survey revealed that they were twice as likely to have been unaware that they could switch (Table 8). Amongst this group, the rural/regional households were far more satisfied with their current supply (60%) than those in inner Melbourne (41%) or outer Melbourne (55%). The regions were similar across most categories, with some exceptions. Over 20% of inner Melbourne households were 'put off' by needing to learn so much in order to change, whereas this did not appear as an issue elsewhere. Not changing as a protest action failed to register in inner Melbourne, but it mattered to over 10% of outer Melbourne households and nearly 5% of rural/regional households.
Table 8: Reasons for not considering switching (%)

<table>
<thead>
<tr>
<th>Reason</th>
<th>Inner n=34</th>
<th>Outer n=120</th>
<th>Rural/regional n=86</th>
</tr>
</thead>
<tbody>
<tr>
<td>Did not know I could</td>
<td>8.8</td>
<td>8.3</td>
<td>16.2</td>
</tr>
<tr>
<td>Satisfied with current arrangement</td>
<td>41.1</td>
<td>55</td>
<td>60.4</td>
</tr>
<tr>
<td>Not got around to it yet</td>
<td>8.8</td>
<td>12.5</td>
<td>9.3</td>
</tr>
<tr>
<td>Waiting for community scheme</td>
<td>2.9</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Waiting for gas competition</td>
<td>2.9</td>
<td>1.6</td>
<td>0</td>
</tr>
<tr>
<td>Waiting or market to develop</td>
<td>2.9</td>
<td>2.5</td>
<td>3.4</td>
</tr>
<tr>
<td>Put off by needing to learn so much</td>
<td>20.5</td>
<td>2.5</td>
<td>0</td>
</tr>
<tr>
<td>Afraid to change</td>
<td>0</td>
<td>2.5</td>
<td>2.3</td>
</tr>
<tr>
<td>See not changing as a protest against privatisation</td>
<td>0</td>
<td>10.8</td>
<td>4.6</td>
</tr>
</tbody>
</table>

Finally, respondents were asked a series of questions to test their knowledge of the reforms, for example, whether they could go back onto their pre-competition tariff if they wanted to do so. Overall, respondents did not demonstrate a good understanding, but there is nothing to suggest that rural/regional households were any less or more likely to know the right answers. As with most householders, they were just as likely to indicate that they simply did not know.

The conclusion of this research is that rural/regional households have the same purchase motivations as customers more generally. However, their attitudes to the impact of the market on price, service and reliability are significantly more pessimistic. Those who were considering switching appear to have more forbearance in the face of search costs. Those in the rural/regional group were less likely to know they could switch, and more likely to be satisfied with their current arrangement. This partly explains low switching rates, but it is also clear that less effort is made to acquire these customers. Retailers made far fewer contacts and offers, and appear to have actively avoided customers with electric off-peak hot water. In terms of corporate strategies aimed at treating rural/regional customers differently – as specific customers – the research concludes that there is discrimination at work. Having said this, the question remains whether this is a result of the imposition of price caps or not, and whether their removal would motivate retailers to compete in this segment of the market.
11.4 Customers in hardship

The research also sought to ascertain whether or not customers experiencing disadvantage – more specifically, fuel poverty – have been subject to corporate strategies aimed at exclusion and/or exploitation. Customers who experience fuel poverty can be regarded as highly constrained in their choices and lacking market power. They may be subject to ‘shedding’ strategies (termination of service by the existing supplier), refusal of service, higher fees and charges, or conditions that reflect lack of choice.

The major barrier to determining the existence of corporate strategies aimed at market segmentation is customer inertia. While customers fail to switch, efforts by retailers to acquire attractive customers and shed unattractive ones are, by definition, largely ineffective. In addition, government policy and regulations currently constrain retailers through the mandatory obligation to offer (the standing offer), procedures around disconnecting customers with a ‘capacity to pay’ problem, and imposition of a price cap on the deemed and standing offer tariffs. The shedding of ‘bad payers’ cannot really occur until the obligation to offer ceases. Moreover, while price caps are in place, the opportunity for retailers to place a premium on access to supply does not exist. Customers can, however, be induced to accept market offers that are more expensive (because the tariff structure is changed, for example), although this plays on their lack of awareness or gullibility, rather than lack of choice.

Retailers may also not have functional technical capacity in the short term to activate sophisticated market segmentation strategies. The need to build or rebuild information technology systems to enable FRC has led to difficulties with their billing and customer information systems. The data mining and categorisation required for market segmentation is premised on fully functioning customer information systems, but it will take time for these to be in place. Further, until competition is very robust and margins have been competed down, the need to assess the value of individual customers will be less urgent.

If segmentation was to appear in Victoria, it could be anticipated as being predicated on readily available data about customers. The primary piece of information retailers have about their customers is whether or not they are eligible for a health care card. New entrant (that is, non-host) retailers are currently exempted from the obligation to offer, and
the survey showed that while concession cardholders switched in proportion to their share of Victorian household population, they did not appear to have switched to new entrants.56

Retailers also have a name, an address and the volume and pattern of consumption for each customer. Increasingly, they will be aware of whether or not the property is rented (the information is sought at varying stages of contact). Some retailers seek to know the household’s size, employment details etc. From this, they may deduce a profile or assign one in the same way as is done in credit scoring.

11.4.1 Public tenants

Public housing in particular areas is highly identifiable and as a consequence avoidable in terms of marketing. Public tenants represented 2.95% of the sample and 3% of the Victorian housing population (ABS 2001). Two57 public housing tenants switched, representing 3.3% of switchers and 18% of public tenants, indicating that public tenants are switching well over their share, but the small numbers do not permit any generalisation that public tenants are or are not discriminated against.

11.4.2 Problem payers

Retailers attempting to identify and avoid potential problem payers face difficulties in distinguishing between ‘can’t pay’ and ‘won’t pay’ customers and between one-off and repeat offenders. Moreover, those pursuing shedding strategies on the basis of their bad debt listing face the risk of alienating a customer who may have been a ‘good’ payer previously and will henceforth be a good payer over the rest of their lifetime. Much of this depends on whether the retailer takes a long-term or short-term view of a customer’s profitability, and whether they are capable of forming a view of whether the customer’s failure is systemic or not. Arrearage is not a particularly effective indicator of which customers to avoid. Nevertheless, it is a cashflow issue, and non-payment a bad debt problem. If a retailer has only the crudest information on which to base its acquisition and shedding plans, ‘bad payers’ as an indicator has some attraction.

56 Of the 16 who switched to a new retailer, three failed to name the retailer.
57 Or three, depending on which question was being answered.
Retailers can block a transfer to a new supplier if the customer has a debt (arrears) over a specified amount determined by the ESC (the amount is not publicly disclosed). This reflects retailers’ fear that the loss of the threat of disconnection will result in customers failing to pay arrears. The survey did not ask if the customer had debt at the time of transfer, and this is a failing of the survey. It did ask if the respondent had been in arrears within the past two years, to which 8.3% (n=576) of the sample stated they had. Of respondents who had been in arrears, two switched to new suppliers (and as a consequence onto market contracts) and a further four moved onto market contracts with their existing supplier (in these cases, their payment history would have been known). In three of the cases, the respondent had moved dwelling.

Arrears occurred across all income brackets. In short, they are not confined to low-income households. It would appear from Tables 9 and 10 that there other are factors that give rise to a household accumulating electricity debt. This is not unanticipated as some customers can afford to pay but forget or avoid doing so. Nevertheless, correlating arrears with dwelling occupancy revealed that public housing tenants’ share of arrears was twice as great as their share of tenure (6%), and private tenants had a 31% share of arrears although they have a 23% share of tenure. Ten out of these 14 private rental households had incomes of less than $20,000 p.a. Home owners/ purchasers were under-represented at about 11% of those with arrears, although making up 63% of households.

### Table 9: Have you been in arrears with your electricity retailer in the past two years? (by income source) (n= 556)

<table>
<thead>
<tr>
<th>Income source</th>
<th>No.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Full-time work</td>
<td>19</td>
</tr>
<tr>
<td>Part-time work</td>
<td>12</td>
</tr>
<tr>
<td>Investment</td>
<td>3</td>
</tr>
<tr>
<td>Self-funded retiree</td>
<td>2</td>
</tr>
<tr>
<td>Age pension</td>
<td>1</td>
</tr>
<tr>
<td>Non-age pension</td>
<td>6</td>
</tr>
<tr>
<td>Unemployment benefits</td>
<td>1</td>
</tr>
<tr>
<td>No income</td>
<td>0</td>
</tr>
<tr>
<td>Supported by family</td>
<td>0</td>
</tr>
<tr>
<td>Savings</td>
<td>0</td>
</tr>
<tr>
<td>Other</td>
<td>3</td>
</tr>
<tr>
<td>Total</td>
<td>47</td>
</tr>
</tbody>
</table>
Table 10: Have you been in arrears with your electricity retailer in the past two years? (by household type) n =48

<table>
<thead>
<tr>
<th>Household type</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Live alone</td>
<td>20.8</td>
</tr>
<tr>
<td>Live with partner</td>
<td>22.9</td>
</tr>
<tr>
<td>Nuclear family</td>
<td>31.3</td>
</tr>
<tr>
<td>Live with children</td>
<td>18.8</td>
</tr>
<tr>
<td>Live with parents</td>
<td>0</td>
</tr>
<tr>
<td>Share with friends</td>
<td>6.25</td>
</tr>
<tr>
<td>Three generation family</td>
<td>0</td>
</tr>
</tbody>
</table>

There were 13 customers who sought to switch and had been unable to do so, of whom three reported multiple rejection. Only two had had problems with paying in the past two years, although another used Easyway which may have been construed by the retailer as indicating a problem payer. The sample of rejected switchers is too small to make generalisations. However, six had off-peak hot water, and such households have already been demonstrated as being subject to discrimination.

No customer who had been disconnected during the previous two years had switched to a market contract, although two had attempted to do so. Only seven people indicated they had been disconnected. One was an age pensioner, one a non-age pensioner and two had incomes between $30,000 p.a. and $39,999 p.a., of whom one was a sole parent with children. Of the remaining two who stated their income, one had income between $40,000 p.a. and $49,000 p.a., and the other more than $100,000 p.a.

The second question the survey sought to explore was the possibility that, rather than excluding customers, retailers may take advantage of their market power and exploit vulnerable customers. Whilst the survey instrument attempted to gather the data, the research was unable to determine for any switching customer the extent of benefits or losses. This arose as almost all customers failed to disclose their new tariff rate. The explanation may be that the task was too complex or too onerous, probably the former. For example, switchers were asked separately whether or not their new price was fixed. Only around 10% appeared to know the answer to this question, which is extraordinary given that price is the major reason for switching. This raises questions regarding the efficacy of the market, but does not permit an answer to the research question. The question therefore of whether some customers are exploited in terms of being induced into
accepting detrimental pricing arrangements remains unanswered, and arguably may require utilising a different research approach.

Finally, whilst systematic market segmentation (on the basis of low-income/disadvantage) per se has not been revealed by the survey, this is not to say that elements do not exist. To provide an illustration of how segmentation can work, loyalty programs are discussed and related to the findings of the survey.

11.5 Loyalty programs

Some electricity retailers have linked their service to wider loyalty programs such as Fly Buys (Pulse 2002) whose membership can be significant in terms of the value of price benefits. It would be fair to assume that households with low fixed incomes are less likely to be members of loyalty programs, given that benefits only accrue with expenditure and there are annual membership costs. Examining the income levels of the respondents (Table 11) found that while interest in loyalty programs was highest amongst those with above median income, with 43% \( (n=431) \) stating that bonus points were ‘very important’, interest from respondents with below median income was almost as high at 41%. A comparison with the source of their income is revealing. If the ‘very important’ and ‘important’ categories are collapsed together, full-time workers are nearly three times more likely to believe loyalty/bonus schemes are important than ‘not important’, while age pensioners and the unemployed are only twice as likely to be of this view. This is not surprising as such schemes require higher levels of expenditure to work. Nevertheless, the extent of interest by those on low fixed incomes suggests that the benefits of such schemes are well understood.

Table 11: Loyalty schemes as a factor influencing shopping

<table>
<thead>
<tr>
<th>Source of Income</th>
<th>Full-time work % ( n =221 )</th>
<th>Age pension % ( n =58 )</th>
<th>Unemployment benefits % ( n =12 )</th>
</tr>
</thead>
<tbody>
<tr>
<td>Very important</td>
<td>42</td>
<td>31</td>
<td>33</td>
</tr>
<tr>
<td>Important</td>
<td>32</td>
<td>34</td>
<td>33</td>
</tr>
<tr>
<td>Not important</td>
<td>25</td>
<td>34</td>
<td>33</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>
An explanation of the behaviour of the low fixed income respondents could be as follows. These respondents fall into two sub-groups: those who have had higher longer-term income in the past (such as those who have retired or were temporarily unemployed), and those who have not been able to acquire assets or savings (other than a modest home, for example). The former may have already been members of loyalty programs, while the latter with small disposal income have probably never joined. Both groups are price sensitive, but only one is able to take advantage of the electricity price discounts offered by this method. Loyalty programs therefore fulfil a useful function for retailers because they act as a screening device that permits them to exclude the more vulnerable group.

11.6 Conclusion

Other than off-peak users, the survey was unable to find evidence of systemic discrimination by electricity retailers against low-income/disadvantaged households. Off-peak users more broadly and rural/regional households generally were clearly being avoided by retailers seeking to acquire new customers. The ESC’s (2004a) review of the effectiveness of competition has subsequently supported these findings. VCOSS (2004a) argued that this avoidance meant that 1 million customers or almost half of the domestic market were effectively excluded from participating in the market.

Given that legislators in many states of the US accepted the argument that redlining would occur unless there were provisions to mitigate such pressures, and that discriminatory service and service withdrawal has been identified in the UK electricity industry, it is surprising that insufficient evidence of segmentation in Victoria has been found. This can be explained by referring to changes in policy that occurred. When the research commenced, the statutory provisions for the obligation to supply (and the price/service package contained in the deemed and standing offers) were anticipated as ceasing at the end of 2003. In the later half of that year the Victorian government extended these protections for a further year. The original research plan had intended that customers be surveyed three times over three years, with the first year (2003) hoping to capture changes as the retailers prepared for 2004 and complete liberalisation. In 2004 the government again extended the legislation, this time to the end of 2007, and negotiated a price path for those years. The price in effect was now also regulated. This meant that the period was not likely to be one in which segmentation could develop. However, changes to the
Electricity Retail Code for full retail competition give strong indication that, despite government policy, the ESC was providing a framework that supported segmentation.

Nor should it be concluded that there was no evidence of differential treatment. Customers in rural and regional areas received far fewer offers than their metropolitan counterparts and as a consequence took up a far smaller share of market contracts, despite more proactive attitude to obtaining a contract. Other customers with higher cost structures, particularly those with off-peak hot water heating, were clearly being avoided, as the ESC has also acknowledged. In relation to low income and/or payment-troubled customers, the results were mixed. Some customers with a known history of arrears had been refused market contracts. On the other hand, some had switched. The main difficulty with the data for these cases was the smallness of the samples: they are too small to support any conclusions that could be generalised. Despite the general conclusion of lack of evidence, and the extension of the safety net arrangements, two areas of examination, loyalty programs and PPM (should they be introduced), will over time provide evidence of differential treatment if not segmentation.

The research plan was also prepared for the possibility that the market would not develop for other reasons. The first survey therefore revealed pervasive customer inertia. While having serious implications for the effectiveness of the market, inertia also inhibits the capacity of retailers to segment their customer base. This inertia was associated with respondents’ attitudes to competition: most had no interest and many were suspicious of the market. Given these two factors, that is, change of government policy and customer inertia, the plan for subsequent surveys was abandoned at this stage as it was felt that little additional data of value would be obtained.

While recognised as an endemic issue in certain markets (like electricity), customer inertia had not been considered in the reform literature as a political or sociological response to reform. Rather it had been regarded as an economic or technical matter. What the survey revealed was that the field of economics in particular may need to assess the validity of the claim that choice/competition is the most desirable method of increasing societal welfare when ‘customers’ themselves overtly reject choice. The respondents to the survey indicated that their choice was not to choose competition. The following chapter reports on this finding and places it within political and policy debates on competition reform.
Chapter 12: Empirical research: Customer inertia

The primary purpose of the survey was to uncover evidence of market segmentation. It was also important to attempt to capture the significant factors concerning the operation of the market. To this end, one factor stood out – customer inertia. This chapter reports on this finding and its implications.

12.1 Introduction

The Victorian electricity industry has been revolutionised over the last decade as a result of two distinct but related policies: privatisation and market liberalisation, or as it is more often referred to, National Competition Policy (NCP). While NCP does not require privatisation, many of its proponents such as the various Commissions of Audit (for example, Officer 1996) established by governments over this period have advocated it. The Kennett government pursued both policies, disaggregating and fully privatising the former SECV and taking the lead in introducing competition into the industry.

The purported benefits of competition were a key element of its reform program. Finance Minister Ian Smith said in a statement of government policy:

all Victorians will ultimately benefit from competition in the Victorian electricity industry, in particular from the empowerment that choice will give them in their dealings with their suppliers…it is expected that…retailers will offer innovative price/service mixes tailored to individual customer’s needs (ORG 1994: A.2.1.3).

Treasurer Alan Stockdale (1994: 5) also stated that:

Our second aim is to increase choice for both domestic and industrial consumers. Marketplace competition plus greater power in the hands of consumers will return benefits to both households and businesses as they gain greater freedom to choose products, prices and suppliers to suit their preferences. Maximum customer choice is designed to ensure that consumers obtain benefit for themselves rather than the benefits of greater efficiency flowing to those able to exploit monopoly rent.
The Bracks government ultimately delivered competition to the household sector in 2002. Minister for Energy Candy Broad (2000: 3) said the government ‘supports the commercial drive in [the electricity] industry. We recognise the benefits that competition and choice can deliver for customers and the State’s economy’.

Remarkably, in developing policies to introduce competition to the household sector, neither the Kennett nor Bracks governments assessed Victorians’ attitudes to competition. Both had reason to believe that this did not enjoy the level of public support that might have been expected. The ORG’s preparatory research for FRC revealed significant resistance. Millward Brown (2001a), on behalf of the ORG, found in April 2001 that 71% of respondents had concerns about competition. This dropped to 55% in July 2001 and rose again in the period from 3 September to 25 November (rolling sample) to 73%. Concerns included costs, reliability, customer service, privatisation, lack of information and foreign ownership (Millward Brown 2001b, 2001c). A year later, consultants working for the ESC’s report on the effectiveness of FRC concluded:

Victorians believe that competition is inevitable and they are not strongly for or against it, however they strongly support putting in place measures to ensure that every Victorian has access to essential services (Wallis Consulting 2002: 33).

This is to beg the question of why Victorians believe competition to be ‘inevitable’. It is well known that privatisation of the electricity industry was and remains deeply unpopular and that competition, as Millward Brown found, elicited troubling levels of concern. Could it be that competition in electricity is a policy that consumers do not endorse? This raises a further intriguing question: could lack of support for competition affect households’ willingness to participate in the market created by government policy? As the ESC (2002: 58) put it: ‘Ultimately, the most important indicator of the effectiveness of competition is the extent to which customers are entering into market contracts’. It reported that, six months after the market had opened, only 5% of customers had switched. Their research found, however, that despite retailers recording certain customers as having switched, some of them did not believe or were unaware that they had done so (Wallis Consulting 2002: 58). Only 7% of households indicated they were ‘very likely’ to switch in the near future. On this

58 Irving Saulwick poll commissioned by Uniting Church’s Commission for Mission in 1995, AGB McNair poll commissioned by the Age (4 Feb. 1995), and the ‘Public Good’ survey conducted in 2001 by the Institute for Social Research, Swinburne University of Technology.
basis, the ESC (2002: 77) had to conclude that ‘the performance observed in the electricity retail market to date is not yet consistent with that of an effectively competitive market’. Nevertheless, they were optimistic that customer inertia was only temporary.

Consumers’ views of and initial experience with competition in electricity provision form the subject matter of this chapter. More specifically, it aims to assess the extent to which Victorians see competition as a desirable policy goal, and to tease out the policy implications.

12.2 Switching

Respondents were asked about competition, the benefits that might flow to Victorians as a result of it, and their own choices since the market opened. A key argument raised by proponents of market-based reform was that it could be expected to lead to price falls, as consumers gain the power to choose the best available deal. After ten years of policy settings intended to foster support for competition in electricity provision, and significant effort on the part of government and retailers to promote the opening of the market to households, it would be expected that domestic customers would exhibit interest in choice.

The ESC (2002) found that around 5% of customers had switched, which in their opinion and that of the government was too little to permit a conclusion that the market was at present effective. My survey found that 13% of customers had switched (see Table 12), but this figure needs to be treated with caution. Firstly, the survey may over-represent switchers as they are more likely to self-select in responding to the questionnaire. Secondly, as will be discussed later in more detail, nearly 50% of the switchers had moved residence, although only 7% of the overall sample had moved since the opening of the market. Few of these switchers/movers indicated they had actively exercised ‘choice’. Discounting these customers, the number of switchers was around 7%, which confirms the customer inertia found by the ESC.
Table 12: Number of customers moving from deemed contract (n=576)

<table>
<thead>
<tr>
<th>Movement from deemed contract to</th>
<th>No.</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market contract with new supplier</td>
<td>34</td>
<td>5.9</td>
</tr>
<tr>
<td>Market contract with existing supplier</td>
<td>25</td>
<td>4.3</td>
</tr>
<tr>
<td>Moved dwelling without knowing to what</td>
<td>19</td>
<td>3.3</td>
</tr>
<tr>
<td>To standing offer contract</td>
<td>1</td>
<td>*</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>79</td>
<td>13.5</td>
</tr>
</tbody>
</table>

There are a number of possible explanations for customer inertia. Householders may be satisfied with their current supply arrangement and not interested in switching. It may be the case that, as the ESC believes, it will take time, additional information and education of consumers for the market to mature. Conversely, it may be the case that householders do not want choice. Customer inertia may also be a direct result of retailers’ marketing strategies. The survey tested customers’ attitudes and experience of the market in order to tease out the implications of customer inertia.

12.3 Customer attitudes

When asked whether they thought competition would mean that they would be better off due to price falls, surprisingly only 10% (n=572) of respondents answered positively (Table 13). NESB customers expressed views similar to those expressed by customers as a whole. Rural customers were twice as likely as their Melbourne counterparts to believe prices would increase. Less than 2% of rural customers thought prices would decrease.

Table 13: Customer attitudes to the price benefits of the electricity market (n=572)

<table>
<thead>
<tr>
<th>Q: Do you think that for you competition in electricity will lead you to paying(^5)*</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Higher prices</td>
<td>29</td>
</tr>
<tr>
<td>Same price</td>
<td>27</td>
</tr>
<tr>
<td>Lower prices</td>
<td>10</td>
</tr>
<tr>
<td>Don’t know</td>
<td>24</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100</td>
</tr>
</tbody>
</table>

\(^5\) Customers were given the option of stating that they thought they would pay higher prices for Green Power, to avoid confusion relating to a higher price for a different product.
Attitudes varied only slightly by income. Respondents with individual incomes under $20,000 p.a. were four times more likely to think that competition would result in them paying higher rather than lower prices. Those with incomes over $20,000 p.a. were around three times more likely to believe they would pay higher rather than lower prices.

It might be expected that the 10% of respondents who felt positively about lower prices in the market would be highly represented amongst those who had taken the opportunity to switch to a market contract. Of the 59 households who thought they would be better off, only 16 actually switched. In relation to customer service, only 23 of the 117 who thought customer service would be better with competition exercised choice.

Economic theory suggests that competition can be expected to lead to improved levels of service. Businesses know that, when service levels fall, customers are likely to shift to another company. However, the respondents to the survey were sceptical about this. Only 20% felt that they would experience improved service, with a higher percentage among NESB customers (30%). 15% thought that customer service would worsen, with 48% thinking it would remain the same. Melbourne and rural customers had about the same degree of pessimism concerning the possibility of customer service levels worsening, but there was a significant difference about whether they would improve, with outer Melbourne customers being three times as likely as either inner Melbourne or rural customers to believe that it would do so (4% versus 12%). This difference can be explained at least in part by the higher support for the market amongst NESB customers and their absence in rural areas.

Retail competition has no impact on reliability of supply but there is a fairly widely held misconception that it does, with almost 44% indicating an impact (Table 14). Only 9% expected reliability would improve, while 19% thought it would deteriorate. As with price and customer service, NESB respondents held more favourable attitudes to the market, with 24% believing that reliability would improve (compared with only 9% of non-NESB respondents).
Table 14: Customer attitudes towards reliability of supply in the private market (n=574)

<table>
<thead>
<tr>
<th>Q: In terms of reliability of supply, do you think that competition will mean that most electricity customers will be</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Better off</td>
<td>9</td>
</tr>
<tr>
<td>Same</td>
<td>41</td>
</tr>
<tr>
<td>Worse off</td>
<td>19</td>
</tr>
<tr>
<td>Varied impact</td>
<td>16</td>
</tr>
<tr>
<td>Don't know</td>
<td>15</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

12.4 Awareness of the market

When asked to name their own supplier in 2001, 21% (n=532) of respondents admitted to not knowing the answer without looking at their bill. One named a gas company and 56 used company names that are out of date. Asked to list names of retailers (Table 15), 4.5% could not name any. Asked if they thought other people knew who supplied them, given the changes to the industry, 41% (n=564) disagreed.

Table 15: Customer’s knowledge of retailers (n=484)

<table>
<thead>
<tr>
<th>Q: How many retailers can you name? (please name)</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 retailers</td>
<td>4.5</td>
</tr>
<tr>
<td>1 retailer</td>
<td>39.5</td>
</tr>
<tr>
<td>2 retailers</td>
<td>33.5</td>
</tr>
<tr>
<td>3 retailers</td>
<td>15</td>
</tr>
<tr>
<td>4 retailers</td>
<td>5</td>
</tr>
<tr>
<td>5 retailers</td>
<td>2</td>
</tr>
<tr>
<td>6 retailers</td>
<td>*</td>
</tr>
<tr>
<td>7 retailers</td>
<td>*</td>
</tr>
<tr>
<td>8 retailers</td>
<td>*</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

As Table 16 indicates, most respondents (54%) failed to recall any retailer contacting them, but 16% recalled receiving more than one contact. Of the 750,000 offers that the
ESC (2002) says retailers made, it is evident that there is considerable unevenness in the distribution across the total of 2.1 million small business and domestic customers. This may suggest, as the ESC indicates, that retailer activity is confined to specific market segments.

Table 16: Retailer activity in the market \((n=552)\)

<table>
<thead>
<tr>
<th>Number of customer contacts initiated by retailers</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contacted by 0 retailer</td>
<td>54</td>
</tr>
<tr>
<td>Contacted by 1 retailer</td>
<td>29</td>
</tr>
<tr>
<td>Contacted by 2 retailers</td>
<td>14</td>
</tr>
<tr>
<td>Contacted by 3 retailers</td>
<td>2</td>
</tr>
<tr>
<td>Contacted by 4 retailers</td>
<td>*</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

‘Offers’ need to be distinguished from the final agreement to contract. For example, an offer can be made on an unsolicited basis that does not preclude the retailer from later withdrawing it should a customer exhibit interest. From these contacts, 18.5% \((n=524)\) of respondents believed they had been made one offer, 6% two offers, and less than 1% three offers. 33% \((n=385)\) of respondents had received letters, with 9% \((n=522)\) approached by telemarketers and 7% \((n=534)\) by door-to-door salespeople. Less than 1% had encountered salespeople in shopping centres. There were no significant differences in the proportion of NESB and non-NESB households being contacted by retailers.

A small number of respondents (9%) actively sought out an offer, although not all were successful in obtaining a contract. While customer interest is low, low participation may also be explained by retailer preference for higher-margin customers.

12.5 **Factors influencing choice**

Respondents were given a list of factors that may have influenced them when considering a choice of supplier (Table 17). They were not asked to rank these factors in relation to each other.
Table 17: Factors that are important in shopping around (%)

<table>
<thead>
<tr>
<th>Comparison of influences on shopping</th>
<th>Very important</th>
<th>Important</th>
<th>Not important</th>
<th>n=</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price</td>
<td>64</td>
<td>25</td>
<td>11</td>
<td>476</td>
</tr>
<tr>
<td>Green Power</td>
<td>30</td>
<td>37</td>
<td>33</td>
<td>443</td>
</tr>
<tr>
<td>Combined bills</td>
<td>31</td>
<td>30</td>
<td>38</td>
<td>460</td>
</tr>
<tr>
<td>Energy efficiency help</td>
<td>20</td>
<td>25</td>
<td>55</td>
<td>434</td>
</tr>
<tr>
<td>Help buying appliances</td>
<td>16</td>
<td>23</td>
<td>57</td>
<td>437</td>
</tr>
</tbody>
</table>

Perhaps predictably, those in full-time work and on higher incomes were more interested in Green Power (renewable energy) deals. During this period, known Green Power offers were more expensive than deemed and standing offer tariffs. Social security beneficiaries were three times more likely to say that Green Power was not important rather than very important. Nevertheless, there was still interest, with just under 20% (n=429) of respondents with incomes under $20,000 saying Green Power was very important or important. The perception at the time (based in reality) that Green Power was more expensive clearly deterred them from switching. There is currently no Green Power deemed or standing offer tariff. Interest in energy efficiency is far less across all income groups, with the exception of social security beneficiaries who rated it equally with Green Power. ‘Dual fuel’ deals have popularity, but these are commonly offered with a price discount, and the survey did not attempt to distinguish between the price incentive and other perceived benefits of combining bills. There was a considerable level of interest in linking the buying of appliances with purchase of electricity. Some retailers currently offer such services.

12.6 Why customers did not switch

Up until this point we have sought to understand why the switching rates in the fully competitive electricity market have been so low. Respondents to the survey indicated a strong interest in price savings but lacked faith in the market to deliver price reductions or better service. The survey also found that retailer activity would appear to be focused on some customer groups but not others.

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60 These are the top five choices out of a set of nine. Support for the other four options was low.
Table 18 shows that, of those respondents who had considered changing but had not done so, 19% \((n=278)\) were still thinking about the possibility. The majority (52%) of customers in this group of potential switchers had been deterred from entering the market by their experience to date, including 42% \((n=40)\) of those respondents who held positive views about the benefits of competition. The perceived ‘hassle’ of changing deterred the most (18%). Insufficient information and inability to compare offers were also problems, while 9% felt the incentives to switch were too small.

**Table 18: Reasons for considering switching but not doing so \((n=278)\)**

<table>
<thead>
<tr>
<th>Reasons</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have not taken next step</td>
<td>19</td>
</tr>
<tr>
<td>Unable to obtain sufficient information</td>
<td>12</td>
</tr>
<tr>
<td>Unable to compare offers properly</td>
<td>13</td>
</tr>
<tr>
<td>Put off by hassle of changing</td>
<td>18</td>
</tr>
<tr>
<td>Did not see anything worth changing for</td>
<td>9</td>
</tr>
<tr>
<td>No supplier made an offer</td>
<td>27</td>
</tr>
<tr>
<td>Other</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

27% had not received an offer. These may be low-value customers who, from a retailer’s perspective, do not warrant the cost of their acquisition.

Of those respondents who had not considered switching at all, 11% answered that they were unaware of competition (Table 19), 15% were anticipating possible switching, but 68% were resistant, either actively or passively. Comments in the ‘other’ category are worth closer inspection: ‘all the same’, ‘can’t be bothered’, ‘can't see the point’, ‘expect minimal impact’, ‘lack of knowledge’, ‘no time to shop around’ and ‘privatisation protest’ were some. None were positive towards competition.

A number of respondents volunteered unsolicited comments. There was only one theme: a belief in the collective public interest of public ownership. The following are two examples:

Believe profit motive will result in me paying more and all companies will be out to screw me out of money, not give it to me.
My belief is that the theory behind privatisation is that competition encourages accountability/responsibility. However, in practice, one government is actually a lot more accountable than a few giant corporations who potentially could set an expensive industry standard. A government body is inherently more accountable than a private company.

Table 19: Reasons for not considering switching (n =241)

<table>
<thead>
<tr>
<th>Reasons</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Did not know I could</td>
<td>11</td>
</tr>
<tr>
<td>Satisfied with current arrangement</td>
<td>55</td>
</tr>
<tr>
<td>Have not got around to it</td>
<td>11</td>
</tr>
<tr>
<td>Waiting to join community buying group</td>
<td>*</td>
</tr>
<tr>
<td>Waiting for gas competition</td>
<td>1</td>
</tr>
<tr>
<td>Waiting for market to develop</td>
<td>3</td>
</tr>
<tr>
<td>Put off by needing to learn so much</td>
<td>4</td>
</tr>
<tr>
<td>Afraid to change</td>
<td>2</td>
</tr>
<tr>
<td>See not changing as a kind of protest against privatisation</td>
<td>7</td>
</tr>
<tr>
<td>Other</td>
<td>5</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

These less than positive views about the market, combined with those who are satisfied with the pre-competition status quo, means that about half of the respondents are not looking to enter the market at this point or are likely to do so. There was nothing to distinguish one income group (or source) from another among these respondents.

12.7 Discussion

The Economic Planning Advisory Council (EPAC 1989) and the Industry Commission (1991a) promoted electricity competition well over a decade ago. There was and remains little literature relating to the impact or possible impacts of market liberalisation of electricity on the household sector. The Hilmer Report (Hilmer 1993a) rapidly became the basis of NCP. Subsequent reforms to a range of sectors, including electricity, were largely based on later Industry Commission (1995) modelling of the Australian economy that anticipated $23 billion worth of savings should competition be implemented. However,
NCP has been criticised for being implemented on the basis of theory rather than ‘economic analysis’ (Quiggin 1999: 74). After ten years of policy settings intended to foster support for competition in electricity provision, and longer for markets more generally, it could be expected that there would be more popular support for the policy, but this is doubtful in relation to essential services. The explanation may partly lie in the lack of substantiation of the claims of benefits flowing to households and the championing of the removal of subsidies that would leave many households as losers rather than winners. Indeed, after a decade of reform, domestic customers in Victoria are on average paying 3% more for their electricity, and some customers 24% more (see Table 2). Relatively few had obtained benefits. In addition, two of the incumbent retailers merged within months of the market opening to households, reducing the number of major players to three. Mergers, withdrawal of service, market segmentation and increasing charges for low-volume customers have been features of deregulated telecommunications and banking. It is not difficult to see why popular opinion is out of step with elite opinion.

Graeme Samuel (2003), then chair of the National Competition Council and now chair of the Australian Competition and Consumer Commission, captures the continuing lack of support for competition policy:

> In a society predicated on the notion of a ‘fair go’, we should also not be too surprised when we see a questioning of policies that may appear to sacrifice fairness for economic growth.

He articulates a collective resistance to elite policy, noting that people are resistant to economic reform because of its perceived impact upon community and because ‘corporations [are] perceived to be delinquent citizens’.

The introduction of competition in the electricity sector to the household level is highly reliant on customer endorsement and participation. The levels of antipathy exhibited by respondents to this survey have antecedents that should make the finding of customer inertia unsurprising. The 1990s witnessed inquiries by both the Senate and the House of Representatives in response to community concerns about NCP. In addition, customer inertia has been evident in other jurisdictions and analogous industries. The decision to
implement FRC when customer endorsement was uncertain was therefore a considerable risk, and arguably a poor basis for policy making.

Domestic customer inertia in the electricity sector may well be enduring. This has important policy implications, some of which were foreseen. SRC International (1998) warned the New South Wales Independent Pricing and Regulatory Tribunal that domestic customers were unlikely to be motivated to switch for amounts that would sustain retailers’ profits. It envisaged that customer inertia would result in retailers raising prices to monopoly levels.

In order to protect customers from such monopoly prices, SRC International argued that the response of governments would be to impose price controls. In Victoria as in the UK, the market opened with price caps already in place. These are a maximum price sanctioned by the regulator or government. Price caps in Victoria were imposed because the incumbent retailers proposed substantial price increases on the eve of the opening of the market. The retailers argue that the tariff that domestic customers are on at the beginning of competition (the deemed tariff) and the safety net (standing offers) need to be higher than the prices offered in the market; competition is stimulated by new entrant retailers perceiving an opportunity to take profits by undercutting incumbents, and hence competing the price down. The Victorian government agreed that prices needed to be above market prices at the outset of competition. This concept of headroom looks just a little like the department store putting its prices up before holding a sale.

The difficulty for government is the possibility of continuing and widespread customer inertia. This would denote market failure and leave customers exposed by default to prices limited only by price caps, that is, government sanctioned monopoly prices. There is already evidence in the UK that customer inertia has resulted in extensive monopoly pricing, raising doubts as to whether the domestic market could ever be considered functionally competitive (Brigham and Waterson 2003: 12).

In addition to what may be sustained customer inertia, the single largest group who are actively participating in the market are low-income (therefore likely to be low-volume) and hence low-margin customers. This suggests that such households are very price sensitive and responsive. Retailers may well instigate changes to their marketing and customer
acquisition programs to minimise the migration of this customer segment because as ‘transactors’ with small margins they dilute profitability. As the ESC (2002) noted, retailers appear at the outset to be avoiding low-volume customers. If this is the case, it would result in a declining number of customers switching unless it was offset by increases in other customer segments, but there is no evidence to suggest that higher-margin customers (other than the small group seeking Green Power deals) are likely to change their attitude to competition.

As this survey also identified, around half of the switchers entered the market as a result of moving dwelling. These customers have higher transaction costs and as a consequence lower the margin available for the retailer. This is especially true of renters, who move on average once every five years, compared to home owners’ average of every seven years. Rental housing is also the growth segment of the housing market increasingly servicing low-income households (Burke and Ralston 2003).

It is already evident that retailers are attracted to acquisition methods that reach wealthier customers while effectively screening out many low-income customers. Loyalty programs are a prime example. Whilst exclusion from the market is disturbing, the alternative is the possibility that price-conscious low-income households may be subject to exploitation by retailers. For example, offers of large cash rebates are attractive to those on low fixed incomes. One Victorian retailer provides such inducements, but these offers also involve tariff structures that can be highly disadvantageous to low-volume users. The upfront rebate benefit may be more than offset by a higher cost of consumption.

The final act of reform would be the expiry of legislation mandating an obligation to offer. Should this happen, supply becomes a matter of choice on the part of retailers, giving them unprecedented market power. Migration onto market contracts at this point will be involuntary. It opens the way for unhindered market segmentation aimed at exclusion of problem payers, or the imposition of exorbitant charges in cases where the customer has no market power. Arguably, given the essential service nature of electricity, all households are price takers, therefore vulnerable and disadvantaged customers are very much at risk of market abuse. Ironically the existence of customer inertia and the ‘protection’ of the deemed and standing offer tariffs currently stymies the dis-aggregation of customers into ‘bordered’ markets.
12.8 Conclusion

This research sought to understand the attitudes and initial experience of households in the recently opened fully competitive electricity market in Victoria. The survey discovered a substantial gap between the views of elite policy makers and the aspirations of ordinary Victorians. This gap can help explain customer inertia in the market. It also found that current participation rates are largely the result of households moving dwelling and/or the experience of fuel poverty. The small margins and high transaction costs may result in retailers attempting to recoup a greater proportion of costs from these customers, or minimise their migration onto market contracts.

There are important policy lessons here for government. It cannot be assumed that competition will emerge simply because a competitive framework has been put in place. Not only is there the risk that customer inertia will result in customers paying higher prices than if there had been no market, but the costs of implementing and running the market, estimated at between $1.5 and $4 billion nationally over the first five years (Energy Action Group 2002), must be recovered from households regardless of the success or failure of the market. Customers may legitimately ask about the adequacy of the analysis that was used to support the Victorian government's decision to proceed with FRC. The issue now is what levels of customer inertia will the government tolerate and for how long. Persistent customer inertia means that, as more time passes, the loss to the community and to the economy more generally mounts. Firstly, there needs to be savings to compensate for the establishment costs of the market. Secondly, inertia means that most customers remain on the deemed tariff. The deemed tariff contains the headroom or planned element of excess profit that was the incentive for new entrants to come into the market and for existing retailers to respond to protect their market share. If customers fail to switch out of choice, retailers can set prices. It is conceivable, as SRC International (1998) has warned, that prices rather than going down may actually rise. If electricity customers effectively pay a monopoly price, economic theory suggests that there will be efficiency losses.

Despite this, customer inertia and the access to service that the deemed and standing offer tariffs provide may be acting to inhibit market segmentation intended to exclude and/or exploit vulnerable and disadvantaged households caught in an emerging residual market. This and other policy implications are explored in the final chapter.
Chapter 13: Conclusion

The market model implies that production is a technical rather than a political process (Ryan 2001: 107).

The Kennett government planned that in 2000 Victorian households would enter a competitive market for electricity. In order to assuage concerns about the possible impacts of reform more generally and to provide stability during the transition period, it legislated for a domestic price path that delivered real price cuts during 1995-2000 (the Electricity Industry Tariff Order). In addition, it cemented the primacy of CSOs in the ideological sense as the concession to social policy in the electricity industry. By doing so it resolved, albeit only temporarily, the perceived conflict between marketisation and welfare needs. Future conflict between social policy objectives and market provision was a legacy bequeathed to the Bracks government.

My central concern has been the potential for market segmentation of domestic electricity customers and the formation of a residual market, and the effect of these on the efficacy of social protections. The reform of the domestic electricity market has demonstrated the danger of assuming a supply-side dominated view of competition as the means of achieving efficiency gains. For orthodox economics, the experience of customer inertia in domestic electricity markets has provided insights into the role of choice that should lead to reflection on the adequacy of neo-liberal theory for practical policy making. Nor can economics overlook the market failure (abuse of market power leading to the formation of a residual market) that arises when there is market segmentation. Residual markets also reveal the limitations of equal opportunity and anti-discrimination statutes and beg the question of what is or is not legitimate discrimination and why. The history of segmentation and of market reform of utilities has served to highlight three models of social protection, and the inadequacy of any model that does not account for the destructive impacts of commodification.

13.1 Findings

Marketing literature and observations of ‘essential services’ markets suggests that mass markets such as electricity are likely to be subject to corporate strategies aimed at market
segmentation. This research attempted to track the possible emergence of market segmentation within the recently deregulated domestic electricity market in Victoria. In particular it was concerned with the potential formation of a residual market or market of last resort serving the least attractive customers.

Initially a series of annual surveys of domestic customers was envisaged as providing the means to obtain the necessary data. It was anticipated that the slated demise of the obligation to supply and price caps would result in retailers preparing for when they could choose which customers they would serve. However, the unexpected extension of the safety net arrangements meant that retailers were unable to shed customers on any scale. The findings of the initial survey also suggested that customer inertia would in any event inhibit segmentation. This meant that any further survey would be unlikely to reveal changes.

The potential always existed for very little to occur in the early years of the market. The experience of deregulated electricity markets elsewhere has been of high levels of customer inertia. Therefore the survey needed to be able to explain ‘whatever’ happened. Customer inertia was indeed what happened. But unlike the ESC or any other governmental research, my survey tested customer attitudes to competition and found a startling homogeneity of views: 90% of respondents were cynical in regard to the purported benefits of competition. Whilst many public opinion surveys over the past two decades have consistently found widespread support for public ownership, none had actually sought opinion about markets. Given the extensive preparation for privatisation and competition reform which Australians have been subject to over many years, the attitude of the respondents was unlikely to change quickly. Attitudes and the safety net (which meant customers were not required to enter the market yet) explained customer inertia.

The first survey did not find any evidence to suggest segmentation on the basis of customers being low-income or of poor credit worthiness, although it did find, as did the ESC, that retailers had avoided off-peak and rural customers. This avoidance related to the impact of price capping arrangements. Despite this negative finding there is evidence to suggest that market segmentation is likely to be a consequence of liberalisation. The experience of the UK points to the role of regulation in assisting the formation of residual
markets. The UK shows that an increasing commercial focus can result in segmentation occurring in the absence of competition. There is actually no contradiction here as regulation is merely permitting market-like behaviour. In this case it is cost reflectivity. In the electricity industry, payment method technologies are explicitly used to enable a claimed actuarial basis for credit management. The pressure from industry in Victoria to introduce PPM is a strong indicator that retailers are seeking to segment their customers. The Victorian reform model created a discriminatory safety net (the standing offer), the Retail Code has been modified in ways that encourage discriminatory credit management, and tariffs have already been significantly rebalanced. An a priori assumption operates so that the market model simply does not countenance the possibility that these arrangements may permit exploitation of vulnerable customers. It is assumed that the existence of multiple retailers will mean that prices will reflect costs. This means it is unnecessary at a regulatory level to scrutinise the actuarial basis for prices. It is this preference for a model over empirical assessment that Sheil (2000) argues resulted in Sydney Water’s contamination crisis and Adelaide’s sewerage treatment malfunction (the ‘Big Pong’).

This evidence suggests that the problem of market abuse is not necessarily related to a lack of providers but rather to the non-discretionary nature of the service. In the developed world, electricity is an essential service and few people voluntarily forego connection. Application of risk premiums that insure retailers against payment default but add to the financial burden of households experiencing fuel poverty is a perverse outcome. From a public policy perspective, it also assumes no relationship to other consumption (such as essential food intake or health services) or the ramifications for a blow-out in budget-funded assistance. It has been claimed that the poor pay more. Segmentation offers a window onto how markets can act to impoverish. Given that a large proportion of the consumption of disadvantaged households is non-discretionary, permitting discrimination in the delivery of essential services is paramount to guaranteeing poverty.

13.2 Limitations

As discussed, the obligation to supply, price caps and customer attitudes constrained possible segmentation. The survey was also subject to other limitations. The newness of the market, its complexity, and poor promotion and education of households by
government meant that respondents were ill equipped to provide data, particularly in relation to switching. The survey instrument needed to balance the requirement to obtain data with ascertaining the limits of respondents' knowledge of the reforms. In retrospect, it may have been better to ensure data collection rather than test the respondents understanding.

Around half of households (as evidenced by other surveys as well) are disinterested in the topic, at least in the sense that they appear to be 'satisficing'.\(^{61}\) The customer segment of most interest – low-income, financially distressed households – proved to be fairly elusive. This is also not surprising, as it is unreasonable to believe that households in crisis will respond to surveys. But the survey was of particular interest to at least one group – age pensioners – and this has probably skewed the results, particularly in relation to attitudes.

### 13.3 Implications

The reforms to the Victorian electricity industry have been costly to implement, but policy makers treated customer acceptance of market conditions of supply as a given rather than ensuring the support was there or would be within an appropriate time frame. The potential for market failure arising from customer inertia should have been seen as a significant risk. Customer inertia while it continues requires the imposition of price caps to avoid monopoly pricing, but price caps undermine the development of the market. It is a vicious circle that may not be breakable. Electricity may be an example of an industry in which the demand characteristics of the customers are a major determinant in whether or not a market can succeed. For economic theory, customer inertia may need to be seen as a defining characteristic in some industries rather than as a transitional issue or temporary barrier that can be overcome. For Australian policy makers, the current assumptions underpinning competition policy need to be revisited as policy settings may be generating economically perverse outcomes. The welfare outcomes of competition policy in a number of industries may actually be sub-optimal.

I have established that redlining is a form of market segmentation of customers. While Colton understood that the non-discretionary nature of essential services meant that some

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\(^{61}\) Meaning they are sufficiently satisfied with supply not to make a change, despite knowing that they may be able to achieve a better outcome if they did so.
of these consumers could be exploited, I have argued that it is not necessarily a lack of suppliers that causes this. In this sense I have redefined the meaning of ‘residual market’. I have established that government intervention can also result in segmentation. I distinguish this outcome by use of the term ‘provider of last resort’ (POLR) and note that the discrimination involved can be either positive or negative. Unfortunately in Victoria the liberalisation has meant that vulnerable consumers are subject to state sanctioned safety net arrangements that constitute the negative form of POLR. Just as Florio (2004) identified exploitation arising from regulation and liberalisation in the UK, I too have been able to demonstrate that regulation, aimed at mimicking the market, contributes to discriminatory practices by retailers.

In the UK, payment methods and associated technologies were instrumental in segmenting the customer base even before supply was deregulated. PPM means the poorest consumers in the UK pay the most for supply. PPM constitutes the residual market. Market segmentation of essential services customers affects not just the vulnerable and disadvantaged consumers but could also mean that attractive customers are cross-subsidised. This undermines the argument that competition engenders economic efficiency. In his discussion of the distributional impacts on households, Florio (2004: 259) makes it clear that the domestic price increases that have resulted from tariff rebalancing constituted for many small customers ‘social hardship’ that was ‘unnecessary for an improvement in allocative efficiency’.

The contest over liberalisation has also resulted in the development of different models or concepts of social protection. This has provided the opportunity to compare safety net arrangements. The UK, for example, did not develop any kind of safety net per se although there was regulatory requirement to protect certain groups such as old age pensioners. The result was an extraordinary degree of segmentation. Only in recent years have the implications of this – a rise in the severity of fuel poverty – come under scrutiny. This has mainly consisted of a large increase in budget-funded transfers to the fuel poor for programs aimed predominately at energy efficiency. There has even been a recent recognition that PPM undermines such efforts. Some states in the US, in contrast, created POLR schemes that, while effectively segmenting customers, included measures such as substantially cheaper tariff rates. There are also a considerable number of programs aimed at energy efficiency or weatherisation as Americans call it. This model adopted
positive discrimination as its premise. Victoria also created a POLR scheme but, because it was based on negative discrimination, it is in effect a residual market. The Victorian government also has a preference for budget transfers in addressing equity concerns. These relate to means testing of income, and little of this assistance recognises or rectifies other causes of fuel poverty. Victoria’s CSOs program is therefore undermined by the discriminatory basis of supply which many eligible customers are required to accept.

Liberalisation and these models of social protection reveal different emphases on social, political and civil rights. In Victoria, the political struggle over reform saw three key ideological tendencies: market model (neo-liberal); universal service (social democratic), and a new consumerism or Third Way type model. The strengths and weaknesses of each of these can be assessed in the light of segmentation impacts. Not only does the market model not necessarily guarantee purported economic benefits, but redlining demonstrates how segmentation is counter-productive in relation to civil rights (equal opportunity, anti-discrimination). The new consumerism model supports market provision but relies very heavily on civil rights, in the form of complaints mechanisms and trade practices law, to shield consumers from market abuse. Yet complaints cannot unambiguously be made in relation to affordability. In practice it seems the right to avoid disconnection for incapacity to pay is not generally accepted. This suggests that civil rights in this context are extremely limited in the absence of concrete socio-economic entitlements. The universal service model specifically provides such entitlements, as well being supported by civil rights regarding basic consumer protection and equal opportunity. By definition, universal service does not permit segmentation. Universal service generally results from the exercise of political rights setting limits on economic behaviour and accordingly constrains individual choice in the civil sphere.

But it is the reaction to redlining in the US that offers insight into the nature of civil, political and social rights and markets. Redlining resulted in legislation such as the Community Reinvestment Act and the Fair Access to Insurance Requirements laws to protect the civil rights of minorities. In the wake of telecommunications and gas liberalisation (and the emergence of redlining in these industries), electricity advocates moved quickly to have anti-redlining provisions included in reform legislation. As part of this package, provisions were made to protect customers from discrimination on the basis of their income or income source. This was new. It made it clear that, in an era of pervasive credit scoring, poor
economic status could not be used as the basis for denial of service or discriminatory service. This is very much an anti-segmentation measure. It uses civil rights to give effect to a socio-economic entitlement. Many states also required cross-subsidisation of disadvantaged customers. The general effect of this set of civil rights is universal service. These civil rights are being bound with socio-economic entitlements because it requires both to prevent the discriminatory impacts of segmentation.

Implicit in this US reaction to market outcomes is a view that the purported actuarial basis for discrimination is not only unfair but based on wrongful assumptions. While I have not tested this (it is a large enough question to warrant a separate piece of research), my lengthy discussion of fuel poverty highlights how consumer disadvantage arises from the combination of ‘vulnerability factors’ and ‘supply features’ (the characteristics of a particular market). If products are tailored to vulnerable customers, perceived risks (such as default on payment) can be addressed. This is what Alwitt and Donley (1996) mean by rebalancing the act of exchange. Commodification, however, is the means by which market power can be asserted. Limits on market power are limits on commodification.

I also argued that compensatory welfare transfers are also subject to the impact of segmentation. Many have argued that lump sum tax transfers are preferable to cross-subsidies. This policy option fails to account for segmentation and market abuse, and indeed such a policy rewards firms who engage in market abuse. This is not to say that transfers aimed at improving income security are not warranted. Rather, there is a need to recognise that such transfers are only one part of a package of measures that are required to overcome the mismatch between customer needs and the supply features of essential services industries. Segmentation acts upon the perceived risks associated with inequality, therefore a package of measures needs to address both actual inequalities and perception of risk. The neo-liberal approach allows retailers to avoid responsibility for the social costs of energy supply. The market model therefore socialises these costs on the one hand (through income support) and privatises them on the other in that households assume the costs of rationing, disconnection, higher prices etc. As the section on fuel poverty showed, many households are not in a position to manage these risks. Tenants, for example, are hard-pressed to address building thermal efficiency. A crude response would suggest that retailers assume a greater share of the social risks because, if they did, the root causes of fuel poverty, or inequality, would become the focus of their attention. What is essential
here is the recognition that domestic consumption of electricity is ‘ordinary’ but that the relationship between supplier and customer is ‘extraordinary’ (Shove and Chappells n.d.). It is this relationship that permits the mitigation of fuel poverty or can be its cause. Utilities do not occupy a neutral position in regard to the distributive impacts of the supply/consumption relationship. As has been indicated, the market model is flawed because segmentation establishes that the goal of efficiency (welfare) is undermined by market abuse. Moreover, the compensatory social welfare measure – the CSO – cannot efficiently overcome this. The alternative is to pool all the risks together, as occurs with universal service, so that customers’ vulnerability factors and the industry’s supply features are addressed together, recognising the relationship between the two.

Finally, these lessons are not confined to utilities but are applicable across banking and finance, telecommunications, housing, health, insurance and education, and the first question which society needs to ask is whether access to essential services should be dependent on discriminatory premiums.
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APPENDIX: SURVEY INSTRUMENT

Dear Householder

This questionnaire is focused on the person whose name appears on the electricity account, and it is assumed that this is the person who will fill out the questionnaire. However, in many households someone other than the account holder may have responsibility for making the decisions about electricity. This person can fill out the questionnaire, but he/she will need to remember that the questions are about the account holder. It must also be about your main place of residence.

We request that you complete this questionnaire and return to the University in the prepaid envelope provided. If you have questions you may telephone me on 03 9214 5243 during business hours.

Thank you
Andrea Sharam
Institute for Social Research
Swinburne University

Q1. What is your postcode?

Q2. Does your name appear on the electricity bill? (please tick)
☐ Yes
☐ No

Q3. Which of the following best describes your household? (please tick)
☐ Live alone
☐ Live with partner
☐ Live with partner and children
☐ Live with children
☐ Live with parent(s)
☐ Live with friends/shared household
☐ Other, please describe

Q4. Please fill in for every person including children in your household

<table>
<thead>
<tr>
<th>Persons in the house</th>
<th>Age (years)</th>
<th>Gender (M/F)</th>
<th>Country of birth</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yourself</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 3</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 4</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 5</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 6</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 7</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 8</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 9</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Person 10</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Please list if there are others in your household

Q5. Is the dwelling you live in
☐ Rented from a private landlord
☐ Rented from the government
☐ Rented from a community organisation
☐ Owned outright by a member of your household
☐ Is being purchased by a member of your household
☐ Other, please state

Q6. Is the account holder’s gross annual income?
☐ Less than $10,000 per year (or less than $193 per week)
☐ $10,000 to $19,999 per year (or $194 to $384 per week)
☐ $20,000 to $29,999 per year (or $385 to $574 per week)
☐ $30,000 to $39,999 per year (or $575 to $769 per week)

(continued next page)
Q7. What is the account holder's income source(s)? You can choose more than one.
- Full time work
- Part time work
- Investments
- Self-funded retiree
- Aged pensioner
- Non-aged pensioner
- Unemployment benefits
- No income
- Supported by family
- Savings
- Other

Q8. Has your household claimed concessions on your electricity bill in the past year?
- Yes
- No
- Don't know

Q9. Do you think most people know who supplies them with electricity now that there have been so many changes?
- Yes
- No
- Don't know/not sure

Q10. Could you say who was the company that supplied you with electricity last year (2001)? (without looking at your bill)
- Don't know

Q11. If you also have mains gas, can you tell us which gas company supplied you last year (2001)?
- Don't know
- Do not have mains gas

Q12. In 2001, which method of payment did you typically use when paying your electricity account?
- In person
- By telephone
- Direct debit
- Mail
- Internet
- Maxi-kiosk
- Varies
- Other, please explain

Q13. In 2001 which of the following did you typically use to pay your electricity bill?
- Cash
- Cheque
- Credit card
- Debit card
- Direct debit
- Other Electronic Funds Transfer
- Varies

Q14. If you do not pay in person is this because?
- Other methods are more convenient
- The nearest place to pay in person is too far away
- Other methods help me budget better
- Other, please describe
Q15. Thinking about when you get your bill, do you check

<table>
<thead>
<tr>
<th>Always</th>
<th>Sometimes</th>
<th>Never</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

How much you consumed against same time last year
☐ ☐ ☐

The accuracy of the figures
☐ ☐ ☐

The amount of GST payable
☐ ☐ ☐

Q16. In terms of prices do you think that competition will mean that most electricity customers will be
☐ Better off
☐ Same
☐ Some better, some worse
☐ Worse off
☐ Don’t know

Q17. Do you think that for you, competition in electricity will lead to you paying
☐ Higher prices
☐ Higher price for Green power
☐ Same price
☐ Lower prices
☐ Don’t know

Q18. In terms of reliability of supply do you think that competition will mean that most electricity customers will be
☐ Better off
☐ Same
☐ Worse off
☐ Some better, some worse
☐ Don’t know

Q19. Do you think that for you, competition in electricity will result in
☐ More reliable supply
☐ Same reliability of supply
☐ Worse reliable supply
☐ Don’t know

Q20. In terms of customer service do you think that competition will mean that most electricity customers will be
☐ Better off
☐ Same
☐ Some better, some worse
☐ Worse off
☐ Don’t know

Q21. Do you think that for you, competition in electricity will mean
☐ Better customer service
☐ Same customer service
☐ Worse customer service
☐ Don’t know

Q22. How well would you describe your understanding of how electricity bills are calculated?
☐ Very good
☐ Fairly good
☐ Fair
☐ Poor
☐ Very poor

COULD YOU PLEASE NOW GET ONE OF YOUR BILLS FROM LAST YEAR - 2001
If you do not have a bill from 2001, GO TO Q25

Q23. Who was your electricity company in 2001?


Q24. Looking at your 2001 bill
(a) What was the pay-by date? ............
(b) How many days did it cover? ............ days
(c) How much was consumed? ............. kwh
Can’t find (a) (b) (c) on bill (please circle)

In the following section we are going to ask you about your experience of electricity supply since January 2002. This is when households were able to shop around for their electricity supplier for the first time.
There have been many changes to the electricity supply in recent years, and we'd like to find out what you understand of these changes.

Q25. Which of the following statements are true or false?

<table>
<thead>
<tr>
<th>Statement</th>
<th>True</th>
<th>False</th>
<th>Don't know/not sure</th>
</tr>
</thead>
<tbody>
<tr>
<td>I do not have to choose an electricity supplier, and can stay how I am</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I must eventually do something about choosing a supplier</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>If I do not choose within the next few months I will miss out on discounts</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>All electricity suppliers must supply me if I request it</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I can go back to my pre-competition tariff if I want</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The government does not regulate any prices</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q26. Since electricity competition began in January 2002 have you moved to another dwelling?
- Yes
- No, GO TO Q29

Q27. In moving after January 13th 2002 you would have had the following options. Please tick which option you chose
- Electricity was on but I have not entered into a contract with any supplier GO TO Q29
- I asked for the 'standing offer' tariff
- I accepted a market offer from the local retailer servicing my new residence GO TO Q36
- I accepted a market offer from my previous retailer GO TO Q36
- I accepted a market offer from a different competing supplier GO TO Q36
- Don't know, GO TO Q29

Q28. Thinking about why you chose the standing offer, was it because:
- Waiting to buy through a community buying group
- Waiting for gas competition
- Waiting for market to develop
- Put off needing to learn so much
- Afraid to change
- See not changing as a kind of protest against privatisation
- Wanted a fully regulated tariff/terms/conditions
- Other

Q29. Have you joined a community or other type of bulk buying scheme?
- Yes
- No, GO TO Q32

Q30. Why did you join a buying group? Was it because:
- Better price
- Thought it would provide better customer service
- Thought it would provide better reliability of supply
- Thought it would be more community and/or environmentally friendly
- To support fundraising
- Followed advice of family or friends
- Prefer to support community enterprise rather than pay private company
- Don't know

Q31. Is the community buying scheme currently supplying you?
- Yes, GO TO Q39
- No, GO TO Q62
- Don't know, GO TO Q62

Q32. Since electricity competition began in January 2002 have you changed to a contract with a new supplier?
- Yes, I am now with...............GO TO Q36
- No
Q33. Since electricity competition began in January 2002 have you moved to a new contract with your existing supplier?

☐ Yes, GO TO Q38
☐ No

Q34. If you have considered changing but have not done so, is this because

☐ Have not considered changing
☐ Simply have not taken next step, GO TO Q 62
☐ Unable to obtain sufficient information, GO TO Q 62
☐ Unable to compare offers properly GO TO Q62
☐ Put off by hassle of changing GO TO Q62
☐ What you saw made you think it was not worth changing GO TO Q62
☐ No supplier made you an offer GO TO Q62
☐ Other GO TO Q62

Q35. If you have not considered changing, is this because

☐ Did not know I could
☐ Satisfied with current arrangement
☐ Simply have not got around to it yet
☐ Waiting to join community buying group
☐ Waiting for gas competition
☐ Waiting for market to develop
☐ Put off needing to learn so much
☐ Afraid to change
☐ See not changing as a kind of protest against privatisation
☐ Other, please explain...................

GO TO Q62

Q36. Thinking about why you chose a new supplier, was it because

☐ Cheaper price
☐ Wanted better customer service
☐ Wanted better reliability of supply
☐ Followed advice of family or friends
☐ Take advantage of combined gas & electricity (dual fuel) offer
☐ Wanted Green power option
☐ Other, please explain....................

Q37. Was your experience of changing supplier?

☐ Smooth – no problems
☐ Difficulty with existing retailer
☐ Difficulty with new retailer

GO TO Q39

Q38. Did you change to a new contract with your current supplier because

☐ Your existing supplier made an offer involving a cheaper price, so you accepted without shopping around
☐ It was the best price available
☐ It was the best price/service package on offer
☐ You followed advice of family or friends
☐ You thought you had to sign quickly or miss out on benefits
☐ You took advantage of a combined electricity and gas offer (dual fuel offer)
☐ Other, please explain....................

About the terms and conditions of your new contract

Q39. When you received the new contract did you

☐ Read it carefully
☐ Skim it
☐ Ignore it, GO TO Q41

Q40. Did the contract confirm what you thought you had agreed to?

☐ Yes
☐ No
☐ Don’t know/not sure

Q41. Are there any fees if you end (terminate) the contract early?

☐ Yes
☐ No, GO TO Q43
☐ Don’t know/not sure, GO TO Q43

Q42. If there any fees for ending the contract early, can you tell me how much it is?

$...........
☐ Don’t know/not sure
Q43. What is the length of your contract?
- No specified term
- 1 year
- 2 years
- 3 years
- 4 or more years
- Don’t know/not sure

Q44. Was there a discount for signing a fixed term contract?
- Yes, how much $.........
- No, GO TO Q 46
- Don’t know/not sure, GO TO Q46

Q45. Did you accept the discount for signing a fixed term contract?
- Yes
- No
- Don’t know/not sure

Q46. Can the retailer terminate the contract early for reasons other than your non-payment?
- Yes
- No
- Don’t know/not sure

Q47. Was there a discount for agreeing to pay by direct debit?
- Yes, how much $.........
- No GO TO Q49
- Don’t know/not sure, GO TO Q49

Q48. Did you accept the discount for paying by direct debit?
- Yes
- No
- Don’t know/not sure

Q49. Can you tell me about any other benefits or discounts?
- Yes, please describe.........................
- No
- Don’t know/not sure

Q50. Are you required to pay a bond or security deposit?
- Yes
- No, GO TO Q52
- Don’t know/not sure, GO TO Q52

Q51. If you have paid a bond or security deposit, can you tell me how much it was? $...........?
- Don’t know/not sure

Q52. Are all parts of the price you accepted fixed for the term of the contract?
- Yes, GO TO Q55
- No
- Don’t know/not sure

Q53. Is only a part of price you accepted fixed for the term of the contract?
- Yes
- No
- Don’t know/not sure

Q54. Has the supplier reserved the right to vary any part of the price during the term of the contract?
- Yes
- No
- Don’t know/not sure

Q55. Since changing your supplier do you/will you pay your bill?
- In person
- By telephone
- Direct debit
- Mail
- Internet
- Maxi-kiosk
- Varies

Q56. Was signing the offer also consent to a credit reference check?
- Yes
- No
- Don’t know/not sure

ABOUT YOUR NEW BILLS

Q57. Have you received a bill since changing to a market contract?
- Yes
- No, GO TO Q62

PLEASE HAVE YOUR NEW BILL IN FRONT OF YOU (or any bill you have received since changing to the new contract)
Q58. How many days did it cover?

□ Does not say
□ Don't know

Q59. Was there a standing charge?
□ Yes, $........ per........ (QTR/MTH)
□ No
□ Don't know

Q60. Does your bill state how many kilowatts of electricity you consumed in total?
□ Yes, I consumed Kwh........
□ No
□ Don't know

Q61. Does your bill state the cost for different amounts of electricity used?
□ Yes, please describe (eg up to the first 1500kwh is 12 cents kwh and all electricity used after that is 15 cents)
□ No
□ Don't know

Q62. How many electricity retailers can you name? (please name)
1.................................................. 2..................................................
3.................................................. 4..................................................
5.................................................. 6..................................................
7.................................................. 8+..................................................

Q63. How many electricity retailers have contacted you?
0 1 2 3 4 5+
□ □ □ □ □ □

Q64. Have electricity companies approached you by
□ Door to door sales?
□ By phone sales
□ By mail
□ In shopping centre
□ Have not been approached
□ Other, please explain...........................

Q65. In comparing offers made by electricity retailers did you find it
□ Easy to compare
□ Fairly easy to compare
□ Very easy to compare
□ Fairly difficult to compare
□ Very difficult to compare
□ Did not compare

Q66. In your experience was obtaining an offer/contract
□ Very easy
□ Fairly easy
□ Easy
□ Difficult
□ Fairly difficult
□ Difficult
□ Very difficult
□ Did not

Q67. Have any suppliers declined to make you an offer/failed to follow through on their offer?
□ Yes, how many?........
□ No
□ Don't know
Q68. When the electricity retailer asked you for your details did they ask for any of the following:
☐ Your name
☐ Your address
☐ If you have been disconnected
☐ Permission to access your credit rating
☐ Number of people living in your home
☐ If you had air-conditioning
☐ If you have gas supply
☐ Your consumption
☐ Your employer
☐ Your entitlements to government concessions
☐ If you have ever been in arrears
☐ Who your pre-competition supplier was
☐ Whether you rent or not
☐ Don't know/can't remember
☐ Other, please describe..........................................

Q70. Are you aware that your bank can charge you fees if there is no money in your account when there is a direct debit from your account?
☐ Yes
☐ No

Q71. Have you been in arrears with your electricity retailer in the past 2 years?
☐ Yes
☐ No, GO TO Q74

Q72. Did you arrange a re-payment plan with your electricity retailer?
☐ Yes
☐ No, GO TO Q74

Q73. Could you afford to make the scheduled re-payments?
☐ Yes
☐ No
☐ Hoped so, but was unsure whether I could meet the commitment
☐ No but it was what I thought the retailer would agree to

Q74. Have you been disconnected by your electricity retailer in the past 2 years?
☐ Yes
☐ No

Q75. Have you had payment difficulties in the past?
☐ Yes
☐ No, GO TO Q77
Q76. Have payment difficulties been because?
☐ Insufficient income
☐ Unemployment
☐ Bills all coming together
☐ Poor health
☐ More people at home than before (e.g. new baby)
☐ Moved into new premises and found it more expensive for electricity
☐ Other, please explain........................................
...................................................................................

Q77. How many bedrooms does your home have?
☐ 0
☐ 1
☐ 2
☐ 3
☐ 4
☐ 5
☐ 6
☐ 7
☐ 8 or more

Q78. How many separate living areas does your home have? (exclude bedrooms, kitchen, bathroom, laundry)
☐ 0
☐ 1
☐ 2
☐ 3
☐ 4
☐ 5 or more

Q79. Would you say your home is
☐ very difficult to heat
☐ fairly difficult to heat
☐ normal
☐ fairly easy to heat
☐ very easy to heat

Q80. When it is cold how many rooms do you typically heat?
☐ 0
☐ 1
☐ 2
☐ 3
☐ 4
☐ 5 or more

Q81. When it is hot how many rooms would you typically cool?
☐ 0
☐ 1
☐ 2
☐ 3
☐ 4
☐ 5 or more

Q82. How many hours per week day would there typically be no one at home?
☐ under 1hr
☐ 1hr – 4hrs
☐ 4hr – 10hrs
☐ more than 10hrs

Q83. Do you have the following forms of heating in your home (please tick)

<table>
<thead>
<tr>
<th>Heating Type</th>
<th>Used</th>
<th>Frequent</th>
<th>Sometime</th>
<th>Never</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mains gas ducted heating</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Mains gas wall heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Bottled gas</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Built in electric space heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Electric portable bar heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Electric portable fan heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Portable Electric oil heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Attached bar heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Wood – open fire</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Wood – heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Electric Slab heater</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Reverse cycle air conditioning</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Built-in oil-fired</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
<tr>
<td>Hydronic</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
<td>☐</td>
</tr>
</tbody>
</table>

(Continues overleaf)
| Solar passive | □ | □ | □ |
| no heating | □ | □ | □ |
| other (describe) | □ | □ | □ |

Q84. What type of heating do you have for hot water
- Off-peak electric
- Electric day rate
- Gas – instantaneous (heat as you use)
- Gas – storage (tank)
- Bottled gas
- Solid wood
- Solar
- Solar/comboination
- Don’t know

Q85. How many of the following cooling appliances do you have?

<table>
<thead>
<tr>
<th>0</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4+</th>
</tr>
</thead>
<tbody>
<tr>
<td>Split system reverse cycle air-conditioner</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Refrigerative air-conditioning unit</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ducted evaporative air-conditioning</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ducted refrigerative air-conditioning unit</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Evaporative air cooler</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ceiling fans</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Portable fans</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Q86. If you have a combined cooling & heating air-conditioning unit, do you use it for?
- Both heating & cooling
- Heating only
- Heating mainly
- Cooling only
- Cooling mainly
- Never use either
- Do not have

Q87. Does your home have any of the following?
- Ceiling insulation
- Wall insulation
- Double glazing
- Draught proofing
- Heavy curtains
- Outside blinds
- Solar passive design
- Shading (trees or shade cloth)
- None of the above

Q88. If you heat your home less than you would like to, is it because you
- Have limited income
- Are environmentally conscious
- Find it too expensive
- Not applicable

Q89. Do you speak a language other than English at home?
- Yes, I speak.................................. at home
- No

Q90. Are you of Aboriginal or Torres Strait Islander origin?
- Yes
- No

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Thank you for completing this survey – your time and effort is greatly appreciated.
List of Publications

Sharam, A. (2003) 'Power failure: Why Victorian households are not plugging into electricity competition', *Journal of Australian Political Economy*, no. 52