

SUBMISSION TO THE COMMISSION FOR ENERGY REGULATION
ON
PROPOSALS ON A ROADMAP FOR DEREGULATION
FROM
THE IRISH HOTELS FEDERATION

29 January 2010

UNDERLYING PRINCIPLE SHOULD BE COMPETITIVENESS ENHANCEMENT

The Irish Hotels Federation (IHF) welcomes the publication of the Proposals on a Roadmap for Deregulation by the Commission for Energy Regulation (CER) and urges that the underlying principle attached to the proposals should be the reduction of energy prices to enhance competitiveness. In its October Statement on Energy, the National Competitiveness Council emphasised that the reduction of energy costs is essential for competitiveness. It noted that...”electricity prices for business in Ireland are significantly out of line with other EU countries. Ireland has the fourth highest industrial electricity price of the EU-27 and is 35.5% more expensive than the Eurozone average. Recent reductions in electricity prices are a positive development but are not sufficient to improve Ireland’s competitiveness” (press release 6/10/10 NCC accompanying the Statement on Energy).

As is stated by CER and acknowledged by the NCC, a number of factors which determine Ireland’s energy costs are outside our control such as the price of imported fuels. However, IHF agrees with the NCC that a number of significant influences are within domestic control.

Regulation needs to bring non-fuel controllable domestic costs into line with competitor economies. Capacity payments could be further reduced. Price support mechanisms for renewable energy should be designed to minimise the adverse competitiveness impact. The carbon windfall should be used to lower electricity prices up to 2012.

ECONOMIC CRISIS

The CER’s regulatory approach should reflect and respond to the serious economic crisis that the hotel industry and the economy in general faces. Economic activity declined sharply in 2009 following an earlier decline in 2008. Government projections indicate a further but smaller decline in economic activity in 2010. Any prospect of significant growth in the coming years depends on export growth which in turn depends substantially on current and future foreign direct investment. Cost competitiveness is an important determinant of export performance. Energy prices influence the foreign investment location decision. Throughout the economy cost competitiveness has been eroded and as already noted, electricity prices are relatively high. There is an urgent need to reduce the overall cost base of the economy if substantial economic recovery is to be a possibility. This includes electricity prices. Because of this, IHF recommends that the underlying principle driving the redesign of regulation should be the reduction of energy prices. In addition the reduction in electricity prices should be implemented as soon as possible to improve the very weak position of the enterprise sector. Specifically, the dominant operator should be allowed to engage in price competition.

COMPETITIVE MARKETS

IHF agrees with the CER that competition in the retail electricity market has increased especially in recent times. However, there is still only a small number of suppliers operating in what is an oligopolistic market with all the possibilities of reduced price

competition which can arise in such markets. Regulation will still be necessary in the “competitive” electricity market to ensure prices remain as low as possible as well as the normal functioning of competition law. Consequently, the issue is mainly one of changed regulation rather than the complete removal of regulation.

IHF COMMENTS ON SPECIFIC PROPOSALS

As requested by CER IHF comments are presented relative to the individual issues and questions posed in the Proposals document. The question and proposal numbers are as appear in the CER document.

Q1

IHF welcomes the proposal to review the market and to define a roadmap for deregulation of the retail market. This is a timely initiative. It is no longer appropriate given the weak state of the economy and the pricing practices of new entrants to restrain the dominant supplier from competing on price.

PROPOSAL 1

Q2

IHF agrees with the proposal to define four individual markets for the supply of retail electricity. It is desirable to separately identify large users, medium business users and small business users in addition to domestic consumers. These different classifications will facilitate an effective monitoring and assessment of electricity prices to different types of users.

Q3

IHF considers that public lighting should be seen as a separate market because of the lack of competition and its price should be subject to controls in the new regulatory regime to ensure that excessive profits are not earned which would increase costs to local authorities which would in turn be partly or fully passed on to the hotel and other enterprise sectors.

Q4

IHF agrees that the domestic sector should be treated as one market sector until and if evidence emerges that suppliers are competing only in specific sub sectors of the domestic sector. This does not appear to be the case at present.

PROPOSAL 2

Q5

IHF agrees with the inclusion of the three indicators in assessing the level of competition but would add a profits indicator to ensure that the small number of competitors does not result in industry level and supplier level pure profits. In the absence of a normal profit indicator the three proposed indicators will not necessarily lead to the lowest prices consistent with sustainability.

Q6

As noted above, IHF is concerned with the phrase “removal of regulation” in the individual markets. At best there will be small numbers of operators in effectively oligopolistic markets. It will still be necessary to ensure that real price competition based on the lowest costs of production results. This will require some continuing regulation even though the basic regulatory control of the incumbent price is removed. At present, price regulation has been largely based on setting levels that acted as a floor for the incumbent dominant supplier to prevent entry limiting price practices. In the future, price regulation will hopefully involve setting maximum prices, which will be lower than at present, that can be charged by suppliers.

Q7

IHF agrees that the brand ESB may present a competitive challenge to independent suppliers although the large market shares won by independents in the domestic sector would not provide evidence of that. However, there is some confusion through the use of the ESB brand in different operations of the market. A solution to this would be to seek a change in the name of incumbent supplier to put it on a par with independent suppliers. This would involve a full dismantling of the ESB group.

PROPOSAL 3

Q8

IHF considers that the measures of competition which should apply in specific markets are acceptable. However, we have a problem with the CER approach. When these measures are operational regulatory price controls will be removed. Effectively, this means that the price of the incumbent will no longer be kept high. Even if the required competition is not attained the maintenance of unnecessarily high prices should be ended. The incumbent should be allowed price at a lower level consistent with what would ideally occur with competition. In practice it is likely that the enterprise sector of relevance to the IHF will display the required characteristics and so the possibility of retaining high minimum prices will not arise.

PROPOSAL 4

Q9

IHF agrees with the proposal to review markets twice a year but we would reemphasise the point at Q8 above that even if a market does not meet the competition requirements the aim should be have as low an electricity price as possible. This will require the CER setting a competition level price rather than the current approach of setting a price at a sufficiently high level which might attract competition. We agree with the CER point made on page 66 that “the existence of price regulation is seen as a constraint to the development of full competition”. Even if actual competition is not present in specific markets the aim of regulation must be to achieve the competition level price as quickly as possible in light of the NCC recommendations and in light of the serious economic problems.

PROPOSALS 5 AND 6

Q10

This problem arises if both regulated (high price) and unregulated (low price) are both served by ESB PES where one market segment is competitive and the other is not. There would be little or no problem if the price of the regulated segment was brought down to the unregulated level allowing for the differences in the types of markets. The problem seems to be based on the continuation of a regulated price which is high compared to the competitive price which is lower. There is no need for the regulated price to be kept high as argued above.

Q11

IHF agrees in principle with the view that regulatory burdens can not be placed on ESB PES if it is to compete on an even basis with other suppliers. However, some of these functions such as non-discrimination, supplier of last resort and universal service obligation will have to be continued. The Proposals document states that these will be reviewed. These can be maintained by imposing like burdens on other suppliers, putting the functions out to tender which may or may not generate interest or leaving them with ESB PES for an agreed fee. The Proposals document does not specify how these functions would be met or if they would be met in the new regulatory regime.

Q12

IHF agrees with the CER that there is a need for regular monitoring to ensure that competitive thresholds are maintained by ESB PES and ESBIE. As identified above IHF does not think competition law will be sufficient in what will be a very specific and oligopolistic market. There are possibly going to be a need for price caps based on best international cost practice. We emphasise again that the drive must be to ensure that electricity prices are internationally competitive whether through competition price controls in the absence of competition.

PROPOSAL 7

Q13

This is a vague proposal. It seems to imply that after price regulation which CER defines as price controls there may be price increases which could cause problems for vulnerable domestic customers. CER suggests that suppliers may be required to offer tariffs to these groups as defined by the Commission. IHF believes that this is inappropriate because specific social policy issues should be dealt with by social policy measures rather than indirectly by commercial suppliers of electricity. However problems of access or geographic isolation are different as they relate to the principle of universal access to electricity. In any event if the CER anticipates that deregulation will result in higher prices it should not be pursuing such a strategy. IHF expects that the main impact of deregulation will be to lower prices as it frees the incumbent to compete on price. IHF accepts that all suppliers should be expected to operate on a good customer charter basis which should be designed by CER. IHF is not in favour of Proposal 7.

Q14

CER sought comments on the interim work programme which will develop the current regulatory framework until the proposed roadmap has been implemented. IHF strongly urges that this should be guided by the October NCC Statement on Energy. Electricity costs in Ireland are high by international standards. There is a need to substantially reduce the cost base of the economy including electricity costs. The immediate concern

of the CER should be to reduce electricity costs. In particular it should pay more attention to driving the domestic costs associated with electricity down to international best practice. IHF recognises the trade off which exists between the maintenance of a specific price level which supports entry and which might eventually result in long lasting lower prices and a lower price level which supports competitiveness and is less attractive to potential entrants. At the present time we are in a very serious economic crisis. Every measure which helps cost competitiveness is worthwhile and is essential. Pending the new roadmap IHF urges that the price control on the dominant supplier should be removed and an immediate price reduction should be implemented. In addition, any other non essential regulatory burdens which increase cost should be removed at least temporarily. Where vertical integration practices in the ESB group result in cost reductions they should be allowed.

The emphasis should be on immediate cost reduction.

SUMMARY

IHF welcomes the CER Proposals. In particular IHF believes that ESB PES should be allowed compete now on price with the new suppliers. In addition, pending the implementation of the new roadmap, non-essential regulatory burdens which increase cost should be removed. There should be a sense of urgency in seeking ways and means to quickly reduce electricity prices. As identified in the October NCC Statement on Energy, Irish electricity prices are high by EU standards, the prices must be reduced and there are ways in which this can be done through reduction in the domestic element of the cost of electricity.