

# Minister's Rule Change Preventing discounts on inflated energy rates

Submission by Dr Martin Gill

Consumers looking for a simple way to compare increasingly complex retail tariffs are relying on 'discounts'. Unfortunately retailer 'discounts' cannot be meaningfully compared. The result is discounts are proving fertile ground for retailers to mislead consumers into making poor energy choices.

## Summary of Submission

There are relatively simple changes the Australian Energy Market Commission (AEMC) could make to address the issue of misleading retailer discounts.

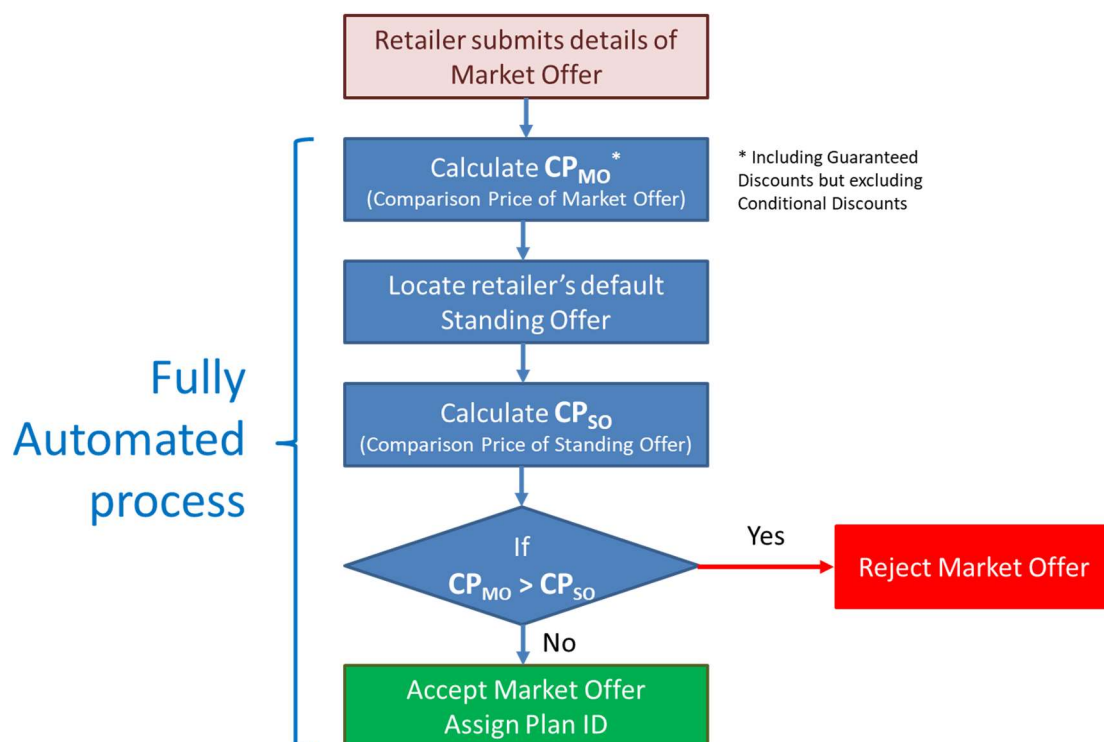
Under existing rules retailers must submit details of all their retail tariffs to the Australian Energy Regulator (AER). The AER then assigns each retail tariff a unique identifier called the 'Plan ID'. In the near future retailers will be required to include the Plan ID in all correspondence with consumers. Hence if the AER does not assign the unique Plan ID, a retailer is unable to offer the tariff to consumers.

This suggests the desirable consumer outcome is achieved by adding a simple check before any new retailer tariff is allocated a Plan ID:

- Retailer submits a new retail tariff to the AER
- The AER "checks the validity" of the new retail tariff (including offered discounts)
  - If the AER analysis finds the tariff "valid" they assign a Plan ID
  - If the AER analysis find the tariff "invalid" they notify the retailer

In the near future all retail tariffs will also provide an estimated annual cost, the so called 'Comparison Price'. This submission suggests the Comparison Price provides a solid and simple foundation for "checks of validity".

A flow chart showing all the steps involved the above proposal is shown below:



This submission compares the numerous advantages of the above solution to the proposed rule change.

## Background to the Minister's rule change request

During 2017 consumer concerns about rapidly rising energy prices forced the Prime Minister to hold a number of meetings with energy retailers. A key focus of the meetings was the issue of energy affordability.

An issue of significant concern was retailer use of misleading discounts. The specific concern was:

Energy offers with large percentage discounts do not always lead to the lowest bills for consumers.

The best way to demonstrate the problem uses an example.

	Retailer A	Retailer B
<b>Discount</b>	<b>40% (on usage)</b>	<b>10% (total bill)</b>
Daily Supply Charge	\$0.89	\$0.90
General Usage (per kWh)	\$0.70	\$0.35
Comparison Price (with discount)	\$2778	\$2135

This is the best tariff even though it offers a lower discount

Comparison Price shows consumers are \$643 better off on this tariff

In the above example one retailer offers a 40% discount with another only offering 10%. Calculating the Comparison Price for the two retailers shows the average consumer is \$643 better off choosing the retailer offering the smaller discount.

The Federal Energy Minister wants to address the problem by amending the National Energy Rules to ensure retailer offered discounts result in lower electricity prices.

The Minister cannot make the change himself, instead he must ask the Australian Energy Market Commission (AEMC) to amend their rules. He has submitted a rule change request to start this process.

### What is a discount?

Retailers across all markets use promises of discounts to attract consumers. Retailers in the energy market are no different. So why are energy discounts seen as a problem?

Many consumers continue to assume energy prices are regulated. The cause of the (incorrect) assumption is the lack of consumer education accompanying the introduction of the contestable energy market. *Assuming* energy prices are regulated allows discounts to be used to compare retail offers, with the largest discount representing the best deal.

**Unfortunately in the energy market promised discounts are almost totally meaningless.**

In the contestable retail energy market prices are **not** regulated. Energy retailers are free to set the multiple different charges used to calculate consumer energy bills including the daily supply charge and all usage charges. They can then choose to offer a discount. The discount can be conditional (typically for paying on time via direct debit) and can be applied to the whole bill or just to specific parts of the bill.

## Retailer discounts cannot be meaningfully compared

### ACCC action on misleading discounts

It would appear regulation already exists to address this issue. The Australian Competition and Consumer Commission (ACCC) has taken action against retailers falsely advertising discounts.

In 2016 the ACCC imposed a financial penalty on a leading electronics supplier. The penalty was imposed after the ACCC found "reasonable grounds to believe the retailer had made false or misleading representation about discounted prices".

The specific case involved the retailer advertising discounts of 20% on a range of their products. The ACCC found immediately before the advertised discount came into effect the retailer had increased the prices. The result was rather than receiving a discount of 20% the actual discount was only 9%.

Interestingly the ACCC has not taken action against energy retailers despite analysis suggesting they are using exactly the same misleading representations about discounts. The question is “Why not?”

#### *Proving discounts are misleading*

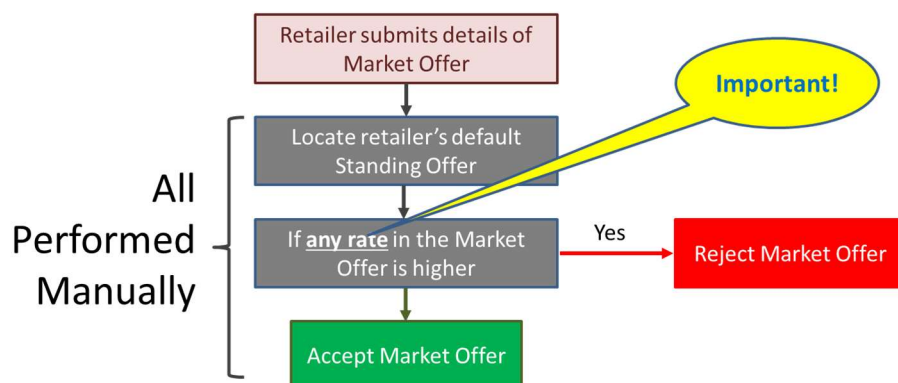
The ACCC’s prosecution of the electronics retailer relied on analysis showing the electronics retailer had inflated prices before offering the discount. Energy retailers are allowed to set their own energy prices. The result is the ACCC cannot apply similar analysis to retail energy tariffs. Without this analysis the ACCC is unable to prove misleading conduct and there is no prospect for a successful prosecution.

#### **The need for a baseline (Allowing retailer discounts to be compared)**

One of the first requirements is the need to develop a methodology enabling meaningful analysis of retailer discounts. The Minister’s proposed rule change suggested using the retailer’s standing offer as the baseline for the analysis. The Minister suggested:

Prohibiting a retailer applying a discount to a market retail contract if any of the rates in the contract are higher than the retailer’s equivalent standing offer rates.

A flow chart of the Minister’s rule change looks like:



Attention is drawn to the statement if ANY RATE in the Market Offer is higher, then the tariff is rejected.

### Why is the standing offer important?

Any consumer using the Government's tariff comparison site, Energy Made Easy, will find the site lists hundreds of different tariffs. Can **ONE** of these tariffs be selected as the baseline for the comparison?



There is one unique Standing Offer for each household

### The Standing Offer

All existing premises have an assigned energy retailer. This is typically the last retailer who sold energy to the previous occupants (or for new premises it is the default retailer). When a new consumer moves in they are automatically placed on the assigned energy retailer's standing offer. The retailer's standing offer provides a default contract between the consumer and the energy retailer.

The important point is there is one unique standing offer for each premise.

### What is a market offer?

Energy retailers are free to make market offers to consumers. Unlike standing offers consumers must agree to accept the terms outlined in the 'market offer'. Most of the hundreds of tariffs offered to consumers are market offers.

Since consumers must agree to accept the market offer retailers make them attractive with discounts, sign on bonuses, inclusions (e.g. movie tickets), free usage days, etc.

### Analysis using the Standing Offer

The Minister's rule change request suggests comparing rates in the standing offer to those in the market offer. If [any of the rates in the](#) market offer are higher than the standing offer then the potential exists for the market offer to increase prices. His rule change proposes banning these undesirable market offers. While this delivers the required outcome, it is probably too restrictive.

### Example: Special Offer to owners of Plug In Electric Vehicles

One retailer has offered a special tariff to owners of Plug In Electric Vehicles. This residential only tariff provides unlimited charging of electric vehicles for a fixed fee of \$1 per day.

#### Unlimited charging for just \$1 a day

Charge your electric vehicle for just \$1 a day – anytime, any day of the week – on our 12-month energy plan. This way you'll always have the certainty of knowing how much it will cost you to charge your car.

A theoretical comparison of this tariff against the standing offer is shown in the following table:

	Standing Offer	Market Offer
Daily Supply Charge	90c/day	90c/day
General Usage	30c/kWh	30c/kWh
Separately Metered Usage	0c/day (not stated)	\$1/day (as advertised)
Daily Supply Charge		
Separately Metered Usage	15c/kWh	Free (as advertised)
Comparison Price	<b>\$3176</b>	<b>\$2446</b>

The Separately Metered Usage Daily Supply Charge is higher than the standing offer so the Minister's rule change would not allow this tariff

Comparison Price shows consumers are \$730 better off

The standing offer does not state the 'Separately Metered Usage Daily Supply Charge' however it can correctly be *assumed* to be 0c/day. The Market Offer fails the Minister's proposed rule since it contains a rate which is higher than the standing offer. This is unfortunate because this tariff is potentially beneficial for consumers with Plug In Electric Vehicles.

The table shows a Comparison Rate as included in Version 5 of the AER's Retail Pricing Information Guidelines (RPIG). This Comparison Rate suggests consumers potentially save \$730 a year on the market offer (using the typical daily average of 16kWh/day and assuming the Electric Vehicle contributes a further 20kWh/day).

The Minister has tried to allow the tariff by suggesting the market offer must be compared to the "[retailer's equivalent standing offer](#)". It is extremely unlikely the retailer will make an Electric Vehicle standing offer. As such interpretation of "equivalent" is required and at that point the rule fails. Retailers will carefully craft their market offers so none are considered to be equivalent to their standing offers allowing them to continue offering large discounts on inflated energy rates.

This is why this submission avoids assessments of "equivalence" by using the Comparison Price as the basis for checking retailer tariffs.

#### Automated checking of retailer market offers

The proposed solution can be implemented far more cost effectively than the Minister's original and AEMC's reworded rules, since both require manual processing. This manual processing must first find the retailer's standing offer, manually evaluate equivalence and carefully compare the rates in the two offers.

Retailers submitting new tariffs must wait for this manual comparison to be performed (the new rules are pointless if they are not enforced).

Under the RPIG the Comparison Price is automatically calculated by the AER when a new tariff is submitted. This submission proposes using existing processes to implement a simple validity check of future retailer tariffs.

#### Right to appeal

The proposal outlined in this submission is intended to allow retailers to experiment with innovative tariffs while still protecting consumers from offers resulting in higher energy prices.

It is acknowledged automated processing using the Comparison Price for the market offer against the standing offer may reject new innovative tariffs of benefit to consumers. Rather than attempt to implement a "perfect" process in the rapidly developing energy market this submission recommends retailers be given the right to appeal.

For the appeals process retailers are required to present their analysis showing how consumers actually benefit on the new tariff. If the retailer's evidence justifies assigning a Plan ID then one is assigned and the tariff is added to the AER's database of retail tariffs.

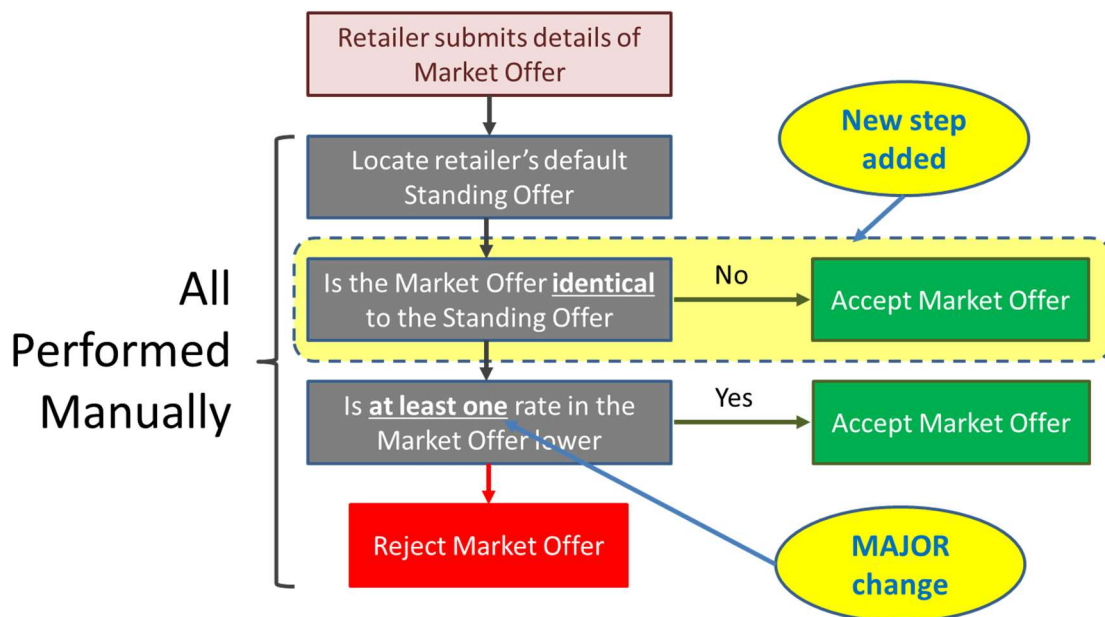
While appeals would require manual evaluation of the retailer evidence it is suggested the process should not be onus. The evaluation involves a similar level of manual processing detailed in both the Minister's original rule change and the AEMC's proposed rule change. Since appeals are only going to be used occasionally, it still indicates the suggested scheme is less expensive than the proposed rules.

Note: The retailer analysis in the appeals process also provides the AER with valuable feedback. This analysis shows where the Comparison Price could be improved. Since the Comparison Price is a new concept it is likely refinement will be required. This appeals process provides retailers with incentives to help the AER improve Comparison Prices.

### The AEMC daft [not sic] rule change

The AEMC have ensured their implementation of the final rule fails to deliver the requested consumer benefits. This outcome is assured by subtle but significant reworking of the Minister's original rule change request.

A flow chart of the AEMC's rewording of the Minister's proposed rule change is shown below:



The first change removes the sensible restriction imposed in the Minister's rule change if "any of the rates in the contract are higher". The AEMC have changed this to allow retailers to list any tariff, provided at least one rate is lower than the standing offer. For example the AEMC rules allow a retailer to double all the usage rates *provided* they decrease the daily charge by 0.001c/day.

	Standing Offer	Market Offer
Daily Supply Charge	90c	89.999c
General Usage	30c	60c
Comparison Price	\$2081	\$3832

Daily Supply Charge is less than the standing offer so AEMC rules accept this offer

Comparison Price shows consumers are \$1751 worse off!

No analysis is required to show consumers would be significantly worse off on this tariff. The example highlights how the AEMC's apparently subtle rewording ensures their rule completely fails to capture the Minister's requirements.

The second reworking places far too much emphasis on "equivalent". The AEMC rule change accepts any tariff provided it includes any difference from the standing offer. For example a retailer can double all the usage rates in a time of use market offer provided they trivially adjust the times, for example increasing the peak period from 8pm to 8:05pm.



	Standing Offer	Market Offer
Daily Supply Charge	90c	180c
Peak	42c (2pm to 8pm)	84c (2pm to 8:05pm) ←
Off Peak (all other times)	21c	42c
<b>Comparison Price</b>	<b>\$1862</b>	<b>\$3723</b>

Retailer has doubled all rates but because the Market Offer uses trivially different times the AEMC rules accept this offer

**Comparison Price shows consumers are \$1862 worse off!**

The above example makes a trivial change to the market offer so it is no longer identical to the standing offer. The AEMC's proposed rule would accept this offer despite clearly failing the Minister's requirements.

The above issues are avoided using the Comparison Price as detailed in the AER's RPIG. If the Comparison Price for the market offer is higher than the standing offer then the AER refuses to assign a Plan ID and the retailer is unable to offer the tariff. No need for complex definitions of "any rate" or "equivalent". The proposed appeals process allows retailers to present their analysis showing how consumers benefit from tariffs which the simple automated processing flag as inappropriate.

The AEMC's decision to carefully reword the Minister's rule change to allow these tariffs is predictable. The AEMC created the contestable energy market and counts the number of different retail tariffs in measurements of the success of their market. They are not going to introduce rules limiting the number of tariffs offered to consumers, even when these tariffs are clearly not in the long term interest of consumers.

#### **Wait there's more! – "The first 20 customers will also get a free set of steak knives"**

Retailers are increasingly using enticements intended to encourage consumers to accept their 'market offers'. These enticements have nothing to do with "energy", for example free movie tickets, discount books, etc.

The AEMC have decided any market offer which includes enticements is excluded from the rule change. They have come to this decision since it is not "equivalent". For example the AEMC allows retailers to double all the rates in the standing offer *provided* they also offer a free "set of steak knives". Clearly such an offer does not deliver the outcome requested by the Minister.

Weak arguments can be presented to support the AEMC's position.

Consider a near future market offer which includes the consumer giving the retailer control of their appliances. Retailers stand to profit from controlling consumer appliances (by reducing demand when the wholesale price of electricity is high). Should this market offer be compared to the standing offer? Absolutely!

Where the AEMC ran into problems was how to compare the rates in the market offer to those in the standing offer. These market offers contain additional terms and rates, not defined in the standing offer. Rather than attempt to solve the problem they simply ignored it providing retailers another means of circumventing the outcome the rule change is supposed to be addressing.

The problem of comparing rates listed in market offers and standing offers disappears when using the Comparison Price.

**The Comparison Price turns all the rates into a single value and that single value is easily compared.**

The suggested appeals process allows retailers to present evidence showing the value of enticements. This value can be subtracted from the market offer's Comparison Price and then compared directly to the standing offer. If it is now lower the AER assign a Plan ID and the retailer is free to offer the tariff.

## The AEMC Rule Making Test

Every rule change the AEMC makes is SUPPOSED to be made in the long term interest of consumers. The Minister has asked them to review current retailer practices affecting the Price consumers pay for electricity.



The Minister's rule change request puts the AEMC in a very difficult position. If they proceed with the current rule change they will for the first time be acknowledging retail competition in the energy market they have created is not in the long term interests of consumers.

Generously it is suggested to avoid this admission the AEMC has adjusted the wording of the Minister's proposed rule change to ensure it fails to address the misleading behaviour of retailers. How the Minister will view their failure to deliver the requested outcome will be interesting!

## Version 5 of the Retail Pricing Information Guidelines (RPIG)

### "Controlled Load"

While the AEMC have suggested adding a civil penalty to retailer breaches of the AER's new RPIG it is suggested they have not fully explored how the RPIG could be used to address the issue raised by the Minister.

Throughout the workshop they provided multiple examples of "Controlled Load" tariffs. Referring to Table 2- Language Requirements in Version 5 of the RPIG. The term "Controlled Load" is now a prohibited term!

**Table 2 – Language requirements**

Prohibited terms	Required terms
Controlled load	Separately metered usage*

It is disappointing the AEMC have not fully explored the positive consumer outcomes delivered by the AER's RPIG. If they had they might also have found the Comparison Price provided a far more robust means of delivering the Minister's requested outcome at a far lower price than their daft [not sic] rule change.

### More work on the Retail Pricing Information Guidelines (RPIG)

The draft of Version 5 of the Retail Pricing Information Guidelines (RPIG) has been circulated for consultation.

In Dr Gill's response he noted preventing retailers offering undesirable tariffs relies on the AER tightening the wording. Clause 95 of the draft states

Retailers have always "been able to" refer to the plan ID but choose not to

95. Retailers must be able to make reference to the plan ID in communication with customers.



The draft version of the RPIG is not worded strongly enough. Specifically retailers have always been 'able to' refer to the Plan ID, however when it is not in their interest they choose not to do so. It is suggested the clause be amended to ensure the intended outcome is delivered. This is achieved by deleting the unnecessary ('weasel') words:

### **95. Retailers must make reference to the plan ID in all communications with customers.**

Dr Gill's submission to the AER consultation on Version 5 of the RPIG is available from

<http://www.drmartingill.com.au/wp-content/uploads/2018/04/Draft-Version-5-AER-retail-pricing-guidelines-Submission-by-Dr-Martin-Gill.pdf>.

## **Conclusion**

The Federal Energy Minister has asked the Australian Energy Market Commission (AEMC) to limit retailers using large percentage discounts to mislead consumers into making poor energy choices.

This submission has proposed a simple approach delivering the outcome requested by the Minister. The proposal utilises processes outlined in the Australian Energy Regulator's (AER's) Retail Pricing Information Guidelines (RPIG). The Comparison Price is used to check any new tariff. If the check fails the AER does not assign the tariff its unique Plan ID. Without the Plan ID retailers cannot offer the tariff to consumers.

The AEMC's response to the Minister's request is disappointingly predictable. They have chosen to carefully reword the Minister's rule change ensuring it totally fails to address the issue.

## **Citation**

Please accurately attribute all quotes and references to this submission. It would be appreciated if references also included the author's website [drmartingill.com.au](http://www.drmartingill.com.au).

## **Comments or Questions?**

The author is happy to receive comments or questions about this submission. He can be contacted at [martin@drmartingill.com.au](mailto:martin@drmartingill.com.au)

## **About Dr Martin Gill**

Dr Martin Gill is an independent consultant specialising in the provision of consumer advice based on a deep understanding of the Australian energy industry and strong analytical skills. As a consultant he has prepared advice for consumer advocates, government regulators, electricity distributors, electricity retailers, asset operators and equipment vendors.

He currently represents the interests of consumers on a range of Standards Australia committees including metering, renewable power systems, battery storage, electric vehicles and demand management.

Dr Gill is a metering expert. During the National Smart Metering Program he facilitated the development of a specification for Australian smart meters. Innovative metering products developed by his teams have been externally recognised with the Green Globe Award, NSW Government's Premier's Award and Best New Product by the Australian Electrical and Electronics Manufacturers Association.