



# CONSUMERS SA

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To whom it may concern,

The Consumers SA is pleased to be able to provide this submission to the *National Energy Retail Amendment (Retailer price variation in market retail contracts) Rule 2014* Consultation. We note that it is the first proposed rule change since the rules commenced in July 2012.

Consumers SA is an independent consumer advocacy body representing the interests of South Australian Consumers.

The Consumer Action Law Centre (CALC) and Consumer Utilities Advocacy Centre (CUAC) proposed a new rule 46A relating to fixed period market contracts. The proposed rule is:

***46A Fixed period market retail contract***

- 1. This rule applies to market retail contracts with a fixed period.*
- 2. For such market retail contracts, all tariffs and charges payable by the customer are not to change for the duration of the fixed term.*
- 3. For avoidance of doubt, for contracts subject to this rule, the retailer is not able to vary the tariffs and charges that affect the consumer.*

Consumers SA strongly supports the proposed rule change as it would be of net benefit to consumers in the longer term. It will improve innovation amongst retailers in managing energy market risks and will provide greater clarity and transparency to consumers in assessing contracts. These lead to a long term positive effect on pricing and a greater level of consumer confidence in engaging with the market.

On the following pages we have detailed our reasoning further and answered the AEMC consultation questions in more detail.

Yours sincerely

Tony Moore  
Secretary

# Consumers SA response to consultation questions

## **Question 1      NERO test**

Are there any other matters that the AEMC should consider in its assessment of the NERO test?

The Commission, in its consultation paper, are considering applying the four following criteria to the NERO test:

- Efficient allocation of costs and risks;
- Effective consumer engagement and participation;
- Provision of a range of products and services consumers value; and
- Independent rivalry and competition between retailers

## **Question 2      Consumer protections test**

a) Is the scope of the consumer protections that the Commission intends to consider appropriate for this rule change request?

b) Should the Commission consider any other factors in assessing the rule change request against the consumer protections test under the Retail Law?

No comment

## **Question 3      Risk allocation in market retail contracts**

Do the current rules result in an inefficient allocation of risks between retailers and consumers in retail energy markets?

It is the role of retailers in the energy market to manage risk on behalf of consumers.

Major cost pressures for retailers are:

- Wholesale pricing
- Retailing costs
- Network charges
- Government taxes and policies

Both wholesale and retail costs should be reasonably easy for retailers to manage. Network charges vary with less predictability, albeit on a five year basis. Government taxes and policies can be a cause of uncertainty, however the development of government regulation should be done in such a manner as to not be unpredictably disruptive with business. Where there is potential for disruption then policies should be implemented with sufficient lead times to mitigate this risk. Further, should the rule be changed to require retail market contracts to include fixed pricing, then this should be taken into consideration in the implementation of both variations of network charges and government policy.

The market is not delivering genuine fixed price choices to consumers. The reasons for this are twofold. Firstly, rules do not require retailers to offer such contracts, and secondly, the Consumers SA would contend that the ambiguity in the terminology used for contracts and the resulting misunderstanding amongst consumers (ie consumers often think that they are getting a fixed price contract when they are in fact not) means that demand for fixed term contracts is somewhat hidden.

**Question 4      Risk premiums**

- a) If the proposed rule is made, would risk premiums be built into fixed period contracts?
- b) How significant would these risk premiums be and would these risk premiums create a permanent increase in the price of fixed period contracts?

As detailed in the AEMC paper, true fixed price contracts attract an additional risk premium. AEMC research suggests that this is in the order of 8%, however Consumers SA is very sceptical as to this being an accurate indication of the true difference in risk between fixed and variable pricing contracts. The limited number of fixed price contracts on offer restricts the competitive pressures on retailers to deliver competitive fixed price contracts.

Given the retailers' heavy reliance on variable price contracts there is no real pressure on retailers to be innovative in the techniques that they use to manage risk within the market.

**Question 5      Transparency and market retail contracts**

- a) When entering fixed period contracts, do some consumers believe that the prices will be fully fixed when in fact they are not? If so, what proportion of consumers are likely to fall into this category?
- b) Are there some consumers that are not aware that fixed period contracts with fully fixed prices are available on the market? If so, what proportion of consumers are likely to fall into this category?

While we do not have statistics on the proportion of consumers that interpret fixed period contracts as also being fixed price, anecdotal evidence would suggest that it is quite high.

In South Australia we are aware of only two retailers that offer fixed price contracts. This is out of eight retailers operating within the state. Given the marketing focus of retailers tends to be based on price and the premium price charged on the fixed contracts, it is not unreasonable to consider that a large proportion of consumers would not be aware of these contracts. Misunderstanding of the pricing nature of fixed period contracts would limit consumer investigation into alternatives that they think they already have.

The AEMC paper talks about the mortgage market as one in which consumers understand the variable nature of pricing. What this market does suggest is that consumers have a strong understanding of the terms 'fixed' and 'variable'. Most mortgage operators will offer both fixed and variable products, hence allowing meaningful comparison by consumers with an easy understanding that the variable pricing option comes with additional risks. In the energy retail market there is a distinct lack of fixed price contracts available and a plethora of variable price contracts marketed with the confusing terminology as fixed term contracts.

**Question 6      Barriers to consumer participation and engagement**

- a) Does the ability for retailers to vary prices lead to a perception for consumers that changing to a new retailer or contract would waste search costs?
- b) To what extent might the existence of exit fees and other transaction costs affect consumer behaviour after a price variation in a fixed period of a *market retail contract*?

Both exit costs and search costs are significant deterrents to consumers in considering changing retailer. Given the immaturity of the energy retail market and the diversity and complexity of contracts on offer, the search costs to consumers cannot be underestimated and may well be more significant than exit costs.

Having engaged in investigating retail options and chosen a provider, to be faced with the unexpected variation of a price during the contract period, a consumer may well feel disheartened by the system and reluctant to re-engage in the search process. Particularly if the other options open to them are also variable price contracts.

**Question 7      Impact of proposed rule on consumer participation and engagement**

- a) Would the proposed rule improve the level of consumer participation and engagement in retail energy markets?
- b) To what extent would the proposed rule place downward pressure on prices in retail energy markets due to improved consumer engagement and participation?

The Consumers SA believe that the proposed rule change would result in an increase in consumer participation and engagement. While other complexities of the market would also need to be addressed, this rule change would be one important step in the maturation of the market.

We acknowledge that if the majority of consumers already believe, incorrectly, that fixed term contracts incorporate fixed prices, then the immediate effects on participation and engagement may be limited. However, the longer term impact in reducing the number of consumers that disengage from the market process through frustration would be significant.

It should also be noted that this issue is just one of a number with the retail market in South Australia that needs to be addressed. Another important issue, and one that would significantly improve consumer engagement and participate is to address the way in which retailers use the pricing of their standard contracts to sell their market contracts. In South Australia the highly variable nature of standard contracts means that comparing contracts on the basis of how much the market rate discounts the standard contract, is a meaningless exercise for consumers, but a key marketing tool for retailers.

**Question 8      Competition between retailers**

- a) How would the proposed rule affect larger retailers compared to smaller retailers?
- b) Would the proposed rule make it more difficult for new entrants to enter retail energy markets?

The Consumers SA believe that the proposed rule change will have a positive effect in increasing competition for fixed price contracts and that there would be no significant increase to the barriers to new entrants above what already exists in the retail market.

**Question 9      Innovation in retail market offers**

- a) If the proposed rule is made, are retailers likely to withdraw or offer shorter fixed period offers from the market?
- b) If the proposed rule is made and the range of market offers available is reduced, what effect will this have on retail competition and prices in retail energy markets over the long term?

Consumers SA believe that the proposed rule change is unlikely to see retailers withdraw fixed period contracts from the market. While the longer fixed period contracts may prove to be unviable, there will remain value to retailers in locking consumers into contracts.

The rule change will also improve innovation and investment in mechanisms to more efficiently manage energy market risks. This will have a long term positive impact on pricing available to consumers.

**Question 10      Application of the unfair contract terms provisions in the ACL**

- a) If the unfair contract terms provisions in the ACL generally apply to price variation clauses in *market retail contracts*, should these provisions be relied on to address the issues raised by CALC and CUAC?
- b) Should changes be made to the retail rules to clarify whether the unfair contract terms provisions in the ACL apply to price variation clauses in *market retail contracts*?

While the provisions of the ACL may be an avenue of redress, for the clarity of consumers it is preferable that these consumer protections are dealt with under the energy retail legislation.

**Question 11      Misleading and deceptive conduct and other ACL provisions**

- a) Should the misleading and deceptive conduct provisions of the ACL be relied on to effectively address the issues raised by CALC and CUAC?
- b) Are there any other consumer protections under the ACL that are relevant to this rule change request?

See question 10.

**Question 12      Impacts of proposed rule**

- a) Taking into consideration the potential benefits and costs of the proposed rule, on balance how would the proposed rule affect competition in retail energy markets?
- b) Considering the issues identified by CALC and CUAC, is the proposed rule a proportionate and appropriate response to address these issues?

Consumers SA strongly support the proposed rule change as being of net benefit to consumers in the longer term. It will improve innovation amongst retailers in managing energy market risks and will provide greater clarity and transparency to consumers in assessing contracts. These will lead to a long term positive effect on pricing and a greater level of consumer confidence in engaging with the market.

**Question 13      Limited pass-through of costs**

- a) Would a rule that requires retailers to manage all costs aside from some limited cost pass-throughs better meet the NERO than the proposed rule?
- b) If so, which types of costs should retailers be allowed to pass-through to consumers and why?

The Consumers SA concern with a limited pass-through of costs approach is that it would maintain the current confusion within the market over the meaning of fixed contracts.

**Question 14      Other alternative rules**

- a) Are there any alternative approaches that could better address the issues raised by CALC and CUAC and minimise the potential costs of the proposed rule?
- b) If so, what could these alternative approaches include and what would be the potential costs, benefits and impacts of these alternatives?

While the Consumers SA's strong preference is for the primary proposal raised by CALC and CUAC to be adopted, in the absence of this, other alternatives that may be:

- Removing the ability to include both variable pricing and exit fees in the same contract
- A requirement for retailers to offer both a variable price and fixed price market contract (with appropriate adjustments to terminology to make this clear)