

Australian Government Rule Change Proposal to the Australian Energy Market Commission

**Long-term standing offer notice rule change proposal**

## 1. Name and address of the rule change proponent

**Name of Proponent:** The Honourable Minister Josh Frydenberg MP, Minister for the Environment and Energy on behalf of the Australian Government.

**Address of Proponent:** Parliament House, Canberra, ACT.

## 2. Summary

The proponent submits this request to the Australian Energy Market Commission (AEMC) to change the National Energy Retail Rules (NERR).

In simple terms, this rule change proposal would place an ongoing obligation on retailers to contact a certain group of retail energy customers, who are on typically higher-priced offers, with the aim of encouraging them to seek out a better alternative.

The proposal adds to the Australian Government's ongoing efforts to put downward pressure on energy prices and assist consumers in getting a better deal.

### Market and standard retail contracts

There are two types of contract that energy retailers are allowed to offer a consumer under the National Energy Retail Law (NERL). These are standard retail contracts (often called standing offer contracts) and market retail contracts.<sup>1</sup> In general terms, the standard retail contract is subject to more restrictions. These restrictions are aimed at providing a guaranteed set of protections to consumers. Market contracts, in contrast, exhibit a greater range of terms, conditions and tariff structures.

Compared with a market retail contract, some of the key features of a standard retail contract are:

- The retailer that is the “designated retailer”<sup>2</sup> for a small customer’s premises must make an offer to provide customer retail services to that small customer<sup>3</sup>:
  - at the standing offer price; and
  - under the retailer’s form of standard retail contract that must be based on model terms which are set out in the rules
- a retailer’s standing offer prices must be published and cannot change more than once every six months;
- retailers cannot charge exit fees.<sup>4</sup>

In all National Energy Consumer Framework (NECF) jurisdictions, retailers and small customers may negotiate to enter into a market contract, however, this choice is more limited in

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<sup>1</sup> See s 20(1) and (2) of the NERL.

<sup>2</sup> The designated retailer is, for new connections, the local area retailer for the relevant area, premises or customer and for existing connections is the retailer that is currently financially responsible in the market for the energy consumed at that connection point.

<sup>3</sup> ‘Small customer’ is defined in s5 of the NERL.

<sup>4</sup> Rule 70(4) of the National Energy Retail Rules.

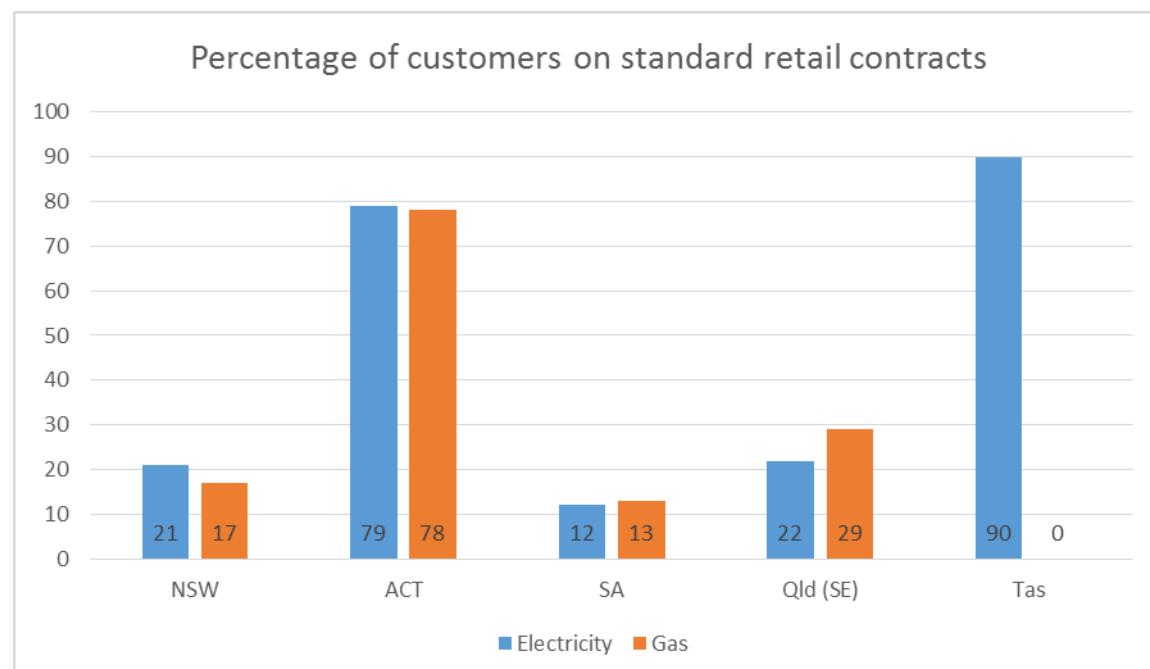
jurisdictions in which energy prices are regulated.<sup>5</sup> Outside those regulated jurisdictions, consumers are typically faced with a wider range of market offers from different retailers.

### The nature and scope of the issues addressed by the proposal

Standard retail contracts are typically more expensive than market retail contracts.<sup>6</sup> Recently, for example, the AEMC found that the difference between the average standing offer and the best market offer for a representative consumer was between \$170 and \$507 per year.<sup>7</sup> A consumer may, therefore, benefit from significant savings in switching from a standard to a market retail contract.

The potential to benefit from switching to a market offer is not limited to a small cohort of consumers, as outlined in Table 2. Even in South Australia – the NECF jurisdiction with the lowest proportion of standing offer customers – more than 1 in 10 consumers are on standard retail contracts.

**Table 2:** Customers on standard retail contracts in NECF jurisdictions<sup>8</sup>



Importantly, standing offer customers tend to be less engaged with the energy market. That is, they are less likely to actively consider whether there are better alternative offers in the market. Research has shown that consumers who have neither investigated alternative offers in the market, nor have switched energy provider in the past 5 years are more likely to report being on a standing offer.<sup>9</sup>

<sup>5</sup> Prices are regulated in the ACT, Tasmania and rural Queensland.

<sup>6</sup> See, e.g., the ACCC Retail Electricity Pricing Inquiry: Preliminary Report, p10:

<https://www.accc.gov.au/publications/accc-retail-electricity-pricing-inquiry-preliminary-report>

<sup>7</sup> In January/February 2017. See AEMC Retail Energy Competition Review 2017, p. 99:

<https://www.aemc.gov.au/markets-reviews-advice/2017-retail-energy-competition-review>

<sup>8</sup> See AER retail performance statistics: <https://www.aer.gov.au/retail-markets/performance-reporting/performance-of-the-retail-energy-market-2016-17>

<sup>9</sup> Newgate Consumer Research 2017, p39: <https://www.aemc.gov.au/markets-reviews-advice/2017-retail-energy-competition-review>. Specifically, the research noted the proportion to be 47% vs. 22% of those on market offers for electricity, and 43% vs. 25% for gas.

## How the proposal addresses the issues

This rule change proposal is specifically aimed at addressing the fact that standing offer customers are:

- less likely to engage with the market and seek out better offers; and
- more likely to be paying more for energy services.

By raising awareness amongst standing offer customers that there may be a better offer in the market, the government believes this will encourage these customers to shop around for a better deal. Encouraging consumer engagement will drive competition, encourage downward pressure on prices and improvements in the variety of pricing, product offerings and the quality of services.

### 3. Description of the proposed rule

In accordance with section 243 of the NERL, the proponent requests the AEMC make a number of changes to the NERR through the creation of a new ‘Rule 59A’.

In basic terms, the rule will have the effect of requiring a retailer to provide notice to its customer if that customer has been on a standard retail contract with that retailer for a period of 12 months or more. This obligation will recur every 12 months until the contract ends.

#### The proposed rule structure

The following sets out the proposed structure of the rule.

##### **59A Long-term notice requirements**

- 1) *This rule applies if a small customer is on a standard retail contract with a retailer and has received customer retail services under the contract for a period of 12 months or more.<sup>10</sup>*
- 2) *The retailer must give the customer a notice (a **long-term notice**) in accordance with this rule.*
- 3) *The long-term notice must be given:*
  - a) *orally, or in writing;*
  - b) *within 40 days of the issue of the first bill issued after each anniversary of the commencement of the contract.<sup>11</sup>*
- 4) *The long-term notice must communicate to the customer:*
  - a) *that the customer has been on a standard retail contract with the retailer for a period exceeding 12 months;*
  - b) *that the customer may use the price comparator to compare offers that are generally available to classes of small customers in their area;*
  - c) *the name and web address of the price comparator; and*

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<sup>10</sup> Note the discussion below on an additional proposal related to deemed customer retail arrangements.

<sup>11</sup> Consistent with a number of other rules in the NERL, 40 days is proposed as an appropriate time-frame. The AEMC may wish to consider whether the period should be calendar or business days. We also note that an alternative approach to the anniversary trigger is discussed below.

- d) *that the customer can request historical billing data and, if they are being sold electricity, energy consumption data, from the retailer that will assist them to use the price comparator.*
- 5) *In giving the long-term notice to the small customer, the retailer must have regard to any guidance published by the AER on the manner and form of the notice.*
- 6) *The AER may, by notice published on its website, exempt retailers with customers located in a particular area from the requirement under this rule to issue long-term notices to customers in that area, if the AER is satisfied, having regard to the availability of market retail contracts in that area, that it would be inappropriate to require notices to be given to customers in that area.<sup>12</sup>*

The government proposes that this new rule be subject to a civil penalty if a retailer fails to comply. Ensuring that breach of this rule can result in a financial penalty will act as an effective deterrent to non-compliance.

#### **Deemed customer retail arrangements**

As drafted, the notice proposal is targeted at consumers who are contracted to a retailer under a standard retail contract.<sup>13</sup> In addition to those customers, some people are deemed to receive energy under terms and conditions that are the same as the retailer's standard retail contract. Broadly, those people are:

- **A carry-over customer:** a customer who continues using energy at a premises after their existing contract expires;<sup>14</sup>
- **A move-in customer:** a customer who starts using energy at a premises without having applied to a retailer for the provision of energy services.<sup>15</sup>

Many of those people who become carry-over or move-in customers would likely sign up to a new contract within a short period of time. For those who do not, a retailer can take steps to 'de-energise' the premises, but this is not guaranteed.<sup>16</sup> It is feasible that some consumers remain on deemed customer retail arrangements for significant periods of time.<sup>17</sup>

NERR rule 53 already requires retailers to contact a customer as soon as practicable after becoming aware that the customer is consuming energy under a deemed customer retail arrangement.<sup>18</sup> Unlike the rule change proposed above, however, the rule 53 obligation is not ongoing. To the extent that deemed customer retail arrangements continue for extended

<sup>12</sup> The construction of this exemption mechanism is intended to provide the AER with flexibility in how or whether the power is exercised.

<sup>13</sup> That is, a contract published by the retailer under NERL s 25.

<sup>14</sup> Note that rule 48 requires retailers to provide notice to customers at the end of a fixed term contract. Unlike this rule proposal, the rule 48 obligation does not recur if the consumer takes no action as a result of the notice.

<sup>15</sup> NERL s 54 governs these arrangements as they apply to 'move-in' and 'carry-over' customers.

<sup>16</sup> A retailer is not obliged to 'de-energise' in these scenarios. Extending the operation of the rule to deemed customer arrangements may require consideration of the interaction with existing notice requirements under NERR rule 115 in relation to de-energisation of premises.

<sup>17</sup> While NERL s54(6), obliges 'deemed' customers to contact a retailer and take appropriate steps to enter into a retail contract as soon as possible, it does not guarantee such customers do not remain on a standard 'arrangement' for lengthy periods.

<sup>18</sup> See NERR rule 53.

periods of time, the government considers the new long-term notice obligations should extend to those consumers and requests the AEMC give consideration to options in this respect.<sup>19</sup>

### The location of the proposed rule

While the AEMC may consider alternative locations for the new rule proposal, it is proposed that the likely best fit is within the ‘other retailer obligations’ of Part 2, Division 9.

Part 2 of the NERR deals generally with customer retail contract requirements, including:

- Allowable or required contractual terms and conditions in retail contracts;
- Pre-contractual procedures that must be followed;
- The manner and basis on which customers are billed;
- How under or overcharging is dealt with;
- The use of security deposits;
- Termination of contracts;
- Transfer of customers and energy marketing practices.

The government notes that while it would seem appropriate to locate the rule within Part 2 of the Rules, the rule doesn’t otherwise clearly fit within the existing Divisions of that Part.

In particular, the basic purpose of this proposed rule is to require a retailer to provide notice to a standing offer customer, however, unlike the standard retail contract requirements in Division 1, the proposed rule is not a contractual requirement. The proposed rule is, on the other hand, broadly analogous to the rule 48 notice in Part 2, Division 7, but this Division deals only with market retail contracts. Division 4, which deals with billing, could be appropriate given the proposal requires notice at the time a bill is provided, however, the best fit appears to be within Division 9.

### Timing of implementation

The government considers this rule to be an important step in protecting consumers from potential detriment. To that end, the government would like the rule to start from as soon as possible in 2018, but recognises that a reasonable period of transition is needed to allow retailers to make necessary changes in compliance with the new proposal. The AEMC may also consider whether it is appropriate to align the commencement of this rule with other rule proposals currently under consideration.<sup>20</sup>

The government notes it is intended that this rule apply to new and existing long term standing offer contracts – this will ensure existing long-term standing offer customers are prompted to consider alternative market offers. The government requests the AEMC consider appropriate commencement and transitional approaches having regard to the potential impact of the new rule on existing agreements.

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<sup>19</sup> The AEMC may consider it appropriate to make a more preferable rule to extend the scope to deemed customer retail arrangements, or, e.g., amend the operation of rule 53 to align with the proposed notice requirements.

<sup>20</sup> See, e.g.: <https://www.aemc.gov.au/rule-changes/advance-notice-price-changes>

#### 4. Explanation of the proposed rule

The structure of the rule has three key components:

- Primary notice obligations
- AER guidance
- AER exemption

##### The primary notice obligations

The primary notice requirements in proposed rule 59A will require a retailer to provide a notice to a small customer who has received customer retail services under a standard retail contract for a period of 12 months or more. To provide a level of flexibility in how retailers must comply with this obligation, the notice may be provided in writing or orally.<sup>21</sup> For example, it is envisaged a retailer could comply with the obligation by contacting the consumer by phone.<sup>22</sup>

The notice must be given with the first bill after each anniversary of the commencement of the contract. It is intended that the obligation continue for as long as the contract remains on foot – that is, for example, until the contract ends because the customer has sought services elsewhere, or has concluded a new agreement with their existing retailer.

The intention behind specifying an anniversary date that reflects the commencement of the standing offer contract is to ensure that consumers receive notice after a consistent period of time (e.g. 12 months). An alternative construction of the rule, which the AEMC may wish to consider, would be to specify an annual date on which a notice is required. On the given date, the notice requirement would be triggered if a consumer has been on a standing retail contract for a specified period prior to that date.<sup>23</sup> Triggering the notice requirement in this way could reduce retailer compliance costs related to IT systems changes.

Sub-rule 59A(4) sets out the key content of the notice.<sup>24</sup> As the main purpose of the notice is to encourage the long-term standing offer customer to engage with the market and shop around for a better deal, sub-rule 59A(4) requires the notice to include information about the Australian Energy Regulator's (AER's) price comparator ([www.energymadeeasy.gov.au](http://www.energymadeeasy.gov.au)), and how to access historical billing and energy consumption data. Improving awareness of the price comparator and how to access billing and consumption data will assist consumers in making informed choices about retail energy offers.

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<sup>21</sup> The rule is intended, in respect of the manner of giving notice, to operate as a contrary intention, per NERL s319(4).

<sup>22</sup> It is noted that NERR rule 65 imposes limits on consumer contact in respect of energy marketing activities. As the proposed notice requirement is not intended to operate as a marketing opportunity, it is not expected that any change to rule 65 is necessary. The AEMC may, however, wish to consider the interaction between the proposal and the operation of rule 65, noting that the government's position is that the notice requirement should apply to all long-term standard retail contract customers (subject to the limits outlined in the proposal).

<sup>23</sup> In this construction, the relevant period could be specified to be, e.g., 6 months. In this way, a consumer who has been on a standard retail contract for 6 months prior to the anniversary date would receive an initial notice at that date and then, again, 12 months later (unless they have ended their contract). A period less than 12 months would avoid the scenario in which, on the anniversary date, a consumer has been on a standard retail contract for a period of 364 days, thereby resulting in the first notice provided 2 years after entering a contract. If the AEMC considers adopting this construction, a range of alternatives may be appropriate to avoid notice being required too soon, or too late after entering a contract.

<sup>24</sup> These are similar to the notice requirements which have been recently incorporated into rule 48A – the notice of benefit change rule. See: <https://www.aemc.gov.au/rule-changes/notification-of-end-of-fixed-benefit-period>

The notice must also communicate that consumer has been on a standard retail contract for a period exceeding 12 months. The intent behind requiring communication of this information is to increase the customer's awareness of the length of time elapsed since they engaged with market alternatives – the longer the period, the more likely the market has shifted since the customer initially engaged with their existing retailer. The longer the period elapsed after entering into a standard retail contract, the more likely a greater range of competitive market offers will exist.

Beyond setting out the main content of the communication to a customer, as described above, the rule is not intended to prescribe the manner and form of that communication. That is, it is intended that the retailer retain some flexibility in the way the information is communicated to the consumer. It is expected that this flexibility should ensure the communication is made in the most effective manner and could be incorporated with other communications or notices which the retailer provides in the ordinary course of their dealings with the consumer.

#### AER Guidance

Within the rules, the AER is sometimes empowered to develop and maintain prescriptive guidelines on a range of matters governing retailer behaviour.<sup>25</sup> While a similar approach could be taken in relation to the notice proposed in this rule change request, the government has proposed a more flexible approach.

Under rule 59A(5), in providing the long-term notice to a customer, a retailer is required to have regard to any guidance published by the AER on the manner and form of the notice. The key elements of this mechanism are:

1. The AER is able to issue guidance on how best to implement the notice obligation, but is not required to do so.
2. The retailer must have regard to such guidance, but is still able to retain flexibility as to how the notice is provided.

It is expected that, on commencement of the new rule, the AER will monitor compliance with the rule. If, for example, the AER identifies features of communications by particular retailers that work effectively, the AER may consider publishing guidance to all retailers on the most effective practices. Over time, such guidance could assist retailers in implementing industry best practice without the need for a more prescriptive approach.

The ability of the AER to flexibly develop and publish guidance over time also allows the AER to draw upon current research about consumer sentiment and practices, retailer behaviour, and shifts in the market related to, e.g., energy price and demand.<sup>26</sup> Thus, the guidance mechanism

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<sup>25</sup> For example, the *Retail Pricing Information Guidelines*: <https://www.aer.gov.au/retail-markets/retail-guidelines-reviews/draft-retail-pricing-information-guidelines-2018>

<sup>26</sup> See also the comments made by the AER on p6 of the *Benefit Change Notice Guidelines Issues Paper*: <https://www.aer.gov.au/communication/aer-invites-submissions-on-benefit-change-notice-guidelines-issues-paper>

provides an effective and flexible way to ensure the rule continues to have the intended effect as the market evolves.<sup>27</sup>

#### AER exemption

Given certain jurisdictions regulate the prices which are available to consumers, the government considers it may be appropriate to exclude the operation of this notice requirement in those regions.<sup>28</sup> This is because any notice which encourages a consumer to shop around for a better deal could be redundant if jurisdictional requirements, or a general lack of effective competition, do not allow for the existence of better deals. Sub-rule 59A(6) attempts to address this matter by providing that notices are not required for customers located in a particular area if the AER is satisfied that the provision of notices to those customers is inappropriate, having regard to the availability of market offer contracts in that area.

The manner in which the exemption mechanism is expressed is intended to provide the AER with significant flexibility as to whether or not the AER uses the power, and how the power is exercised.

While the government would prefer that the notice requirements be applied as broadly as possible with as few exemptions as possible, the AEMC may consider expanding the exemption power beyond the scope proposed. If the AEMC does consider expanding the scope of the power, it is suggested that exemptions be limited to scenarios in which there would be no consumer benefit in receiving the notice.

## 5. Contribution to the National Energy Retail Objective

The National Energy Retail Objective, as stated in the NERL, is:

“...to promote efficient investment in, and efficient operation and use of, energy services for the long term interests of consumers of energy with respect to price, quality, safety, reliability and security of supply of energy.”

The government views this rule change proposal as, fundamentally, promoting the efficient operation of energy services in the long term interests of consumers. The proposal aims to address consumer disengagement that appears more prevalent in the cohort of consumers that are on standard retail contracts.

For an individual consumer, the rule change may lead to savings on energy costs. In aggregate, however, better engaged consumers drive competition. This can put downward pressure on prices and encourage improvements in the quality of service, and is clearly in the long-term interests of consumers.

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<sup>27</sup> The AER could also rely on relevant international behavioural research to aid development of the guidance. A good example of such research would be the *Cheaper Market Offers Letter Trial* conducted by the UK energy regulator OFGEM, which considered the positive effect of providing notices to long-term standing offer customers: <https://www.ofgem.gov.uk/publications-and-updates/results-cheaper-market-offers-letter-trial>

<sup>28</sup> While full retail contestability exists within all NECF jurisdictions, competition in some jurisdictions remains limited and, consequently, so is the availability of market retail contracts.

Given the second arm of the rule-making test in s 236(2)(b) of the NERL, it is also noted that the implementation of this proposed rule is inherently compatible with the development and application of consumer protections for small customers. Measures to encourage a consumer to engage with the market, and to assist a consumer to seek out a better offer, are well aligned with existing consumer protections in the NERL and NERR. The government considers the proposed rule is, at its core, a means to empower consumers to take advantage of the benefits of the existing regulatory framework and competitive energy retail markets.

## 6. Benefits, costs and implications of the proposed rule

### Benefits

As stated above, the practical benefit of making this rule is that it will encourage standard retail contract customers to engage with the market, with the potential outcome of finding a much better deal. Given the disparity between the cost of energy under a standing offer compared with some market offers, individual consumers could secure significant savings in moving to better market offers.

Encouraging greater consumer engagement will, in turn, result in more efficient operation of energy services in the retail market, which is consistent with the long-term interests of consumers. A further key benefit of the rule is that it will build consumer trust in the market and limit the risk of bad consumer experiences.

### Risks, Implications and Treatment

Risk	Treatment
<i>Cost of contact with consumers on an ongoing basis.</i>	<p>Any obligation to provide notice to a customer may result in some cost to the retailer. Ultimately, the risk and cost posed by the obligation is best managed by the retailer, and the retailer will, within the scope allowed by the rule and other provisions of the law, have some flexibility in the manner and form by which the notice is provided.</p> <p>That said, given the number of customers to which the obligation applies will be relatively small compared with the total number of customer in the market, the government considers that any cost associated with this obligation can be readily absorbed by retailers.</p>
<i>Potential reduction in protections for those moving off standing offer.</i>	<p>Encouraging consumers to move from a standard to market retail contract may result in those consumers losing the consumer protection benefits which underpin the standard retail contract.</p> <p>The notice does not, however, oblige the consumer to make the change or oblige a retailer to offer a market retail contract to a given consumer. It is ultimately within the power of the consumer to choose to remain on a standard retail contract, and for some consumers this may be the best outcome.</p> <p>The government views this risk as being limited.</p>