



Australian Energy Market Commission

CONSULTATION PAPER

NATIONAL ENERGY RETAIL AMENDMENT (REGULATING CONDITIONAL DISCOUNTING) RULE

PROPONENT

The Honourable Angus Taylor, Minister for Energy & Emissions Reduction, on behalf of the Australian Government

1 AUGUST 2019

RULE

INQUIRIES

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Reference: RRC0028

CITATION

AEMC, Regulating Conditional Discounting, Consultation paper, 1 August 2019

ABOUT THE AEMC

The AEMC reports to the Council of Australian Governments (COAG) through the COAG Energy Council. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the COAG Energy Council.

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1 INTRODUCTION

On 18 February 2019, the Honourable Angus Taylor, Minister for Energy & Emissions Reduction, on behalf of the Australian Government, submitted a rule change request to the Australian Energy Market Commission (the Commission) to regulate conditional discounting practices by energy retailers.

This consultation paper has been prepared to facilitate public consultation on the rule change request and to seek stakeholder submissions. This paper is structured as follows:

- Chapter 1 summarises the rule change request and sets out the Commission's proposed timing for the rule change request
- Chapter 2 sets out background information relevant to the rule change request
- Chapter 3 sets out a range of issues for stakeholder comment
- Chapter 4 sets out the proposed assessment framework for consideration of the rule change request
- Chapter 5 explains how stakeholders can submit responses to this consultation paper.

1.1 Rule change request

The rule change request proposes that the level of conditional discounts for gas and electricity retail offers be restricted to the reasonable cost savings that a retailer expects to make if a consumer satisfies the conditions attached to the discount. The proponent noted that the request is based on recommendation 33 of the Australian Competition and Consumer Commission's (ACCC) Retail Electricity Pricing Inquiry (REPI).¹

The rule change request outlines two key policy objectives:

- remove the excessive penalties on customers (particularly vulnerable customers) who pay after the due date, which are effectively resulting in those customers paying the highest prices in the market²
- improve the comparability of market offers by simplifying and reducing conditional discounts, thereby reducing barriers to effective consumer engagement and enhancing competition.³

The rule change request includes a proposed rule. If made, the request would amend Rule 45A of the NERR, and new rules would be made (Rule 46C and Rule 46D).⁴

Copies of the rule change request may be found on the AEMC website, www.aemc.gov.au.

1 Australian Government, Improving consumer outcomes and competition by regulating conditional discounting, rule change request, 18 February 2019, p. 2.

2 Ibid p. 3.

3 Ibid

4 Please note that the National Energy Customer Framework (NECF) does not apply in Victoria, and as a consequence, retail rule changes, including this rule change will not apply in Victoria.

1.2 Timing of the rule change process

On 1 July 2019, the Default Market Offer (DMO) came into effect through the Electricity Retail Code of Conduct (the Code). The Code was made under the *Competition and Consumer Act 2010 (Cth)* (CCA). The Commission expects that the Code will impact the issues raised by the proponent because it places restrictions on retailers conditional discounting practices. The Commission has extended the standard 4-week consultation period to 7 weeks to allow stakeholders more time to observe the impact of the Code on conditional discounting practices before making submissions.

At this stage, the Commission proposes the timeframe noted in Table 1.1 for the remainder of the rule change request.

Table 1.1: Proposed rule change request timetable

RULE CHANGE STAGE	DATE
Consultation paper released	1 August 2019
Submissions on consultation paper due	19 September
Draft determination	28 November
Submissions on draft determination due	16 January 2020
Final determination	27 February 2020

2 BACKGROUND

2.1 What are conditional discounts?

The proponent defines a conditional price discount as "the amount by which a price otherwise payable under a contract is, or would be, reduced as a consequence of complying with one or more provisions of the contract."⁵

The AER has defined conditional discounts as "a discount applied to an energy bill based on a certain condition being met".⁶ Conditional discounts could be defined as arrangements under an energy contract where customers receive lower daily and/or usage rates off their energy consumption when certain payment condition(s) are fulfilled by the customer during the term of that contract. The most common types of conditional discounts are:

- pay-on-time
- direct debit.

The Commission's preliminary view is that conditional discounts refer specifically to *payment* conditions fulfilled *during the term* of a contract. This also appears to be the proponent's intent.

2.2 Conditional discounts in the retail market

Conditional discounts have been a common feature of retail pricing practices. Conditional discounts peaked at 78 per cent of market offers in 2017,⁷ decreasing to 47 per cent of market offers in 2019.⁸ Conditional discount rates have also increased significantly, from an average of 5-10 per cent rates in 2014 to 30-40 per cent rates in 2018.¹⁰ Some stakeholders have noted that the popularity of these discounting practices have been driven by its "marketing value", i.e. the ability of large discounts to attract customers to sign up.¹¹

2.3 Why is the issue being raised now?

Major inquiries into the energy retail sector by the ACCC (REPI) and an independent panel commissioned by the Victorian Government (the Independent and Bipartisan Review of the Electricity and Gas Retail Markets in Victoria - also known as the Thwaites Review) have identified energy retailer practices that may have been driving customer dissatisfaction. In outlining the motivating factors for its investigation, the ACCC noted that "retailers have made pricing structures confusing and have developed a practice of discounting which is opaque and not comparable across the market."¹² These inquiries recommended that

5 Australian Government, Improving consumer outcomes and competition by regulating conditional discounting, rule change request, 18 February 2019, p. 9.

6 Australian Energy Regulator, Annual report on compliance and performance of the retail energy market, December 2018.

7 Figures refer to offers in New South Wales, South Australia and south east Queensland for responding retailers: AEMC, 2017 Retail Energy Competition Review, 25 July 2017, pp. 228, 242, 290.

8 AEMC, 2019 Retail Energy Competition Review, 28 June 2019, p. 82.

10 ACCC, Retail Energy Pricing Inquiry - Final Report, July 2018, p. 257.

11 Discussion with stakeholder, July 2019.

12 ACCC, Retail Energy Pricing Inquiry - Final Report, July 2018, p. iv

Commonwealth and Victorian governments propose changes to retail market rules and practices, including this rule change request.

2.4 Recent changes to the retail market

The DMO was a recommendation¹³ of the ACCC to the Commonwealth government in REPI.¹⁴ The introduction of the DMO through the Code restricts the way retailers advertise energy offers that use conditional discounts. Under the Code, the two most relevant changes in place from 1 July 2019 are:

- electricity retailers must not advertise a conditional discount as the most conspicuous price-related matter in the advertisement¹⁵
- each conditional discount mentioned in an offer must state the difference between the unconditional price and the conditional price; this must be expressed as a percentage of the reference price.¹⁶

The Code does not apply to jurisdictions with retail price regulation, and therefore does not apply in Tasmania or the ACT. Additionally, the Code only covers electricity offers.

In May 2018, the Commission made a rule which prevented energy retailers from offering conditional discounts rates to be set above standing offers.¹⁷

2.4.1 Interaction between NERR and the Code

The Commission notes that any changes to the NERR within this rule change will need to be consistent with the Code. While the Commission has always had to have regard to provisions of the Competition and Consumer Act, these have tended to be economy-wide provisions, rather than energy industry-specific rules. The Commission expects that to the extent of any inconsistency, the Code provisions will override NERR provisions. The Code will therefore be a factor in the Commission's decision-making in this rule change process.

2.4.2 Penalties under common law

The Commission understands that a provision in a contract that seeks to impose a penalty on a contracting party is not enforceable under common law. Courts have historically taken the view that where a party is obliged to pay an amount of money to the other party (due to breaching a term of the contract), and that amount is much greater than, or out of proportion to, the damage or loss suffered by that other party, then that amount may be regarded as a penalty.

The Commission notes that the existence of common law restrictions on conditional discounting would not undermine its ability to make energy specific restrictions on such conduct.

¹³ ACCC, Retail Energy Pricing Inquiry - Final Report, July 2018, p. 252

¹⁴ Victoria has also introduced its own retail offer cap mechanism, the Victorian Default Offer - VDO.

¹⁵ Australian Government, Electricity Retail Code of Conduct, s. 14 (2)

¹⁶ Ibid, s. 12 (3)

¹⁷ Please refer to AEMC, Preventing discounts on inflated energy rates, final rule determination, 15 May 2018.

3 DETAILS OF RULE CHANGE REQUEST & ISSUES FOR CONSULTATION

Taking into consideration the assessment framework set out in Chapter 4, a number of issues have been identified for consultation. Stakeholders are encouraged to comment on these issues as well as any other aspect of the rule change request or this paper.

This chapter outlines:

- the issue identified by the proponent
- the materiality of the issue, including the impact of recent changes to retail markets
- consideration of energy offers not covered by the Code
- solutions proposed by the proponent and alternative solutions.

3.1 Issues identified and their materiality

3.1.1 Offer comparability & anticipation energy plan costs

Proponent's description of the issue

The proponent notes that the size of conditional discounts has increased from around 5 to 10 per cent in 2014 to up to 30 to 40 per cent in 2018.¹⁸ High advertised discounts seen over the past years may be particularly attractive to customers seeking to manage their costs. Two problems have emerged from this.

Firstly, customers are often drawn to higher discounts, even when these don't necessarily equate to the best offer in the market. The ACCC found that the increase in discounts has in many cases not coincided with similarly deep savings in retail electricity bills.¹⁹ Uneven base rates from which offers are discounted off have made it harder for customers to assess suitable offers to meet their circumstances.

Secondly, competition between retailers on a conditional discount offer basis means that customers and energy retailers may focus on headline discount figures rather than the conditions necessary to achieve these (such as a pay-on-time condition). This exposes customers who are unable to accurately anticipate their ability to pay to higher energy prices. The proponent indicates that low conditional discount realisation rates indicate that a significant number of discount customers do not accurately anticipate their ability to fulfil contract conditions.²⁰

Analysis of materiality of the issue

As set out in section 2.4, the introduction of the Code on 1 July 2019 prevents retailers from advertising conditional discounts as the most prominent feature of their electricity offer.

¹⁸ Australian Government, Improving consumer outcomes and competition by regulating conditional discounting, rule change request, 18 February 2019, p. 3

¹⁹ Ibid.

²⁰ Ibid, p. 2.

Furthermore, conditional discounts must be advertised against the reference price in accordance with the Code's requirements.²¹

These changes may have two effects that may diminish the materiality of the problem of offer comparability. Firstly, all electricity conditional offers (outside of the ACT and Tasmania) must now be calculated in reference to a common base (the DMO), meaning that discount rates offered by retailers will now be comparable from a common base. This is expected to increase offer comparability when customers access these offers. Secondly, these changes may limit the ability and willingness of retailers to promote offers with conditional discounts to customers. This may reduce customer access and visibility to conditional discount offers, potentially removing issues of comparability altogether.

The Commission also notes that the AER has drafted new Retail Energy Pricing Guidelines, designed to help retailers comply with new regulatory requirements for the advertisement of energy plans, including on online media such as Energy Made Easy. These changes should also improve offer comparison.

QUESTION 1: OFFER COMPARABILITY

- (a) Will comparability issues for conditional discount offers continue to be material with the introduction of the Code?
- (b) What other factors may be present that contribute to the difficulty of offer comparability?

3.1.2

Excessive penalties for customers who do not realise discount conditions

Proponent's description of the issue

The proponent considers that when customers do not meet the conditions of conditional discounts they are required to pay significantly higher rates and that these effectively constitute customers paying "penalty" energy rates. The proponent considers that significant portions of different residential customer groups fail to realise conditional discounts. For example, based on the final REPI report the proponent considers that 76 per cent of all residential customers realise conditional discounts, while this number is 41 per cent for customers on a hardship program.²² The Commission notes that despite the fact that realisation rate for vulnerable customers are low, these customers make up about 1.4 per cent of residential customers.²³

The realisation rates noted above gave rise to the proponent's concerns over excessive penalties, especially because of the increase in the magnitude of conditional discounts

²¹ Specifically, the ACCC noted that each advertisement must include "for each conditional discount, the difference between the conditional price and unconditional price, stated as a percentage of the relevant reference price", ACCC, Guide to the Electricity Retail Code, June 2019, p. 7.

²² Australian Government, Improving consumer outcomes and competition by regulating conditional discounting, rule change request, 18 February 2019, p. 6

²³ AER, Quarterly Retail Performance Report Q3 2018-19, June 2019.

experienced since 2014.²⁴ The proponent's analysis indicates that the costs to an average customer of not meeting a pay-on-time discount could lead to an increase of up to 50 per cent of that customer's annual bill.²⁵ The proponent considers this increase in the annual bill is not representative of additional costs to retailers from holding debt for customers. In effect, customers who miss payment conditions while they are on high conditional discount offers may be paying some of the highest rates in the market.²⁶

Vulnerable customers are most exposed to these practices, leading to the entrenchment of inequitable outcomes in the market. These types of customers often live in volatile employment, health and social circumstances, which might impede them from prioritising energy plan payments.²⁷

Analysis of materiality of the issue

The introduction of the DMO through the Code caps electricity standing offers.²⁸ The reduction of the base rates from which conditional discounts are set may limit the magnitude of conditional discounts and, by extension, the increased prices customers pay when they miss discount conditions.

Similarly, the magnitude of conditional discounts may be limited by the restriction on advertising conditional discounts as the most conspicuous feature of an energy offer. Retailers may want to continue to advertise large headline discounts, however the restriction noted above may mean that large discounts advertised will now be unconditional. These changes may result in the magnitude of conditional discounts being smaller, thus reducing the impact of customers missing discount conditions.

In regard to the impact on vulnerable customers from large conditional discounts there are recent changes and other regulatory requirements that are also worth considering. For example, in August 2017, seven major energy retailers committed to the Commonwealth government that customers on a hardship program "will not lose any benefit or discount for late payment."²⁹ Furthermore, under section 44 of the NERL, retailers are required to include processes to review the appropriateness of a hardship customer's market retail contract as part of their customer hardship policy. A retailer should therefore be reviewing how appropriate a large pay-on-time discount is for a hardship customer who has a history of failing to meet discount conditions.

24 Ibid p. 3.

25 Ibid, p. 3.

26 Ibid.

27 Ibid, p. 2.

28 Conditional discounts are usually set off relatively high base rates; this is done by retailers to inflate the magnitude of the discount offered to customers.

29 Office of the Prime Minister of Australia, Press conference with the Treasurer, The Hon Scott Morrison MP and the Minister for the Environment and Energy, The Hon Josh Frydenberg MP, Press conference transcript, 9 August 2017, p. 2, 4.

QUESTION 2: EXCESSIVE PENALTIES

(a) Do stakeholders agree with the characterisation of substantially higher prices paid by customers when they miss conditional discount conditions as excessive "penalties"?

(b) What customer groups are most at risk of failing to realise conditional discounts? How significant are these groups as a proportion of the energy customer base? (e.g. [i] Should payment plan customers be considered? [ii] Hardship customers make up 1.4 per cent of all customers according to AER data).

(c) Do stakeholders have views on the ability of vulnerable customers to anticipate their energy plan costs and ability to pay?

(d) What internal rules do retailers have in place to ensure customers on a hardship program do not lose any benefit or discount for late payment (in line with the commitment announced on 7 August 2017 noted above)? Are retailers still committed to this approach now that the DMO has been introduced?

3.1.3

Key data points needed to establish materiality of issue

The Commission will seek to gather market data on conditional discounting practices to inform its assessment of the issues raised by the proponent and their materiality. The Commission will be able to access certain key data points needed to inform this rule change, namely:

- Price dispersion of retail offers on Energy Made Easy
- Magnitude of discounts offered in retail market on Energy Made Easy
- Proportion of customers in vulnerable categories such as hardship programs, payment plans, concession programs, etc.

In addition to these points, the Commission would like to request stakeholders to provide it with the data set out in question box 3 below. The Commission notes that pricing uptake data is likely to be commercially sensitive. Where retailers are able to provide this data the Commission will include it in its analysis where possible, but only publish it in aggregate form such that individual retailer data remains confidential.

QUESTION 3: KEY DATA NEEDED TO ESTABLISH MATERIALITY

The Commission requests data from stakeholders on the following:

- Price dispersion data on residential customer contracts, i.e. actual uptake and prices of customer contracts in the post-1 July 2019 period, including the magnitude of discounts in these contracts, the difference between highest and lowest market offers, etc.

- Uptake of different types of market offers (including conditional & guaranteed discounts, as well as other types of market offers), both before and after the introduction of the Code.
- Realisation rates of conditional discounts contracts, i.e. the percentage of customers on conditional discounts who satisfy conditions each payment cycle and earn the discount.
- Information on the scale and effectiveness of retailers' hardship programs with regard to conditional discounts and customers being on appropriate contracts. Including processes in place to comply with their obligations under s. 44 of NERL regarding the review of the appropriateness of a hardship customer's market retail contract.
- Evidence of the impact of conditional discount on retailer debt management. Retailers may want to compare trends in debt levels during periods before and after conditional discounts were introduced.

3.2 Energy offers not covered by the Code

The proponent indicated that where feasible, restrictions on conditional discounts should apply to gas contracts for small customers and to all small electricity customers in the NEM.³⁰ The Commission notes that the Code does not apply to gas offers generally or electricity offers in the ACT or Tasmania.

While the Code does not apply to electricity offers in the ACT and Tasmania, other regulatory mechanisms do constrain conditional discount levels in these jurisdictions to some degree. For example, the combination of jurisdictional price regulation of standing offers and the Commission's May 2018 rule³¹ that prevents discounts from being set from base rates above standing offers means that conditional discounts can only be set from the regulated standing offer rates in these jurisdictions.³²

In contrast, retailers in the ACT and Tasmania may advertise conditional discounts as the most conspicuous price-related matter in an offer. While Tasmania currently has limited levels of retail energy competition, retail competition has been increasing in the ACT since 2015.³³ There is potential for conditional discounts to become a material part of retail pricing competition in the future in these jurisdictions.

There are fewer restrictions on conditional discounting for gas offers in all jurisdictions. With no retail price regulation applying, retailers are free to set their standing offers at any level. This raises the prospect of the comparability of offers and the excessive discount issues raised by the proponent continuing for small gas customers. A potential limitation to this is

30 Australian Government, Improving consumer outcomes and competition by regulating conditional discounting, rule change request, 18 February 2019, p. 8

31 AEMC, Preventing discounts on inflated energy rates, final rule determination, 15 May 2018.

32 The Commission expects that the standing offer would effectively become a common reference price in these jurisdictions because retailers would be incentivised to maximise discount rates to attract customers. However, the Commission notes that no explicit obligations exist for retailers in this regard.

33 AEMC, 2019 Retail Energy Competition Review, 28 June 2019, p. 35.

that retailers generally advertise electricity and gas offers simultaneously and in similar forms. This may mean that where there is reduced prominence of conditional discounting for electricity, a similar reduction may be observed in the retail gas market.

QUESTION 4: ENERGY OFFERS NOT COVERED BY THE CODE

- (a) Do stakeholders consider gas offers should be subject to conditional discount limitations, in line with electricity offers?
- (b) How has the introduction of the Code impacted the prominence and magnitude of gas offers?
- (c) Do retailers expect conditional discounts to become a material issue in the ACT and/or Tasmania?

3.3

Solutions

3.3.1

Solutions raised by proponent

The proponent identified four solutions to regulate conditional discounting options. These are outlined below:

Option 1 - Customer screening

Using a principles-based approach recommended by the Thwaites Review.³⁴ This solution would require energy retailers to take reasonable steps to make conditional discounts offers available to customers whose needs and circumstances match the risk profile for conditional discounts.

The proponent noted that similar obligations exist for certain financial service providers. These providers are required to conduct lending responsibly by making reasonable inquiries about the customer's financial situation. This will enable the provider to make a decision regarding a suitable service given the customer's circumstances.

The proponent did not favour this solution because it expected that it would be hard to apply and enforce in practice.

The Commission notes (as set out in section 3.1.2) that a similar requirement already exists for hardship customers in section 44 in the NERL. Energy retailers are required to have a process for reviewing the appropriateness of a hardship customer's market retail contract in accordance with the purpose of their customer hardship policy.³⁵ Section 43 of the NERL also defines the purpose of a retailer's customer hardship policy to be "to identify residential customers experiencing payment difficulties due to hardship and to assist those customers to better manage their energy bills on an ongoing basis".³⁶

³⁴ Independent Review into the electricity and gas markets in Victoria, August 2017, p. 51.

³⁵ National Energy Retail Law (South Australia) Act 2011, s. 44 (f).

³⁶ Ibid, s. 43.

Box 1 outlines an example of a customer screening policy adopted in the telecommunications industry. This may align with the proponent's solution.

BOX 1: SCREENING OF TELECOMMUNICATIONS CUSTOMERS

The Telecommunications Consumer Protection (TCP) code provides consumer safeguards for mobile, landline and internet customers. The code is enforced by the Australian Communications and Media Authority (ACMA).

- Changes to the code in June 2019 will require telecommunications companies to run credit and income checks before offering post-paid plans worth more than \$1,000 a year or more than \$45 a month and explain the financial implications of the service offered.
- The objective of the changes is to ensure the consumers are in a position to meet the financial commitments of the contract while enabling companies to recover costs.
- When a provider concludes that a consumer would be unable to meet their financial obligations under the contract, they must advise the consumer of the outcome of the credit checks and provide the consumer with information about alternative products or services that may meet their needs, such as lower-cost contracts or pre-paid services.
- Civil penalties are in place for companies that breach the code.

Source: Communications Alliance Ltd, C628: 2019 Telecommunications Consumer Protections Code, July 2019.

Option 2 - Banning conditional discounts

The proponent raised the possibility of a ban on conditional discounts from retail electricity market offers. Prohibiting conditional discounts would address the confusion associated with multipart pricing and remove the risk of high priced penalties on vulnerable consumers.

The proponent noted that a ban on conditional discounts could result in retailers having limited tools to incentivise customers to pay bills on time. This might create further risks for retailer debt management, which might harm customers' long term interests in the form of higher energy prices when these are adjusted for additional risk.

However, it is also possible that increased limitations on conditional discounts would mean that energy retailers may have greater incentives to use different pricing strategies to attract customers. One retailer indicated that from 1 July, they would introduce a "loyalty incentive", offering customers that are with the retailer for a fixed period a higher guaranteed discount rate.³⁷

Option 3 - Simple percentage cap on conditional discounts

The proponent raised the option of conditional discounts being capped to a certain percentage. The proponent did not discuss how this percentage would be arrived at.

³⁷ Discussion with stakeholders, June 2019

The proponent noted that a simple cap may not reflect the individual circumstances of a particular retailer. For example, the costs of a consumer not meeting a pay on time or direct debit condition may be greater for certain retailers than for others.

Option 4 - Limit conditional discounts to reasonable costs to retailers

The proponent identified this option as its preferred solution. Under this solution the AER would issue a guideline determining reasonable costs a retailer might incur when a customer is unable to realise a conditional discount. The guideline would effectively set a cap for conditional discounts that can be put to customers. The proponent suggested that civil penalties would be required to incentivise compliance.

The proponent noted that the application of an AER guideline should allow for a reasonable level of flexibility in how retailers continue to design market products and allow the market and other stakeholders to help inform the restriction through consultation on the guideline.

Limiting conditional discounts to reasonable costs may allow for more efficient risk allocation than a complete restriction on conditional discounts. A retailer under this type of restriction is likely to be better able to manage consumer debt as it can pass through, or allocate, the reasonable costs of that debt to the customers that can manage the debt. At the same time, customers would not be faced with costs substantially above the risk incurred by the retailer because the discount would be limited to the costs.

A slight variation of this approach would be to enshrine the reasonable cost in the rules but not require the AER to produce a guideline. This approach may be preferred as it enables retailers, who are best positioned to understand their costs and their customers, to provide a potentially more accurate estimate of reasonable costs.³⁸ The AER could then include monitoring of conditional discount levels within its regular compliance and enforcement activities and request information from retailers where a conditional discount may be above reasonable costs.

QUESTION 5: SOLUTIONS

General questions:

- (a) Are there any alternative solutions that should be considered by the Commission?
- (b) What benefits and detriments have stakeholders identified on the options outlined by the proponent?

Implementation questions specific to different options:

Option 1

- (c) What systems and processes do retailers have in place to screen customers? What is the scale and effectiveness of these screening processes?

³⁸ This type of solution was put forward by the Essential Services Commission in their issues paper: ESC, Ensuring energy contracts are clear and fair, Issues paper, 5 June 2019, p. 24.

(d) What processes are in place by retailers to give *vulnerable* customers opportunities to shift from offers which are not suitable to their circumstances?

(e) What customer data/factors should retailers consider when determining the suitability of an energy offer to each customer? Would vulnerable customers easily be able to provide this information? What action should retailers take when the information cannot be supplied by the customer?

Option 2

(f) If conditional discounts were banned how would retailers manage credit risk?

Option 3

(g) Do stakeholders have views on the appropriate level of the simple price cap on conditional discounts? What methodology could be employed to determine this level?

Option 4

(h) If a reasonable cost limitation was imposed, should this limitation be enforced through an AER guideline or should this be left to retailers?

(i) Should the Commission determine that an AER guideline is the most appropriate instrument to determine "reasonable costs", which costs and factors should be included in the estimate?

(j) Should the Commission determine that retailers are best placed to determine "reasonable costs", are there any specific compliance or disclosure requirements necessary to satisfy the regulator of the accuracy of the estimate?

4 ASSESSMENT FRAMEWORK

4.1 Achieving the NERO

The Commission may only make a rule if it is satisfied that the rule will, or is likely to, contribute to the achievement of the national energy retail objective (NERO).³⁹ This is the decision-making framework that the Commission must apply.

The NERO is:⁴⁰

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 Commission must also, where relevant, satisfy itself that the rule is "compatible with the development and application of consumer protections for small customers, including (but not limited to) protections relating to hardship customers" (the "consumer protections test").⁴¹

Where the consumer protections test is relevant in the making of a rule, the Commission must be satisfied that both the NERO test and the consumer protections test have been met.⁴² If the Commission is satisfied that one test, but not the other, has been met, the rule cannot be made.

There may be some overlap in the application of the two tests. For example, a rule that provides a new protection for small customers may also, but will not necessarily, promote the NERO.

4.2 Making a more preferable rule

Under s. 244 of NERL, the Commission may make a rule that is different (including materially different) to a proposed rule (a more preferable rule) if it is satisfied that, having regard to the issue or issues raised in the rule change request, the more preferable rule will or is likely to better contribute to the achievement of the NERO.

4.3 Proposed assessment framework

The Commission will assess the rule change request against an assessment framework focussed on a consideration of consumers and the promotion of their interests in the long term.

The Commission is seeking stakeholder views on its proposed assessment framework which includes criteria to assess whether the proposed rules are likely to promote the NERO, namely the impact the rule has on:

- promoting competition

³⁹ Section 236(1) of the NERL.

⁴⁰ Section 13 of the NERL.

⁴¹ Section 236(2)(b) of the NERL.

⁴² That is, the legal tests set out in s. 236(1) and (2)(b) of the NERL.

- risk allocation
- administrative and implementation costs.

These principles are discussed in more detail below.

Promoting competition

Where feasible, providing for consumer choice in the provision of services generally leads to more efficient outcomes. Competitive markets which enable consumers to choose also tend to be more flexible to changing conditions because they provide incentives for participants to innovate and minimise costs over time.

Competition is a process by which inefficient costs are discouraged. It lowers the combination of supply-side and demand-side resources at any given moment in time, as well as through time. Competition provides incentives for market participants to provide service standards that consumers value, including with regard to price levels. Competition should therefore promote efficient levels of electricity consumption.

The proposed alternatives for regulation of conditional discounts will be assessed for how they facilitate consumer choice in service provision through competitive markets.

Risk allocation

Generally, the Commission considers that risks should rest with those parties best placed to manage them. Placing inappropriate risks on customers (or specific customer groups), who may not be best placed to manage these risks, is likely to result in higher prices if these risks cannot be managed and reduced over time. Conversely, placing risk with market participants (who may be better placed to manage them) will only be passed on to consumers in terms of higher prices where competition permits.

In this rule change request the primary risk allocation issue is whether retailers or consumers (and groups of consumers) should bear the risk of late payment and to what degree.

The Commission will consider solutions that facilitate a more efficient allocation of risk between market participants and consumers. The Commission will also consider whether existing "safety net" provisions are adequately protecting vulnerable customers and how solutions proposed may complement these.

From a retailer perspective, the Commission will closely consider how regulation of conditional discounting practices impact the ability of energy retailers to manage credit risk. For example, the Commission will consider the impact that lower incentives for customers to pay on time (and other conditions) will have on retailers' operations.

Administrative and implementation costs.

Changes to regulatory frameworks come with associated costs. These costs include both those imposed to implement change and the ongoing costs associated with new rules. These costs result from necessary changes to information technology systems, billing arrangements and other market process.

Any solutions raised by stakeholders need to be assessed for the most efficient implementation. This is necessary so that the implementation and ongoing costs, ultimately borne by consumers, do not exceed the benefits of introducing a solution.

The Commission will therefore consider the costs (both implementation and ongoing costs) associated with each option.

QUESTION 6: ASSESSMENT FRAMEWORK

- (a) Do you agree with the assessment framework outlined by the Commission?
- (b) Are there any other considerations the Commission should take into account?

5 LODGING A SUBMISSION

Written submissions on the rule change request must be lodged with Commission by 19 September 2019 via the Commission's website, www.aemc.gov.au, using the "lodge a submission" function and selecting the project reference code RRC0028.

The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated.

Where practicable, submissions should be prepared in accordance with the Commission's guidelines for making written submissions on rule change requests.⁴³ The Commission publishes all submissions on its website, subject to a claim of confidentiality.

All enquiries on this project should be addressed to Conrad Guimaraes on (02) 8296 0649 or conrad.guimaraes@aemc.gov.au.

⁴³ This guideline is available on the Commission's website www.aemc.gov.au.

ABBREVIATIONS

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
Commission	See AEMC
NEL	National Electricity Law
NEO	National electricity objective
NERL	National Energy Retail Law
NERO	National energy retail objective
NGL	National Gas Law
NGO	National gas objective