THE HON CHRIS BOWEN MP
MINISTER FOR CLIMATE CHANGE AND ENERGY

MS24-001337

Ms Anna Collyer
Chair
Level 15
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Dear ~~Ms Collyer~~ Anna

Please find attached a rule change proposal to amend the National Energy Retail Rules to remove grandfathering arrangements that allow some legacy contracts to include unreasonably large conditional discounts.

This necessary change was recommended by the Energy and Climate Change Ministerial Council (ECMC) which, on 19 July 2024, agreed that I submit the attached rule change request to the Australian Energy Market Commission (AEMC) in my capacity as Chair of ECMC. This rule change request forms the final part of a broader package of rule change proposals to amend the National Energy Retail Rules (NERR) which I submitted to you separately on 12 August 2024.

The proposed rule seeks to ensure that any contract including a conditional discount is required to meet the requirements for conditional discounts set out in the NERR, following the AEMC's 2020 *Regulating conditional discounting* rule change process. It proposes to remove grandfathering arrangements allowing for some consumers to remain on legacy contracts with unreasonably large conditional discounts, in line with the ACCC's recommendation in its December 2023 *Inquiry into the National Electricity Market* report.

I endorse this rule change request and ask that the AEMC progress with its initiation.

Yours sincerely

CHRIS BOWEN

ATTACHMENT A

Removing unreasonable conditional discounts
Request to make a rule

Name and address of the person making the request

The Honourable Chris Bowen MP
Minister for Climate Change and Energy
Parliament House
Canberra ACT 2600

Statement of issue

Some retailers offer high priced energy plans, with large discounts that only apply if a customer meets certain conditions (e.g. pay-on-time or direct debit discounts), known as 'conditional discounts'. If consumers do not meet these conditions, they may be subject to large costs in the form of high underlying energy prices.

From 1 July 2020, the Australian Energy Market Commission (AEMC) implemented a rule change which limits conditional discounts and conditional fees to the "reasonable costs" the retailer is likely to incur when payment conditions are not met (Regulating conditional discounting). However, this rule only applies to new contracts entered into after 1 July 2020, meaning customers on plans which commenced before this date may still face unreasonable costs.

In deciding to limit this rule to new contracts only, the AEMC considered that:

- exposure and experience to the risks and rewards of conditional discounts means that consumers on existing contracts with conditional discounts are more likely to be able to make an informed decision
- the introduction of the Default Market Offer (DMO) would improve comparability of plans, making it unlikely that engaged consumers would stay on plans with conditional discounts
- strengthened hardship guidelines from October 2019 mean that 'existing consumers that frequently miss conditional discounts and are in hardship should be moved onto more appropriate tariffs by their retailers'.

However, the Final Determination also found that:

> *…many consumers have not been well-placed to meet contract conditions, and that an imbalance in risk allocation between parties exists. Where risk allocation between retailers and consumers is no longer balanced or efficient, targeted restrictions on the level of conditional contract terms may be appropriate. Where such a restriction is set at reasonable costs, this approach would not unduly limit retailers' pricing freedom, while also providing a degree of protection for consumers* (p i).

In their 2023 analysis, the Australian Competition and Consumer Commission (ACCC) assessed that these types of concerns remain and, given current cost of living pressures, large conditional discounts which are beyond reasonable costs unnecessarily expose customers to the risk of higher prices. This is supported by analysis of retailers' data, which shows that customers on legacy market offers with large conditional discounts – who do not achieve their discounts – risk paying significantly more than the default offer.

To support this analysis, the ACCC collected data on flat rate electricity prices charged to approximately 5 million residential customers between 1 August 2022 and 1 August 2023. About 6% of residential customers on flat rate market offers paid calculated annual prices 25% or more above the default offer in 2022, assuming that conditional discounts were not achieved (for those who had them). Further, the customer-weighted average conditional discount for this group was 29%, indicating they have not changed plan or retailer in the last 3 years since the AEMC's implementation of the new rule in 2020.

This indicates there is a proportion of consumers on legacy plans with conditional discounts higher than that deemed reasonable by the AEMC Final Rule of 27 February 2020 (and ESC Final Decision of 28 February 2020).

That these legacy plans remain in the market 4 years after the AEMC's decision demonstrates market forces have been insufficient to drive customers on these contracts toward lower risk 'reasonable cost' conditional discount contracts, or other contracts.

The ACCC's Inquiry into the National Electricity Market report from June 2024 stated that 91% of residential customers and 85% of small business customers in the sample on plans with conditional discounts achieved the discount.

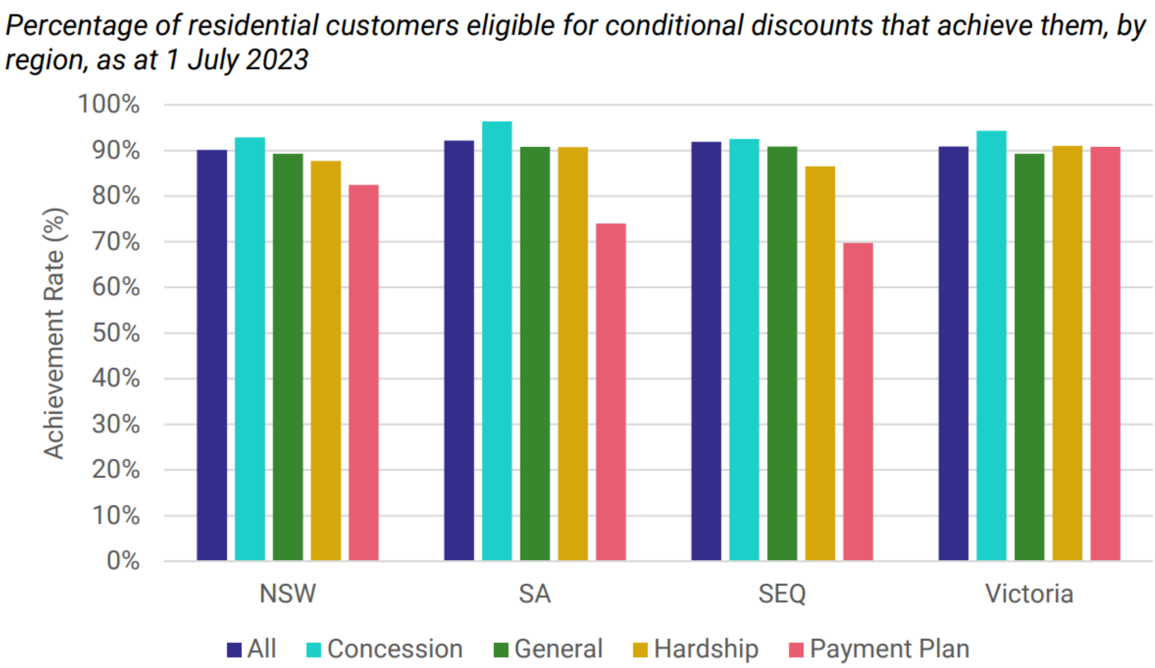

Figure 1: ACCC's Inquiry into the National Electricity Market June 2024 report on achievement rates of conditional discounts.

Figure 1 demonstrates that achievement rates for customers were fairly constant across regions however, it did vary depending on the type of customer. While most residential customers achieve the conditional discount, hardship customers and customers on payment plans were more unlikely to achieve the discounts in the data. The non-achievement of the conditional discount imposes a penalty on customers, which would disproportionately affect a vulnerable customer compared to an 'average' customer.

Using a residential customer on a flat rate tariff in the Endeavour Energy distribution region as an example, the ACCC assessed the extent to which a customer is financially impacted for not meeting a significant conditional discount.

Using the Default Market Offer's model annual usage assumptions, a customer on an offer with a **20% conditional discount** that is priced **25% above the Default Market Offer** would pay an annual price of $2,228 (provided they met the relevant conditions in each period). However, if the customer was not to meet the relevant conditions on the 20% conditional discount, they would pay a significantly higher price on their electricity bill, especially in instances where the conditions were frequently not met.

Assuming that a customer pays for electricity on a quarterly basis, the ACCC assessed the differences in price outcomes if a conditional discount was not met:

Frequency a consumer achieves their conditional discount	Annual price of their electricity bill	Cost of not achieving their conditional discount
100%	$2,228.00	$0.00
75%	$2,367.25	$139.25
50%	$2,506.50	$278.50
25%	$2,645.75	$417.75
0%	$2,785.00	$557.00

ACCC Inquiry into the National Electricity Market (December 2023), Box 3.2, page 62.

In December 2023, the ACCC recommended policy makers should investigate how best to reduce the number of customers on legacy plans with large conditional discounts as a matter of priority. The June 2024 report's findings additionally support this recommendation. This rule change request responds to this recommendation.

Background

The ACCC's Inquiry into the National Electricity Market (p 9), released in December 2023, found that consumers who do not regularly engage in the market experience higher prices – with this impacting a significant number of customers who remain on plans with large conditional discounts and high underlying prices. The ACCC's above recommendation originated from this inquiry.

It is noted that when consulting on the proposed rule to regulate conditional discounting in 2020, some stakeholders expressed concern about application of the rule to existing contracts. Considering the ACCC's recent findings that there are a number of these contracts still in the market, a strong case can be made to support the AEMC considering applying the rule to contracts that existed prior to the 2020 rule change taking effect, and before those contracts are renewed or varied.

Description of the proposed rule change

This rule change request seeks to do this by removing the grandfathering arrangement in the AEMC's Final Determination (Regulating conditional discounting, Part 4.5.4) to ensure that any conditional discounts are limited to reasonable costs. This could be achieved by either:

- amending Rules 46C and 52B of the National Energy Retail Rules (NERR), inclusive of any consequential rule changes, to ensure no contract or offer in the market can include a conditional offer higher than reasonable costs, or
- as the exception for energy plans prior to 1 July 2020 is captured under Rule 2 in Schedule 3, Part 12B, the AEMC may be able to revoke this exception without altering the current rules.

Transition considerations

The intent of the rule change is to ensure consumers are not paying more than the price they would pay if they met the conditions of their contract. There may be issues for consumers if a retailer does not have an energy plan available at the conditional price. The AEMC will need to consult retailers to determine how the rule could be implemented. Retailers could consider implementation pathways such as the following:

- move customers onto a plan made available after commencement of the AEMC's final determination (Regulating conditional discounting) where the new conditional price is equal to or better than their existing conditional price, or
- keep their customers on their existing plans but reduce the conditional discount value (and high underlying energy prices) such that the conditional price and all other elements of plan remain the same.

This approach would provide retailers with flexibility to choose the less burdensome option while fulfilling the intent of the proposed rule change.

It is recognised that retailers will need to engage with consumers to obtain their explicit informed consent if they are being moved to a new plan or to provide notice if there are changes to the conditional discount value and underlying tariff. The AEMC will need to consult with retailers and consider what a reasonable transition timeframe would be for retailers to either move customers to new plans or to reduce the conditional discount value of existing plans.

How the proposed rule change will address the issue

The proposed rule change will limit large conditional discounts to reasonable costs as expressed by the AEMC – ensuring consumers are not subject to unfair costs. The change will also overcome current inequities between consumers on plans prior to 1 July 2020 and after this date, by limiting all plans with conditional discounts to reasonable costs.

Retailers are already broadly familiar with the requirement, and the changes that would be needed to implement the rule change, given the rule already applies to all new contracts.

How the proposed rule change will or is likely to contribute to the achievement of the National Electricity Objectives

The National Energy Retail Objective (NERO), set out in the *National Energy Retail Law* 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:
>
> a. price, quality, safety, reliability and security of supply of energy; and
> b. the achievement of targets set by a participating jurisdiction—
>   i. for reducing Australia's greenhouse gas emissions; or
>   ii. that are likely to contribute to reducing Australia's greenhouse gas emissions."

The relevant aspect of the NERO for this request is the price of energy services in the long-term interests of consumers of energy.

The proposed rule change advances the NERO by ensuring consumers do not face unreasonable costs, in the form of high underlying energy prices, if conditions of their energy plan are not met. Consumers will have a clearer understanding of the costs they are likely to face, and this amendment will reduce risk of shock from high underlying prices.

Further, the Government's rule change request which led to the AEMC's 2020 Final Determination noted the change as:

> *"fundamentally, promoting the efficient operation of energy, electricity and natural gas services in the long term interests of consumers. The proposal aims to improve the transparency of retail energy pricing arrangements. Complex pricing structures have been found to serve as a significant barrier to effective consumer engagement in the market and can reduce the price benefits household and small business receive from shopping around. Improving transparency and simplicity of pricing structures is therefore supportive of effective competition.*
>
> *The rule change enables consumers to make more empowered and informed decisions noting conditional discounts have the potential to confuse consumers about the benefits of their offer and their expected bills. The proposal may also ensure many consumers are able to better plan for their energy bills by limiting potential exposure to unforeseen costs and disproportionate late fees to the extent possible, in this way curbing the potential for bill shock. The proposed rule encourages improvements in equity, consumer understanding of, and confidence in, the retail energy market, and is clearly in the long-term interests of consumers."*

As this new proposal seeks to extend the 2020 rule change to apply to existing contracts, these contributing factors are also applicable.

Expected costs, benefits and impacts

Expected benefits

Consumers will benefit from not paying unreasonable costs if they do not meet conditions of their energy plans. It will also provide consumers with certainty over the costs they pay and reduce risk of shock from high underlying prices.

This will act to promote the long-term interests of consumers by reducing the risk of unreasonably high transaction costs associated with engaging with the market.

Expected costs

The proposed rule change would impose a cost to retailers operating in National Energy Retail Law (NERL) jurisdictions, by requiring them to remove conditional discounts with higher than reasonable costs. There is a risk that any resulting loss in revenue may be passed on to retailers' broader customer base. However, it is anticipated that cost-spreading would be subject to competitive pressures.

There may also be a small cost to retailers of providing evidence to the Australian Energy Regulator (AER) regarding the value of the conditional price discount. The AEMC will need to assess and consider these costs. The cost posed by the reporting obligation could be outweighed by the enduring benefit offered to consumers by way of better price discovery and working to ensure the aggregate effect of conditional discounting more closely reflects the efficient price to serve.

There is a risk that removing large conditional discounts may reduce consumer engagement in the short term. There could also potentially be a cost to consumers on plans with conditional discounts where the non-compliance cost is unreasonable, but they comply with the conditions. Those consumers able to comply with the conditions would lose access to a plan that they were benefiting from.

Expected impacts

Conditional discounts incentivise consumers to act to meet their condition – for example, paying on time. Under the proposed rule, retailers will still be allowed to offer conditional discounts, but the quantum of such discounts will be limited by reference to the reasonable costs to the retailer of a consumer's failure to meet the relevant conditions. Limiting the quantum of the discount should maintain an incentive for customers to, for example, pay on time or by direct debit, while ensuring retailers can recoup the reasonable losses for non-compliance.

Consumer advocates, community-based organisations and market bodies approached in early targeted consultation were supportive of the proposal to remove conditional discounts with unreasonable non-compliance costs. Retailers pointed to some consumers placing a high value on discounts and the need for consumers to be able to exercise choice.