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NATIONAL ENERGY RETAIL AMENDMENT (REGULATING CONDITIONAL DISCOUNTING) RULE

Submission to the Australian Energy Market Commission

ABOUT US

Set up by consumers for consumers, CHOICE is the consumer advocate that provides Australians with information and advice, free from commercial bias. CHOICE fights to hold industry and government accountable and achieve real change on the issues that matter most.

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INTRODUCTION

Consumers need clear and fair pricing in the energy market. The Australian Energy Market Commission (AEMC)'s draft National Energy Retail Amendment (Regulating Conditional Discounting) Rule presents an opportunity to help consumers get the clarity and fairness they deserve. The AEMC's updated Rule takes into consideration the harms caused by unfair discounting practices, but does not provide enough consumer protections to prevent these harms from occurring in future.

Conditional discounts are a marketing tactic that tricks consumers into thinking that they are getting a better deal for their energy, while exposing them to harm. Retailers are taking advantage of consumers who experience confusion and inertia in a complex marketplace. They are misleading customers into paying more for energy by making it difficult to compare offers and offering customers contracts with conditions that they cannot meet. We know this practice is rife: of the 5,940 gas and electricity retail market offers available in March 2018, 80 percent were offered with discounts.[1]

Conditional discounts can be characterised as 'late payment penalties' because they result in a substantial cost to consumers, who are already paying some of the world's highest prices to access energy. Pay on time discounts can be as high as 43% of usage charges, which can translate to hundreds of dollars' worth of late fees if a customer pays their bill just one day late. Residential customers cannot pay their bills before the due date 27% of the time - a number that grows to 59% of people experiencing hardship.[2]

Conditional discounts are by design a misleading marketing tactic and by nature are unreasonable. CHOICE supports the ban of conditional discounts. Any late fees that energy companies can charge should be restricted to a singular, low, capped late fee that is determined by the Australian Energy Regulator (AER).

CHOICE's comments will focus on the regulation of conditional discounts for electricity, but CHOICE supports similar interventions to be enforced in the gas market.

Recommendations

[1] AEMC (2018), *Retail Competition Review - Final Report*, Sydney, pg8.

[2] ACCC (2018), *Retail Electricity Pricing Inquiry - Final Report*, Melbourne, pg264.

1. The AEMC should ban conditional discounts in the energy market and any discounts offered to consumers should be guaranteed.
2. The AEMC should direct the AER to determine the amount of a singular, low, capped late payment fee. Regulators should draw on the amount charged for late payment by other utilities to determine what this fee should look like.
3. The AEMC should design conditional discounting regulation to benefit all consumers. The AEMC should assume that all households can be harmed by conditional discounting practices and should not assume that people who do not access a hardship scheme are able to pay exorbitant late penalties.

Conditional discounting practices are designed to be detrimental

Conditional discounts are a marketing tactic that tricks consumers into thinking that they are getting a better deal for their energy, while exposing them to harm. In many cases, the discount figure has not corresponded to similar savings in retail electricity bills, creating a distorted energy market in which consumers struggle to select energy offers that meet their needs.[3] CHOICE agrees with the AEMC's previous suggestion that 'price dispersion, which sees considerable price differences for the same service in the energy market, is driven by discounting practices' rather than market segmentation based on customer needs and preferences.[4]

CHOICE's first preference is that conditional discounts are banned altogether. Any discounts that are offered to consumers should be guaranteed. Conditional discounts are designed to unfairly penalise people who cannot pay their bills on time and a policy short of a complete ban on such offers will continue to enable retailers to harm consumers.

Changes to the Electricity Retail Code of Conduct

The introduction of the Default Market Offer (DMO) through the Electricity Retail Code of Conduct (the Code) places restrictions on the way retailers can advertise conditional discounts. The two most relevant changes are:

- Electricity retailers must not advertise a conditional discount as the most conspicuous price-related matter in the advertisement; and
- 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.[5]

These changes will be helpful for people switching. For consumers who switch between energy offers, discounts are front of mind, with 84% of Victorian consumers considering discounts 'very important' in their decision to switch retailers.[6]

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[3] Australian Energy Market Commission (2019), National Energy Retail Amendment (Regulating Conditional Discounting) Rule Draft Determination, Sydney, p4.
[4] AEMC (2018), *Retail Competition Review - Final Report*, Sydney, pvi.
[5] Ibid. p4.
[6] Newgate Research (2017), Consumer research for the Victorian Government's review of the state's energy market, prepared for the Victorian Department of Environment, Land, Water and Planning, May 2017, slide 23.

Though these changes are positive, they do not go far enough - they do not prevent retailers from providing people with harmful offers. They also do not help people currently affected by conditional discounts. It is very likely that people currently on offers with conditional discounts may remain at risk of late payment penalties until an existing contract's benefit is reset, or the term of the contract is extended or renewed.[7]

Disclosing conditional discounts fails to address the issue at hand. Low conditional discount realisation rates indicate that a significant number of conditional discount customers do not accurately anticipate their ability to fulfil contract conditions.[8] Even with greater transparency in the advertisement of conditional discounts, people will continue to overestimate their ability to pay. Research into the impact of behavioural biases in the energy market supports this and shows that people will place a high value on immediate rewards at the expense of their long-term intentions.[9] An additional concern is that more transparent advertising of conditional discounts may lure people into a false sense of security by creating a perception that these discounts have been made considerably safer. Without a ban on conditional discounting practices consumers will continue to be at risk of substantial harm.

Recommendation 1

1. The AEMC should ban conditional discounts in the energy market. Any discounts offered to consumers should be guaranteed.

Designing effective regulatory solutions

If conditional discounts are to continue, it is important that they are capped at a low amount set by the regulator. The AEMC has suggested that the introduction of the Default Market Offer 'may limit the magnitude of conditional discounts and, by extension, the increased prices customers pay when they miss discount conditions.'[10] Though the Default Market Offer has reduced energy prices in the NEM, CHOICE maintains that the top-down design of the Default Market Offer is too similar to the design of previous standing offers and does not effectively communicate the actual costs of providing energy as an essential service to consumers. We believe that this approach is less effective at driving down costs and achieving fair default offer

[7] Australian Energy Market Commission (2019), National Energy Retail Amendment (Regulating Conditional Discounting) Rule Draft Determination, Sydney, p10.
[8] Australian Energy Market Commission (2019), National Energy Retail Amendment (Regulating Conditional Discounting) Rule, Sydney, p5.
[9] Australian Energy Market Commission (2016), *Applying behavioural insights to regulated Markets*, Prepared by the Behavioural Insights Team, London, p10.
[10] Ibid. p7.

prices than what was put forward by the ACCC as part of their *Retail Electricity Pricing Inquiry*.[11] As a result, the impact of the Default Market Offer on the size of conditional discounts is likely to be minimal.

Capping conditional discounts

Any late payment penalties that are incurred by consumers should be limited to a low, capped fee that is determined by the AER. CHOICE's first preference is that this fee is restricted to a total dollar amount, as opposed to a percentage amount. This would provide energy customers with a clear understanding of the penalty to expect if they cannot pay their bill on time and will restrict the penalty to a small, capped amount. Retailers would still retain the choice to charge a lower fee or no fee at all.

Industry are very likely to exploit a situation where the AER enshrines a reasonable cost to retailers but does not produce clear guidelines about this cost.[12] The definition of 'reasonable' in the context of late payment fees has been tested by ANZ, who defended their dishonour fees and over-limit fees on credit cards against a class action in 2014. The decision upheld the bank's position that the size of late payment fees could be justified by a range of business activities.[13] This outcome gives far too much flexibility to businesses to bundle high costs into a late payment fee in a way that harms customers.

Retailers cannot be left to solely determine what a "reasonable cost" is - they need more guidance and limits. No late fee that is inflicted on consumers as a result of a forgone conditional discount is a 'reasonable' fee. Conditional discounts are by design a misleading marketing tactic and by nature are unreasonable. Retailers have been deliberately designing unfair energy contracts to exploit consumers. Though enshrining a 'reasonable cost' requirement in the rules would narrow the ways in which retailers can harm consumers, it will not be enough to effectively prevent harm. The AEMC should ensure that any late payment penalties incurred by consumers are limited to a low, capped fee determined by the AER, so that retailers cannot exploit regulatory loopholes to the detriment of consumers.

Recommendation 2

[11] ACCC (2018), *Retail Electricity Pricing Inquiry - Final Report*, Melbourne, p252
[12] Australian Energy Market Commission (2019), *National Energy Retail Amendment (Regulating Conditional Discounting) Rule*, Sydney, p.11.
[13] Barnett, Katy (2015), 'Paciocco v Australia and New Zealand Banking Group Ltd: Are Late Payment Fees on Credit Cards Enforceable?', *Sydney Law Review*, Vol.37(4).

2. The AEMC should direct the AER to determine the amount of a singular, low, capped late payment fee. To determine what this fee may look like, regulators should draw on the amount charged for late payment by other utilities.

Recommendation 3

3. The AEMC should design conditional discounting regulation to benefit all consumers. The AEMC should assume that any and all households can be harmed by conditional discounting practices, and should not assume that people who do not access a hardship scheme are able to pay exorbitant late penalties.

Supporting people experiencing vulnerability

Large numbers of households continue to be penalised for not being able to pay their bills on time and individual penalties can be hundreds of dollars. The March 2019 *Monitoring of supply in the National Electricity Market* Report lists a recent example of a market offer contract in which a household can receive a “34 per cent discount off the entire bill. If conditions are not met, then the annual price amount increases by $859 to $2528, which is $364 more than the most expensive offer with no discount attached ($2164).”[14]

Conditional discounting practices are still causing substantial harm, and retailers’ recent actions to reduce the number and the size of conditional discounts on the market have not done enough to protect consumers when they access this essential service. One missed conditional discount can have severe impact, and this must be prevented through effective regulation.

For a single adult with no children, the poverty line was a very frugal (50% of median household disposable income) $433 a week ($353 after housing costs are deducted) in 2015-16.[15] CHOICE has observed missed discounts adding over $560 in late payment penalties to a household energy bill. In instances where a late payment penalty is as high as $560, the additional penalty alone, excluding usage and daily supply charges, already exceeds the weekly income of an individual living below the poverty line.

Excessive late payment penalties can not only exacerbate people’s experiences of vulnerability, but precipitate them. Anyone can be vulnerable, and vulnerability can be permanent, temporary, or situational. A *single* missed energy payment could result in hundreds of dollars worth of late

[14] Ibid. p.ii. Note: Assumes a consumption level of 1200 kWh per quarter based on the AER’s annual average consumption figure of 4811 kWh for Victoria
[15] Ibid. p21.

fees, which may suddenly push a household into financial vulnerability and in some circumstances, a cycle of debt. Given this, changes to conditional discounts should assume that many people experiencing vulnerability may not be easily identifiable as people who cannot afford to pay their energy bills.

Any changes to conditional discounting regulation should be designed to benefit all consumers in the National Energy Market (NEM). The AEMC should assume that all households can be harmed by conditional discounting practices, and should not assume that people who do not access a hardship scheme are able to pay exorbitant late penalties.