Australian Energy Market Commission Forum

Presentation: Jo Benvenuti, Executive Officer, CUAC

Topic: The Consumer Action /CUAC Rule Change Solution

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Venue: Novotel Melbourne on Collins

- Gerard Brody (Consumer Action) has outlined the problems that result from Rule 46 of the National Energy Retail Rules (NERR) which allows retailers to unilaterally vary tariffs under market retail contracts, including fixed term contracts.

- CUAC and CALC have proposed a new rule, 46A: a simple solution that during a fixed term contract, the tariffs and charges the customer pays are fixed, and do not change.

- Our solution has the following benefits:
  - It more efficiently allocates **risk**. An established economic principle is that the party in the best position to minimise the costs associated with a particular risk should bear that risk. There are different factors that affect energy prices, including wholesale costs, network costs, government charges, and retailer costs. The ability of retailers to manage these costs varies, but in all cases it is cheaper for retailers to manage these risks than for consumers – even where those risks are out of the retailers' control. Retailers are always *relatively* better at managing energy risks than consumers – it's what they do.

  - It recognises community **expectations**. Consumers expect the terms of a fixed term contract to stay the same during the life of the contract – that's the whole point of *having* a contract! CUAC research in 2012 found only around half of Victorian consumers (53%) knew energy retailers could change prices in the middle of a contract, but 94% supported removing their ability to do so.

- The breach of these expectations plays heavily into low levels of **trust** and perceptions of **fairness**. As Gerard has explained, energy markets are complex and effective choice is difficult. With more certainty around the prices consumers face in a contract, they would participate more confidently in the market, and have greater perceptions of trust and fairness.

- Our solution recognises the **limitations of consumers in the complex energy market**. We all want better informed, more confident consumers. But it's clear that the current system is extremely complex, In Victoria as an example, on the government's My Power Planner comparator, there are 3,500 electricity tariffs available at any one time. When a consumer enters their specific consumption details they will typically then access 100 - 250 offers that apply to their unique situation.

- While some retailers offer "rate freeze" contracts, it is not clear that consumers understand their point of difference – i.e. that other fixed term contracts *don't* fix rates. Our solution recognises the **lessons from behavioural economics** about barriers to effective consumer choice, and would reduce search costs and transaction costs.

- Our solution **addresses a significant risk to effective competition and the long term interests of consumers.** It is not in the long term interests of consumers to have the experience of engaging in the market only to find that the goal posts have shifted and prices have changed in what they thought was a fixed deal. Why would they search again for another deal when there is nothing preventing this happening all over again? We believe the risk to the market is that customer participation will reduce over time as they lose trust in the market itself.

Counter-arguments/Problems with alternative solutions

We have examined the views put to the AEMC in response to our proposal and I want to respond to some of them up front.

"You will limit competition and innovation"

Our solution does not ban flexible or variable price contracts, it simple recognises that consumers don't want or expect variable prices in fixed term contracts. Small retailers have proven (in Victoria) that they are able to offer fixed term, fixed price contracts, or do without them – we don't believe our rule would make it significantly more difficult for new retailers to enter the market, or limit product innovation. If your 'product innovation' revolves around raising prices when consumers don't expect you to or in a way they think is unfair, we'd be better off without it.

"You will force up prices"

The threat is that retailers will charge a risk management premium. We acknowledge that there might be an initial jump, but it should be small and shouldn't lead to future price rises. Our solution really just provides for greater transparency, less bill shock, more salient price rises, more appropriate contract choices, and confidence in a market that does what it says in the long term – which we believe will assist consumer choice and help put downward pressure on prices.

"A fact sheet and no exit fees should suffice."

To that we say information is not sufficient: as Dr Paul Harrison has explained, consumers suffer from barriers including choice paralysis, incomplete understanding/limited capacity, bounded rationality, and inertia. Contracts with better information would still be inefficient from a risk perspective to address the problems we have identified.

- Wallis: only 55% of consumers check prices after signing contract.

Conclusion: It's what consumers want

Our reason for starting the rule change process was very simple: we asked consumers what they thought about unilateral price variation, and the overwhelming response was that they thought it was unfair, and wanted it stopped. This is the genesis of our solution. Our solution makes sense on the grounds of efficiency, and trust, and consumer protection, but it's also what consumers expect and what they've told us they want.