



VCOSS response

ACCC Retail Electricity Pricing Inquiry: Preliminary Report

November 2017

Introduction

VCOSS welcomes the Australian Competition and Consumer Commission (ACCC) preliminary report on retail electricity pricing. VCOSS is engaging with the inquiry from the perspective of Victorian electricity consumers, particularly people on low incomes and people experiencing vulnerabilities relating to disability, age, housing conditions and other factors. We therefore comment in this submission on areas of further analysis and potential regulatory reforms relevant to the Victorian retail market.

We note the ACCC's final report will be delivered in June 2018, by which time we expect the Victorian government will be beginning to implement any recommendations it accepts from the report of the Independent Review Panel on electricity and gas retail markets in Victoria.¹ To the extent possible, we ask the ACCC to consider how any reforms adopted by the Victorian government interact with the ACCC's final analysis and recommendations.

Final report analysis

We welcome the depth of analysis in the preliminary report and the matters flagged for further review. Outlined below is the particular analysis we would like to see in the final report.

Retail costs and margins

The ACCC has found retail costs and margins are highest in Victoria in both percentage and dollar terms, with retail costs comprising almost 20 per cent of the bill, and the retail margin comprising 9 per cent of the bill. The ACCC suggests competition has not had a significant effect on curtailing retail costs in Victoria, and has found customer acquisition costs were relatively higher in Victoria than other states over the period examined.² We seek the ACCC's views on the particular features of the Victorian market that are producing higher retail costs and margins than other NEM jurisdictions, including any role played by:

- The complexity of the Victorian electricity market and lack of price transparency, and whether this results in less competitive pressure on retail costs and margins.
- The particular costs of competition in Victoria.

¹ Professor John Thwaites, Patricia Faulkner AO and Terry Mulder, *Independent Review of the Electricity & Gas Markets in Victoria*, August 2017.

² Australian Competition and Consumer Commission, *Retail Electricity Pricing Inquiry: Preliminary Report*, 22 September 2017, 73.

- The costs of wholesale electricity acquisition for the Victorian retail market—are there any factors leading to relatively higher costs for Victorian retailers, including any greater wholesale price volatility and associated hedging costs?
- The costs of complying with a different regulatory regime in Victoria.

We are particularly interested in the ACCC's analysis of a) costs to serve and b) costs to acquire and retain customers. The preliminary analysis shows costs to serve are the larger component of retail costs at around twice the size of costs to acquire and retain, and that any decrease in costs in recent periods is largely due to a downward trend in costs to serve.³

We look forward to the final analysis of these different costs, and request specific analysis of whether retailers are likely to be able to achieve further efficiencies in costs to serve. This is important from a Victorian perspective because of the Independent Review Panel's recommendation for a regulated 'Basic Service Offer' that does not include customer acquisition and retention costs, and is based on the efficient cost to run a retail business.⁴

The ACCC's analysis could assist stakeholders to understand: a) the extent to which removal of acquisition and retention costs will reduce the overall price; b) efficient costs to serve; and c) differences in cost proportions among retailers (given ACCC analysis shows smaller retailers typically have higher costs to acquire and retain).⁵

We also request the ACCC's analysis of whether the costs to acquire and retain customers are offset by price savings for customers in a competitive market.

Passing on wholesale cost reductions

The preliminary analysis shows wholesale costs were relatively flat in nominal terms from 2007-08 to 2015-16, and decreased in real terms. Despite this, average Victorian residential retail prices on a cents per kWh basis increased by 44.2 per cent in real terms over the same period.⁶ VCOSS is interested in ACCC analysis of the factors that constrain wholesale cost reductions being passed on to customers, and whether price regulation (such as price caps or benchmarking that tracks wholesale pricing) or other regulatory reforms could help ensure retail pricing reflects wholesale pricing.

Distribution of energy offers and pricing—what are low-income and vulnerable households paying for electricity?

We are very pleased the ACCC is collecting data on what people are actually paying for electricity and will present this in the final report. In the view of VCOSS and its members, it is critical for this analysis to include, to the greatest extent possible, a socio-economic analysis of offer types and pricing among different household groups, including those on standing offers, different types of market offers, and 'off-market' offers. To inform good policy-making, it is important we learn about the distribution of offer types and pricing among:

- low-income households
- social and private renting households and owner-occupied households

³ Ibid 74.

⁴ Professor John Thwaites, Patricia Faulkner AO and Terry Mulder, *Independent Review of the Electricity & Gas Markets in Victoria*, August 2017.

⁵ Australian Competition and Consumer Commission, *Retail Electricity Pricing Inquiry: Preliminary Report*, 22 September 2017, 74.

⁶ Ibid 41, 76.

- different age groups
- households in regional and urban locations
- households in retailers' hardship programs or on payment plans.

Without this information it is more difficult to develop regulatory strategies to assist low-income and vulnerable households, and to assess the merits of regulatory reforms that may cause a redistribution of costs among households.

Overcoming complexity and making electricity more affordable

The ACCC notes an 'effective retail market is founded on engaged customers that have the ability to consider available options and shop around, thereby driving competition between retailers'.⁷ We have doubts about whether wide-scale engagement can be achieved in the electricity market, given entrenched barriers to participation among many low-income and vulnerable households, including digital exclusion, language and communication barriers, severe personal stress and competing household demands that make engaging with the energy market a low priority or an impossibility.

More broadly, it is likely energy will remain an inherently difficult service for most people to understand, due to the complexity of energy unit pricing and tariffs, and the intangible nature of energy. Tariffs could become even more complex as the energy market transitions.

We comment below on some of the reform considerations the ACCC has highlighted.

Comparison rates

Significant regulatory reforms are required to help achieve a more effective retail market, including marketing actual pricing to customers (rather than confusing headline discounts), and creating a marketplace for comparing energy offers (online government comparator tools have not achieved this due to low rates of use). We therefore welcome the ACCC's discussion of comparison or reference pricing. For comparison/reference pricing to be meaningful and create price transparency, this form of pricing will need to become standard across all forms of electricity marketing and not just be included on the bill.

Brokerage and automated switching services

Another way of tackling a lack of price transparency and comparability is to introduce an independent brokerage service for residential customers, as recommended in VCOSS's first submission to this inquiry.⁸

We are also interested in any role an independent broker could play in offering automated switching services. While we welcome the ACCC's consideration of third party automated switching services,⁹ we are concerned commercial switching services have the potential for poor customer outcomes in a similar way to commercial online comparison tools; for example, if commercial switching services were to accept commissions from energy retailers

⁷ Ibid 126.

⁸ Victorian Council of Social Service, *Retail electricity supply and pricing: Submission to the Australian Competition and Consumer Competition inquiry*, July 2017.

⁹ Australian Competition and Consumer Commission, *Retail Electricity Pricing Inquiry: Preliminary Report*, 22 September 2017, 137-138.

or have ownership interests that compromise the service. VCOSS considers it preferable to investigate an independent, government-backed automated switching service.

We also ask the ACCC to consider the feasibility of an automated switching service that not only transfers customers based on price, but offers information about service quality.

Pay-on-time discounts

The ACCC 'considers it likely that the trend towards pay on time discounts was initially a response by electricity retailers to regulation banning or capping late payment fees'. We agree with this analysis, and the ACCC's observation that the size of many discounts does not appear to reflect the actual costs savings to energy retailers.¹⁰ We encourage the ACCC to consider a similar recommendation to that made by Victoria's Independent Review Panel, to cap the costs incurred by customers for failing to meet offer conditions such as pay-on-time discounts, and for this cap to not be higher than the reasonable costs to the retailer of non-compliance. The current 'penalties' for not paying on time are likely to far exceed the actual business costs of late payment. These excessive costs are particularly detrimental to people on low, unpredictable incomes who face entrenched barriers to paying on time.

In addition to capping costs for not meeting pay-on-time conditions, regulatory reforms should tackle the wider issue of headline discounts undermining competition. Pay-on-time discounts are symptomatic of a complex, dysfunctional market with little price transparency and comparability. As the ACCC's analysis shows, discounts can be used as a deliberate tool of obfuscation to hide inflated, uncompetitive pricing.¹¹ Important reforms to tackle this practice include the introduction of comparison/reference pricing, and market-wide brokerage and switching services to drive competition on actual pricing and restrict the potential for new forms of ambiguous and potentially misleading marketing.

Lower-priced energy offer for low-income and vulnerable households

We note the ACCC is considering whether retailers should be required to provide a lower-priced tariff, with no conditional discounts, to vulnerable customers, concession card holders and people in hardship programs. This could be provided on an opt-out or opt-in basis.¹²

VCOSS has previously recommended the creation of a targeted low-cost tariff for groups such as concession card holders, given the best market offers can include features that effectively exclude some people on low incomes, such as pay-on-time and direct debit conditions, and use of online-only retail services.¹³ The ACCC's review also shows:

Many retailers actively seek to maximise the number of 'high value' customers and minimise potentially 'low value' customers. When it comes to acquiring new customers, many retailers run credit checks on prospective consumers before they accept their application. Some retailers also specifically target their marketing to more affluent socio-economic areas.¹⁴

¹⁰ Ibid 130-131.

¹¹ Ibid 129-130.

¹² Ibid 131.

¹³ Victorian Council of Social Service, *Making energy markets work: Submission in response to the review of electricity and gas retail markets in Victoria*, 3 March 2017.

¹⁴ Australian Competition and Consumer Commission, *Retail Electricity Pricing Inquiry: Preliminary Report*, 22 September 2017, 143.

At this stage we consider a low-cost tariff should be provided on an opt-in basis. While there would be challenges associated with informing people about an opt-in tariff, this appears preferable to an opt-out model, because it would not disadvantage low-income and vulnerable households who have already accessed better priced offers elsewhere in the market.

We seek the ACCC's analysis of the distributional impact of a targeted low-cost tariff (based on application to hardship program participants only, hardship program participants plus concession card holders, etc), in order to ensure low-income households outside the targeted groups are not burdened with higher pricing.

Other forms of price regulation

The ACCC has found a high level of price dispersion, particularly in Victoria. This dispersion has only increased since publication of the preliminary report. In Victoria, the difference between the best and worst electricity market offers (as at July 2017) ranges from \$820 per annum in the Citipower network to \$1090 per annum in the AusNet network.¹⁵

VCOSS considers this degree of price dispersion reflects the difficulty people have engaging with the market, and the widespread use of intentionally confusing marketing and contracting practices.

A high and growing level of price dispersion severely disadvantages people who have the least capacity to engage with the market, or who are excluded from lower-priced offers. Excessively priced electricity is unsustainable for people on low incomes and those experiencing vulnerabilities, including people who:

- have constrained incomes and limited or no ability to accommodate price increases
- cannot reduce energy use because they live in poor-quality, energy inefficient housing as a result of severe affordable housing shortages and lax regulation of private and social rental housing
- cannot have solar installed and rely exclusively on grid-based electricity
- predominantly (or exclusively) use electricity to run their households because of high gas costs or lack of alternative fuel sources (for example, one household in VCOSS's *Power Struggles* report had 'voluntarily' disconnected from gas because she could not afford both gas and electricity)¹⁶
- have household members with disability- or age-related needs that increase electricity use.

Given the vital role of energy in sustaining people's health, enabling education and employment, and allowing people to care for themselves and their families, we ask the ACCC to consider whether some form of price regulation is merited. We note Victoria's Independent Review Panel has recommended retailers be required to provide a 'Basic Service Offer' that is not greater than a regulated price, which would be set by the Essential Services Commission.¹⁷

¹⁵ St Vincent de Paul Society and Alviss Consulting, *Victorian Energy Prices July 2017*, 4.

¹⁶ Victorian Council of Social Service, *Power Struggles: Everyday Battles to Stay Connected*, August 2017.

¹⁷ Professor John Thwaites, Patricia Faulkner AO and Terry Mulder, *Independent Review of the Electricity & Gas Markets in Victoria*, August 2017.

VCOSS seeks the ACCC's consideration of a full range of price regulation measures and whether they can help reduce energy costs for low-income and vulnerable households, including price caps, price supervision, and/or a targeted low-cost energy offer for low-income households, and the distributional impact of price regulation measures.

Benefit periods

VCOSS previously noted its concerns about benefit periods in its first submission to this inquiry. Following the ACCC's preliminary report, we reiterate our concern that benefit periods may not be a legitimate contracting practice at all, and query the usefulness of regulatory reforms that will simply give customers more information about benefit periods and price changes at the end of benefit periods.

Victoria's Independent Review Panel has recommended retailers be required to advise a customer of the retailer's best offer in advance of a price or benefits change, and for retailers to roll customers onto the nearest matching, generally available offer at the end of a contract or benefit period, unless the customer opts for another offer.¹⁸ While we welcome these types of reforms, they do not overcome more fundamental problems with benefit periods, including that even with upfront information about price changes, benefit periods cause confusion from the outset and undermine comparability, because people cannot compare like contract terms and terminology.

In our view, benefit periods are not necessary to protect retailers' interests (normal contract terms can be used to manage pricing risks etc) and have been designed to deliberately obfuscate pricing and trick the customer into remaining with the retailer long-term.

Best practice concessions policy

We support the recommendation that immediate action should be taken by state and territory governments to review concessions policy to ensure people are aware of their concessions entitlements, that concessions are well-targeted and structured to benefit those most in need, and that there is consistency between concessions where appropriate.¹⁹ VCOSS supports the Victorian percentage-based concessions model which ensures the concession is proportionate to energy consumption.

Conclusion

VCOSS is very pleased the ACCC is undertaking this inquiry and exercising its powers to compel information from retailers. We are particularly looking forward to the analysis of what people are actually paying for electricity, and ideally a socio-economic analysis of this data. We trust the ACCC's final recommendations will comprise a robust set of reforms that recognise the essential nature of energy, and prioritise the needs of low-income and vulnerable households, particularly those who have little or no capacity to reduce their grid electricity consumption.

¹⁸ Ibid.

¹⁹ Australian Competition and Consumer Commission, *Retail Electricity Pricing Inquiry: Preliminary Report*, 22 September 2017, 156.