

FIX IT!

How to fix the energy market rule making process to improve competition and consumer outcomes



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The Consumer Advocacy Panel ceased operations on 30 January 2015. Its functions have been transferred to Energy Consumers Australia, established on the same date.

The views expressed in this document do not necessarily reflect the views of the Consumer Advocacy Panel, Energy Consumers Australia or the Australian Energy Market Commission.

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Executive Summary

Consumer advocates use a range of tools in their efforts to improve the effectiveness of competition in consumer markets and improve consumer outcomes. These include research and policy analysis, initiating legal action, campaigning and communications, and direct advocacy to industry and decision-makers.

Since 2012, consumer advocates have been able to propose a ‘rule change’ to the National Energy Retail Rules (**NERR**), which regulates the sale and supply of electricity and gas to retail customers in subscribing states and territories.¹ Proposing a rule change initiates a process of consultation and determination by the Australian Energy Market Commission (**AEMC**). This rule change process is a new way consumer advocates can seek to improve consumer outcomes.

Consumer Action Law Centre (**Consumer Action**) and the Consumer Utilities Advocacy Centre (**CUAC**) partnered to make the first rule change under the NERR. The experience of being the first proponents of a retail rule change is documented in this assessment of the efficiency and effectiveness of the rule change framework and its ability to deliver good consumer outcomes.

Our experience is that a retail rule change is an extremely resource intensive and lengthy process. The process is too cumbersome for it to be a viable avenue for consumer advocates to improve energy market regulation that promotes the long-term interests of consumers. Further, we consider that the retail rule change and related institutional framework is not able to effectively respond to a dynamic and changing retail energy market. For consumer representatives this is a significant concern—it means that the national energy market processes are incapable of promoting good consumer outcomes.

This report draws on the findings of an evaluation report, published simultaneously, prepared by Alviss Consulting for Consumer Action and CUAC, with a peer review by Dr Gill Owen, titled *FIX IT! An analysis of the first retail rule change in Australia’s energy markets*. This report includes analysis and post-project reflections from the perspective of Consumer Action and CUAC, and makes recommendations that would improve the functioning of retail energy markets and regulation in Australia.

The structure of this summary report is as follows:

- Section 1 – Background to the rule change process
- Section 2 – Observations of the AEMC processes and assessment
- Section 3 – Discussion of an alternative to the rule change process

Recommendations are made both to improve the current AEMC rule change process as well as to replace the rule change process with an alternative market review mechanism.

¹ South Australia, Queensland, Tasmania, New South Wales and the Australian Capital Territory

Recommendations

Recommendations to improve the rule change process

1. That the AEMC reviews the rule change process and examines options for a much more flexible multi-layered rule change process where particular issues can be fast-tracked.
2. That the COAG Energy Council initiates a review of the AEMC's information gathering powers with the aim to ensure that the AEMC has the powers necessary to thoroughly investigate market issues and industry practices.
3. That the AEMC clearly articulates its expectations regarding the level of evidence to be provided by rule change proponents and evidence that will be collected by the AEMC during a rule change review.
4. That the AEMC develops a guideline for its public fora, organised as part of review processes, that can enhance debates and include views from expert non-stakeholders.
5. That the AEMC consult on and develop a framework for how explanations of consumer behaviour informed by behavioural science inform its decision-making.

Recommendation to replace the rule change process

6. That the COAG Energy Council consult on alternative mechanisms to the Retail Rule change process that can ensure that the national framework for retail markets is responsive and progresses in line with market developments.
7. That the COAG Energy Council's Review of Governance Arrangements for Australian Energy Markets consider the benefit of one national energy regulator being responsible for energy market reviews.

1. Background: the first retail rule change

Consumer Action and CUAC have combined expertise in the Victorian energy sector that spans 15 years of energy market reform. This reform has included: disaggregation of the energy market; privatisation of energy businesses; the development of consumer protections; price deregulation; and, more recently, the rollout of smart meters to improve demand side participation. Consumer Action's direct work with consumers through the MoneyHelp telephone financial counselling service and its consumer legal advice line, combined with CUAC's research and policy analysis and expertise, provides a strong basis from which to advance advocacy that promotes consumer interests.

Consumer Action and CUAC were prompted to initiate the rule change due to concerns about the fine print of fixed-term consumer contracts which enabled retailers to unilaterally change their prices. Consumer complaints indicated that consumers found this practice unfair. Many consumers believed that the price they signed up to in a contract would be fixed for the term of that contract or the contract's 'fixed benefit period'.² Many consumers were surprised and disappointed that the price they were charged increased, or any represented discount disappeared, when the retailer unilaterally increased the price before the expiration of the contract period. Consumers were also commonly charged an exit fee if they tried to change retailer following a price increase.

Consumer Action and CUAC were also concerned about the impact of in-contract price hikes on competition. Economic theory suggests that for markets to be competitive, consumers need to be engaged and participating in the market, by comparing market offers and switching to products that suit their needs. However, the ability of retailers to change the price during a contract disengages consumers—there may be little point shopping around if a retailer can simply increase its prices after the consumer has signed up.

This issue had been acknowledged and debated for some time in Victoria when Consumer Action and CUAC decided to undertake a rule change request. In 2011, for example, the Victorian Essential Services Commission (**ESC**) consulted on the issue, as there were strong views about the unfairness of unilateral variations. However, as the introduction of the National Energy Customer Framework (**NECF**) was pending in Victoria the consultation did not progress.

Both Consumer Action and CUAC conducted research, on separate occasions, into general contract terms and conditions as well as specifically fixed term contract terms.³ In 2012, CUAC conducted a survey of 507 consumers, asking for their experience with, and opinions on, fixed term energy contracts. The results indicated that 86% of the consumers surveyed thought that current arrangements are unfair and 94% believed that a change in the regulations is needed to prevent retailers changing prices during fixed term contracts.

² Fixed benefit period means a period of a market retail contract during which a benefit (such as a price discount) is available to the customer. It does not mean that the price from which the discount is made cannot be increased.

³ Consumer Action, 2011, *Just Sign Here: A review of Victorian energy contract terms and conditions*; CUAC, 2012, *Fixing up fixed term contracts for energy consumers*.

The preparation of the rule change was a significant undertaking. The two organisations received a grant of \$50,000 from the Consumer Advocacy Panel to support research and associated work, but the effort contributed by both organisations far exceeded that amount.

The rule change application required detailed economic and legal analysis, which formed part of a 70 page application. Following 6 months of development, the application was submitted to the AEMC in October 2013. The final determination was released in October 2014, exactly 12 months after the submission of the application.

The proposed rule change would have prevented retailers from offering a fixed-term or 'fixed benefit period' contract that allowed for prices to increase during the contract term or 'fixed benefit period'. Consumer Action and CUAC argued that this change would improve consumer understanding of energy offers and mean that consumers would be more confident in making choices. Ultimately, this would improve the effectiveness of competition to the benefit of consumers.

In its final determination, the AEMC decided that the issues requiring a regulatory response were narrower than that argued by the proponents, and therefore rejected the proposed rule change. The AEMC's position was that some consumers could be better informed about contract terms and conditions, and that this was the only issue that required a regulatory response. The AEMC's solution was thus to improve disclosure, transparency and consumer information.

A key concern for the AEMC was the potential effect the proposed rule could have on energy prices and consumer choice. The AEMC considered it likely that retailers would build a risk-premium into prices if they were unable to change the price during the contract term. Alternatively, the AEMC predicted that retailers might cease to offer fixed term contracts all together.

Fundamentally, the AEMC did not agree that there was evidence that unilateral price variations contributed to consumer disengagement, relying on the fact that many consumers have switched energy offers. It did acknowledge that some consumers are not well informed with respect to the terms and conditions of their energy contracts, particularly with respect to whether prices can vary during fixed-term contracts. This formed the basis of its alternative rule change, designed to better inform consumers about terms of contracts that allow for unilateral price variation.

2. AEMC processes and assessment: observations

Consumer Action and CUAC's experience suggests that improvements can be made to AEMC's processes and assessment so that the rule change process advances the long-term interests of consumers. These include the way in which evidence is gathered and interpreted, and the resource intensiveness and time involved in the process.

2.1 The cost and time involved in a rule change

For over 18 months the rule change project was a key activity for Consumer Action and CUAC. This is clearly a significant impost on the resources of two advocacy organisations. While the Consumer Advocacy Panel funded some expenses associated with the project, the use of internal resources and staff also meant that both Consumer Action and CUAC had to prioritise and disengage from other planned activities and issues. Consumer Action and CUAC had anticipated that a rule change request would be a time demanding exercise and were committed to allocate the necessary resources to maximise the chance of a positive outcome for consumers.

The rule change also involved contributions from a large number of other parties, including other consumer groups, energy retailers, government departments and ombudsman bodies. Each of these bodies contributed submissions—38 submissions were made to the consultation paper, and 20 submissions were made to the draft determination.

While Consumer Action and CUAC maintain that the issue raised through the rule change is an important one for consumers and the effectiveness of competition, it is worth comparing the extent of the investigations made and resources expended for what was a relatively minor regulatory change proposal. The proposal was to add one additional 'rule' to a rule book of over 170 rules. Given the rule would apply to only one class of contracts, the proposal was relatively minor in terms of the way in which energy supply and sale is regulated overall.

It took approximately 66 weeks from when Consumer Action and CUAC commenced the rule change project to the final determination. For 52 of those weeks, the application was subject to the AEMC's review.

There are other regulatory processes that are more flexible and less costly. For example, the Australian Competition & Consumer Commission (ACCC) currently offers different processes for merger reviews. If there are no substantive competition concerns, the ACCC typically finalises a review within eight weeks. This is because significant business transactions (or other business decisions) are at stake, but if we extend that logic, energy market rules that may cause consumer harm should arguably be allowed a fast-tracked review as well.

It is important that the AEMC has adequate time to consider the issues raised and seek stakeholder input. There is, nonetheless, a case for considering the introduction of a much more flexible multi-layered rule change process where certain issues can be fast-tracked.

Recommendation 1:

That the AEMC reviews the rule change process and examines options for a much more flexible multi-layered rule change process where particular issues can be fast-tracked.

2.2 The role of 'evidence'

2.2.1 The evidence burden

The AEMC's draft and final determinations cited 'insufficient evidence' as a reason not to accept the proposed change. This raises the question as to which party bears the burden of providing evidence to substantiate a rule change proposal—is it the rule change applicant, or is the AEMC whose role it is to undertake the necessary research and analysis?

Following early discussions with the AEMC, Consumer Action and CUAC considered that for a rule change application to be successful, it must demonstrate the case for change and cite evidence to substantiate that case. In its guidelines for rule change proponents, the AEMC states that 'requests that statements of fact be supported with evidence where possible and include quantitative and qualitative analysis to support statements regarding the effect of the proposed rule'.⁴

Given this, Consumer Action and CUAC's rule change application included economic analysis prepared by a respected regulatory economist and a significant legal analysis of relevant consumer protections that enhance consumer choice.

Consumer Action and CUAC's reflections on preparing the proposal

Preparation of the rule change application was a significant undertaking, particularly undertaking the economic and legal analysis designed to demonstrate that our proposed Rule would better achieve the market objectives. In initial discussions with the AEMC, we were led to believe that this analysis should be substantial and robust.

Shortly before we submitted the rule change application the responsible team at the AEMC changed and we did register a difference in expectations between the two teams. The new team, for example, was of the view that the initial application was too extensive.

Several retailers argued that Consumer Action and CUAC's rule change request contained insufficient evidence to support their arguments.⁵ These arguments appeared to be convincing for the AEMC, although it is difficult to see how the applicants could have easily obtained the necessary 'evidence'.

Particularly for a consumer organisation, it can be both difficult and expensive to obtain information about retail practices and consumer experience in the energy market. Consumer Action and CUAC could have collected contract and tariff data over time to ascertain frequency of price changes to new customers, although this would have delayed the project by several years. Even if such analysis was undertaken, only retailers and consumers themselves know what happens to prices for existing customers. As such, evidence of contract and tariff data would in all likelihood have been dismissed. Another option would have been to survey a large number of consumers. However, in reality, consumer organisations do not have the resources to undertake large-scale surveys.

⁴ AEMC, Guidelines for proponents, 3 at www.aemc.gov.au/Energy-Rules/National-gas-rules/Rule-making-process/Guidelines-for-proponents-preparing-a-rule-change.aspx

⁵ See, for example, submissions to the AEMC's Consultation Paper by Alinta Energy, Simply Energy, Momentum and ERAA.

Consumer Action and CUAC wanted to push some of the evidence burden back on to the AEMC, believing the AEMC was better resourced and placed to investigate retailers' claims. Despite these efforts, the AEMC kept asking for more evidence and rejected requests from the proponents to investigate stating that it did not have the information gathering powers to do so.⁶

An example of this relates to evidence of "price baiting" (i.e. offering low prices and then increasing the price shortly after the consumer has entered a contract). Some consumer groups argued that price baiting occurred in the market but the AEMC responded that they needed evidence in support of the claim. At the same time, the AEMC noted that the retailers had stated in their submissions that price baiting does not occur.⁷ The AEMC was basically facing a word against word situation that arguably should have triggered an investigation. The AEMC, however, dismissed the issue based on insufficient evidence. While the AEMC may not have the capacity to investigate all claims that may arise during a rule change review, an investigation into the price-baiting issue could at least have occurred had the AEMC had the powers to do so.

It is crucial that an agency such as the AEMC has sufficient information gathering powers in order to investigate specific market issues. Only then will it have the capacity to obtain the 'evidence' required to substantiate any rule change proposal.

Recommendation 2:

That the COAG Energy Council initiates a review of the AEMC's information gathering powers with the aim to ensure that the AEMC has the powers necessary to thoroughly investigate market issues and industry practices.

Recommendation 3:

That the AEMC clearly articulates its expectations regarding the level of evidence to be provided by rule change proponents and evidence that will be collected by the AEMC during a rule change review.

2.2.2 The quality and type of evidence

In absence of "evidence", the theoretical context underpinning arguments play an important role. Promotion of the National Energy Retail Objective, which is one of the 'rule change tests', involves economic considerations. This objective was explained by the second reading speech introducing the National Energy Retail Law:

The long term interest of consumers of energy requires the economic welfare of consumers, over the long term, to be maximised. The long term interests of consumers in competitive energy markets are promoted through the application and development of consumer protections to enable customers to participate in the market with confidence, support effective consumer choice and ensure ongoing access to energy on reasonable terms as an essential service.

Consumer Action and CUAC recognised an economic case would need to be made for the rule change request to be successful. Therefore a substantial component of the rule change application was its economic analysis. This work drew on insights from behavioural economics to explain consumer decision-making. The analysis contained in AEMC's draft and final

⁶ AEMC, *Retailer price variations in market retail contracts*, Rule determination, 23 October 2014, 29

⁷ AEMC, *Retailer price variations in market retail contracts*, Draft Rule determination, 31 July 2014, 27

determinations, however, suggests that it would place most emphasis on ‘traditional’ economic analysis, and less emphasis on behavioural economics.

For example, the AEMC’s determinations suggests that it believes that outcomes such as ‘maximum choice’ and ‘lowest price’ are more important to effective competition than transparency, simplicity and consumer confidence. This is perhaps based in ‘traditional’ economic theory, with a strong preference for market-based solutions: establish the necessary conditions for suppliers to compete, and efficiency that satisfies consumer preferences will result. At least in the context of this rule change, the AEMC were less convinced by consumers’ experience and behavioural economic theory to explain consumer biases and imperfect decision-making.

The approach taken by AEMC to its public forum for the rule change demonstrates this further. In organising the forum the AEMC consulted with Consumer Action and CUAC, but the AEMC was resistant to the suggestions for speakers. Consumer Action and CUAC, for example, believed that the discussion would benefit from a presentation by an expert on behavioural economics but the AEMC would not allow additional time for this. The result was that CUAC gave up some of its allotted time to address the forum in order to make time for a presentation on consumer behaviour.

Given this, the public forum did not enhance the debate beyond what had already been stated in written submissions. All speakers, except the behavioural expert, had submitted written responses to the consultation paper and, naturally, reiterated the same information and views. While it can be difficult to identify potentially interesting speakers without having received submissions from them, it is possible to take a more lateral approach by inviting representatives from similar, but different industries, or academics with relevant expertise.

The AEMC has in the past invited external expertise to address public fora taking place during a rule change review. During the review into economic regulation of network service providers, for example, two professors were invited.⁸ Given the proponents referred to behavioural economics several times in their application and subsequent submissions, the AEMC could easily have sought to invite an expert in this field. Similarly, invitations could have been extended to other experts being able to speak to different issues raised on other stakeholder submissions.

Recommendation 4:

That the AEMC develops a guideline for its public fora, organised as part of review processes, that can enhance debates and include views from expert non-stakeholders.

The AEMC’s analysis of its consumer research is another example of its approach to different traditions of economic thinking. As part of the rule change, the AEMC contracted Newgate Research to explore community reactions to retailer price variations in market contracts. Newgate produced a substantial report of its qualitative and quantitative research. The qualitative research involved 162 participants attending focus groups. The quantitative component surveyed 2,213 participants using telephone and online questionnaires.

⁸ Professor George Yarrow and Professor Stephen Littlechild presented at the AEMC’s public forum on 9 May 2012.

One issue that was investigated was whether price variations negatively affect competition and efficiency. Respondents were asked whether they would prefer a contract that had a variable price that would give them an estimated 9 percent saving or a fixed price contract that would give them a saving of 1 percent. In the quantitative survey, 45 percent of respondents preferred the variable offer with the greatest saving, 31 percent preferred the fixed price with the lower saving and 20 percent wanted “something else”.⁹ On the basis of this research, the AEMC stated: “The Newgate consumer research clearly indicates that surveyed residential and small business consumers have varying appetites for bearing risks.”

In the submission to the draft determination, Consumer Action and CUAC criticised the AEMC’s selective use of this research finding. For example, the AEMC downplayed the fact that when the qualitative sample was asked this question, they found it “somewhat difficult to absorb”. Further, the proponents argued that the fact that 25 percent of respondents answered “something else” or “don’t know” may indicate confusion associated with the question.

Consumer Action and CUAC also question the usefulness of the AEMC’s comparison of fixed term, fixed price contracts to fixed term, variable price contracts in order to ascertain potential risk premiums and consumer preferences. The argument that consumers prefer fixed term contracts has not been tested independently of receiving a better price.

The AEMC placed less reliance on other findings of the research, including the finding that consumers were generally frustrated and distrustful of energy retailers. This finding might indicate that competition may be ineffective or that steps could be taken to improve the effectiveness of competition to benefit consumers.

It would be helpful for the AEMC to explore a broader basis for its decision-making that recognise the way in which consumers experience the energy market. For example, principles of behavioural economics include some relevant considerations:

- The way products and services are framed will influence consumer take up as well as the effectiveness of competition. The proliferation of energy plans promoting discounts and savings off energy use and/or supply charges under those plans is an example. Consumers tend to focus on the amount of the discount, even though the base rate of plans offered by different retailers vary significantly, meaning the discount is not a useful comparison point. The way in which fixed term market contracts are 'framed' to provide certainty was also core to the concern raised in the rule change.
- Complexity, for example the number of offers available and the inconsistent and incomparable way in which offers are presented, mean that consumers are often overloaded with unhelpful information and subsequently unable to make a decision ('status quo bias').

Consumer Action and CUAC noted in our submission to the AEMC consultation paper that other regulators have welcomed the analytical power of behavioural findings. For example, the Chairman of the Australian Securities & Investments Committee has stated:

⁹ Based on 1,833 residential consumers across the NEM. The remaining 4% stated something else or they did not know.

... regulators around the world are considering behavioural science, and insights from it, to better understand how investors [consumers] really behave. For example, over and over behavioural research shows that consumers:

- have a bias towards the default option
- prefer a small reward today over a larger one later
- tend to disengage when faced with complexity and too many options, and
- are influenced by nudges, framing and, most importantly, their relationship with the person delivering the message.¹⁰

While the AEMC did acknowledge in its final determination that consumers may exhibit status quo bias and that this may temper competition, it did not believe this was significant. The AEMC stated this does not “necessarily mean that retailers have an incentive not to manage risk”.¹¹ To inform the weight it puts on different forms of evidence and analysis, the AEMC could develop a framework and approach to analysing consumer behaviour, drawing from insights from behavioural economics. It could consider the work of other regulators in this regard, including UK’s Ofgem.¹²

Recommendation 5:

That the AEMC consult on and develop a framework for how explanations of consumer behaviour informed by behavioural science inform its decision-making.

2.3 Observations from other consumer groups

In December 2014, Consumer Action and CUAC sought feedback from other consumer groups (members of the National Energy Consumer Roundtable) on the rule change project as well as the AEMC’s process. The comments listed below represent the various views expressed.

Questions	Feedback
Do you think the rule change process is a viable and effective avenue for consumer advocates to improve energy retail market arrangements for consumers?	“Yes it could be, but not if the process is based solely on a contest of opinions from stakeholders and not substantive independent analysis.” “Should be, but doesn't seem to work. Hugely resource and time intensive.”
Knowing more about the rule change process do you feel encouraged to use the process as a means of reform?	“Not really, but if it's the only process then it's the one we have to use.” “It seemed like an incredible investment of time and resources – I'm not sure we would make the investment with such a low likelihood of getting an outcome.”

¹⁰ Greg Medcraft, ‘Regulating for Real People’, Address to ASIC Annual Forum 2014, [http://asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/ASIC-Forum-2014--Opening-address--24March2014.pdf/\\$file/ASIC-Forum-2014--Opening-address--24March2014.pdf](http://asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/ASIC-Forum-2014--Opening-address--24March2014.pdf/$file/ASIC-Forum-2014--Opening-address--24March2014.pdf).

¹¹ AEMC, *Retailer price variations in market retail contracts*, Rule determination, 23 October 2014, 25

¹² See, eg, Ofgem, 2011, *What can behavioural economics say about GB energy consumers?*, available <https://www.ofgem.gov.uk/publications-and-updates/what-can-behavioural-economics-say-about-gb-energy-consumers-1>

	"Maybe the process needs to be changed to be more effective and less complicated."
What, if anything, could the AEMC do to make the process more accessible for consumer groups?	"Set up a Customer Council, like the AER has done, or at very least commit to twice yearly customer forums attended by the Commissioners and CEO, to build their own knowledge of the way real consumers behave/make decisions. Employ a behavioural economist." "I'm not aware of aspects of the process that limited accessibility. My understanding of the deficiencies of the process is about the way the decision was made." "The problem is really the AEMC's mindset. They just don't get that people need help from regulation to prevent bad behaviour. Consumers' can't just be given MORE information and be expected to fend for themselves."
Do you have any other comments about CALC/CUAC's proposal?	"CALC/CUAC could have had more success if they had worded their rule change differently. Rather than completely ban price changes in fixed term contracts, there may have been another option more palatable to the AEMC and retailers to ban the use of the word fixed if the price is variable." "I think it was a good proposal and congratulate CALC and CUAC for pursuing it." "A bold and admirable step. Those who go first make it easier for those who would come next."
Do you have any other comments about the rule change process?	"The rule change process is far too slow to be useful in the rapidly changing market. It needs to be reformed."
Do you have any other comments about the AEMC's final decision?	"Again, frustrating but not unexpected." "Disappointing but entirely expected."

3. An alternative to the rule change process

In the previous section, recommendations were made that might improve AEMC's rule change processes from a consumer perspective. However, this report suggests that there needs to be more fundamental reform.

3.1 Retail market reviews

Energy retail markets are rapidly changing but there is no easy mechanism to ensure that the rules are aligned to the market they actually seek to govern. This causes just as much of a challenge for rule makers and regulators as it does for consumer groups. Without the ability to implement responsive and efficient rules to address consumer issues and market inefficiencies, there is a real risk that consumers lose confidence, and interest, in energy retail markets to the detriment of effective competition.

One potential option is to schedule regular retail market reviews, for example every three years. Rather than rely on individual applications to make changes to energy retail rules, retail market reviews could undertake substantial analysis and consider whether there needs to be changes to the regulatory framework.

A significant short-coming of the existing rule change process is that there is no method by which to evaluate the impact of a rule change. Regular reviews would be able to evaluate changes previously made and consider whether they have operated to promote the long-term interests of consumers and the energy market objective.

Such a review process would:

- Evaluate the consumer experience to understand the current market issues;
- Assesses the impact of changes to the market, including the impact of technology and new types of energy services;
- Involve a consultative process that incorporates input from a range of consumer stakeholders, energy industry and government;
- Involve consultation on its terms of reference to ensure stakeholder issues are considered;
- Obtain relevant data and information from energy suppliers, using robust information gathering powers;
- Draw upon complaint data and expertise from ombudsman schemes;
- Utilise insights from behavioural science that explains consumer behaviour;
- Produce a report that recommends changes to regulatory instruments so that consumers are empowered and confident to exercise choice;
- Implement changes to regulatory instruments following a final report.

In response to the Consumer Action and CUAC rule change request, the AEMC amended the NERR to specifically require retailers to:

- disclose terms or conditions that provide for the variation of prices as part of the existing requirement to obtain the explicit informed consent of consumers to the entry into a market retail contract; and
- provide information about when they will notify consumers of variations to prices as part of existing product disclosure information provided on contract entry.

The AEMC believed that these requirements will mean that consumers are more informed and engaged so that they are likely to make better choices in retail energy markets. However, there is no existing market mechanism through which this can be tested.

In other markets, questions have been raised about the effectiveness of information and disclosure as a consumer protection measure. The recently completed Financial System Inquiry noted “mandated disclosure is not sufficient to allow consumers to make informed financial decisions”.¹³ There is no reason to suspect that consumers approach energy product information differently to financial product information. At the very least, there should be an opportunity to test the effectiveness of disclosure in facilitating consumers making informed and effective choices. A scheduled market review process could undertake this necessary analysis.

Recommendation 6:

That the COAG Energy Council consult on alternative mechanisms to the Retail Rule change process that can ensure that the national framework for retail markets is responsive and progresses in line with market developments.

3.2 Institutional arrangements and accountability

Replacing the rule change process with an alternative review mechanism raised the question of which body should be responsible for the process.

Consumer organisations have recently suggested that the separation of rule-maker and regulator in energy market institutions is not serving the long-term interests of consumers.¹⁴ The COAG Energy Council is currently reviewing the governance arrangements in the national energy market. In this context, consideration should be given to folding the responsibilities of the AEMC into that of the AER, so that there is one body responsible for regulating retail energy markets and promoting the long-term interests of energy consumers.

There are a number of reasons to suggest that the existing institutional structure, particularly the division between the AEMC as rule-maker and market reviewer and the Australian Energy Regulator as market regulator, creates problems for addressing consumer issues that might be resolved through rule changes.

Firstly, it is arguably problematic that the same agency that undertakes effectiveness of competition reviews also assesses retail market rule change proposals. When the AEMC finds that a retail market is first displaying effective competition it becomes difficult for the AEMC to later take the view that competition in the market can be ineffective.

For example, in response to concerns about potential price-baiting practices raised through the rule change process, the AEMC argued that price-baiting could not be a problem because price-baiting can only occur in markets where competition is ineffective. However, the AEMC’s review into effectiveness of competition in 2014 found that competition was effective.¹⁵ Such

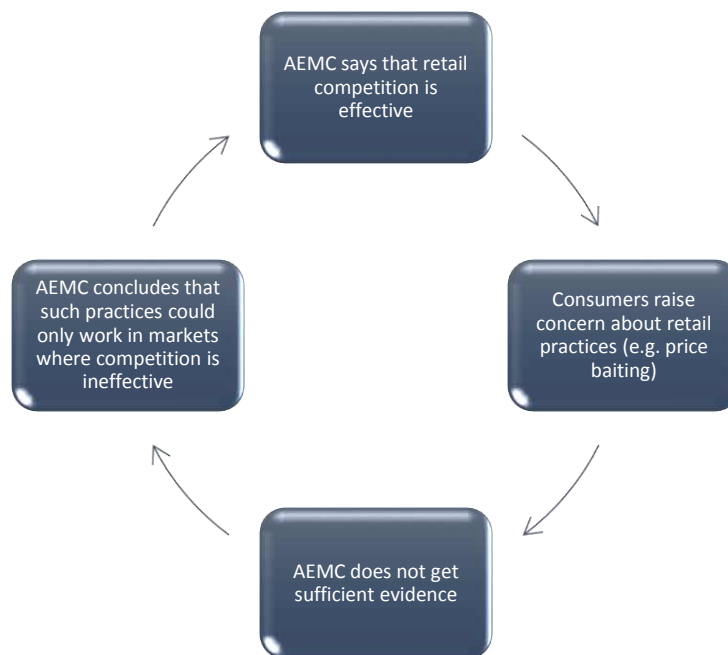
¹³ Financial System Inquiry, 2014, *Final Report*, available <http://fsi.gov.au/publications/final-report/>

¹⁴ Energy Users Association of Australia, *Submission to Senate Inquiry into the Performance of Electricity Network Providers*, p 23; Consumer Action Law Centre, *Submission to Senate Inquiry into the Performance of Electricity Network Providers*, p 7.

¹⁵ AEMC, 2014, *2014 Retail Competition Review*, available <http://www.aemc.gov.au/Markets-Reviews-Advice/2014-Retail-Competition-Review>

a finding perhaps inhibits the AEMC from making any rule change which argues that competition may be ineffective or could be made more effective.

The following diagram explains this conundrum:



Secondly, the AEMC lacks accountability measures that apply to other regulators and market institutions. Unlike regulatory determinations of the AER, determinations of the AEMC are not subject to merits review. Merits review allows a person affected by a decision to have that decision reviewed by a separate decision-maker. The review considers the merits of the initial decision and decides whether or not a correct and preferable decision should be made. It has become quite common for determinations of the AER to be challenged and overturned via merits review.

Decisions of the AEMC are subject to judicial review. Judicial review is far narrower form of review compared to merits review, considering only the lawfulness of the decision-making not the substantive decision. It considers matters such as whether the decision-maker took into account all relevant information, excluded irrelevant matters, and reached a conclusion that, on the weight of the evidence, is reasonable in the circumstances.

There is some uncertainty with the appropriate law around this, given it is not clear that an AEMC determination is an 'administrative decision' or a 'legislative decision'. Given a new rule will have a general rather than specific application (i.e. apply to all retailers), it is likely that it is legislative in character. As such, the *Administrative Decisions (Judicial Review) Act 1977* (the AD(JR) Act) will also not apply and any judicial review must be via the common law. The AD(JR) Act improves access to judicial review compared to the common law, by removing technical requirements such as issuing a prerogative writs, making review for error of law simpler, and expanding remedies available. The technicality and cost involved in a common law judicial review is likely to make it out of reach for many consumer organisations.

The nature of the AEMC's determination also limits the grounds of review, with the grounds of 'improper purpose' and 'proportionality' the most relevant. Both these grounds are difficult to establish. To be successful on judicial review, an applicant would have to demonstrate that the long term interests of consumers (i.e. the objective of the law) were not taken into account.

In the absence of any explicit failure by the AEMC to follow the relevant statutory process or to take into account submissions received (as opposed to simply not giving them adequate weight), the AEMC's rule change decisions are unlikely to be judicially reviewable due to the broad powers conferred upon it which include making a more preferable rule or no rule at all if it considers that doing so would better serve the long-term interests of consumers.

Given the AEMC's existing role in assessing the effectiveness of competition and given the limited accountability measures imposed on it, alternative institutional arrangements should be considered.

There are a number of other options available. The AER could undertake the scheduled market review and make recommendations, however it does not have the power to change rules. COAG Energy Council could undertake the review, but given its decision-making involves compromise among up to seven jurisdictions, it is unlikely to be able to respond in a timely manner to market developments.

Recommendation 7:

That the COAG Energy Council's Review of Governance Arrangements for Australian Energy Markets consider the benefit of one national energy regulator being responsible for energy market reviews.

4. A final word of thanks

Consumer Action Law Centre and the Consumer Utilities Advocacy Centre thank the many organisations, businesses, policymakers and institutions that contributed to, or otherwise engaged in, the first Retail Rule Change request. Much has been learned, and we hope our reflections and recommendations will assist in delivering good consumer outcomes in Australia's national energy market, now and in the future.

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