ENERGY CONSUMERS AUSTRALIA

A Suite 2, Level 20, 570 George Street
Sydney NSW 2000
PO Box A989
Sydney South NSW 1235
T 02 9220 5500
W energyconsumersaustralia.com.au
@energyvoiceau
/energyconsumersaustralia
/energyconsumersaustralia

ABN 96 603 931 326

31 October 2023

Gavin Fox
General Manager, Market Performance
Australian Energy Regulator
By email: DMO@aer.gov.au

Submission to the Australian Energy Regulator Default Market Offer Prices 2024-25 Issues Paper

Dear Gavin,

Energy Consumers Australia welcomes the opportunity to provide feedback to the Australian Energy Regulator's (AER) Default Market Offer 2024-25 Issues Paper. In the context of continued cost-of-living pressures on households and small businesses, robust price protections are critical to ensuring consumers have access to an essential service at a fair and affordable price.

The Default Market Offer (DMO) and reference price were introduced in 2019 in response to the Australian Competition and Consumer Commission's Retail Electricity Pricing Inquiry which found there was a need to protect consumers on standing offers from being charged unreasonably high prices and help consumers better navigate a complex energy market. Both needs have been amplified by increasing cost-of-living pressures and highlight the important role the DMO plays as a consumer protections tool.

For this reason, we again highlight the need to ensure the DMO remains centred around the reason for its introduction: to protect consumers. We reiterate arguments made in our previous submissions that a retail margin of 10% for residential consumers and 15% for small businesses does not give adequate weight to the AER's objective to protect consumers from unreasonable prices.

In addition to amendments within the scope of this review, we also draw attention to issues which are making the intended protections of the DMO apply to an increasingly small cohort of consumers. These issues include:

- Consumers on market offers are not protected by the price cap,
- The changing energy market is reducing the relevance of the reference price,
- Changing usage behaviour is complicating the determination of an annual usage amount,
- The objectives of the price cap and reference price differ when determining an annual price.

The retail margin is too high to protect consumers from unreasonable prices

Rising cost-of-living pressures continue to impact the ability of consumers to keep up with repeated hikes in energy bills. Over half of households and small businesses in our June Energy Consumer Sentiment Survey (ECSS) said they were more concerned about their ability to pay their electricity bill than they were a year ago. Half of all small businesses, and a third of households, say they have either asked their retailer for help managing bills in the last year or expect to do so in the near future[1].

[1] Energy Consumers Australia, Energy Consumer Sentiment Survey, June 2023, available: https://ecss.energyconsumersaustralia.com.au/sentiment-survey-june-2023/

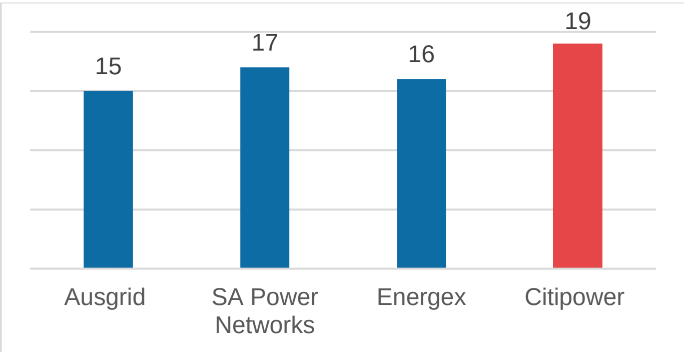
As argued in our submission to the DMO 5, these circumstances reinforce the need to ensure the DMO gives adequate weight to its objective to "reduce unjustifiably high standing offer prices and continue to protect consumers from unreasonable prices"[2].

A retail margin of 10% for households and 15% for small businesses is too high to achieve this. We don't believe sufficient evidence has been provided as to why it is needed.

While we accept that the Essential Services Commission differs in its objectives when setting the Victorian Default Offer, despite its lower retail margin, Victoria continues to see competition and incentives for consumers to engage in the market.

Our ECSS revealed Victorians are more likely to engage in the market, with 54% saying they had either changed, or considered changing, energy company or plan in the past year compared to 43% in NSW and 44% in South Australia. We also see that Victorian networks have the greatest number of retailers with advertised market offers (Figure 1).

FIGURE 1: NUMBER OF RETAILERS WITH ADVERTISED MARKET OFFERS



Source: St Vincent de Paul Tarriff Tracking Reports for NSW, SA, QLD and VIC, July 2023

We believe there is significant risk and headroom built into other elements of the cost stack that further negate the need for such a high retail margin. Customer acquisition and retention costs, for example, are near irrelevant to these customers as they do not engage with advertising and are not moving between retailers. We also know that consumers on payment plans and in hardship programs are less likely to be on a retailer's standing offer and therefore bad and doubtful debt costs are also less relevant[3]. We believe it is not reasonable, therefore, that in addition to these costs, standing offer customers are also being asked to pay a 10-15% profit margin.

We also maintain that there should not be a difference between the margins for residential and small business consumers, as outlined in our submission to the DMO 5 Issues Paper. While small businesses have historically not been considered vulnerable in the same way as residential consumers, our ECSS tells us that they are more likely to be concerned about paying energy bills and more likely to have reached out, or intend to reach out, to their retailer for help with bills. We also know

[2] Australian Energy Regulator, Default market offer prices 2024-25 Issues Paper, October 2023, p. 1, available: https://www.aer.gov.au/retail-markets/guidelines-reviews/default-market-offer-prices-2024%E2%80%9325/initiation-0

[3] Australian Energy Regulator, Retail Performance Data, Q3 2022, available: https://www.aer.gov.au/retail-markets/performance-reporting/retail-energy-market-performance-update-for-quarter-3-2022%E2%80%9323

that small businesses are more likely to be on a standing offer which only further demonstrates the need for the DMO to protect small business consumers.

Consumers on market offers are not protected by the price cap

The ACCC's Retail Electricity Pricing Inquiry report highlighted the harm caused by the "loyalty tax", where disengaged consumers were paying considerably more than consumers that frequently shopped around. This was associated with standing offer customers due to the unjustifiably high prices retailers were placing on these offers.

Despite some limitations, such as the high retail margin, the introduction of the DMO has limited the "loyalty tax" on standing offer customers. Since its introduction, with the exception of last year when volatile wholesale conditions pushed standing offers up significantly, we have seen standing offer prices decline at a steadier rate than market offers[4].

However, we believe there remains a loyalty tax that is increasingly impacting consumers on market offers. Less than 9% of households are on a standing offer in DMO jurisdictions, a number which has declined since the introduction of the DMO[5]. These are the only consumers whose prices are directly capped by the DMO. For the vast majority of consumers who are on market offers, there is no cap on the price retailers can charge them.

We have consistently seen advertised market offers priced below the DMO for each network, with some exceptions last year. However, these prices apply to new customers and therefore only to consumers who have chosen to engage with the market. There is less known about the prices being paid by a retailer's existing customers, many of whom may have seen their prices increase at the end of their contract period.

We know from our Energy Consumer Sentiment Survey (ECSS) that most consumers are not engaged in the market and do not actively shop around. Despite increased messaging around switching and the incentive of rising energy costs, 59% of households said they had not even considered shopping around. Only 14% said they had either changed energy company or switched plans with their current retailer. Further, almost half of all households said they looked into switching less than once every two years.

Despite a lack of data on the prices paid by existing customers, ECA has heard anecdotal evidence that consumers on market offers received price change notifications that their market offers would be increasing to a price above the reference price. In some of these cases, these notifications had been received only shortly after the consumer had first moved on to the offer. We are concerned by this behaviour considering the number of consumers who are not engaged with the energy market and are therefore unlikely to move off these high prices. We therefore believe that the DMO is not offering the protection for disengaged consumers that it was intended to.

---

[4] St Vincent de Paul Society, Observations from the Vinnies' Tariff-Tracking Project, October 2022, available: https://www.vinnies.org.au/advocacy/energy/energy-national

[5] Australian Energy Regulator, Retail energy market performance update for Quarter 3 2022-23, June 2023, available: https://www.aer.gov.au/retail-markets/performance-reporting

The changing energy market is reducing the relevance of the reference price

The reference price acts as a point of comparison for consumers comparing simple plans based on price. With over a fifth of households saying that they did not switch energy plans or retailers as it was too complicated, complex, or time-consuming[6], we believe that tools aimed at helping consumers to navigate what is becoming a progressively complex energy market are important.

However, we are seeing ever more products and services enter the market that do not fit the definition of a standard 'vanilla' energy plan. These may be plans with cost-reflective tariffs, that offer cheaper EV charging, are bundled with the purchase of CER products, or offer access to a virtual power plant. As was noted by the Department of Industry, Science, Energy and Resources' 2022 review into the DMO and Reference Price, the reference price will struggle to apply to these types of offers[7].

Consumers are already indicating to us that they consider factors beyond a single end price when looking for a new energy plan. Our ECSS revealed that feed-in tariffs, for example, were an important factor for 18% of all households the last time they looked around for an energy plan. With the variety of offers that are being introduced into the market to meet a diverse range of consumer desires, a tool that can be only used for simple price comparisons will become less relevant. It is unable to give any indication of potential risks, or benefits, of plans that offer any additional features or complexities. For example, the reference price may indicate a smaller discount for a solar plan compared to a regular plan, but if it offers high feed-in tariffs it may be the best option for a consumer with solar.

Changing usage behaviour is complicating the determination of an annual usage amount

Facilitated by these new products, consumers are becoming increasingly diverse in how they use (and produce) energy. Our most recent ECSS found that a third of households believe that in the next three years they will change their usage behaviour to use electricity at times when it is cheaper. Another 29% said they would investigate purchasing personal generation options such as solar or batteries.

As noted in the Issues Paper, the AER must "determine 'broadly representative' annual supply amounts for residential and small business customers in each distribution region"[8]. However, determining a 'broadly representative' usage for households and small business customers will become increasingly difficult with the continued adoption of CER and changing usage behaviour. Going forward, a single usage amount will reflect how fewer and fewer consumers actually use energy.

As a price cap, this has the potential to cause harm if a consumer uses more than the defined amount. For example, during the volatility of last year, we saw some retailers utilise inclining block tariffs to charge standing offer customers considerably more if they used more than the DMO's consumption level[9].

---

[6] Energy Consumers Australia, Energy Consumer Sentiment Survey, June 2023, available: https://ecss.energyconsumersaustralia.com.au/

[7] Department of Industry, Science, Energy and Resources, Directions from the review of the Default Market Offer and Reference Price, January 2022, available: https://consult.dcceew.gov.au/review-of-dmo-and-reference-price

[8] Australian Energy Regulator, Default market offer prices 2024-25 Issues Paper, October 2023, p. 27, available: https://www.aer.gov.au/retail-markets/guidelines-reviews/default-market-offer-prices-2024%E2%80%9325/initiation-0

[9] St Vincent de Paul, NSW Energy Prices, August 2022, available: https://cms.vinnies.org.au/media/yjspuxgh/01_nsw_energy_prices_july_2022.pdf?path=yjspuxgh%2F01_nsw_energy_prices_july_2022.pdf

As a reference price, it also has the potential to cause harm. The AER, in their Issues Paper, notes that “any time of use pattern aiming to represent all customers is unlikely to capture many possible drivers in individual usage patterns such as climate or individual household characteristics”[10]. However, if a consumer’s actual usage differs greatly from the profile determined by the AER, the discount advertised by the reference price will be unlikely to apply. This could lead to higher than anticipated bills if, for example, they use more energy in peak times than the AER’s pattern outlines. This was an issue identified in the ACCC’s June Inquiry into the National Electricity Market which found that, while some consumers benefit from time of use plans, consumers who could not, or did not understand how to, take advantage of cost-reflective plans could end up paying more[11].

The objectives of the price cap and reference price differ when determining an annual price.

As demonstrated throughout this submission, the DMO has multiple functions and therefore multiple objectives. This complicates the process for the AER to make decisions on how best to set an annual price and for stakeholders to comment on the best approach for consumers. Determining annual usage load profiles, for example, requires different considerations when setting a price cap rather than a reference price.

The DMO must keep up with a rapidly changing energy market

The DMO and reference price play a crucial part in the broader consumer protections landscape. However, its current benefits as a price cap and as a reference price are relevant to an increasingly small portion of consumers. While we note that many of the issues raised in this submission may lie beyond the scope of this Issues Paper, we also believe that a rapidly evolving energy market is already complicating the process of determining an annual price.

In the short term, the AER should look to determine prices that appropriately protect consumers through the tools it currently has available to it. However, Energy Consumers Australia looks forward to further working with the AER to address these broader issues and ensure that in the future, the DMO both protects consumers and helps empower them to benefit from a transitioning energy system. If you have any questions on this submission, please reach out to alice.g@energyconsumersaustralia.com.au.

Yours sincerely,

Jacqueline Crawshaw
Director Energy Services and Markets

[10] Australian Energy Regulator, Default market offer prices 2024-25 Issues Paper, October 2023, p. 28, available: https://www.aer.gov.au/retail-markets/guidelines-reviews/default-market-offer-prices-2024%E2%80%9325/initiation-0

[11] Australian Competition & Consumer Commission, Inquiry into the National Electricity Market, June 2023, available: https://www.accc.gov.au/about-us/publications/serial-publications/inquiry-into-the-national-electricity-market-2018-25/inquiry-into-the-national-electricity-market-june-2023-report