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**3 April 2018**

**Re: Bipartisan Independent Review of the Electricity and Gas Retail Markets in Victoria: Victorian Government Interim Response and Consultation Paper**

AGL notes the release of the Victorian Government's Interim Response (Interim Response) to the Final Report of the Independent Review of the Electricity and Gas Retail Markets in Victoria (Thwaites Report) that was released in August 2017.

AGL is one of Australia's leading integrated energy companies with over 3.6 million electricity and gas accounts in New South Wales, Victoria, Queensland and South Australia as well as being the owner, operator and developer of a diverse power generation portfolio including base, peaking and intermediate generation plants, spread across traditional thermal generation and renewable sources.

As an energy retailer in Victoria with almost 1.2 million customer accounts, AGL appreciates this opportunity to respond to the Thwaites Report, the Interim Response, and associated Consultation Paper and to work with the Government in making effective and practical reforms to the Victorian retail energy market.

The Thwaites Report made 11 broad recommendations for reforms to improve the working of retail energy markets and AGL has previously noted it is generally supportive of the intent of recommendations 3 to 11. It did not believe recommendations 1 and 2, namely the introduction of a regulated Basic Service Offering (BSO) and removal of Standing Offers, were supported by evidence it would benefit customers or deliver practical solutions.

To that end, AGL is pleased to see the Interim Response identified that:

- recommendations 5 to 11 are accepted and to be progressed;
- recommendation 3 is accepted and will be implemented by the Essential Services Commission (ESC), after further consultation with industry to ensure that it is workable;
- despite support for its intent, recommendation 4 cannot be implemented effectively as currently worded and is being consulted upon with industry through the Consultation Paper; and
- the Government requires additional consultation with industry on recommendations 1 and 2 before it decides whether to implement them. This is essential as AGL believes that adopting these reforms as proposed in the Thwaites Report will be highly damaging to Victorian energy consumers and to the competitive energy industry.



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AGL's detailed feedback to the Consultation Paper and especially Recommendations 1,2 and 4 are contained in Appendix 1 of this submission.

Whilst AGL supports the immediate actions proposed in the Interim Response, it has been extremely concerned by many facets of this review to date and has similar misgivings about the future process, namely:

- the limited timetable that is being provided to stakeholders for consultation;
- the use of the Thwaites Report as ultimate justification for the Government's decisions when the report was released without public review, contains significant errors and shows a limited understanding of the workings of the retail energy market;
- that the Australian Competition and Consumer Commission (ACCC) is holding a public inquiry into the competitiveness of retail electricity prices yet the Victorian Government is choosing to discount its findings by sticking to an accelerated timetable;
- despite the recent commitments from major energy retailers to reduce the costs of energy, genuine consideration is not being provided working with industry to implement changes that are in the best interests of consumers; and
- that the Thwaites Report and associated discussions with the Victorian Government have been focussed on the retail electricity market in Victoria, yet the Interim Response seems to assume that all recommendations can be directly applied across both the electricity and gas retail markets without amendment.

These process issues are outlined in more detail in the following sections.

### **Consultation timetable**

AGL notes that these recommendations result in significant impacts to retailers and customers, and should be afforded a best practice consultation process.

The recommendations were released in the Thwaites Report in August 2017 but there was no consultation or review of the findings despite many concerns being expressed by industry.

The Government's timeline and intention to progress the recommendations have only been made known since the release of the Interim Response on 11 March, providing less than 3 weeks of consultation time. Given the broad impacts of these recommendations, stakeholders should be given more time to consult internally and develop more considered alternatives that improve outcomes for energy consumers.

Public participation is a critical input to government activity and developing effective strategies, programs and projects. The Victorian Auditor-General's Office (VAGO) acknowledges that failing to adequately engage the public risks alienating the community and creating negative impacts through poorly informed and implemented decisions.<sup>1</sup>

Consequently, AGL encourage the Government to extends its consultation timetable, and consider completing a full Regulation Impact Statement (RIS).

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<sup>1</sup> VAGO – better practice guide 2015 <https://www.audit.vic.gov.au/sites/default/files/20150130-Public-Participation-BPG.pdf>



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## Concerns with Thwaites Report

The Thwaites Report was published in August 2017 and made 11 major reform recommendations to the Victorian Government. Most of these recommendations are not controversial and focus on making marketing information more easily comparable, better clarity of market contracts, fairer marketing practices and improved protection of vulnerable customers. These have largely been supported by AGL and broader industry in submissions to the review<sup>2</sup>.

However, a central and contentious recommendation of the Thwaites Report was for price re-regulation through a BSO. This was based on the analysis by its consultants that gross margins for average electricity customers in Victoria were at much higher levels than other states.

The Australian Energy Council (AEC) asked Oakley Greenwood to review this analysis<sup>3</sup> and it identified major problems with the methodology used as well as basic errors in the calculations. Some of the major flaws Oakley Greenwood identified in the analysis included:

- the retail prices used in the analysis of gross margin were greatly overstated<sup>4</sup>;
- the assumptions on market offers and conditional and unconditional discounts were based on a total sample of 36 customers' bills which are highly unlikely to be representative are also likely to overstate the retail prices used;
- that wholesale cost data was subjectively derived from a period that underestimated wholesale cost;
- errors in estimating the costs of the Victorian Energy Efficiency Scheme (VEET) and the Feed-in-tariff schemes which underestimated the cost of these schemes for small customers; and
- they assumed lower residential switching rates than reality.

The Oakley Greenwood report found that these flaws overstate the gross margin calculations by at least 30 per cent. Given these concerns, AGL does not believe the Government can rely upon the analysis in the Thwaites Review as the justification for market changing reforms such as its recommendations 1 and 2.

## ACCC Inquiry

The ACCC is also holding a public inquiry into the supply of retail electricity and competitiveness of retail electricity prices and released its Preliminary Report to the Federal Government on 16 October 2017.

The report covers many industry issues and found that network costs have been a primary driver for electricity price increases in NEM jurisdictions. It used data collected from industry to examine the components of an average residential customer bill in the NEM and by jurisdiction and found that gross margins were increasingly similar across all states in 2015-16.

Although the report found that gross margins had increased substantially since 2007-08, it also determined that this was mainly due to increases in retail costs. As a result, electricity retailers' net margins have been between 5-10 per cent and Victorian residential customer bills have similar average retail margins (in dollar

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<sup>2</sup> AGL submission Feb 2017

[https://engage.vic.gov.au/application/files/2114/9023/4832/AGL\\_Submission\\_including\\_attachments.pdf](https://engage.vic.gov.au/application/files/2114/9023/4832/AGL_Submission_including_attachments.pdf)

<sup>3</sup> <https://www.energycouncil.com.au/media/9731/20170919-ogw-review-of-the-thwaites-report.pdf>

<sup>4</sup> The retail prices used in the analysis were the median price offer for each retailer. Retailers have a large spread of prices, but it is public information that most customers are on discounted market offers below the median price. Assuming a median therefore overstates the retail prices and the gross margin analysis.



terms) to other states. Furthermore, the report indicated that in Victoria, retail margins had remained flat in the last two years.

These preliminary findings in many ways contradicted the modelling and analysis of the Thwaites Report. The ACCC also concluded that it will not intervene in the retail energy market until it is sure that an intervention will improve the market and not have unintended consequences to the detriment of electricity consumers. This considered approach is a stark contrast to the Victorian Government's apparent plan to dramatically intervene in the competitive Victorian retail market without consideration of the consequences.

The ACCC also identified areas of the retail electricity market that need reform such as reducing complexity, improving vulnerable consumers' access to appropriate products and encouraging further market engagement and is expected to provide its final report by 30 June 2018.

The Victorian Government currently plans to release its own Final Response in June 2018. It would be sensible for the Government to take the opportunity increase the length of its consultation period to take advantage of the analysis and recommendations in the ACCC's Final Report and to accommodate these findings in its own Final Response and planned Code amendments in Victoria.

### **Recent commitments by AGL and other major retailers**

As highlighted in the Interim Response, AGL and other major retailers announced in November 2017 additional rebates to reduce the costs of energy for Standing Offer customers in Victoria. This resulted in savings of between \$250 and \$450 per annum compared to what these customers would have paid in 2018. It is important to note that even prior to this, AGL has been providing similar rebates to Standing Offer customers with eligible concessions for several years.

These commitments in conjunction with the reforms to the retail market being driven by the:

- industry commitments to the Prime Minister;
- AER Rule changes; and
- the recommendations already accepted through the Interim Response;

should allow industry to demonstrate the retail market is working in the best interests of consumers.

The Victorian Government has seemed to recognise this by consulting further with stakeholders of the application and scope of the Basic Service Offer, the abolishment of standing offers, appropriate alternatives, and their effect on Victoria's energy sector (Recommendations 1 and 2).

However, the Government is releasing its Final Response in mid-2018 and has indicated it will make its decision on recommendations 1 and 2 of the Thwaites Report by the end of 2018. AGL believes that these timeframes will not allow the Government to adequately assess any improvements in the retail energy market and any decisions will be made based on outdated information.

### **Retail Gas Market**

There was little focus on the retail gas market in the Thwaites Report and little consideration as to whether the summary recommendations would be directly applicable to both fuels. AGL's continued discussions with the Government on the recommendations, whether they are applicable, how they can be implemented, and any alternatives solutions have also centred on the retail electricity market. Similarly, the retail market



reforms that are being progressed through Rule changes and because of the Prime Minister's commitments are also centred on the electricity market.

Therefore, it was surprising to AGL that the Interim Response has assumed that the recommendations are to be applied equally in the retail gas market.

Many of the retail market reforms may be able to be implemented across the retail energy markets but some, such as the establishment of a reference price signal for the gas market and consideration of any BSO applying equally to gas customers, are highly problematic. The differences between deriving applicable reference prices for the cost of gas supply and cost of electricity supply are significant due to the major differences in the wholesale, distribution, and transmission segments of the supply chain. This was clearly demonstrated previously under retail price regulation when setting a regulated retail electricity price could be derived on an industry basis but assessing a regulated retail gas price was highly dependent on a single retailer's contracted supply position.

AGL submits the Government needs to be cognisant of these differences and give these matters greater consideration when making its Final Response, not just which recommendations should be accepted but also whether they will apply across the retail energy market or to the retail electricity market only.

AGL's detailed responses to the Consultation Paper, in Appendix 1 of this submission, highlight that the introduction of a BSO and abolition of standing offers, as considered by the Thwaites Report will:

- not function in the manner assumed by the Government;
- severely damage the competitiveness and functioning of the Victorian energy industry;
- have other potential unintended consequences; and most importantly
- have adverse customer impacts including, but not limited to, many energy consumers paying more, less customer choice, pricing reform and innovation being slowed and a subsequent lessening in the take-up of new technologies.

It also highlights that even the introduction of the reforms to market contract periods, practices and variations, as envisaged by recommendation 4, will not work in practice despite recognition by industry that changes are needed.

Given the scope of these issues and the need to design alternatives that would limit negative impacts, AGL strongly suggest the Victorian Government address the identified process issues as a priority as it will improve the likelihood that the Government's Final Response can incorporate all stakeholders feedback and up to date information and make informed decisions regarding the reforms being considered for energy consumers.

If you wish any further information, please contact me on (03) 8633 6207 or Patrick Whish-Wilson on (02) 9921 2207.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Elizabeth Molyneux'.

Elizabeth Molyneux  
GM of Energy Markets Regulation



## Appendix 1: AGL Response to Consultation Paper

### **Introduction of Basic Service Offer (BSO) and abolition of Standing Offers (Recommendations 1 and 2)**

1. Are there any specific considerations the Government should be aware of if standing offer contracts were to be replaced with a regulated BSO?
2. Would the services and service standards associated with a regulated BSO be the same as those existing under the standing offer terms and conditions?
3. Would a BSO based on a 'flat tariff' apply to general usage only or should it incorporate controlled load and/or solar tariffs (as is the case for standing offers)? What are the benefits and challenges associated with different approaches?
4. What other principles should the ESC consider in setting the BSO maximum regulated price profile? Should these principles differ between a BSO for electricity and a BSO for gas, residential and small business customers?
5. Are there alternatives for setting the BSO maximum regulated price profile? For example, should the ESC 'simply' set a BSO tariff or a specific tariff structure that must be applied by retailers?
6. What are the likely effects of a regulated BSO, as described above, on the energy markets (electricity and gas wholesale, distribution and retail markets, and residential and small business customers)?
7. Are there any alternative design options for price regulation (to those outlined above) that would achieve the Review's intended outcomes?
8. How should the potential benefits and effects of a regulated BSO be assessed following implementation?
9. How should a regulated BSO be incorporated into Victoria's energy sector regulatory framework?

The Interim Response has acknowledged that further analysis is required regarding the scope and application of the BSO and its effect on Victoria's energy sector. AGL would submit that the analysis needs to be widened to first determine whether a BSO is warranted rather than refining the scope or how it is to be implemented.

The Thwaites Report has proposed that a BSO would be a 'no frills', unconditional offer, available if requested by a customer. The ESC would regulate the price and terms and conditions of this offer, and retailers would remain able to offer alternatives to this BSO in the competitive market, including by offering lower or higher priced offers based on innovation or services valued by customers.

The Consultation Paper notes that concerns around the introduction of a regulated BSO have focused on:

- the effect on the availability of innovative products and services in Victoria's energy retail sector;
- the effect on the retail energy sector; and
- unintended effects on customers and their engagement in the energy market.

AGL believes this is a significant understatement of the concerns raised by stakeholders regarding the impact this regulatory instrument will have on the Victorian energy market.



Firstly, the Thwaites Report assumptions on how its proposed BSO will work in practice are illogical and ignore the realities of the retail market. A regulated BSO will not simply become a “no fuss’ product for disengaged customers. Given it is proposed that the BSO is constructed without customer acquisition and retention costs then the BSO price will be determined at below the average cost of supply and will therefore be also utilised by engaged customers.

Retailers are likely to respond by removing any market offers that are below this regulated price point and the large percentage of engaged Victorian energy customers that currently access these types of heavily discounted market offers will pay more than they do today. The BSO will become the regulated price floor.

The Thwaites Reports expectation that retailers will be able to compete for value-add products is highly unlikely to occur given the given the many market reforms underway to improve transparency of pricing. These reforms are to ensure that any communication, marketing material and customer bills will have a clear focus on price comparison to ensure customers are informed. AGL supports these reforms which will improve the retail market in the absence of a BSO. However, under the BSO regime, the clear focus on comparing products by price only will largely ignore any value add services or product innovations. This makes the Thwaites Report’s view of a continuation of competition in the market highly unlikely.

The BSO is also likely to severely inhibit network pricing reform which will decrease innovation, the take-up of new technologies and customer choice. Without price and product variation in the market, competition will slow or cease and the expected negative impacts on energy customers, retail businesses and the Victorian economy, that AGL and other stakeholders have been highlighting will eventuate.

The accompanying removal of Standing Offers and replacement by the BSO is also problematic as it ignores the use of Standing Offer price as the reference price for current market contracts.

This dual use of Standing Offer price by retailers for discounted products has been driven by regulators to avoid the previous confusion that existed when a retailer’s reference price differed from its published Standing Offer rate. Reversing this process will not be simple or quick and any solution will lead to further confusion for customers.

10. Are there alternatives to introducing a regulated BSO and revoking standing offers?

a. How would these alternatives achieve the objective and principles set by the Review?

b. How would these alternatives affect other Review recommendations?

c. What would be the likely effect of these alternatives on Victoria’s energy sector and energy consumers?

d. Would these alternative approaches cause any distortions or inequities between different groups of customers?

AGL in its discussions with Government has suggested a range of alternatives to the BSO since the release of the Thwaites Report.

However, constructing a suitable alternative can only be done if the Government is able to articulate what is the primary objective of the BSO or what problem it is specifically trying to solve?



- Impact of high prices on Standing Offer customers?

If this is the perceived issue, then AGL and other major retailers have committed to relieve the impact of high prices on standing offer customers in 2018. This type of commitment can be extended across the industry.

It is important to recognise that Standing Offer customers make up less than 10 per cent of AGL's Victorian electricity customers and 90 per cent of these are now being provided significant discounts or rebates because they are concession customers or have been disengaged from the market for a sustained period of time.

Less than 1 per cent of AGL's Victorian electricity customers (around 5,000 customers) are paying Standing Offer prices and they are predominantly customers that have moved in to premises and are yet to, or only recently provided AGL with their customer details.

Introducing a potentially damaging regulatory instrument such as the BSO to resolve an issue arising from a small cohort of customers does not appear to be good public policy. Especially considering the range of market reforms being introduced to improve clarity for customers on what their current price is and to provide clear comparisons of other available offers.

- Impact of price on Vulnerable customers?

Similar to the issue on Standing Offer prices, AGL has been providing any concession customer on a Standing Offer a voluntary discount for the last 2 years. This internal decision was taken to ensure concession customers are not disadvantaged by being disengaged from the market and could easily be implemented within the regulatory framework.

Moreover, AGL's customer data infers that vulnerable customers are most likely to be on heavily discounted products and are therefore those most likely to be negatively impacted by the introduction of the BSO.

If the price impact on vulnerable and concession customers is the primary issue for the Government then introducing a BSO that only applies to concession customers may be a reasonable alternative to the general BSO structure.

- Providing a clear price signal?

If the Government's objective is establishing a clear price signal for the market for a reasonable price of energy that will allow consumers to compare prices, then there is no need to embed a regulated tariff within the regulatory framework.

The Interim Response has already tasked the ESC with producing a reference price signal or reference BSO. AGL believes the terms of reference for construction of this reference price is poorly determined because it ignores many retail costs and therefore will estimate a reference price below the average cost of energy supply. However, the framework exists, and it can be utilised accordingly as a reference price signal without introducing the BSO.

AGL would submit that the setting of a price signal for the market would be better served by including all retailer costs and some competition headroom. AGL would point to Queensland where a regulated electricity price is set for regional Queensland but is directly comparable to the deregulated southeast Queensland market.

This regulated electricity price includes all costs and additional headroom and provides the Government and southeast Queensland customers with an effective price comparison or signal. This price allows the Queensland Government to assess the reasonableness of annual price changes by retailers and better





enables the regulator to monitor the Standing Offer prices of retailers as well as the spread of their market offers.

Most importantly, this reference price does not impact on the effective functioning of the competitive market as it is only a price signal.

As mentioned previously, the setting of a reference price for electricity is much simpler than setting a reference price for gas because of the significant contractual and supply differences between these markets. AGL has serious concerns about the ability of the Government to determine a gas price that would be a useful reference signal.

- Require a regulated price?

If the Government's objective is the introduction of a regulated price into the retail market, AGL would still submit that it reconsiders the BSO structure and instead focus on re-regulating price using a method that would have less harmful consequences for the energy market.

The Government is clearly cognisant that a return to any form of price re-regulation will mean that it becomes responsible for:

- the health and competitiveness of the retail market;
- annual changes to energy prices, even if these changes are in response to input costs that are outside its control; and
- explaining these price movements to consumers.

Despite the Thwaites Report assumptions, the introduction of the BSO will not provide a regulated pricing framework that:

- absolves these responsibilities from Government; or
- provides any additional improvements when compared to traditional price cap regulation.

More worrying is that using a BSO is likely to significantly damage competition and economically harm Victorian retail businesses.

As such, AGL proposes that if the Government is seeking price re-regulation then it reconsider other regulated price models used previously that managed to sustain some level of competition within the regulated framework.

11. Are there any specific considerations of which the Government should be aware of if the reserve power to regulate prices was strengthened? What should be the trigger for regulation and when or under what circumstances should the regulated price requirement end?

The Australian Energy Market Commission (AEMC) undertake regular reviews of the effectiveness of competition in Victoria and other jurisdictions. If it finds that competition in the market for electricity is not effective, then the jurisdiction may re-regulate prices.

AGL does not see the need for the re-regulation of prices to be based on market conditions monitored by the ESC as it is hard to imagine how an ESC review of a market would differ greatly from the AEMC findings of the same market.



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### **Marketing Information (Recommendation 3)**

Recommendation 3 proposes changes to the information provided by energy companies to customers, including marketing material and bills. The Government has requested the ESC review the Energy Retail Code to give effect to these market reforms.

AGL supports the intent of these reforms but suggests the Government recognise that in instances, the wording from the Thwaites Report recommendation does fulfil the stated intent in a cost-effective manner. AGL hopes to work with the ESC to ensure these reforms are both workable and effective.

### **Contract periods, practices and variations (Recommendation 4)**

These recommendations respond to concerns that customers on 'market' offers are paying higher prices for energy than they should because of opaque and varying processes at the end of benefits period, and contract and behavioural barriers to consumer engagement with the market.

Industry has generally supported the intent of these recommendations but AGL is pleased that the Government acknowledges that issues exist with their implementation.

AGL considers that the intent of Recommendation 4 is to improve engagement, transparency and ensure customers are informed at the time of consent. By ensuring these steps are properly managed, customers can make informed decisions about contract types and benefits that suit their needs and preferences.

AGL consider that regulating contract behaviour can cause significant issues for both customers and retailers, and fails to focus on achieving the correct outcomes – which is an informed customer base exercising discretion and flexibility to consider energy options.

Contract practices in any industry should encourage customer engagement though the provision of right information at the right time for an informed decision process and the industry have flexibility for product innovation and servicing. By regulating contract types, the Government risk limiting customer choice and potentially creating unintended negative outcomes. This can include a scenario where retailers, unable to predict the future state of the energy market in five – ten – fifteen-years, will need to moderate offerings for customers upfront to manage potential risk.

AGL recommend that Recommendation 4 be subject to a robust Regulation Impact Statement process to assess the different policy options overall costs and benefits. This would support the Consumer Policy Research Centre's recent report on the Five Preconditions of Effective Consumer Engagement<sup>5</sup> which notes the importance of building customer confidence and trust in demand-side engagement through empowerment. Finally, AGL note that customers respond differently to various price and non-price offerings. Consequently, price competition in the form of discounts (as well as credits and vouchers) is the main feature of retail product offerings in Victoria but other product and service features are used to enhance the value of the energy offer.<sup>6</sup>

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<sup>5</sup> <http://cprc.org.au/research-areas/making-consumer-decisions-easier-and-fairer/report-release-five-preconditions-effective-consumer-engagement/>

<sup>6</sup> AGL submission Feb 2017

[https://engage.vic.gov.au/application/files/2114/9023/4832/AGL\\_Submission\\_including\\_attachments.pdf](https://engage.vic.gov.au/application/files/2114/9023/4832/AGL_Submission_including_attachments.pdf)[https://engage.vic.gov.au/application/files/2114/9023/4832/AGL\\_Submission\\_including\\_attachments.pdf](https://engage.vic.gov.au/application/files/2114/9023/4832/AGL_Submission_including_attachments.pdf)



12. What is the most appropriate approach to implementing Recommendations 4A to 4E?

13. How can these recommendations be implemented in a timely manner?

*Recommendation 4A: Require retailers to commit to fix any prices they are offering for a minimum of 12 months. During this period, the market contract prices cannot change. Retailers may request an exemption from the ESC to address unforeseen changes in the network costs.*

AGL note the concern that the current rules do not regulate how often, or by how much, retailers can change their prices. AGL's current business practice is to vary Victorian customer's market offers an average of once per 12 months. However, requiring retailers to fix prices for a minimum of 12 months will create significant operational challenges and costs to retailers and is not a workable solution.

There are many instances in which a customer's price may need to be varied, which includes instances that will transition customers to a better tariff. Such an example includes where a customer is in a distributor cross-over zone and may be placed on a higher tariff. While retailers have controls in place to mitigate this risk, there remains the possibility that it will occur from time to time, and retailers will need to adjust the customers tariff.

By setting prices for 12 months, retailers would essentially be managing daily price changes (reprice event) for customers – a process that is resource intensive and currently happens twice a year. The staff and system implications of this are enormous and retailers would be more likely to undertake monthly reprice events and therefore would need to price for the increase risk of potential shifts in the energy market for that time, increasing the price to customers.

Fixed price contracting shifts the direct risk from customers to the service provider, but that risk is ultimately covered in costs to those customers. Retailers will set prices at a level that incorporates any price impact changes in their initial offer calculations, meaning the base cost to a customer for their offer will rise. While a fixed-price contract gives the customer more predictability about the future costs, this predictability comes at a higher price. The increased risk borne through lack of fluidity in price means the end price is likely to be higher than in a competitive market where prices can adjust as the market demands.

Even the possible exemption for unforeseen changes in networks costs is problematic and limited in consideration. Exemptions should be broader than network costs as there are instances in which network reviews can be re-opened outside of the five-year process. For example, Transmission and Distribution Network Service Providers can apply for a revocation and substitution of determinations within the five-year period which retailers are unable to plan for. There are also other unforeseen, non-network situations that could arise and would need to be considered. For example, the closure of Hazelwood in 2017 had a significant impact on wholesale costs that retailers needed to account for. Retailers can currently respond to events such as the Hazelwood closure by using reprice events or changing market offers.

#### Previous regulatory consideration of fixed price contracts

In 2014, the Consumer Action Law Centre (CALC) and the Consumer Utilities Advocacy Centre (CUAC) submitted a rule change request for fixed prices for duration of contract period. The AEMC conducted extensive stakeholder engagement and consumer research and concluded that the key issues raised by the rule change request was that some customers may be entering contracts unaware that their prices may change but ultimately, did not support the rule change request.



Instead, the AEMC developed a proportionate response to this matter by requiring retailers to specifically disclose to customers (i.e. adjustments to call scripts and notifications) whether prices can vary and provide notice of this event.

It is important to note that the AEMC concluded that the proposed rule change for fixed prices for the duration of a contract could have resulted in increased prices and reduced choice for consumers.<sup>7</sup> They found that about 60 percent of the costs that make up a retail energy bill are determined by processes external from individual retailers. If retailers were unable to change their prices to pass on unmanageable changes in their costs when they occur, prices would be likely to increase.

The AEMC also concluded that if retailers were unable to change their prices it may reduce or stop offering some types of contracts which the AEMC considered could reduce customer choice of contracts and reduce the effectiveness of retail competition.

Market behaviour over the last decade has demonstrated that more flexibility in product offers are being provided by retailers. In the last two years this has included retailers offering fixed term offers that guarantee fixed energy prices to customers for a set period (typically 12 – 24 months).<sup>8</sup> AGL recommend the Government examine the development and uptake by consumers of these products before moving to regulation.

*Recommendation 4B: Require retailers to clearly disclose to customers the length of time any offered prices will be available without change.*

Upfront disclosures about the term of the rate and the timeframe help inform the customer and mitigate any customer detriment regarding price or benefit alterations.

By ensuring that the upfront disclosure information is fit for purpose and easy to understand, customers are more informed and there is less reason to regulate the back end of a contract. Any other options would essentially penalise a customer who pays on time, as retailers will be incentivised to remove these options and benefits from contracts to mitigate future energy market change risks, and ultimately these customers will pay more on their bills.

AGL support upfront disclosures such as this recommendation. AGL are also supportive of the prohibition of the word “fixed” unless the retailer uses it to describe the prices being fixed for a period. The use of “fixed benefit period” is a source of confusion for customers and impacts positive customer outcomes. This is particularly the case when customers consider that “fixed benefit” relates to price and therefore may be unclear on the purpose of the variation disclosure.

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<sup>7</sup> <https://www.aemc.gov.au/sites/default/files/content/61206757-b4ad-4faa-a2a8-8d672e515cc4/Final-determination-information-sheet.pdf>

<sup>8</sup> These include AGL Essentials (guaranteed no rate rises for 12 months available through digital channels), EnergyAustralia’s Secure Saver (no energy prices rise for 2 years), Origin’s Predictable Plan.



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*Recommendation 4C: Require 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.*

Requiring retailers to move customers to the nearest matching offer at the end of a contract creates several risks to customer choice and pricing/product behaviour of retailers. This will also be in direct conflict with explicit informed consent requirements for fixed term contracts that are used by many retailers.

This requirement ultimately inhibits customer choice and is likely to mislead customers. If customers are informed that their contract has not changed, or has changed to a retailers best matching offer, this may flag to the customer that no shopping around is required. While it may reduce price dispersion it will mean that the most price sensitive customers see an increase in their overall bill. Furthermore, this approach may lead to greater levels of customer inertia. If the customer is informed that their offer is not changing, or is the nearest matching offer, they may be less inclined to shop for a new offer.

#### Contract practices

The Australian Consumer Law offers protections against unfair contract terms and provide protection to customers about the type of information made available to ensure customers are informed and not induced by misrepresentations. There are also laws that protect customers from unfair contract terms. As a result, retailers ensure there is adequate disclosure and incorporate notification in Energy Price Fact Sheets and agent call scripts to make sure the customer is aware of their rights. Any failure of a retailer to do this should be a matter of enforcement within the current framework, with appropriate regulatory assessment of the issue and solutions.

In lieu of this assessment, the regulatory response to increase front-end contract regulation will essentially be a band aid solution to a potential systemic or non-related issue.

AGL support an approach that aligns with the Prime Minister Commitment to notify customers at the end of their benefit period. The ESC amended the Energy Retail Code to align with part of this change to the National Energy Retail Rules. The second part of the changes relate to the AER developing Benefit Change Notice Guidelines to prescribe the information retailers are required to provide to customers in the end of benefit notice. The AER are undertaking consumer behavioural research and stakeholder engagement to inform this process. AGL recommend Victoria align with this additional work being completed by the AER to ensure consistency in approaches and to leverage off existing research and engagement.

AGL does support the Government considering the restriction of a retailer's ability to switch customers to a standing offer at the end of their market offer contract.

*Recommendations 4D: Any conditional discount or other benefit offered for paying on-time or on-line billing should be evergreen. Customers should not lose the discount or other benefit when the contract ends.*

*Recommendation 4E: Costs incurred by customers for failing to meet offer conditions are to be capped and not be higher than the reasonable cost to the retailer.*

Pay-on-time discounts are offered as an incentive because it helps AGL manage cashflow. If this option is not available, or is impacted in such a way that it does not result in this ability, then there is little incentive to continue to offer these benefits as they currently are and will likely need to adjust this approach going forward. Further, a fixed period provides retailers the ability to adapt to a changing energy market. If retailers are unable to know the future price, then any upfront benefit may not be sustainable.



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Based on these recommendation, retailers will be less inclined to offer customers specials such as sign up bonuses or other incentives that tend to drive growth and encourage competition, such as a free month of power or loyalty schemes. As previously described to the Government<sup>9</sup>, AGL ensures that customers are sent a letter which informs them that they will be automatically rolled over onto a new plan if they take no action. This plan is either a continuation of their current benefit or the current AGL discounted market offer at that point in time. The 'continuing offer' letter is the main recontracting letter and it goes to most customers.

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<sup>9</sup> AGL submission Feb 2017  
[https://engage.vic.gov.au/application/files/2114/9023/4832/AGL\\_Submission\\_including\\_attachments.pdf](https://engage.vic.gov.au/application/files/2114/9023/4832/AGL_Submission_including_attachments.pdf)