2 July 2019

Ms Kate Symons
Acting Chair
Essential Services Commission
Level 37, 2 Lonsdale Street
Melbourne, Victoria 3000

Email: RetailEnergyReview@esc.vic.gov.au

Dear Ms Symons

RE: Issues Paper: Ensuring Energy Contracts are Clear and Fair

Origin Energy appreciates the opportunity to provide a submission in response to the Essential Services Commission's (ESC) Issues Paper Ensuring Energy Contracts are Clear and Fair.

We recognise the significant progress that the ESC has made in implementing reforms to make retail energy contracts clearer and fairer. This current consultation is focussed on implementing reforms associated with discounting practices. We agree that it is vitally important to make comparing offers simple for customers so that they have the knowledge and tools to make informed decision regarding their choice of electricity plans.

However, in achieving this goal it is also vitally important that these current policy recommendations are treated as a package and complement each as other as well as the reforms that have already been made. Where there is a spectrum of options within recommendations (as is particularly the case with recommendations 4A and 4C), the ESC should consider selecting the more conservative option. Some of the options open to the ESC are quite significant changes to the market; these options only make sense if they are implemented in isolation rather than as part of a package. Selecting the more conservative options will reduce implementation cost and difficulty, as well as the likelihood of unintended consequences—such as reducing offers at the bottom end of the market. We note that the ESC does have the discretion to review and change the Energy Retail Code without a third party requesting it. Accordingly, the ESC can review the impact of these options and whether they have satisfied the policy intent of the recommendations in due course.

We also believe the ESC ought to pay particular attention to how the VDO interacts with any proposed policy recommendations. When used as an anchor for price comparisons, the VDO addresses many of the key concerns around comparing offers. We believe that the VDO when supplemented with recommendations around price certainty (4A), will go a significant way to addressing the objectives of this round of reforms.

Origin's views on these issues and other matters set out in the ESC's paper are set out below.

Recommendations Relating to Contracts

Recommendation 4A – Fixing Contract Prices

The ESC highlight that the intent of recommendation 4A is to give customers certainty that their prices will not change soon after they sign up to a new contract. We fully support providing customers with certainty regarding when and why there is a price change.

The ESC propose that this could be achieved by requiring retailers to: 1) fix tariffs of all market contracts for at least the first 12 months; or 2) have at least one generally available offer fixed for 12 months; or 3) give customers the choice of whether they want a fixed tariff for 12 months or not.

The ESC also invites stakeholders to provide other options for implementing recommendation 4A. We believe that the ESC's recommendations provide a solid base but feel there would be benefit in better aligning the price change process for both market and regulated contracts.

The ESC is required to make a VDO determination every 12 months. This determination will update the underlying input costs of the VDO in much the same way that a retailer also reviews and updates their tariffs. We consider that if the regulated price is updated at a defined point each year, to create consistency between when a regulated price changes and when a market price changes, it would be sensible to align these processes.

By doing this, the customer develops an understanding of when prices changes occur for all products; irrespective of whether they are on a VDO or a market contract.

In terms of how this relates to meeting recommendation 4A, we propose that all market contracts should be fixed, but with the provision that these tariffs can be changed at the same point in time when the VDO changes. This will allow retailers to review any changes in their underlying input costs at the same time as the regulator; better aligning the use of respective cost information.

We believe this addresses the issue of customer certainty because the customer knows the date that there will be any price change (regardless of whether they are on a VDO or a market contract). Furthermore, provisions to re-open a market price outside of this time should be consistent with the conditions that apply to the VDO for unforeseen events.

We believe this approach will also compliment recommendations 3F (end of benefit notifications) and 3G (best offer on bills). Together, these provide customers with certainty about when their pricing changes and the availability of alternative offers in a simple collective approach.

This makes the market much more transparent and provides a disincentive for retailers to create products that have attractive initial pricing and then large price increases, which the Thwaites review identified as a practice of concern.

Furthermore, allowing retailers an opportunity to manage their input cost risk will mean relatively lower prices because the need for retailers to factor in a risk premium for any adverse movement in upstream costs that they cannot not manage is reduced.

This is an approach that has been effective in Queensland that restricts retailers changing prices once every six months; although our proposal will go further than this by restricting it to once a year. We believe our proposed alternative meets the intent of recommendation 4A of providing customers with price certainty and balances the cost risks to retailers.

Recommendation 4B – Fixing Contract Prices

The intent of recommendation 4B is to provide customers with certainty about how long their prices will remain unchanged when they sign up to a new contract.

Our proposed approach to implementing 4A sets a defined date on which an annual price change will occur. It is clear and unambiguous; all prices change on the same date irrespective of whether they are regulated or market contracts.

By having this consistency and repetition, the customer will become familiar with the certainty around the price change process. For example, if they enter into a market contract in October, they will be informed that their prices will change in January (assuming this is the VDO price change date). It is clear and straightforward for the retailer to administer and it is clear and easy for the customer to understand. And because it is the same for every year and every product, this is likely to promote customer understanding and acceptance.

We believe our proposed alternative meets the intent of recommendation 4B and balances the cost risks to retailers with providing a simple pricing solution for customers.

Recommendation 4C – End of Benefit and Contract Periods

Recommendation 4C requires retailers to roll customers onto the nearest matching generally available offer at the end of a contract or benefit period. The ESC has stated that the intent of recommendation 4C is to give customers confidence that if they do not take action at the end of a benefit or contract period, they will not be on a significantly more expensive plan. We consider that meeting the intent as expressed by the ESC will drive a better outcome for customers than a literal application of the recommendation.

It is also important to recognise that as a result of the implementation of recommendations 3F and 3G, customers will now receive a notification at the end of their benefit period advising them of best offers available and how to access the VDO. However, there are nevertheless issues with this approach.

In this regard, we believe it is useful address this issue in terms of how it applies to a contract term and a benefit term.

<u>End of Contract</u>

The ESC has proposed that when a customer's market contract ends, and they take no action, that the customer could be rolled onto the VDO. We think this is pragmatic solution to meet the intent of this recommendation. This avoids issues around obtaining the customers Explicit Informed Consent (EIC) and should be relatively straightforward to implement.

<u>End of Benefit period</u>

Applying this recommendation to end of benefit arrangements is not as clear as for the end of a fixed benefit period. For example, a customer on a contract with a two-year fixed benefit period may receive a 6 per cent discount for the first twelve months of a contract and then a 3 per cent discount for the second twelve-month period. The current definition of a fixed benefit period is very broad and if recommendation 4C was applied literally this would require the retailer to move the customer at the end of the 6 per cent benefit period. This is despite the customer having provided EIC for, and standing to benefit from, the subsequent benefit period.

Origin does not consider that in this instance it is in the customer's best interest to be rolled on to a different 'nearest matching' offer following the change from the initial benefit period; especially if the benefit is lower than the VDO. The 'end of benefit' and 'best offer on bill' notifications that customers receive prompt them to review their pricing and, if they are not on the best offer, provide a simple way to engage and get a better deal.

At the end of benefit, we believe the treatment of contracts and fixed benefits ought to be the same, that is the customers goes on to a rate the equivalent of the VDO.

We also seek clarification that if a customer's fixed benefit discount overlaps with a change to the VDO that the customer's percentage discount is preserved. Specifically, if a customer enters into a twelve-month fixed benefit contract of a 6 per cent discount off the VDO reference price, in the event that the VDO changes, the customer will continue to receive a price of 6 per cent off the revised VDO. As a result, the customer's price may change but the discount benefit is retained.

This will avoid the practice of initial short deep discounts followed by lower discounts. Complemented with recommendations 3F and 3G we believe that for the requirement to roll customers on a nearest matching offer is not beneficial for customers on a contract where there is a tiered benefit.

Recommendations Relating to Discounting

Recommendation 3A – How Discounts are Presented

Origin supports marketing in dollar terms with the use of the VDO as a reference price. We support the use of the VDO as an anchored price point.

However, this may be difficult to achieve for domestic gas for the following reasons:

- wholesale gas prices are significantly more difficult to benchmark;
- despite there being 3 distribution networks, there are significantly more pricing zones (in the order of 15 pricing zones) which has the potential to create significant confusion in the presentation of benchmarks; and
- gas involves multi step tariffs and therefore small changes in volume can have significant impacts on a customer's bill (i.e. the standard deviation for average gas usage is far greater than the standard deviation for electricity usage).

For these reasons, we propose that the ESC undertake further consultation with retailers and other stakeholders to develop an appropriate benchmark for gas retail prices.

Recommendation 4D – Making Discounts Evergreen and Recommendation 4E – Ensuring Discounts are Cost-Reflective

Recommendation 4D requires that any conditional discount for paying on time or on-line billing should be evergreen. The intent of this recommendation is for customers who sign up for a discount to receive the discount on an ongoing basis and do not end up paying substantially more because of the discount expiring.

We agree that circumstances where a customer signs on to substantial conditional discounts for a fixed period only to face a substantially higher price when the condition expires ought to be addressed. We believe that the key harm to be resolved is customers paying higher prices when their conditional discounts end. This issue will be dealt with via recommendation 4C. Providing an evergreen discount will not resolve this problem and may create perverse unintended consequences.

There are two elements to this harm: 1) the initial advertised discounts are unsustainably high; and 2) the price customers are rolled on to when their contract or benefit expires is uncertain.

The issue of unsustainably high discounts results from the practise of discounts being marketed off retailers' own standing offer prices or the conditional discount is misrepresentative of the benefit. If a retailer uses a high base for its discount, the advertised discount will be misrepresentative of the true value to the consumer. However, the requirement for retailers to use the VDO as an anchor for marketing resolves this issue; it eliminates misrepresented discounts.

While this ensures consistency across retailers regarding how prices are marketed, there is still the potential harm that a retailer may offer deep discounts but with conditions. To address this, the ESC proposes to cap conditional discounts to limit the penalties faced by customers who fail to meet their offer conditions.

We believe that limiting the conditional discount on a cost reflective basis will significantly diminish this outcome.

Therefore, the use of the VDO as an anchor and limiting conditional discounts will meet the intent of removing unsustainably high discounts from the market. When the benefit expires, the customer will be able to access the VDO which means that if the customer is switched on to the VDO at the end of their contract period the price will not substantially more than what they are currently pay. As a result, the implementation of 4E meets the policy intent without the need for evergreen discounts.

Furthermore, under recommendation 4C, if a customer were to move from an offer with a conditional discount to another offer with some other form of benefit, it does not follow that the customer should retain their existing conditional discount in addition to the 'nearest matching' offer benefit. Nor does it follow that a customer who moved from a market offer to the VDO should retain a benefit. The VDO is the 'fair price' safety net and applying a benefit to the VDO removes any remaining difference between the VDO and a market offer.

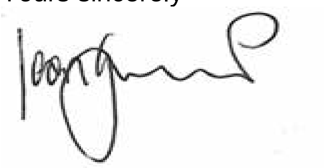
Therefore, recommendations 4C and 4E are likely to reduce the consumer detriment that can be associated with missed conditional discounts. Based on this, the harm sought to be addressed by recommendation 4D is already addressed. A further layer of requirements to implement 4D is likely to create confusion regarding whether discounts can be doubled up, or whether a new discount supersedes the previous one.

Closing

Origin agrees that it is important customers are provided price certainty. We recognise that the ESC is bound by its terms of reference. However, this should not preclude the ESC from determining the best way of achieving the intent of these reforms as a package that complement each as other as well as the reforms that have already been made.

If you have any questions regarding this submission, please contact Courtney Markham in the first instance on [redacted].

Yours sincerely



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