

5 November 2014

Energy White Paper Taskforce
Department of Industry
GPO Box 9839
Canberra 2601

Dear Sir/Madam

Re: Submission to the Energy Green Paper

The Consumer Action Law Centre (**Consumer Action**) welcomes the opportunity to provide the following submission to the Department of Industry on the Energy Green Paper.

Consumer Action Law Centre is an independent, not-for profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

Australia's energy market is rapidly changing, with the unprecedented fall in energy demand, the rapid penetration of small-scale solar generation into the market and the current proliferation of demand-side products and services to assist consumers better manage their consumption for more efficient use of market assets. The combined effect of these trends in the long term is hoped to be a more integrated market that makes efficient use of investments and allocates only efficient costs to consumers. However in the short term, the most marked effect is the increasing complexity for the 'average' consumer.

There is great opportunity in developing a market that engages the demand-side to deliver "energy productivity", which is a key focus of the Green Paper. However, complexity threatens the realisation of the very purpose of demand-side reforms—namely a more efficiently operated and priced energy market. In the face of very high levels of complexity, in a market that consumers already find difficult to understand, the likelihood that consumers will become overwhelmed by opportunities and choice and opt to make no choice at all (or ill-informed choices that are not actually suited to their circumstances) is high. There is a very real risk is that reforms will simply lead to increasing consumer distrust of the market as energy bills rise for those staying on standing offers and standard energy products, and increasing numbers of consumers exiting from the market by going off-grid as storage technologies become affordable. Inefficient signals being sent back to the market about consumer preferences will exacerbate the situation.

In light of this it is imperative that the Energy White Paper does not miss the opportunity to take a long view of the next 20 years of the National Energy Market (**NEM**). A forward-looking White Paper must make sure that the NEM's governance and regulations are responsive and capable of delivering a

Consumer Action Law Centre

Level 7, 459 Little Collins Street
Melbourne Victoria 3000

Telephone 03 9670 5088
Facsimile 03 9629 6898

info@consumeraction.org.au
www.consumeraction.org.au

functioning market where competition is effective, consumers are engaged, and the benefits of effective asset utilisation are realised.

In its current form, the Energy Green Paper misses this opportunity. The White Paper must go further, ensuring that rapidly changing energy products and services do not leave regulators and rule makers behind. This would expose consumers to detriment and erode already low consumer trust.

There are numerous examples of poor consumer outcomes from exactly this situation in the energy market already—the Victorian roll out of smart meters and take up of Time of Use pricing to name a few. The White Paper must prioritise learning from past mistakes and not risk the value of the *Power of Choice* reforms or the potential of new technologies to increase consumer engagement and benefit. More detailed comments on how the governance and regulatory framework needs to evolve to meet the needs of the 21st century energy market are provided by theme below.

The Next 20 Years of the NEM

The Green Paper acknowledges that "our energy market is changing" and that "new energy technologies can emerge quickly". These two statements will characterise the coming decades in the NEM. New demand-side technologies and services, unleashed by the penetration of smart meters, will develop rapidly to meet consumer needs (which they may not have realised that they have yet) or fill market gaps. The opening up of competition in the energy market will also provide space for new market players, providing a web of companies and services that consumers can contract for their supply, demand and energy management. Consumption patterns will also change in response to price signals and more consumers expected to exit the network altogether.

Energy market innovation over the last decade has moved at an unprecedented pace. Examples include the rapid uptake of rooftop solar worldwide (and consequent plummet in prices) and the rise of electric vehicles with companies such as Tesla producing commercially available long-range models. Closer to home, the change to cost-reflective network tariffs is already underway in Victoria with distribution businesses investigating their preferred options as part of the current distribution price resets, each business suggesting different tariff structures in their area. This will lead to a 'confusopoly' where consumers stand little chance of understanding which tariff best suits their needs.

Rapid innovation provides great opportunity for consumers to find products and services that better suit their needs. However it can also come at a cost if innovation outstrips the ability of regulation to provide adequate consumer protection. The next 10-20 years in the NEM will test Australia's regulatory framework and its ability to manage the risk that consumers will be unable to find a good deal in an overwhelmingly complex market. If consumers are unable to engage, or don't trust a market which does not protect their interests, new technologies will not be adopted and the purpose of reform will not be realised.

It is therefore important to have planned for innovation, and the technologies and services that could have a role in Australia's future energy market. We welcome the Green Paper's commitment to a scenario-based assessment of the challenges and risks facing Australian electricity networks over the next two decades, to be led by the COAG Energy Council. We encourage the Department of Industry to make this project a priority in the White Paper and believe that it should be accompanied by

ambitious timeframes, as energy market innovation is already threatening to run away from our ability to appropriately guide it to manage risk.

While the CSIRO Future Grid Forum scenarios could be a useful starting point for this work, we believe a comprehensive assessment needs to go further, looking at the full suite of emerging technologies and the risks of consumer disengagement in the face of unprecedented choice and complexity.

Consultation with consumer groups will be fundamental to the value of this assessment task, and recommend that it is a clear commitment in the final White Paper.

Responsive Governance

Australia's energy market rules and regulations must be robust to new products, services and business models if they are to manage the risk of consumer disengagement by protecting consumer interests. It is vital that rule makers and regulators do not adopt a 'wait and see' approach, but are capable of proactive provision of market development guidance that does not leave consumers exposed to detriment, as this will only serve to undermine trust and exacerbate the current levels of disengagement and lack of trust.

A salient example of this is the industry-led roll out of smart meters and Time of Use (**TOU**) tariffs in Victoria. In the absence of appropriate regulatory oversight, the benefits and costs to consumers were not adequately considered, and the Victorian Auditor General found that there had been an "inequitable, albeit unintended, transfer of economic benefits from consumers to industry."¹ The report also found that "the regulatory regime [did] not give the industry enough incentive to manage risks and associated costs that consumers are likely to pay."

The release of the Auditor General's findings led to a moratorium on the roll out of TOU pricing in Victoria, amidst concerns that vulnerable consumers would be disproportionately impacted by flexible tariff structures. Retrospective regulation was introduced to protect consumers before TOU tariffs were rolled out. As a result of this process and the media it attracted, consumers have low trust in smart meters and little interest in TOU pricing in Victoria, with uptake currently at less than 0.3% of Victorian households.

The NEM market institutions—including the COAG Energy Council, Australian Energy Market Commission (**AEMC**) and Australian Energy Regulator (**AER**)—need to be capable of proactively identifying emerging market trends, and be equipped with adequately swift powers and resources to respond to these trends. The NEM governance bodies are currently not nimble enough to keep pace with the innovation we have seen to date, and the resultant regulatory challenge.

For example, Consumer Action in partnership with the Consumer Utilities Advocacy Centre proposed the first retail rule change in October 2013. The rule change proposal involved significant preparatory work, including consumer and economic research, that took months to prepare. The AEMC's rule change process took exactly one year to complete, with a determination proposing a change in the

¹ Victorian Auditor General's Office (2009). *Towards a 'smart grid' - the roll-out of Advanced Metering Infrastructure*. Accessed at: <http://www.audit.vic.gov.au/publications/2009-10/111109-AMI-Audit-Summary.pdf>

retail rules released this month. If this process is to guide future rule change processes, consumers will be forced to wait one to two years after a regulatory issue is identified for this issue to be addressed. Given the pace of market change, this delay means that potential reforms that are designed to improve competition and "energy productivity" will be too late to capture benefits. This critical issue must be more clearly addressed in the Energy White Paper.

The COAG Energy Council must focus its efforts on a high level strategic overview of the NEM, rather than detailed implementation issues that are best left to the AEMC, and prioritise the governance challenges identified in its scenario assessment. This will be critical to ensure that the NEM rules can guide the development of this market to ensure market benefit flows by protecting the interests of consumers.

Consumer Action believes that the first priority should be a review of the energy market governance bodies (particularly the AEMC and AER) to ensure that they are robust to the challenge of a more diverse, competitive and consumer-facing market, and have a clear mandate to effectively protect consumers' interests as the critical plank in unlocking market benefit. This review should not rule out major reform to the governance bodies to increase their efficacy and responsiveness, or increasing funding as required.

We wish to add one point in relation to the AER. Various state ministers and governments have agitated for reform of this body, and that it be separated from the ACCC. The Harper Review on Competition Policy has similarly recommended the creation of an "Access and Pricing Regulator" which would subsume the AER's functions as well as the economic regulatory functions of the ACCC in sectors such as telecommunications and water. These proposals will proliferate regulatory bodies in direct contrast to Federal Government policy to reduce the number of government agencies and bodies. Further, there are significant benefits in maintaining one national regulator responsible for competition, consumer protection and economic regulation. These functions all inter-relate and are based on an economic understanding that fair and effective markets are in the long-term interests of consumers. Maintaining the AER and ACCC relationship also ensures skills are shared between these institutions, and the broad focus of the ACCC contributes to it being less likely that the AER becomes captured by the industry it regulates—a significant risk for industry-specific regulators.

Effective Demand-side Participation

The Energy Green Paper focuses heavily on the use of flexible network tariffs to deliver a more efficient energy market, and provide affordability outcomes for consumers. While this is an important element of the reforms needed in the energy market to control cost increases, focussing too heavily on this single element of demand-side reform—which is already underway through *Power of Choice* review reforms—misses the opportunity to consider what policies and programs may be required to pull through other innovations which may assist consumers manage their energy consumption.

As previously stated, there will be many new products and services that may have a role to play, and the government should avoid picking winners. Rather it should ensure that a competitive demand-side market is developed, where consumers can understand the energy supply and demand choices available to them and make meaningful decisions about their preferences. Only in this way will efficient signals be sent back to market participants and innovators about the needs of consumers.

In order to bring about effective demand-side participation, the government must consider the technologies and services themselves, but also the way in which consumers are likely to engage with new products and what this means for the communication of benefits to consumers and their likely uptake.

The Green Paper states that “the COAG Energy Council is working to better understand what information and resources will best support consumer needs in future, including that provided by industry and governments.” We applaud this commitment and encourage a commitment to deeper engagement with the consumer advocacy sector as the Energy Council undertakes this task.

To that end, we attach a copy of our recent research report, *Smart Moves for a Smart Market: Simple steps to ensure consumer protections keep pace with innovation in a hi-tech energy market*.² This report assessed many of the emerging demand-side products and services for potential consumer benefit and detriment, and contextualised this with a survey of the views and concerns of over 300 real consumers. In it we identify key issues for consumers in a complex marketplace, including:

1. The framing of products and services

Consumers are more likely to choose a product or service that is framed as low risk or includes a reward.

2. The impact of choice overload

If consumers have to compare too many products or services, more often than not they will choose not to change from what they already have.

3. The use of approximate measures in decision making

Where the information available to consumers to inform their decision is too complicated, or choices too vast, consumers will base decisions on approximate measures.

4. The influence of default biases

Consumers value things more once they have already 'owned' them. They are therefore more likely to accept the status quo, or the existing product, over change.

5. Use-pattern mistakes

Consumers will make decisions thinking they can change their behaviour to receive an offered benefit, when in reality change is unlikely, leading to consumer detriment.

We also identify priority areas for the energy market to consider in the development of new products and services if consumers are to be engaged, including that:

- Consumers must see the benefit early on;
- Privacy and data security must be addressed from the outset;
- Market access must be provided to all consumers, regardless of socio-economic background;
- Information must be clear and relevant;
- Flexibility will be essential; and
- Some level of standardisation of products and services will be necessary.

The importance of getting these elements right cannot be overstated in a complex market that relies on the informed engagement of consumers to unlock market benefit. Research undertaken for Ofgem in the context of their 2011 retail market review, on the layout of bills etc and use of language to

² <http://consumeraction.org.au/wp-content/uploads/2014/08/Smart-Moves-for-a-Smart-Market-eVersion.pdf>

encourage consumer participation recommended that “if we want consumers to understand the energy market sooner rather than later, we have to begin by favouring their existing knowledge”.³ The White Paper needs to acknowledge the logical extension of this—that to deliver lasting and effective reform in the NEM, we need to start where consumers are and provide products and services that play into the way they already make decisions, and not wait for them to become perfectly informed and rational economic decision makers.

A recent article by Nicholas Biddle and Katherine Curchin argues that behavioural insights—in addition to economic considerations—must form part of public policy developments by government. They argue that “real humans are not worse than economic man. We’re just different and we deserve policies made for *Homo sapiens* and not *Homo economicus*”.⁴ It is no longer acceptable to allow markets to emerge and innovate on the basis of classical economics alone.

The NSW Government has adopted these ideas through its Behavioural Insights Unit, which is part of the Department of Premier and Cabinet.⁵ To date, work has focused on how consumers engage with government services, but there are opportunities to consider how consumers engage within markets. This can include the use of 'nudges'—amending choice architecture to influence people’s behaviour in a predictable way without forbidding any options or significantly changing their economic incentives. Defaults are another powerful measure to consider, especially in essential service markets. For consumers who do not engage, perhaps due to disadvantage or vulnerabilities, defaults would ensure "safe" products and services are delivered. While there are default options available in today's retail energy market, i.e. the standing offer, it is ironic that these provide for the least "safe" option because they are generally priced much higher than market offers.

There is significant opportunity to apply behavioural insights to 'demand response' policies and programs. Rather than the traditional approach of establishing pricing structures that incentivise consumers to choose new products and services, by recognising that consumers are bad at calculating complex formulas or understanding risks in contractual terms and conditions there is significant potential to enhance energy productivity through demand load control. This has been used successfully in Queensland by Energex, where air conditioner cycling and remote control of pool pumps has contributed to reduced energy use at times of otherwise high demand. This has been achieved without the loss of amenity or the need for consumers to make complex choices.⁶ Consumers can be reticent about remote control of appliances, due to the lack of trust of industry 'taking control' of appliances. There is a need to consider behavioural research to inform the development of these policies and programs so as to ensure energy productivity goals are realised.

We believe that the findings from behavioural economics and insights must be considered by the government, in the context of the White Paper and more broadly, in the development of consumer protections that are suited to the 21st century energy market. It is critical that consumers are able to

³ Lawes Consulting (2011). *Retail Market Review: Energy bills, annual statements and price rise notifications; advice on layout and the use of language*. Accessed at: <https://www.ofgem.gov.uk/ofgem-publications/39652/laweslangagereport.pdf>

⁴ Biddle, N. and Curchin, K. (2014). *The promise and perils of giving the public a policy 'nudge'*. Published in *The Conversation*, 1 May 2014. Accessed at <http://theconversation.com/the-promise-and-perils-of-giving-the-public-a-policy-nudge-24887>

⁵ <http://bi.dpc.nsw.gov.au/>

⁶ See case study on page 73 of *Smart Moves for a Smart Market* or go to <https://www.energex.com.au/residential-and-business/rewards-for-air-conditioning-pools-and-hot-water>

confidently engage in the market and trust that their product choices will benefit them. Consumer Action will work with industry and governments to inform the development of these consumer protections. We encourage the Department of Industry and COAG Energy Council to be involved.

Energy Affordability

Network tariff reform, as well as increasing demand-side technology and participation, will create winners and losers. While the Green Paper contends that low-income and vulnerable consumers should stand to benefit from more flexible network tariffs, we do not believe this will always be the case. The new market creates high potential for non-participation and consumer disadvantage (see section 2.3 of *Smart Moves for a Smart Market* in Appendix 1). In particular, low-income and vulnerable consumers may have less ability to shift their demand, as will families with children,⁷ and those living in rental housing will have limited ability to influence the appliances in their home to make use of the benefits of smart metering.

Low-income people are much more likely to live in poor housing stock and have less control over their energy consumption from fixed appliances. They are therefore much more likely to be high energy consumers, and spend a greater proportion of their income on energy bills. In 2012, low-income households spent approximately 12 per cent of their income on energy, compared to just 5.3 per cent for all households combined. In terms of household energy alone, these figures change to 5.4 per cent and 2 per cent respectively.⁸

It is therefore critical that the government supports reforms involving targeted energy productivity measures designed to help with the overall affordability of energy for low-income and vulnerable Australians, but also to ameliorate the impacts of changing pricing structures on those that will not benefit. Household energy productivity can assist low-income households gain greater wellbeing for the energy that they can afford or do use, or attain an acceptable level of wellbeing at lower cost. In the context of rising energy prices (and especially while government-supported incomes rise more slowly), this is extremely important.

The Greenhouse and Energy Minimum Standards (**GEMS**) are an important part of the productivity programs required, and we encourage government to maintain the program in its existing form. Low-income consumers will always gravitate to the lower performing end of the product market, given their lack of access to upfront capital to invest in more efficient appliances—it is therefore critical that we ensure that there are minimum product standards which protect consumers from buying very inefficient appliances. We are also very supportive of the clear labelling which the GEMS program delivers to assist consumers to compare products.

However the GEMS program alone will not be sufficient to increase the energy productivity of Australian households, and particularly those of low-income and vulnerable Australians. With the abolishment of the Household Energy Saver Scheme (**HESS**), there is a gap in the household energy

⁷ Nicholls, L and Strengers, Y (2014). *Changing demand: Flexibility of energy practices in households with children*. RMIT University. Accessed at <http://mams.rmit.edu.au/5wj0prabkxjv1.pdf>

⁸ Australia Bureau of Statistics (2013) *4670.0 - Household energy consumption survey, Australia: Summary of results, 2012*. Accessed at:

[http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/4670.0~2012~Media%20Release~Households%20spend%20\\$99%20per%20week%20on%20energy%20\(Media%20Release\)~10000](http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/4670.0~2012~Media%20Release~Households%20spend%20$99%20per%20week%20on%20energy%20(Media%20Release)~10000)

productivity policy suite, which must be addressed. It is critical that the Energy White Paper makes a firm commitment to a new in-home energy productivity service, targeted at low-income and vulnerable groups.

In this context, Consumer Action would welcome a National Productivity Plan as long as it was accompanied by an appropriately resourced in-home program to assist disadvantaged Australians manage their energy bills and expenditure. Alone, a National Productivity Plan will not go far enough to address the real energy affordability need amongst consumers right now.

The White Paper must also commit to the maintenance for the Renewable Energy Target (**RET**) in its current form. The government's own modelling found that the maintenance of the RET was the best way to keep energy prices low in Australia. With energy prices becoming increasingly unaffordable for many Australians, we strongly support the RET both for its role in transforming Australia's energy sector and its ability to lower wholesale energy prices. Importantly, the RET has encouraged new energy firms into the market place, producing more effective competition in the retail sector. There is an ongoing need to support effective competition in the retail sector, so that it can play its role in ensuring prices and services are in accordance with consumer needs and requirements.

Finally, we believe it is critical to energy affordability that the government takes a serious view on the impending increase in gas prices across the NEM states. The White Paper must deliver programs that keep the cost of gas for households down, and that help consumers manage any increase in costs. Consumer Action supports the position of the Consumer Utilities Advocacy Centre on the residential gas market in their submission to the Energy Green Paper.

Conclusion

Australia's energy market is becoming more complex as the nature of energy demand changes, and consumers are exposed to greater opportunities for demand-side participation. During this dynamic time, innovation will be the key to ongoing prosperity, but also to consumers realising the benefits of new products and services in managing their energy expenditure. For this new market to be competitive, productive and fair, it will be vital to empower consumers to engage with it.

If consumers fail to engage, or can't engage in an informed way, there is a real risk that the market will not achieve its intended aims of peak load reductions, increasing the productivity of existing network infrastructure, delaying new network investment, decreasing the price of energy and providing better outcomes for consumers.

Further, if consumers are left behind because the market has been designed for the privileged few, there is significant potential for inequity, hardship and adverse impacts to the already most vulnerable members of our communities.

Simple steps to ensure innovation and consumer protections keep pace will enable this emerging market to be truly smart.

Within this context we recommend that the White Paper:

1. Prioritise the COAG-led scenario-based assessment of the next 20 years of the NEM, and broaden it to commit to a broad suite of scenarios, ambitious timelines and consultation with consumer groups in its development.
2. Commit to a COAG-led full review of the suitability of the current market governance institutions to effectively regulate in a 21st century energy market, with recommendations from this review not ruling out major reform to the governance bodies or increased funding.
3. Consider the findings of *Smart Moves for a Smart Market* and applies its principles to all demand-side policies and programs delivered by the White Paper.
4. Undertake to develop a new consumer protection framework in consultation with consumer groups and industry in light of the findings of *Smart Moves for a Smart Market* and other relevant consumer-focussed research.
5. Commit to the retention of the GEMS program in its current form.
6. Commit to a new in-home energy efficiency program for low-income and vulnerable households.
7. Commit to the maintenance of the RET in its current form.